

UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF NEW YORK

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IN RE:

WILLIAM L. REED

CASE NO. 00-65582

Debtor Chapter 13

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APPEARANCES:

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Hon. Stephen D. Gerling, Chief U.S. Bankruptcy Judge

**MEMORANDUM-DECISION, FINDINGS OF FACT,  
CONCLUSIONS OF LAW AND ORDER**

Under consideration by the Court is the Fourth Amended Chapter 13 Plan ("Plan") filed by William L. Reed ("Debtor") on June 12, 2002. Opposition to the Plan's confirmation was filed by Manufacturers and Traders Trust Co. ("M&T") on June 18, 2002.<sup>1</sup> M&T contends that the Plan is not

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<sup>1</sup> The chapter 13 trustee, Mark W. Swimelar, Esq. ("Trustee") also filed an objection to the Debtor's Plan on June 28, 2002, which he later withdrew, having received confirmation from the Debtor

feasible. In addition, M&T argues that the Plan violates § 1325(a)(1) and (3) of the United States Bankruptcy Code, 11 U.S.C. §§ 101-1330 (“Code”), in that the Debtor is not eligible for chapter 13 relief as provided in Code § 109(e).

The confirmation hearing to consider the Debtor’s Plan was held on September 10, 2002, at Binghamton, New York, and an evidentiary hearing was conducted on October 30, 2002, in Utica, New York (“October 2002 Hearing”). Following testimony by a number of witnesses, including the Debtor, the parties were afforded an opportunity to file memoranda of law. The matter was submitted for decision on November 29, 2002.

### **JURISDICTIONAL STATEMENT**

The Court has core jurisdiction over the parties and subject matter of this contested matter pursuant to 28 U.S.C. §§ 1334, 157(a), (b)(1) and (b)(2)(L) and (O).

### **FACTS**

The Debtor filed a voluntary petition pursuant to chapter 13 of the Code on November 13, 2000. Debtor is employed by Extended Stay America Management, Inc. (“ESA”) to develop real estate parcels on which to construct hotels. Debtor testified at a prior hearing on July 26, 2001 (“July

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regarding his obligation to pay certain expenses associated with his children’s college education.

2001 Hearing”), that he is involved with the zoning and planning for the real estate parcels and oversees the construction of the hotel before turning it over to the company to operate. At the time of the July 2001 Hearing, he testified that he earned \$86,500 per year. At the October 2002 hearing, it was Debtor’s testimony that he is currently earning approximately \$90,000 per year. His net monthly take home pay is \$5,491.12, an increase of \$566.78 from that listed previously in his schedules. *See* Debtor’s Amended Schedule I, filed June 12, 2002. He also identifies \$3,850 per month from rental income. *See id.* His wife, Millicent Reed, testified that she was employed as Director of Career Services at the College of Hotel Administration at Cornell University, earning approximately \$60,000 per year.<sup>2</sup> She acknowledged her willingness to contribute to their children’s college education, as well as household expenses, thereby supplementing the Debtor’s income. According to Amended Schedule I, she intends to contribute \$1,291.52 per month. Thus, the Debtor’s total monthly income is \$10,612.64. *See id.*

Debtor’s monthly expenses, including expenses associated with certain rental property owned by him, total \$10,130.67, a decrease from the \$12,356 listed in his prior schedules. *See* Debtor’s Amended Schedule J, filed June 12, 2002.<sup>3</sup>

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<sup>2</sup> According to Amended Schedule I, filed June 12, 2002, Debtor’s wife earns a monthly income of \$3,640.40 after payroll deductions.

<sup>3</sup> A comparison of the schedule of expenses filed on June 12, 2002, with that filed August 17, 2001, shows a decrease in the amount of monies associated with income property expenses from \$6,900 to \$3,450. Debtor also testified that he currently has approximately \$3,000 to \$4,000 set aside as a reserve.

