

UNITED STATES BANKRUPTCY COURT  
For the Southern District of Iowa

In the Matter of

Case No. 87-977-C

RICHARD D. FLANERY and  
RUTH E. FLANERY,

Chapter 7

Debtors.

ORDER ON MOTION TO COMPEL CREDITOR TO PAY OVER PROCEEDS

On December 1, 1987, debtors' motion to compel creditor, Guthrie County State Bank (hereinafter "creditor"), to pay over proceeds came on for hearing before this court in Des Moines, Iowa. George W. Appleby appeared on behalf of the debtors and Mark S. Lorence appeared on behalf of creditor.

FACTUAL BACKGROUND

On April 13, 1987, debtors filed their joint Chapter 7 bankruptcy petition with this court. On April 17, 1987, creditor filed a motion to lift stay in order to foreclose on its security interest on two real estate notes it held against debtors. The notes were secured by, among other things, equipment and machinery. Creditor contended that debtors had no equity in the collateral and had not offered any adequate protection to the creditor.

On May 15, 1987, the Honorable Lee M. Jackwig, Bankruptcy Judge for the Southern District of Iowa, filed a consent order lifting the automatic stay. The order permitted creditor to

foreclose on its security interest in, among other things, debtors' machinery and equipment but with the exception that debtors retained their right to claim as exempt farm machinery or proceeds therefrom in the amount of \$20,000 pursuant to Chapter 627 of the Iowa Code. The order further noted that the automatic stay was not lifted as to such property.

In June of 1987, debtors retained as exempt four pieces of machinery and thirteen tools. Debtors then voluntarily turned over to creditor all the farm machinery not retained as exempt and creditor liquidated that property.

On September 25, 1987, debtors filed a motion to compel creditor to pay over proceeds of the machinery sale in the amount of \$20,000 minus the value of the retained-as-exempt machinery. Debtors claimed they turned over machinery to creditor only with the understanding their interest up to \$20,000 would be fully respected. During the hearing, creditor's attorney denied such an understanding existed.

On November 30, 1987, creditor filed a resistance to debtors' motion and argued it should be denied for two reasons: 1) impossibility of accurately determining the difference in value between \$20,000 and the retained machinery; and 2) proceeds from the sale of collateral should not be considered exempt property.

## DISCUSSION

The issue in this case is whether this court can order creditor to pay over proceeds from the sale of debtors' otherwise exempt property when debtors voluntarily turned over such property to the creditor.

The concept of exempt property is designed to let the debtor retain a few basic essentials for a fresh start. In re Van Iperen, 819 F.2d 189, 191 (8th Cir. 1987). Iowa Code section 627.6 (1987) sets out the general exemptions for a debtor in bankruptcy. Section 627.6(12) allows a farmer to exempt up to \$10,000 of implements and equipment reasonably related to a normal farming operation. However, there is no provision in section 627.6 allowing a debtor to exempt cash.

For the following reasons, debtors' motion to compel creditor to pay over proceeds is denied. First, as a general rule, proceeds from the voluntary sale of exempt property are not exempt in the absence of a statute providing therefor. Millsap v. Faulkner, 236 Iowa 848, \_\_\_\_ 20 N.W.2d 40, 41 (1945). In the case at bar, debtors voluntarily turned over otherwise exempt property to the creditor who then liquidated it. Furthermore, this court is not aware of any statute which provides an exception to the general rule that proceeds from the voluntary sale of

debtors' otherwise exempt property are not exempt. Thus, debtors are not entitled to a court order compelling creditor to pay over proceeds.

Second, as noted earlier, the concept of exempt property is designed to let the debtor retain a few basic essentials for a fresh start. Van Iperen, 819 F.2d at 191. However, "[m]oney, even proceeds from the sale of collateral, does not have this quality when it is in the hands of a third party who has properly used state collection procedures." Id. In the case at bar, the proceeds are in the hands of creditor, a third party. Furthermore, pursuant to the May 15, 1987 consent order lifting the automatic stay, creditor held a foreclosure sale, a proper state collection procedure, to liquidate debtors' voluntarily turned over and otherwise exempt property. Therefore, since creditor holds these proceeds and is a third party who properly used state collection procedures, these proceeds violate the concept of exempt property.

Debtors' mistake in this case was to voluntarily surrender otherwise exempt property to the creditor. Debtors were entitled to up to \$20,000 of exemptions in farm machinery and equipment pursuant to the Iowa Code section 627.6(12). However, by choosing to retain as exempt less than \$20,000 worth of machinery and then attempting to exempt the balance of the exemption in cash, debtors lost forever the voluntarily turned

over property and the proceeds therefrom because claimed-as-exempt proceeds violate both Iowa case law and the concept of exempt property.

CONCLUSION AND ORDER

WHEREFORE, based on the foregoing analysis, the court concludes that proceeds from the voluntary sale of debtors' otherwise exempt property are not exempt property.

THEREFORE, IT IS ORDERED, that debtors' motion to compel creditor to pay over proceeds is overruled.

DATED this 8<sup>th</sup> day of January, 1988.

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RUSSELL J. HILL  
U.S. BANKRUPTCY JUDGE