



## FINDINGS OF FACT

The court finds the undisputed facts to be as follows:

1. On April 26, 1993, Debtor purchased her homestead at 232 N. Market, Solon, Johnson County, Iowa.

2. Debtor financed the purchase of her homestead through a loan from Midland Savings Bank FSB, 606 Walnut, Des Moines, Iowa. Debtor executed a mortgage (First Mortgage) on the homestead to secure the promissory note (First Note) of \$39,600.

3. On May 6, 1993, the First Mortgage was filed in Johnson County.

4. On July 21, 1995, Debtor borrowed \$31,145.89 from AmerUs Bank (formerly Midland Savings Bank FSB), 206 Sixth Avenue, Des Moines, Iowa. Debtor executed a mortgage (Second Mortgage) on the homestead to secure this promissory note (Second Note).

5. On August 16, 1995, the Second Mortgage was filed in Johnson County.

6. On November 5, AmerUs (the Bank) filed a petition in the Iowa District Court for Johnson County to foreclose the two mortgages.

7. On November 25, 1997, the Bank released the Second Mortgage. The release states that full payment has been made.

8. On November 28, 1997, the Bank released the First Mortgage. The release states that full payment has been made.

9. On December 17, 1997, the Second Mortgage release was filed with the Johnson County Recorder.

10. On January 27, 1997, the First Mortgage release was filed with the Johnson County Recorder.

11. On March 3, 1997, Debtor filed a voluntary petition for chapter 7 bankruptcy.

12. On March 25, 1997, the chapter 7 schedules were filed. On Schedule A, Real Property, Debtor listed the property at 232 N. Market. The property was valued at \$63,000, and secured claims was stated as \$0. On Schedule C, Property Claimed as Exempt, no claim of

homestead was listed. On Schedule D, only two creditors, Montgomery Ward and University of Iowa Community Credit Union, were listed as holding secured claims. The Bank was listed on Schedule F, as holding an unsecured nonpriority claim for two promissory notes and mortgages; mortgages released 12/97 and 1/98.

13. On April 24, 1998, Debtor filed an amended Schedule C claiming a homestead exemption pursuant to Iowa Code § 561.2 and § 561.16. The exemption was valued at \$63,000 for the property located at 232 N. Market, Solon, Iowa.

14. As of May 14, 1998, the First Note had not been paid; \$35,979.76 of principle and \$6,334.26 of accrued interest (\$9.7391 per diem after 5/14/98) for a total of \$42,314.02 was still due.

15. As of May 14, 1998, the Second Note had not been paid; \$25,574.19 of principle and \$6,654.55 of accrued interest (\$9.2837 per diem after 5/14/98) for a total of \$32,228.74 was still due.

16. On June 16, 1998, the Bank filed a Motion to Lift the Automatic Stay in order to proceed with the foreclosure action that it had commenced in the Iowa District Court. Debtor resisted the motion.

17. On June 19, 1998, Debtor filed a Complaint to Determine the Validity and Extent of any lien that the Bank might have on the homestead property. Debtor included a Motion to avoid any such lien.

18. On June 23, 1998, Debtor was granted a Discharge from all dischargeable debts.

### **DISCUSSION**

Rule 7056 incorporates Federal Rule of Civil Procedure 56 and provides for motions for summary judgment in adversary proceedings in bankruptcy cases. Summary judgment is appropriate when "there is no genuine issue of material fact and the moving party is entitled to a judgment as a matter of law." F.R.Civ.P. 56(c). The facts must be viewed in the light most

favorable to the opposing party. Matsushita Electric Industrial Co., Ltd., v. Zenith Radio Corp., 475 U.S. 574, 587-88, 106 S.Ct. 1348, 1356-57 (1986), Johnson v. Enron Corp., 906 F.2d 1234,1237 (8th Cir. 1990). The court is not to weigh the evidence, but rather determine whether there is a genuine issue of fact for trial. Johnson, 906 F.2d at 1237.

