

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA

In Re:)
)
Michael W. Johnson and) Bankruptcy No. 02-60544
Barbara Johnson,) Chapter 13
)
)
Debtors.)

**NOTICE OF MOTION AND MOTION FOR MODIFICATION (DATED SEPT. 7, 2004)
OF CHAPTER 13 PLAN (DATED MAY 23, 2002) AFTER CONFIRMATION
PURSUANT TO 11 U.S.C. § 1329**

1. Michael Farrell, trustee for the bankruptcy estate of Michael W. and Barbara Johnson, by and through his counsel, Lowell P. Bottrell, hereby moves the court for relief requested below and gives notice of hearing.

2. The Court will hold a Hearing on this motion at 10:00 a.m., on September 28, 2004, in the U.S. Bankruptcy Court, 205 U.S. Post Office Courthouse Building, 118 South Mill Street, Fergus Falls, Minnesota 56537.

3. Any response to this motion must be filed and delivered no later than 10:00 a.m., on September 23, 2004, on all parties required to be served pursuant to Local Rule 9013-3, which is three days before the time set for this hearing, (excluding Saturdays, Sundays, and holidays) or filed and served by mail no later than September 17, 2004, which is seven days before the time set for the hearing (excluding Saturdays, Sundays, and holidays). UNLESS A RESPONSE OPPOSING THE MOTION IS TIMELY FILED, THE COURT MAY GRANT THE MOTION WITHOUT A HEARING.

4. The court has jurisdiction over this motion pursuant to 28 U.S.C. §§ 157 and 1334, Fed. R. Bankr. P. 5005 and Local Rule 1070-1. This proceeding is a core

proceeding. The petition commencing this Chapter 13 case was filed on May 30, 2002. The case is now pending in this court.

5. This motion arises under 11 U.S.C. § 1329 and Fed. R. Bankr. P. 3015. This motion is filed under Fed. R. Bankr. P. 9014 and Local Rules 9013-1 – 9019-1(d).

6. This case was originally filed as a chapter 13 case on May 30, 2002. At that time in their Schedule B, the debtors did not identify that they had any beneficial interest in any trusts or interests in any life estate.

7. Their chapter 13 bankruptcy plan dated May 23, 2002 was confirmed by an order dated July 24, 2002. Their plan of reorganization provided for a payment to the unsecured creditors of approximately 10%.

8. The debtors were to pay under their plan of reorganization the sum of \$630.00 per month for 36 months for a total sum of \$22,680.00. The debtors are current on their payments as of August 30, 2004.

9. Subsequent to the confirmation of their plan of reorganization, the debtors have learned that Barbara Johnson was the beneficiary under two trusts in which she received life insurance proceeds. First, she was a beneficiary under the Marvel E. Dyrdal Trust Agreement dated March 28, 1990. Next, she was also a beneficiary interest holder under the Dyrdal Family Irrevocable Trust Agreement dated March 30, 1994. See Amendments to Schedule B dated August 18, 2004, item no. 19. According to the those schedules, Barbara Johnson, one of the debtors in these proceedings, received \$70,052.00 on May 28, 2004, from the Marvel E. Dyrdal Trust Agreement via a Pacific Life Insurance Policy and \$41,248.00 on the same date from the Dyrdal Family Irrevocable Trust via a Sun Life Insurance Policy. The total sum received was the sum

of \$111,300.00. These sums of the money are in the possession of the debtors and have not been turned over to the chapter 13 trustee, Michael Farrell.

10. Based upon information provided by the debtors' attorney, Barbara Johnson's mother died approximately Thanksgiving of 2003 and her father died in March of 2004. The debtors, after they received the proceeds, brought this to the attention of the trustee.

11. Despite having amended their schedules, the debtors have not modified their plan consistent with 11 U.S.C. § 1329. The debtors are obligated to amend the plan consistent with 11 U.S.C. § 1329 to increase their payments as the debtors have not completed payments under the plan of reorganization and they should be required to pay the unsecured class of creditors those net monies received, if any, from the receipt of the inheritances or distributions from trusts. Therefore, Class IX dealing with claims of the unsecured creditors should be modified to increase their distribution to reflect these proceeds that are available from these distributions. A one time lump sum from these trusts should be paid to the estate to be paid only to the unsecured class of creditors, Class IX. This modification should not affect future plan payments and should not change the amounts due to this or other creditors.