Debtor and his wife reside at 162 Genung Road, Ithaca, New York (“Residence”).<sup>4</sup> As previously found in the Court’s Memorandum Decision, Findings of Fact, Conclusions of Law and Order, dated May 15, 2002 (“May 2002 Decision”)<sup>5</sup>, the Residence was appraised at \$240,000. M&T filed a proof of claim on March 12, 2001, in the amount of \$299,395.76 in connection with its mortgage on the Residence. At the October 2002 Hearing, James C. Countryman (“Countryman”), Assistant Vice President and Senior Loan Recovery Officer for M&T, testified that the principal on the two loans on the Residence, as of the date of filing, totaled \$283,561.33. Amended Schedule J shows monthly mortgage payments of \$1,548.67 during the five years of the Plan.<sup>67</sup>

John Novarr (“Novarr”) testified that he had been active in real estate development in the Ithaca area for approximately 25 years. He acknowledged an acquaintance with the Debtor, whom he had met approximately 20 years ago while working as a loan officer. He testified that he had built the Debtors’ Residence approximately 12 years ago. He described it as being located in an upscale section of Ithaca. According to Novarr, the residential housing market in the Ithaca area had “skyrocketed” this year and prospective home buyers were actually offering more than the asking price to obtain quality

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<sup>4</sup> At the July 2001 Hearing, the Debtor testified that there is an apartment located above the garage at the Residence for which the Debtor receives rent of \$380 per month.

<sup>5</sup> In the May 2002 Decision the Court denied confirmation of Debtor’s Third Amended Plan based on the finding that the Debtor had failed to establish that it was feasible.

<sup>6</sup> Debtor previously testified at the July 2001 Hearing that the monthly payments to M&T on the Residence prepetition totaled \$2,600.

<sup>7</sup> By Order, dated July 10, 2002, the Court required the Debtor to make adequate protection payments of \$4,000 per month to M&T on its mortgages, “until such time as an Order may issue confirming a plan in this case” or the granting of relief from the automatic stay as requested by M&T by motion dated June 3, 2002.

residential housing.

In addition to his employment with ESA, the Debtor also owns certain commercial real property. He owns a four unit apartment complex at 1065 Dryden Road, Ithaca, New York (“Fourplex”), which is appraised at \$201,000.<sup>8</sup> According to the proof of claim filed by M&T on March 12, 2001, the indebtedness on the Fourplex pursuant to its mortgage is \$301,455.56. Countryman testified that as of the date of filing the principal balance on the Fourplex amounted to \$290,663.42.

According to the Debtor’s amended schedules, he estimates generating \$3,450 per month in rental income. It was his testimony that all the units in the Fourplex were currently rented. He acknowledged having some difficulty in the past keeping them fully occupied when they were on well water. However, they are currently on municipal water and, as a result, he experiences only occasional vacancies.

Novarr testified that there is always a rising market for good student housing. He explained that enrollment at Cornell University seems to increase each year. Yet, he did not believe that the university had any more beds on campus than it did 10 years ago. As a result, he testified that there was an increase of \$35 per bedroom per month for the present school year. While the university has plans to build more student housing, he estimated that it would be a “long time” between the site planning and the actual construction.

The Debtor previously testified that he owns an interest in two other properties in Ithaca, New

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<sup>8</sup> In its May 2002 Decision, the Court made a finding as to the value based on an appraisal admitted into evidence at the July 2001 Hearing as Debtor’s Exhibit 2. *See* May 2002 Decision at 4.

York, which he views as long-term investments, and for which he currently derives no income. He also testified that at present there is no equity in either of the two properties.

One of the properties is located at 120-124 W. State Street, Ithaca, New York (“State Street property”). The State Street property is apparently owned by Quick Associates, a partnership which includes both Novarr and the Debtor. Novarr testified that the property is located in downtown Ithaca and includes a 12,000 square foot office building. He also testified that the four individual partners personally guaranteed the mortgage obligations.

The other property is located at 505 E. Seneca Street, Ithaca, New York (“Seneca Street property”). It was Novarr’s testimony that the Seneca Street property is owned by Cornell University. The Debtor and Novarr’s wife, Patricia, have a 30 year lease on the property, on which is located an apartment building jointly owned by them.

The Plan provides for payments to Elmira Savings Bank and Loan (“ESBL”) with respect to mortgages on the Seneca Street property and the State Street property outside of the Plan. Michael Wayne (“Wayne”), Vice President of ES&L, testified that as of the petition date, \$192,512.92 was owed on the first mortgage on State Street property and \$47,265.34 on the second mortgage. Wayne testified that \$99,656.57 was owed on the mortgage on the Seneca Street property. It was his testimony that the three mortgages were current as of the date of the hearing. Debtor lists the claims of ESBL as contingent obligations. *See* Schedule D.

