UNITED STATES BANKRUPTCY COURT
For the Southern District of Iowa

In the Matter of

THOMAS D. SCANLAN, Case No. 86-2870
ELAINE R. SCANLAN,
Engaged in Farming, Chapter 7

Debtors.

ORDER ON RESISTANCE TO MOTION TO AVOID LIENS

On March 11, 1987 a resistance to motion to avoid liens filed by the Farmers Home Administration (FmHA) on January 23, 1987 came on for telephonic hearing in Des Moines, Iowa. The debtors filed a motion to avoid liens on January 9, 1987. Linda R. Reade, Assistant United States Attorney, appeared on behalf of the FmHA and W. Edward Anstey appeared on behalf of the debtors. The case has been submitted on briefs.

FACTUAL BACKGROUND

The debtors filed a joint petition for relief under Chapter 7 on October 23, 1986. The debtors are farmers. They seek to avoid the FmHA's liens in the following property:

Eight cows, eight calves and one bull
One 4010 John Deere tractor
One 4-14" John Deere plow
One 4 row IHC cultivator
One 14' Kewanee disc
One John Deere planter
One John Deere baler
One New Idea siderake
One Valley livestock trailer
Twelve Farrowing crates
One 1982 Honda moped

The debtors first borrowed from the FMHA in 1978.

Since then they have executed a number of notes and security agreements. The nature of these notes are summarized as follows:

NOTES

Date of Note	Amount of Note	Disposition
May 15, 1978	$ 9,350.00	Not paid, rescheduled
April 6, 1979	10,050.00	Subsequent loan
July 7, 1980	4,000.00	Not paid, rescheduled
Feb. 5, 1982	4,435.64	Rescheduling July 7, 1980 Amount
Feb. 5, 1982	4,982.95	Rescheduling May 15, 1978 Amount

Upon executing the May 15, 1978 note, the parties executed a security agreement giving the FmHA a security interest in, among other things, the Valley livestock trailer. Also, it is undisputed the FmHA possessed a purchase money security interest in the disc, planter, baler and siderake when these items were purchased by the debtors in 1979.

DISCUSSION

I. Retrospective Application of Exemption Amendments

The FmHA contends that application of the 1986 amendments to the Iowa exemption statute (amendments) is impermissible under the Fifth Amendment to the United States Constitution. The court disagrees.

The debtors claim farm equipment valued at $3,450.00, cattle valued at $4,800.00 and a Jeep CJ7 valued at $3,790.00 as exempt.

It is undisputed the debtors' obligations to the FMHA arose prior to May 31, 1986, the effective date of the amendments.[1] Before May 31, 1986, Iowa law provided for a maximum farm machinery exemption of $5,000.00. Iowa Code section 627.6(10)(d)(1985). The value of musical instruments, one motor vehicle and interest in certain wages and tax refunds also were included in the $5,000.00 limitation. Additionally, only two cows and two calves and feed for the animals for six months could be claimed exempt. Iowa Code section 627.6(5)(1985). Id. Accordingly, under preamendment law the debtors would not have been able to claim the farm equipment and the jeep exempt because their combined value exceeded $5,000.00. Furthermore, the debtors' cattle claim exceeded the number permitted by preamendment law.

The Iowa legislature amended section 627[2] by creating a separate farm machinery and livestock and feed for livestock exemption subsection that sets a $10,000.00 limitation. 86 Acts, ch. 1216, section 6 (now codified at Iowa Code section 627.6(11)(a). Under postamendment law, a vehicle may be claimed exempt under section 627.6(9)(b) subject to a $5,000.00 maximum limitation.

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[1] Had the obligations arisen after the effective date of the amendments, there could be no question the amendments would be applicable. Further, there is no question of applicability of the amendments to the 'gap period' between the date of enactment and the effective date given this court's ruling that the amendments are applicable to obligations that had arisen prior to the effective date. Cf. Matter of Eakes, No. 83-1647-C (Bankr. S.D. Iowa, filed August 21, 1984) aff'd sub no. United States of America v. Eakes, No. 84-714-A Civ. (S.D. Iowa, January 18, 1985) (finding that the holding in United States v. Security Industrial Bank, et.al., 459 U.S. 70, 103 S.Ct. 407, 74 L.Ed. 2d (1982), where in the Supreme court determined that section 522(f)(2) of the 1978 Bankruptcy Code does not apply retroactively to abrogate liens acquired before the Code's enactment, did not apply to liens acquired between the enactment date (November 6, 1978) and the effective date of the Code (October 1, 1979)).

