

UNITED STATES BANKRUPTCY COURT  
For the Southern District of Iowa

In the Matter of

GERALD L. SCHAEFER and  
SUSAN D. SCHAEFER,

Debtors.

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Case No. 89-00722-C H  
Chapter 7

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**ORDER--MOTION TO AVOID LIEN**

On June 22, 1989, a hearing was held on Debtors' Motion to Avoid Liens, and resistance thereto by Farmers Home Administration (hereinafter "FmHA"). Paul M. Goldsmith appeared on behalf of Debtors and Kevin R. Query appeared on behalf of FmHA. At the conclusion of said hearing, the Court took the matter under advisement with a stipulation of facts and briefing deadline of July 14, 1989. The Court considers the matter fully submitted.

This is a core proceeding pursuant to 28 U.S.C. §157(b)(2)(A). The Court, upon review of the pleadings, arguments of counsel and brief submitted, now enters its findings and conclusions pursuant to Fed.R.Bankr.P. 7052.

**FINDINGS OF FACT**

1. Debtors filed their Chapter 7 petition on April 4, 1989.
2. Debtors listed implements and equipment related to their farming operation in their schedule B-4, claiming them exempt pursuant to Iowa Code §627.
3. The following implements and equipment are subject to a security interest in favor of FmHA created by a security agreement dated May 2, 1978: Keewanee 3 pt. blade, 2 3 pt. bale movers, Allis

Chalmers 3 pt. bottom plow, Heston 3 pt. chisel plow, Allis Chalmers 15 ft. disc, JD 400 15 ft. hoe, 7 shank NH 3 tool bar. The above-described equipment will hereinafter be referred to as "Pre-Code Equipment".

4. On May 10, 1989, Debtors filed a motion to avoid the FmHA lien on certain implements and equipment, including the Pre-Code Equipment.

5. On May 22, 1989, FmHA filed a resistance to Debtors' motion to avoid liens, asserting that by reason of the May 2, 1978 security agreement, FmHA's interest in the Pre-Code Equipment arose prior to enactment of the Bankruptcy Code and therefore could not be avoided pursuant to §522(f).

6. The May 2, 1978 security agreement secured an operating loan, evidenced by a May 2, 1978 note in the amount of \$37,080.00 (hereinafter "Operating Note"). The Operating Note was consolidated with two other notes in a promissory note dated May 13, 1983, (hereinafter "Consolidation Note").

7. The May 2, 1978 security agreement secured an emergency loan, evidenced by a May 2, 1978 note in the amount of \$13,350.00 (hereinafter "Emergency Note"). The Emergency Note was rescheduled in a promissory note dated January 25, 1989 (hereinafter "Rescheduling Note").

8. The Consolidation Note contains the following language:

If "Consolidation and subsequent loan,"  
"Consolidation," "Rescheduling," or  
"Reamortization" is indicated in the "Action

Requiring Note" block above, this note is given to consolidate, reschedule or reamortize, but not in satisfaction of the unpaid principal and interest on the following described note(s) or assumption agreement(s) (new terms):

<u>Face Amt.</u>	<u>Int. Rate</u>	<u>Date</u>	<u>Original Borrower</u>	<u>Last Install Due</u>
\$37,080.00	8 %	5/7/78	Gerald L. Schaefer	5/7/85
\$ 7,000.00	8½%	2/16/79	Gerald L. Schaefer	2/16/86
\$14,000.00	14.25%	3/15/82	Gerald L. Schaefer	3/15/83

The "Consolidation and subsequent loan" square set forth in the "Action Requiring Note" block on the Consolidation Note is checked. The \$37,080.00 note listed above is the Operating Note.