The Debtor proposes to cramdown M&T’s mortgages on the Residence and the Fourplex and to pay the secured portion, based on the appraisals submitted by the Debtor, over four years, amortized over 30 years at an interest rate of 4.21% with a balloon payment five years from the date of filing of

the Petition, or November 13, 2005.<sup>9</sup>

Edward Kelly (“Kelly”), a loan officer with Wells Fargo, who had testified at the July 2001 Hearing, was asked whether it would be possible for the Debtor to obtain financing assuming he had just received a discharge upon completion of his chapter 13 plan payments. It was Kelly’s testimony that it would be necessary to obtain a letter from the Trustee regarding the Debtor’s payment history in the case. Debtor’s credit score would have to be at least 680 and he could not have made any late payments while in bankruptcy. Debtor would also have to have a minimum of 28:36 income to debt ratio, i.e. his housing payment divided by his income could not exceed 28% and his total expenses divided by his income could not exceed 36%. Kelly was uncertain whether the Debtor would be able to obtain a conventional loan with a 95% loan to value ratio, explaining that it would be determined on a case by case basis at the time of the application for financing. Kelly testified further that Wells Fargo also deals with between five and fifteen lenders that might be willing to make a non-conforming loan to someone in the Debtor’s position even if the loan to value ratio was as high as 100%.

In addition to the secured claims of M&T and ESBL, Debtor has listed a secured claim of the New York State Department of Labor in the amount of \$401.03. The IRS also holds a priority claim of \$19,716, for which the Debtor has provided full payment under the terms of the Plan. Debtor lists unsecured claims of \$433,900.01, including \$219,833 identified as being owed to Novarr on a “loan

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<sup>9</sup> As noted in the Court’s May 2002 Decision, at a hearing held on April 9, 2002, the Debtor agreed to make the payments through the Trustee, with the exception of the balloon payments to be made on the Residence and the Fourplex to M&T at the end of the 60 months. The proposed interest rate is based on the Court’s prior May 2002 Decision. On October 30, 2002, the date of the evidentiary hearing, the rate for Treasury bonds with a maturity of five years was 2.21%. *See* Debtor’s Exhibit C.

for partnership capitalization” and listed as “contingent.”<sup>10</sup> Debtor also lists an unsecured claim of Cornell University Real Estate as “disputed” in the amount of \$65,997.99.<sup>11</sup>

The Debtor’s Fourth Amended Plan provides for monthly payments of \$153.34 for 60 months for distribution to the unsecured creditors in Class 5 by the Trustee. It is estimated that the payments will provide a dividend of 2.5%. In addition, the Debtor is to make a monthly payment to the Internal Revenue Service (“IRS”) of \$328.63 on its priority claim.

## **DISCUSSION**

### Debtor’s Eligibility pursuant to Code § 109(e)

This is the fifth chapter 13 plan proposed by the Debtor since filing his Petition on November 13, 2000. M&T filed an objection to the confirmation of the Debtor’s original plan filed with his Petition, on January 8, 2001. On July 26, 2001, the Court conducted an evidentiary hearing, which was, in part, the subject of the Court’s May 2002 Decision, denying confirmation of the Debtor’s Third Amended Plan. M&T also filed an objection to the confirmation of the Debtor’s Amended Plan, filed on August 17, 2001, on September 25, 2001. The issue of the Debtor’s eligibility to file a chapter 13 petition was raised by M&T for the first time on June 18, 2002, in its opposition to confirmation of the Debtor’s Fourth Amended Plan.

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<sup>10</sup> According to the proof of claim filed by Novarr, the debt amounts to \$224,146.

<sup>11</sup> According to the proof of claim filed on behalf of Cornell University Real Estate on January 22, 2001, the Debtor owes \$5,505.06.