Debtor asks the court to determine the validity and extent of the liens claimed by the Bank on her real property located at 232 N. Market, Solon, Johnson County, Iowa, and permit her to avoid any such liens. Debtor received two loans, the first on April 26, 1993 and the second July 21, 1995. She granted mortgages on the real estate to secure the promissory notes for the loans. The mortgages were filed with the Johnson County Recorder on May 6, 1993, and August 16, 1995, respectively. The Bank released the First Mortgage on November 25, 1997 and released the Second Mortgage on November 28, 1997. These releases were filed with the Johnson county recorder on January 27, 1998 and December 27, 1997. The releases state that the debt has been paid in full.

Debtor claims that at the time of the filing of her chapter 7 bankruptcy petition no liens attached to her homestead, and it is fully exempt property. Alternatively, if any mortgages existed at the time of the petition, they were equitable mortgages that sprang into existence at time that the recorded mortgages were released. Debtor argues that the equitable mortgages are transfers that can be avoided as preferences under § 547 or through the trustee's "strong arm" powers of § 544. Debtor contends that pursuant to § 522(h), a chapter 7 debtor can exercise the these lien avoidance powers.

The Bank states that the mortgages were released inadvertently due to a clerical error. The Bank further states that Debtor is in default on the loans, and no consideration was given for the mortgage releases. Consequently, the liens are valid, and the Bank's claims are fully secured. Since the liens are still valid no avoidable transfer took place. The Bank additionally argues that Debtor cannot exercise the trustee's "strong arm" powers of § 544.

The court begins by determining what interests the Bank might have in Debtor's real property. "Property interests are created and defined by state law." Butner v. United States, 440 U.S. 48, 55, 106 S.Ct. 914, 918 (1979), Van Der Heide v. LaBarge, 164 F.3d 1183, 1185 (8th Cir. 1999). "In the absence of any controlling federal law, 'property' and 'interests of property' are creatures of state law." Barnhill v. Johnson, 503 U.S. 393, 398, 112 S.Ct. 1386, 1388 (1992). Therefore, in order to make its determination, the court must look to Iowa law.

In Iowa, "[t]he lien of mortgage is presumed to continue until the debt is paid ..." Cherry v. Welsher, 192 N.W. 149, 151 (Iowa 1923). "It is elementary that, if the original mortgage is released through mistake, it may be restored in equity and given its original priority, except as to subsequent purchasers for value." Cherry, 192 N.W. at 151. "A court of equity will not permit a party to take and enjoy the benefits of ignorance or mistake of law on the part of another party who knew and did not correct." Shalla v. Shalla, 23 N.W.2d 814, 822-23 (Iowa 1946) citing Faxon v. Baldwin, 114 N.W. 40; 2 Pomeroy, Eq.Jur. (3rd Ed.), §§ 721, 847.

It is clear, that under Iowa law, the Bank has liens that are valid against Debtor. These liens encumber the real estate designated in the mortgages. The liens arose at the time that the security agreements were formed, April 26, 1993 for the First Mortgage and July 21, 1995 for the Second Mortgage. Contrary to Debtor's contention, no new obligation arose, be it labeled equitable mortgage or lien, at the time the Bank inadvertently released its mortgages. Iowa's highest court has clearly stated that if the mortgage is released in error, the lien of mortgage "continues" until the debt is paid. Id., Johnson v Meyer, 198 N.W. 654, 656 (Iowa 1924).

The Bank's liens are currently unperfected. The liens are evidenced by the mortgage agreements. Under Iowa Code 558.1<sup>1</sup>, these agreements are "instruments affecting real estate." In order to perfect the liens, these instruments must be recorded, otherwise they are not valid

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<sup>1</sup> Iowa Code 558.1 states: All instruments containing a power to convey, or in any manner relating to real estate ... shall be held to be instruments affecting the same; ...

against subsequent purchasers for value. Iowa Code 558.41.<sup>2</sup> When the Bank released the mortgages and subsequently recorded the releases, the liens lost perfected status. The rule in Iowa is "well settled" that the release of a mortgage is prima facie evidence of the payment of a debt. Shalla, 23 N.W.2d at 821. Consequently, subsequent purchasers for value without notice would take the property free of the encumbrances. Id., Cherry, 192 N.W. at 151, Sioux City & Leeds, 76 N.W. 838 at 839. In order to reestablish the priority of the mortgages, the Bank must request the court of equity to reinstate the mortgage. Shalla, 23 N.W.2d at 822, Cherry, 192 N.W. at 151.