12. The trustee may call as witnesses in this case the trustee, Michael Farrell, to testify as to the plan of reorganization and the distributions that have been made to those creditors and the remaining debt owed to the unsecured creditors. The trustee may also call Barbara and Michael Johnson to testify as to the distributions received from the various trusts and the payments to the unsecured creditors and availability of money consistent with the plan of reorganization.

WHEREFORE, the chapter 13 trustee requests that the court modify the plan of reorganization confirmed in this case consistent with 11 U.S.C. § 1329 to take into consideration the net proceeds received from monies from the distribution of the various trusts.

Dated this 7th day of September, 2004.

/e/ Lowell P. Bottrell
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Attorneys for Trustee

VERIFICATION

I, Michael J. Farrell, chapter 13 bankruptcy trustee for the estate of Michael W. and Barbara Johnson, declare under penalty of perjury that the foregoing is true and correct according to the best of my knowledge, information and belief.

Dated this 7th day of September, 2004.



Michael J. Farrell, Chapter 13 Trustee

111744\motion to modify

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA

In Re:)
)
Michael W. Johnson and) Bankruptcy No. 02-60544
Barbara Johnson,) Chapter 13
)
)
Debtors.)

**MEMORANDUM IN SUPPORT OF MODIFICATION (DATED SEPTEMBER 7, 2004)
OF CHAPTER 13 PLAN (DATED MAY 23, 2002) AFTER CONFIRMATION
PURSUANT TO 11 U.S.C. § 1329**

I. FACTS

This case was originally filed as a Chapter 13 case on May 30, 2002. The debtors' chapter 13 bankruptcy plan dated May 23, 2002 was confirmed by an order dated July 24, 2002. The debtors' plan of reorganization provided for a payment to the unsecured creditors of approximately 10%. The debtors were to pay under their plan of reorganization the sum of \$630.00 per month for 36 months for a total sum of \$22,680.00. The debtors are current on their payments as of August 30, 2004.

Subsequent to the confirmation of their plan of reorganization, the debtors have learned that Barbara Johnson was the beneficiary under two trusts in which she received life insurance proceeds. First, she was a beneficiary under the Marvel E. Dyrdal Trust Agreement dated March 28, 1990. Next, she was also a beneficiary interest holder under the Dyrdal Family Irrevocable Trust Agreement dated March 30, 1994. See Amendments to Schedule B dated August 18, 2004, item no. 19. According to the those schedules, Barbara Johnson, one of the debtors in these proceedings, received \$70,052.00 on May 28, 2004, from the Marvel E. Dyrdal Trust Agreement via a Pacific Life Insurance Policy and \$41,248.00 on the same date from the Dyrdal Family

Irrevocable Trust via a Sun Life Insurance Policy. The total sum received was the sum of \$111,300.00. These sums of the money are in the possession of the debtors and have not been turned over to the chapter 13 trustee, Michael Farrell.

Based upon information provided by the debtors' attorney, Barbara Johnson's mother died approximately Thanksgiving of 2003 and her father died in March of 2004. The debtors, after they received the proceeds, brought this to the attention of the trustee.

Despite having amended their schedules, the debtors have not modified their plan consistent with 11 U.S.C. § 1329. The debtors are obligated to amend the plan consistent with 11 U.S.C. § 1329 to increase their payments as the debtors have not completed payments under the plan of reorganization and they should be required to pay the unsecured class of creditors those net monies received, if any, from the receipt of the inheritances or distributions from trusts. Therefore, Class IX dealing with claims of the unsecured creditors should be modified to increase their distribution to reflect these proceeds that are available from these distributions. A one time lump sum from these trusts should be paid to the estate to be paid only to the unsecured class of creditors, Class IX. This modification should not affect future plan payments and should not change the amounts due to this or other creditors.

II. LAW AND ARGUMENT

A. PROPERTY OF THE ESTATE & DISPOSABLE INCOME

Unlike a Chapter 7 liquidation case, after-acquired property is included in a Chapter 13 estate. 11 U.S.C. § 1306(a)(1) provides that all property of the estate includes all property of the kind as specified in §541 that is acquired by the debtor “after the commencement of the case, but before the case is closed, dismissed, or converted. . . .” Courts have consistently held that lottery winnings and inheritance received post-petition is property of the bankruptcy estate. In re Nott, 269 B.R. 250 (Bankr.M.D.FI. 2000); In re Guentert, 206 B.R. 958 (Bankr.W.D.Mo.1997); In re Easley, 205 B.R. 334 (Bankr.M.D.FI 1996). FI 1996); In re Cook, 148 B.R. 273 (Bankr.W.D.MI 1992); In re Corneil, 95 B.R. 219 (Bankr.W.D.Okla.1989); In re Euerle, 70 B.R. 72 (Bankr.D.NH 1987); In re Koonce, 54 B.R. 643 (Bankr.D.S.C.1985).