In addressing who may be a chapter 13 debtor, Code § 109(e) provides that “[o]nly an individual with regular income that owes, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts of less than \$269,250 and noncontingent, liquidated, secured debts of less than \$807,750 . . . may be a debtor under chapter 13 of this title.” 11 U.S.C. § 109(e).<sup>12</sup>

Debtor’s Summary of Schedules, filed November 13, 2000, shows \$1,159,117.78 in secured claims; \$25,403.77 in unsecured priority claims, and \$433,182.34<sup>13</sup> in unsecured claims. On their face, these amounts would have caused the Debtor to be ineligible to file a chapter 13 petition. However, a number of the claims have been labeled as disputed or contingent, thereby removing them from consideration when determining eligibility. For example, the Debtor identifies two obligations owing to ESLB, both of which he labels as contingent. The first is an obligation incurred by the Debtor, individually and as a partner of Quick Associates, in connection with the office building located at the State Street property. *See* M&T’s Exhibits 1 and 2. The second is an obligation incurred apparently by the Debtor and Novarr’s wife in connection with the apartment building at the Seneca Street property. *See* M&T’s Exhibit 3. According to the testimony of Wayne, ESLB’s representative, payments on these obligations were current.

Wayne testified that \$239,778.26 was owed on the State Street property and \$99,656.57 was owed on the Seneca Street property. These figures represent an amount which is approximately

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<sup>12</sup> The current debt limits set forth in Code § 109(e) are \$290,525 and \$871,550, respectively, and are applicable to cases filed as of April 1, 2001. The debt limits identified above were in effect from April 1, 1998, through March 31, 2001.

<sup>13</sup> In the Debtor’s Amended Summary of Schedules filed on August 17, 2001, the Debtor lists unsecured claims totaling \$433,900.01.

\$245,058 less than that listed by the Debtor in Schedule D of \$484,000 and \$100,492, respectively. Combining the figures provided by Wayne and the secured claims of M&T of \$249,000 and \$201,000, Debtor's secured claims total approximately \$789,435, which is within the limits set forth in Code § 109(e) for secured claims.

With respect to the unsecured claims of \$433,900.01, the Debtor lists a debt to Novarr of \$279,333. M&T concedes that the debt is contingent. *See* M&T's Memorandum, filed November 27, 2002. There is also a debt listed as "disputed" and being owed to Cornell University Real Estate in the amount of \$65,997.99. According to the proof of claim filed on behalf of Cornell University Real Estate on January 9, 2001, the amount owed is \$5,505.06. Subtracting the claim of Novarr and the claim of Cornell University Real Estate to the extent of approximately \$60,500, from \$433,900, leaves a total of \$154,567 in unsecured claims. M&T correctly asserts that the unsecured portion of its claims should also be included. *See In re Scovis*, 249 F.3d 975, 983 (9<sup>th</sup> Cir. 2001) (citations omitted). M&T's total unsecured claims amount to \$141,851.32. When combined with the \$154,567 in unsecured claims, the total unsecured debt amounts to approximately \$295,418, which does exceed the unsecured debt limits set forth in Code § 109(e), without including the priority claims of \$25,403.77, as listed in Schedule E.

Neither the Code nor the Federal Rules of Bankruptcy Procedure place a time limit on challenging a debtor's eligibility pursuant to Code § 109(e). A majority of courts have concluded that the eligibility requirements of Code § 109(e) are not jurisdictional and may be waived if not raised. *See In re Verdunn*, 210 B.R. 621, 623-24 n. 12 (Bankr. M.D. Fla. 1997) (citations omitted).

Several courts have addressed the validity of raising the issue of eligibility after confirmation of

a chapter 13 plan. In those cases, the courts have concluded that confirmation is *res judicata* as to that issue. *See, e.g., In re Nikoloutsos*, 199 B.R. 624 (Bankr. E.D.Tex. 1996), *aff'd on other grounds sub nom. Nikoloutsos v. Nikoloutsos*, 222 B.R. 297 (E.D. Tex. 1998), *rev'd on other grounds*, 199 F.3d 233 (5<sup>th</sup> Cir. 2000); *In re Jones*, 134 B.R. 274 (N.D.Ill. 1991). However, in the matter *sub judice* no plan proposed by the Debtor has ever been confirmed.