[2] Some confusion has arisen concerning the correct numbering of the subsections under Iowa code section 627.6. The confusion apparently has resulted from the striking of former subsection 5. All Iowa statutory citations in this order are taken from the official Iowa Code (1987) unless otherwise noted.

The issue of whether the application of the amendments to obligations created prior to May 31, 1986 is permissible under the 5th Amendment has been resolved in this district by the appeal decision in the case of Matter of Reiste, No. 87-153-B (S.D. Iowa, filed May 11, 1987). Chief District Judge Harold D. Vietor upheld Bankruptcy Judge Michael J. Melloy's[3] ruling that retrospective application of the amendments did not constitute an uncompensated taking. Judge Melloy had incorporated by reference in the Reiste opinion the conclusions of law set out in In re Punke, 68 B.R. 936 (Bankr. N.D. Iowa 1987). The Reiste decision and conclusions of law pertaining to the takings issue found in Punke are incorporated by reference in the instant case.

Parenthetically, this court notes that the FmHA did not object to the debtors' claim of exemptions within thirty days of the first meeting of creditors as required by the order dated November 12, 1986 and Bankruptcy Rule 4003(b).[4] Also, no motion has been filed under Bankruptcy Rule 9006(b) to enlarge the time within which to file such an objection. Yet, the FmHA has objected to the amount of the debtors' exemption claim in response to the debtor's motion to avoid liens. In many lien disputes similar to this one, debtors

[3] Sitting by designation.

[4] Bankruptcy Rule 4003(b) provides in part that:

> The trustee or any creditor may file objections to the list of property claimed as exempt within 30 days after the conclusion of the meeting of creditors held pursuant to Rule 2003(a) or the filing of any amendments to the list unless within such period, further time is granted by the court.

Local Rule 4005 provides that "[a]ny objection to debtor's claim of exemptions shall be filed no later than 15 days after the conclusion of the §341 Meeting of Creditors." Given the conflict between the notices routinely issued by the clerk's office, in accordance with Bankruptcy Rule 4003(b), and Local Rule 4005, the local rule is considered null and void. The court notes that in the proposed amendments to the bankruptcy rules, Bankruptcy Rule 4003(b) remains essentially unchanged from its present form. Proposed Bankruptcy Rule Amendments, Rule 4003(b) (1986).

have questioned whether a creditor who fails to object timely to a debtor's claim of exemptions may object to the exemptions when resisting a motion to avoid liens.

A number of courts have addressed this issue and the results are varied. In the case of In re Grethen, 14 B.R. 221 (Bankr. N.D. Iowa 1981), the late Judge William W. Thinnes held that a creditor's knowledge of the fact the debtor planned to move to avoid liens under section 522(f) did not constitute "excusable neglect" for noncompliance with the time limit for objecting to exemptions. The court emphasized that the time limit was established to set a cutoff point at which debtors could be certain of the objections that had been made. The court also noted that if creditors were allowed to wait until section 522(f) actions were commenced, the time limitation rule would be undermined and more delay would result. See also, In re Keyworth, 47 B.R. 966, 970 (D.C. Colo. 1981)(to allow an untimely objection "would be to impermissibly amend Rule 4003(b) which is clear and unequivocal"); In re Blum, 39 B.R. 897 (Bankr. S.D. Florida 1984)(30-day objection period not met and no enlargement of time requested pursuant to Bankruptcy Rule 9006(b)(3)). Other courts have held to the contrary. For instance, in In re Roehrig, 36 B.R. 505 (Bankr. W.D. Ky. 1983) the court found that failure to object timely to the debtor's exemption claim did not mandate that the property be deemed exempt. The court reasoned that if the exemptions were allowed to stand, the debtor would be creating a class of exemptions apart from

the federal exemptions set forth in section 522(d) or the state exemptions authorized by section 522(b). Id. at 507-508.

This court is persuaded by the reasoning set forth in the Grethen decision. Compliance with rules such as Bankruptcy Rule 4003(b) is imperative if onerous caseloads are to proceed as expeditiously as possibly. Moreover, a maxim of statutory construction is that a statute should be interpreted so as no t to render one part inoperative. Mountain States Tel. & Tel. Co. v. Pueblo of Santa Ana, ___U.S.___ 105 S.Ct. 2587, 2595, 86 L.Ed.2d 168 (1985). Permitting a creditor who fails to object timely to exemption claims to make that objection in resistance to a section 522(f) motion renders Bankruptcy Rule 4003(b) meaningless. Finally, the concern expressed in the Roehrig opinion that strict adherence to the thirty day limit would create a new class of "exemption by declaration" is overcome by the recognized rule that there must be a good faith statutory basis for the exemption. In re Bennett, 36 B.R. 893, 895 (Bankr. W.D. Ky. 1984).