11 U.S.C. 1325 (b)(2) defines “disposable Income” as income received by the debtor that is not reasonably necessary to support the debtor, the debtor’s dependants, or the debtor’s business. In re Koch, 109 F.3d 1285, 1289 (8th Cir. 1997). The definition of disposable income neither includes nor excludes income on the basis of its exempt or non-exempt status and thus exempt property shall also be included in the disposable income test. Id.; In re Florida, 268 B.R. 875, 880 (Bankr.M.D.FI. 2001). See also In re Taylor, 212 F.3d 395 (8th Cir. 2000)(holding that an ERISA-qualified pension should be considered in the calculation of a petitioner’s disposable income). Courts have consistently held that post-petition inheritance represents disposable income. In re Bass, 267 B.R. 812 (Bankr.S.D.Ohio 2001)(holding that wage increases, tax refunds, inheritances, gifts, lottery proceeds, and insurance proceeds are disposable income); In

re Jacobs, 263 B.R. 39 (Bankr.N.D.N.Y.2001)(holding for purposes of plan modification, a windfall to the debtor where the debtor receives lottery winnings or an unexpected inheritance constitutes a substantial change and is disposable income); Agribank v. Honey, 167 B.R. 540 (W.D.MI 1994)(holding inheritance is disposable income).

B. SECTION 1329 - - MODIFICATION OF PLAN AFTER CONFIRMATION

11 U.S.C. § 1329 provides that the Chapter 13 trustee may request modification of a confirmed plan prior to the completion of the plan for three purposes:

(a) At any time after confirmation of the plan, but before the completion of payments under such plan, the plan may be modified, upon request of the debtor, the trustee, or the holder of an allowed unsecured claim, to –

(1) increase or reduce the amount of payments on claims of a particular class provided for by the plan;

(2) extend or reduce the time for such payments; or

(3) alter the amount of the distribution to a creditor whose claim is provided for by the plan to the extent necessary to take account of any payment of such claim other than under the plan.

Section 1329(b)(1) makes the requirements of Section 1325(a) applicable to any modification under subsection 1329(a). See 11 U.S.C. § 1329(b)(1)

The policy underlying §1329 is consistent with the general policy of Chapter 13 of the Bankruptcy Code:

Section 1329 is intended to promote the ability to pay standard to allow upward or downward adjustment of plan payments in response to changes in a debtor's circumstances which substantially affect the ability to make future payments. Accordingly, post confirmation plan modification is usually sought by a debtor when there has been an unanticipated and substantial decrease in income (e.g., unemployment) or by an unsecured creditor or the trustee when the debtor experiences an increase or windfall (e.g., an inheritance or lottery winning).

In re Nott, 269 B.R. 250 (Bankr.M.D.FI. 2000) citing In re Trumbas, 245 B.R. 764, 767 (Bankr.D.Mass.2000). In this case at bar, the debtors received proceeds in the amount

of \$111,300.00. This substantial, unanticipated change clearly is a windfall to the debtors.

1. BEST INTEREST TEST – - SECTION 1325 (A)(4)

Accordingly, the “best interest test” must be met. 11 U.S.C. § 1325(a)(4), often referred to as the “best interest test”, states as follows:

(4) the value as of the effective date of the plan, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under Chapter 7 of this title on such date.

Debtors are likely to argue that the words “as of the effective day of the plan” refer to the effective date of the original plan. Consequently, the Debtor’s are likely to argue that this values applied as of the date of the original hearing where confirmation was approved, remain the values to be included in the application of 11 U.S.C. § 1325(a)(4) at the time that a modification is considered by the Court. The leading case following this analysis is In re Forbes, 215 B.R. 183 (8th Cir. BAP 1997). In the Forbes case, not only did the Court hold that the best interest test must be performed with valuations taken from the original confirmation, it held that the best interest test should not even be a factor in the post-confirmation modification. Id. at 191-92.