9. The Rescheduling Note contains the following language:

If "Consolidation and subsequent loan," "Consolidation," "Rescheduling," or "Reamortization" is indicated in the "Action Requiring Note" block above, this note is given to consolidate, reschedule or reamortize, but not in satisfaction of the unpaid principal and interest on the following described note(s) or assumption agreement(s) (new terms):

<u>Face Amt.</u>	<u>Int. Rate</u>	<u>Date</u>	<u>Original Borrower</u>	<u>Last Install. Due</u>
\$13,350.00	3.0000 %	5/2/78	Gerald L. Schaefer	5/2/85

The "Rescheduling" square set forth in the "Action Requiring Note" block on the Rescheduling Note is checked. The \$13,350.00 note listed above is the Emergency Note.

10. On July 17, 1986, Debtors executed another security agreement covering the Pre-Code Equipment and other property of Debtors, granting a security interest in said property to FmHA.

**DISCUSSION**

Section 522(f)(2)(B) allows a debtor to avoid a lien which impairs a properly claimed exemption if such lien is:

(2) a nonpossessory, nonpurchase-money security interest in any--

...

(B) implements, professional books, or tools, of the trade of the debtor or a dependent of the debtor....

In interpreting section 522(f)(2)(B), the Eighth Circuit has held that "tools" and "implements" include large pieces of farm machinery.

In re LaFond, 791 F.2d 623, 627 (8th Cir. 1986).

In the case *sub judice*, Debtors sought to avoid the lien on farm implements and equipment including the Pre-Code Equipment. FmHA objected on the ground its security interest in Debtors' Pre-Code Equipment was given prior to November 6, 1978, the date of the enactment of the Bankruptcy Code. Liens granted prior to said enactment date cannot be avoided under §522(f). U.S. v. Security Industrial Bank, 459 U.S. 70, 82 (1982). However, 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). The Pre-Code Equipment is subject to an FmHA security interest given prior to November 6, 1978. Therefore, Debtors cannot avoid FmHA's lien on the Pre-Code Equipment unless a novation occurred after November 6, 1978.

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 (Iowa 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).

In determining whether a novation occurred in the case sub judice, the Court finds Matter of Dukes, slip op. (Bankr. S.D. Iowa February 29, 1988), a prior decision in the Southern District of Iowa analyzing a promissory note with language identical to the Consolidation Note and Renewal Note in this case, instructive. In Dukes, the Court stated:

The debtors are correct in pointing out that the factors this court utilizes in assessing the parties' intent are 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. See Matter of Scanlan, No. 86-2870-W, slip op. at 12, (Bankr. S.D.Iowa, July 30, 1987). However, there is no need to resort to rules of construction where the intent of the parties is expressed in clear and unambiguous language. State v. Starzinger, 179 N.W.2d 761, 764 (Iowa 1970).

Dukes, at p. 5.

In the case *sub judice*, the parties' intent is clearly manifested in the language of the Consolidation Note and Renewal

Note. The language states that "this note is given to consolidate, reschedule, or reamortize, but not in satisfaction of the unpaid principal and interest on the (Operating Note or Emergency Note)." Consequently, the Court must conclude that the parties did not intend to extinguish the Operating Loan Note or Emergency Note, and a novation did not occur. The Pre-Code Equipment is thus subject to a lien granted prior to November 6, 1978, and therefore the lien on the Pre-Code Equipment cannot be avoided under §522(f).

**CONCLUSION AND ORDER**

WHEREFORE, based on the foregoing analysis, the Court concludes that the Pre-Code Equipment is subject to a lien granted prior to November 6, 1978, and therefore the lien on the Pre-Code Equipment cannot be avoided under §522(f).

WHEREFORE, because no resistance was filed to Debtors' motion to avoid lien on the remainder of the property described in Debtors' motion to avoid lien, the lien on this property is avoided under §522(f).

IT IS ACCORDINGLY ORDERED that Debtors' motion to avoid lien on the Pre-Code Equipment is denied. Debtors' motion to avoid lien on the remainder of the property described in Debtors' motion to avoid lien is granted.

Dated this 1st day of December, 1989.

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RUSSELL J. HILL  
U.S. BANKRUPTCY JUDGE