As stated above, the FmHA has failed to comply with the thirty day requirement of Bankruptcy Rule 4003(b). The undersigned realizes that the practice of her predecessor had been to permit creditors to object to exemptions after the thirty day period had expired. No doubt the FmHA as well as many other creditors in the Southern District of Iowa have

relied upon this practice. In fairness to the FmMHA, its objection will be considered timely filed. However, by virtue of this order, the FmHA is are put on notice that, unless the requirements of Bankruptcy Rule 9006(b) are met, future failure to object to the debtor's exemption claims within the thirty day time period prescribed by Bankruptcy Rule 4003(b) will preclude consideration of such an objection in a section 522(f) action.

II. Lien Avoidance On Cattle

With respect to this and the following divisions of this decision, the-debtors have the burden of demonstrating that all the elements of lien avoidance under section 522(f) are satisfied. In re Shands, 57 B.R. 49, 50 (Bankr. S.C. 1985); Matter of Weinbrenner, 53 B.R. 571, 578 (Bankr. W.D. Wisc. 1985). With respect to this burden one court has stated:

> [I]n order to obtain the requested relief, the debtors have the burden of demonstrating that: 1) they have exemptions which have been granted; 2) that the lien being avoided is a judicial lien or nonpurchase money security interest; 3) that such lien or interest impairs the above exemptions and therefore 4) as a matter of law they are entitled to have such liens or interests avoided under S 522(f).

In re Clark, 11 B.R. 828, 831 (Bankr. W.D. Pa. 1981).

The FmHA challenges the ability of the debtors to avoid liens on the livestock under 11 U.S.C. 522(f). The FmHA's challenge is well taken.

11 U.S.C. section 522(f) provides in part that:

> Notwithstanding any waiver of exemptions, the debtor may avoid the fixing of a lien on an interest of the debtor in property to the extent that such lien impairs an exemption to which the debtor
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> would have been entitled under subsection
>
> (b) of this section, if this lien is--
>
> (2) a nonpossessory, nonpurchase-money security in any—
>
> (A) (a]nimals ... that are held for the personal, family, or household use of the debtor or a dependent of the debtor;

Iowa Code section 627.6(11) permits farm debtors to hold as exempt from execution, any combination of the following not to exceed a value of $10,000.00:

> a. Implements and equipment reasonably related to a normal farming operation.
>
> b. Livestock and feed for the livestock reasonably related to a normal farming operation.

11 U.S.C. section 522(b)(1) permits states to "opt out" of the federal exemption scheme. Iowa had done so by virtue of Iowa Code section 627.10. "Although a state may elect to control what property is exempt under state law, federal law determines the availability of lien avoidance." Matter of Thompson, 750 F.2d 628, 630 (8th Cir. 1984). In Thompson, the

Eighth Circuit Court of Appeals ruled that lien avoidance under section 522(f)(2)(A) is available for those animals held primarily for personal, family, or household use. Therefore under this subsection, the debtors herein may avoid the liens in the livestock and feed for livestock used for such purposes. Liens on livestock and feed held for commercial use cannot be avoided under this subsection.

The eight cows, eight calves and one bull claimed exempt by the debtors exceed the number of animals reasonably needed for personal, family, or household use of the debtor. In their brief, the debtors contend they are entitled to at least two cows and two calves for personal use. The court finds that in this instance, two cows and two calves kept for personal use is reasonable.

III. Purchase Money Security Interest

The debtors fail to establish that the FmHA has a nonpossessory nonpurchase money security interest in the disc, rake, baler and plow. In response to the FmHA's assertion that it possesses a purchase money security interest in these items, the debtors argue that the FmHA forfeited its purchase money status by failing to perfect timely its security interest. The debtors rely on Iowa Code section 554.9312(4) in support of this argument.

Iowa Code section 554.9312(4) provides:

> A purchase money security interest in collateral other than inventory has priority over a conflicting security interest in the same collateral or its proceeds if the purchase money security interest is perfected at the time the debtor receives possession of the collateral or within twenty days thereafter.