Obviously, it is the trustee’s position that the words “as of the effective day of the plan” refer to the “effective date of the modification” and consequently require that this test be applied as of the date of the modification. Otherwise, 11 U.S.C. § 1329 would have no meaning. The Forbes decision has been highly criticized by other Courts on this issue. All these courts held that the “best interest test” is applied as of the effective day of the modification. In re Stinson, 302 B.R. 828 (Bankr.D.Md. 2003); In re Morgan,

299 B.R. 118 (Bkrcty.D.Md.2003); In re Jefferson, 299 B.R. 468 (Bkrcty.SD.Ohio 2003); In re Profit, 269 B.R. 51 (Bankr.D.Nev.2001); In re Nott, 269 B.R. 250 (Bankr.M.D.Fla.2000); In re Barbosa, 236 B.R. 540 (1999), aff'd 243 B.R. 562 (D.Mass.2000); aff'd 235 F.3d 31; In re Martin, 232 B.R. 29 (Bkrcty.D.Mass.1999); In re Guentert, 206 B.R. 958 (Bankr.W.D.Mo.1997); In re Walker, 153 B.R. 565 (Bankr.D.Or.1993).

First, the legislative history clearly indicates that Congress intended “as of the effective day of the plan” to mean the effective date of the modification:

In applying the standards of proposed 11 U.S.C. §1325(a)(4) to the confirmation of a modified plan, “the plan” as used in the section will be the plan as modified under this section, by virtue of the incorporation by reference into this section of proposed 11 U.S.C. §1323 (b). Thus, the application of the liquidation value test must be redetermined at the time of the confirmation of the modified plan. In re Morgan, 299 B.R. 118, 124-25 (Bkrcty.D.Md.2003) citing H.R.Rep. No.595, 95th Cong., 1st Sess. 431 (1977), U.S. Code Cong. & Admin.News pp.5787, 6386, 6387.

Moreover, the Forbes case cites and relies on Judge Lundin’s treatise. However, Judge Keith Lundin writes in his updated treatise:

For purposes of the measuring whether a proposed modification satisfies the test in §1325(a)(4), it might be reasonable to liquidate the estate on the effective date of the plan as modified. The effective date of the modified plan will probably be either the date of the entry of the order approving the modified plan or some later date defined by the plan.

In re Morgan, 299 B.R. 118, 124 (Bkrcty.D.Md.2003) citing Keith M. Lundin, Chapter 13 Bankruptcy, 3d Ed. §254.1.254-2 (2000 & Supp.2002).

To apply the best interest test as of the date of the initial confirmation date yields an inequitable result, i.e, the debtor receives a significant windfall, while the claims of the unsecured claimants would receive only a small percentage of their claims. A

chapter 7 liquidation hypothetically occurring on the date of the modification would yield to the unsecured creditors a pro-rata distribution of the proceeds in question. In view of Congress's intent in enacting Chapter 13 to encourage debtors to repay their debts to the best of their ability, it would be in direct contradiction to allow Debtors to retain inheritance proceeds without first satisfying their unsecured claims. Therefore, after a review of the existing caselaw, consideration of the language of §1325(a)(4) and the legislative history for the modification provisions, the Court should determine that the appropriate date for performing the liquidation analysis required by §1329(b) and 1325(a)(4) is the effective date of the modified plan.

2. BEST EFFORTS/DISPOSABLE INCOME TEST - - SECTION 1325(B)

Moreover, the "Best Efforts/Disposable Income test" must be met as well. The "best efforts/disposable income" test, located at 1325(b), provides in part that:

- (1) If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the court may not approve the plan, unless, as of the effective date of the plan - -

(B) the plan provides that all of the debtor's projected disposable income to be received in the three-year period beginning on the date that the first payment is due under the plan will be applied to make payments under the plan.

The trustee contends that the debtor is required to perform the "disposable income/best efforts tests" in analyzing modification of a plan. The Debtor's likely position is that this test does not apply to post-confirmation plan modifications.

There is a split in authority as to whether 1325(b) applies to post-confirmation modification. Again, the Debtor likely will rely on the Forbes case. While recognizing that the omission of §1325(b) from §1329(b)(1) may have been an oversight, the Forbes

court declined to require the application of the “best efforts” test to post-confirmation plan modification because the subsection was omitted from §1329(b). In re Forbes, 215 B.R. at 191. However, again, the Forbes decision has been criticized by other Courts and by Judge Lundin’s Treatise, on this issue as well, holding that the best efforts test is applicable in postconfirmation plan modifications. In re Martin, 232 B.R. 29, 36 (Bkrtcy.D.Mass.1999).