In *In re Sullivan*, 245 B.R. 416 (N.D. Fla. 1999), the IRS challenged the debtor's eligibility approximately ten months after the debtor filed her chapter 13 petition but prior to confirmation of her plan. The debtor had listed a debt to the IRS of \$224,106.55, based on a letter from the IRS approximately one year before the debtor filed her petition. *Id.* at 417. Approximately four months after commencement of the case, the IRS filed a proof of claim for \$297,323.24, of which \$250,023.28 represented a priority claim. *Id.* This was subsequently amended to reflect an unsecured priority claim of \$244,897.16 and a general unsecured claim of \$29,991.49. *Id.* Unsecured claims totaled \$270,529.68. The court cited to *Lucoski v. I.R.S.*, 126 B.R. 332 (S.D.Ind. 1991) for the premise that "even if the schedules reflect the eligibility requirements are met, if it is determined within a reasonable time that the debts exceed the statutory maximums, the case must be dismissed or the debtor may be given the opportunity to convert to a different proceeding under the Bankruptcy Code." *Id.* at 338. In *Sullivan* the IRS explained that its delay in filing its motion to dismiss on eligibility grounds was the result of the fact that the parties had been involved in negotiations to resolve the debtor's objection to its claim. When the IRS realized that the parties were going to be unable to resolve the matter, it filed its motion to dismiss prior to the plan being confirmed. *See Sullivan*, 245 B.R. at 418. The district court concluded that under the circumstances it could not say that the IRS had waited an unreasonable

amount of time to file its motion and affirmed the bankruptcy court's dismissal of the debtor's case. *Id.*

The district court in *Sullivan* indicated that "the question of eligibility may be waived if and when a creditor waits an unreasonable length of time to raise the issue . . . ." *Id.* In the matter presently before this Court, the Debtor filed his chapter 13 petition, along with his original plan, in November 2000 and since then has submitted four other amended plans for consideration by the Court. M&T has been active in the case over the past two years and was a party to the evidentiary hearing conducted in July 2001, which addressed the feasibility of the Debtor's Third Amended Plan. Nevertheless, M&T never raised the issue of eligibility until June of 2002. The only explanation given by M&T for the delay in objecting to the Debtor's eligibility was the fact that many of the debts listed by the Debtor in his schedules were labeled as "contingent" or "disputed," leading anyone reviewing the schedules to believe that the Debtor was eligible to file a chapter 13 petition.<sup>14</sup>

But for the inclusion of the unsecured portion of M&T's claims, the unsecured claims identified by the Debtor in Schedules E and F would have fallen within the parameters of Code § 109(e). M&T was well aware of the Debtor's intent to bifurcate its claims into secured and unsecured portions since the filing of the Debtor's original plan on November 13, 2000. The Court concludes that under these circumstances M&T's failure to raise the issue of eligibility for approximately two years while it was an active participant in the case is an unreasonable length of time. Accordingly, the objection by M&T to the Debtor's eligibility pursuant to Code § 109(e) is deemed waived.

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<sup>14</sup> Debtor listed M&T's claims as "disputed." When questioned by M&T's counsel, Debtor explained that he did not dispute the amount of M&T's claims or the fact that he was in default on the payments to M&T. His only dispute concerned the amount of arrears.

### Feasibility of Debtor's Fourth Amended Chapter 13 Plan

As was discussed in its May 2002 Decision,

Code § 1325(a)(6) requires that the Court determine whether the Debtor will be able to make payments under the Plan. 11 U.S.C. § 1325(a)(6). This determination is measured by whether the Debtor's Plan has a reasonable likelihood of success, and it is the Debtor's burden to show that he "has the present as well as the future financial capacity to comply with the terms of the Plan." *In re Fantasia*, 211 B.R. 420, 423 (1<sup>st</sup> Cir. BAP 1997) (citation omitted). Because the Debtor proposes to make a final balloon payment, the necessity of demonstrating that the funds will be available at the time the payment is due is particularly critical. *Id.*; *see also In re Wagner*, 259 B.R. 694, 700 (8<sup>th</sup> Cir. BAP 2001) (requiring that there be "[a] definite declaration as to the source and the amount of funds necessary to enable the debtor to make the plan payments . . .").

May 2002 Decision at 7-8.

At the October 2002 Hearing, the Debtor presented evidence addressing each of the concerns expressed by the Court in its May 2002 Decision. Based on his Amended Schedules I and J, filed on June 12, 2002, and the testimony of Debtor's wife, it appears that the Debtor has sufficient monthly disposable income to make the monthly payments of \$153.34 for distribution to unsecured creditors and \$328.63 for payment to the IRS on its priority claim.