Since the court has determined that the Bank has valid unperfected liens on Debtor's real property, it must now determine whether the liens may be avoided. Debtor argues that pursuant to § 522(h)<sup>3</sup>, she may exercise the trustee's avoidance powers of § 544(a)(3).<sup>4</sup> The Bank responds that the § 544 powers are not available to her. It maintains that the liens are consensual and, therefore, under § 522(g)(1)<sup>5</sup> they are not avoidable.

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<sup>2</sup> Iowa Code 558.41 states in pertinent part: An instrument affecting real estate is of no validity against subsequent purchasers for a valuable consideration, without notice, or against the state or any of its subdivisions during and after condemnation proceedings against the real estate, unless the instrument is filed and recorded in the county in which the real estate is located, as provided in this chapter.

<sup>3</sup> Section 522(h) provides:

The debtor may avoid a transfer of property of the debtor or recover a setoff to the extent that the debtor could have exempted such property under subsection (g)(1) of this section if the trustee had avoided such transfer, if-

- (1) such transfer is avoidable by the trustee under section 544, 545, 548, 549, or 724(a) of this title;
- and
- (2) the trustee does not attempt to avoid such transfer.

<sup>4</sup> Section 544 provides in pertinent part:

(a) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by-

(3) a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser and has perfected such transfer at the time of the commencement of the case, whether or not such a purchaser exists.

<sup>5</sup> Section 522 states in relevant part:

(g) Notwithstanding sections 550 and 551 of this title, the debtor may exempt under subsection (b) of this section property that the trustee recovers under section 510(c)(2), 542, 543, 550, 551, or 553 of this title, to

The Ninth Circuit has addressed this very issue. That court has concluded that the Bankruptcy Code requires that a debtor must meet five conditions before it may exercise avoidance powers under § 522(h). DeMarah v. United States (In re DeMarah), 62 F.3d 1248, 1250 (9th Cir. 1995). The conditions are:

- (1) the transfer cannot have been a voluntary transfer of property by the debtor;
- (2) the debtor cannot have concealed the property;
- (3) the trustee cannot have attempted to avoid the transfer;
- (4) the debtor must exercise an avoidance power usually used by the trustee that is listed within § 522(h); and
- (5) the transferred property must be of a kind that the debtor would have been able to exempt from the estate if the trustee (as opposed to the debtor) had avoided the transfer pursuant to one of the statutory provisions in § 522(g). Id.

The debtor who fails to satisfy any one of these conditions, lacks standing to exercise the avoidance powers under § 522(h). LaBarge v. Benda (In re Merrifield), 214 B.R. 362, 365 (B.A.P. 8th Cir. 1997), see also In re Kidlow, 232 B.R. 686 (Bankr. S.D. Ohio 1997).

In this case Debtor fails to meet the first condition. Debtor does not dispute that she is in default in payment, and money is still owed to the Bank. She does not dispute that she entered into the security agreements voluntarily. The liens that continue against the real property are consensual in nature. Consequently, Debtor lacks standing to avoid the liens under § 522(h).

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the extent that the debtor could have exempted such property under subsection (b) of this section if such property had not been transferred, if-

- (1)(A) such transfer was not a voluntary transfer of such property by the debtor; and
- (B) the debtor did not conceal such property;

**ORDER**

IT IS THEREFORE ORDERED AS FOLLOWS:

- (1) The Debtor/Plaintiff's Motion for Summary Judgment is DENIED.
- (2) The Defendant's Motion for Summary Judgment is GRANTED.
- (3) The court determines that AmerUs Bank has two unperfected liens encumbering Debtor's property at 232 N. Market, Solon, Johnson County, Iowa.
- (4) The Debtor/Plaintiff's Motion to Avoid Liens is DENIED.
- (5) The release of the mortgages is hereby canceled, and the mortgages are restored.

Dated this \_\_\_\_\_ day of February, 2000.

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RUSSELL J. HILL, CHIEF JUDGE  
U.S. BANKRUPTCY COURT