The argument for inclusion of the test as a requirement is that under Section 1325(a), which provides in pertinent part, ‘Except as provided in subsection (b), the court shall confirm a plan if – (1) the plan complies with the provisions of this chapter and with other applicable provisions of this chapter and with other applicable provisions of this title. . . .’ 11 U.S.C. §1325. In re Martin, 232 B.R. at 36. Therefore, Section 1325(b) is implicated by both section 1325(a)’s preface “except as provided in subsection (b)” and by Section 1325(a)(1)’s blanket application of the chapter provisions. Moreover, Judge Lundin, in his treatise, comes to the following conclusion:

Though there is no illuminating legislative history, the language of §§ 1329 and 1325 favors the interpretation that the disposable income test applies at confirmation of a modified plan. Policy arguments favor application of the disposable income test at confirmation of a modified plan....Applying the projected disposable income test at confirmation of a modified plan would go a long way to eliminating the "danger" that a Chapter 13 debtor would experience a significant improvement in financial condition after confirmation of the original plan and not share that good fortune with prepetition creditors. The logic of the projected disposable income test does not support its application at modification of a confirmed plan....If the projected disposable income test is applied again and again, each time the trustee or the holder of an allowed unsecured claim moves for modification of a plan after confirmation, then the concept of "projected" is meaningless...This conundrum only serves to emphasize that the interaction of the disposable income test in § 1325(b) and the modification of plans under § 1329 was not well conceived. The 1984 amendments enabling the Chapter 13 trustee and allowed unsecured claim holders to seek postconfirmation modification have exacerbated these problems of statutory

construction. It is unlikely that the drafters of § 1329(b) intended to preclude modification of all plans that have survived two years after the first payment was due under the original plan and in which unsecured claim holders cannot be paid in full in less than three years.

In re Martin, 232 B.R. at 36-37 citing 2 Keith M. Lundin, Chapter 13 Bankruptcy §6.46 (2nd ed.1994).

Such a large windfall is the type of occurrence that falls squarely under 1329. Large inheritances mandate modification as much as any downturn in circumstances would. Receiving in excess of \$100,000 is a cause to pay more than a 10% dividend to unsecured creditors. It is only equitable that the creditors be allowed to share in the windfall. Therefore, after a review of the existing caselaw, the Lundin treatise, consideration of the language of §1325, the Court should determine the disposable income test applies at confirmation of a modified plan.

III. CONCLUSION

For the reasons stated above, the Chapter 13 Trustee requests that the Court modify the plan of reorganization confirmed in this case consistent with 11 U.S.C. § 1329 to take into consideration the net proceeds received by the debtors.

Dated this 7th day of September, 2004.

/e/ Lowell P. Bottrell
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UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA

In Re:)
)
Michael W. Johnson and) Bankruptcy No. 02-60544
Barbara Johnson,) Chapter 13
)
)
Debtors.)

DECLARATION RE: ELECTRONIC FILING

Title of Document to be Electronically Filed: Motion to Modify Chapter 13 Plan

Filing Date: September 7, 2004

I, Michael J. Farrell, declare under the penalty of perjury, that I am the person who signed the above named document, that the information provided in the document is true and correct, that I consent to the document being electronically filed with the clerk of the United States Bankruptcy Court on September 7, 2004 and that I understand that this Declaration Re: Electronic Filing is to be filed with the clerk no later than five days after the above named document has been electronically filed.

Executed on: September 7, 2004

Signed: _____



Name and Address of Subscriber:

Michael J. Farrell
P.O. Box 519
Barnesville, MN 56514
Chapter 13 Bankruptcy Trustee of the
Estate of Michael W. and Barbara Johnson

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA

In Re:)
)
Michael W. Johnson and) Bankruptcy No. 02-60544
Barbara Johnson,) Chapter 13
)
Debtors.)

**ORDER APPROVING MODIFICATION
OF CHAPTER 13 PLAN (DATED MAY 23, 2002)**

This matter came before the court on a motion by the trustee to modify the chapter 13 plan. The court made its findings and conclusions on the record. Based on the Local and Federal Rules of Bankruptcy Procedure, it is

HEREBY ORDERED THAT:

The debtors shall modify their plan of reorganization such that the unsecured creditors shall receive a one time payment of the sum of \$111,300.00 from the following trusts: the Marvel E. Dyrdal Trust Agreement dated March 28, 1990 and the Dyrdal Family Irrevocable Trust Agreement dated March 30, 1994. These sums shall represent the total obligation needed for the debtors to contribute for monies received from these Trusts. This order does not relieve the debtors of liability of paying their monthly payments under the plan of reorganization. The remaining terms and conditions of the plan dated May 23, 2002 where not in conflict with this order, shall remain in full force and effect.

Dated this 28th day of September, 2004.

Dennis D. O'Brien
United States Bankruptcy Judge