This provision and the fact the FmHA may not have perfected its security interest within the twenty day period have no bearing on whether the FmHA has a purchase money security interest in the items in question. This provision simply establishes a priority among creditors who have conflicting security interests in the same collateral.

IV. Pre-Code Liens and Novation

Relying on U.S. v. Security Industrial Bank, 459 U.S. 70, 103 S.Ct. 407, 74 L.Ed.2d 235 (1982), the FMHA asserts that the debtors cannot avoid the FmHA's security interest in the Valley livestock trailer since the FmHA's security interest in the trailer arose prior to the enactment of the 1978 Bankruptcy Code. The debtors contend that this preCode security interest in the trailer has been extinguished by means of a novation.

In U.S. v. Security Industrial Bank, supra, the United States Supreme Court held that Congress did not intend to apply 11 U.S.C. section 522(f) retrospectively to security interests obtained prior to the Code's November 6, 1978

enactment date. Security Industrial, 459 U.S. at 82. Courts have recognized an exception to this rule where pre-Code liens have been extinguished and replaced by loans and security agreements executed after the enactment date. See In re Avershoff, 18 B.R. 198 (Bankr. N.D. Iowa 1982); Matter of Hallstrom, Case No. 86-370-C (Bankr. S.D. Iowa, filed September 8, 1986).

With respect to novations, the Iowa Supreme Court has stated:

> It is the general and well-recognized rule that the necessary legal elements to establish a novation are parties capable of contracting , a valid prior obligation to be displaced, the consent of all the parties to the substitution, based on sufficient consideration, the extinction of the old obligation, and the creation of new one.

Wade & Wade v. Central Broadcasting Co., 288 N.W. 439, 443 (1939). The critical element is the intention of the parties to extinguish the existing debt by means of a new obligation. Tuttle v. Nichols Poultry & Egg Co., 35 N.W.2d 875, 880 (Iowa 1949).

A number of factors must be examined to determine whether new loan arrangements create a novation. Such factors include: whether new money was advanced, whether the debtors' payments were increased, whether additional collateral was provided by the debtors and whether a new security agreement was executed. Matter of Ward, 14 B.R. 549, 553 (S.D. Ga.

1981); Averhoff, 18 B.R. at 202. The undersigned adopts her predecessor's conclusion that a mere change in the interest rate for the benefit of the lender does not constitute a novation. Matter of Buttler, Case No. 84-1716-C (Bankr. S.D. Iowa, filed on January 26, 1985).

It is undisputed that on May 15, 1978 the FmHA loaned the debtors $9,350.00 and, in return, the debtors signed a promissory note and executed a security agreement the pledging the trailer as security for the note. The debtors executed a number of other promissory notes with the FmHA after May 15, 1978. None of these notes show that new money was advanced to the debtors to pay off the May 15, 1978 obligation. In fact, the documents show the contrary. The original loan is marked "not paid, rescheduled." On February 5, 1982 the debtors executed a promissory note to the FmHA which rescheduled the May 15, 1978 note. Language in the note states that "this note is given to... reschedule ... but not in satisfaction of the unpaid principal and interest on the [May 15, 19781 note...." Further, no additional collateral nor an additional security agreement was given with respect to the February 5, 1982 note. Therefore, it follows that there was no novation of the preenactment note and security agreement. Accordingly, the debtors fail to carry their burden of proof and are precluded from avoiding the FmHA's preenactment lien in the Valley livestock trailer.

CONCLUSION AND ORDER

WHEREFORE, based upon the foregoing analysis the court finds that the debtors may claim farm machinery, livestock and feed for livestock exempt pursuant to Iowa Code section 627.6(11) (1987). The court further finds that two cows and two calves are a reasonable amount of livestock for the debtors' personal use pursuant to 11 U.S.C. 5 522(f)(2); that the FMHA possesses a purchase money security interest in the Kewanee disc, the New Idea side rake, the John Deere square baler and the John Deere plow; and that the May 15, 1978 note and security agreement involving the Valley livestock trailer arose prior to the enactment of the new Bankruptcy Code and were not the subject of a novation.

THEREFORE, the motion to avoid liens is denied with respect to the disc, side rake, baler, plow, bull, six cows, six calves and the livestock trailer. With respect to the other items delineated in the debtors' motion, lien avoidance is granted.

Signed and filed this 30th day of July 1987.

LEE M. JACKWIG

U.S. BANKRUPTCY JUDGE