At the time of the July 2001 Hearing, the rate for Treasury bonds with a maturity of five years was 4.70%. In its May 2002 Decision, the Court concluded that the appropriate rate of interest payable on the claims of M&T secured by the Residence and the Fourplex should be two percentage points above the rate for the Treasury bonds or 6.70% based on the U.S. Court of Appeals for the Second Circuit's decision in *In re Valenti*, 105 F.3d 55 (2d Cir. 1997). At the time of the July 2001 Hearing, the Court concluded that the Debtor's estimated revenues would be insufficient to cover the

debt service beginning in the first year of the Plan at an interest rate of 6.70%.<sup>15</sup> *See* May 2002 Decision at 16.

The date of confirmation is the date on which the appropriateness of the proposed interest rate is to be determined. *See In re Scott*, 248 B.R. 786, 793 n. 7 (Bankr. N.D. Ill. 2000). At the October 2002 Hearing, the Debtor offered evidence that the rate for Treasury bonds with a maturity of five years was 2.21%. Accordingly, the Debtor is proposing to pay the secured portion of M&T's claims at a rate of 4.21% with a balloon payment to be made five years from the date of filing of the Petition, or November 13, 2005. It is fortuitous for the Debtor that interest rates have decreased over the past year. Although not presented with evidence of the yearly payments at an interest rate of 4.21%, it is evident to the Court that with a drop of approximately 2.5 percentage points from that previously considered by the Court, Debtor's estimated revenues should be sufficient to cover the debt service.

The remaining issue for consideration by the Court is the feasibility of the Debtor's Plan with respect to the proposed balloon payment in approximately three years. As discussed in the Court's May 2002 Decision, plans proposing a balloon payment are subject to careful scrutiny on the issue of feasibility. *See* May 2002 Decision at 16.

The Debtor presented no evidence of the amount that he intends to borrow in November 2005 in order to make the balloon payment. However, Kelly testified that lenders, both conventional and non-conforming, were willing to provide financing to individuals who had completed a chapter 13 plan.

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<sup>15</sup> The Court had made its calculations on the basis of an interest rate of 6.50% and found that there was there was only an excess of \$25 between the Debtor's net income of \$15,270 per year and the amount of debt service of \$15,245 at the lower interest rate. On that basis, the Court concluded that the Debtor's net income would be insufficient to cover the debt service at the higher rate of interest.

He was unable to predict with any certainty whether the Debtor would qualify for a conventional mortgage in November 2005. It was his testimony that there were a number of companies that would consider offering non-conforming financing with loan to value ratios of between 95% and 100%, depending on credit scores, payment history and income statements, as well as a current appraisal.

In support of his contention that the value of the real property in Ithaca, New York, was likely to appreciate over the next few years, the Debtor offered the testimony of Novarr. Novarr indicated that available rental property to meet the housing needs of students enrolled at Cornell University was at a premium. In fact, he testified that over the past year there had been an increase of approximately \$35 per month per bedroom. Novarr also testified that the Debtor's residence was located in an upscale Ithaca area community, and that there was a high demand for such property, with buyers often offering more than the asking price for such prime residential property. Kelly also testified that real estate values in the Ithaca, New York, area had risen 3-5% in just the past year.

Given the decrease in interest rates and the income of both the Debtor and his wife available to meet their expenses and pay their unsecured creditors, the Court concludes that the Debtor has established that his plan is feasible insofar as he proposes monthly payments of \$481.97. Based on the real estate market in Ithaca, New York, and Kelly's testimony concerning the availability of financing to debtors with regular income and good payment histories during the life of their plan, the Court concludes that the Debtor has established a reasonable likelihood that he will be able to obtain financing to make the balloon payment in three years. He is current on his plan payments and has been able to make the adequate protection payments to M&T as required in the Court's Order of July 10, 2002.

Based on the foregoing, it is hereby

ORDERED that confirmation of the Debtor's Fourth Amended Plan is granted.

Dated at Utica, New York

this 14th day of January 2003

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STEPHEN D. GERLING  
Chief U.S. Bankruptcy Judge