UNITED STATES BANKRUPTCY COURT
For the Southern District of Iowa

In the Matter of

JAMES W. EVERSOLE,
SANDRA K. EVERSOLE,

Debtors.

Case No. 87-824-W

Chapter 7

ORDER ON OBJECTION TO PROPERTY CLAIMED AS EXEMPT AND RESISTANCE TO MOTION TO AVOID LIENS

On July 7, 1987 a telephonic hearing on objection to property claimed as exempt and resistance to motion to avoid liens was conducted in Des Moines, Iowa. The Farmers Home Administration (FmHA) objected to property claimed as exempt on May 11, 1987. The debtors resisted on May 19, 1987. On May 14, 1987, the debtors moved to avoid liens. The FmHA resisted on May 26, 1987. Linda R. Reade, Assistant U.S. Attorney, appeared on Behalf of the FmHA and Norman L. Springer, Jr. appeared on behalf of the debtors. The case has been submitted on briefs and certain documents.

The debtors filed a joint petition for relief under Chapter 7 on March 27, 1987. They are farmers. According to Schedule B-4, they claim farm machinery, valued at $7,180.00, exempt pursuant to Iowa Code section 627.6(11) (a). The debtors moved under 11 U.S.C. section 522(f) to avoid the liens the FmHA has on the machinery.

The FmHA has objected to the exemption claim and motion

to avoid liens on a number of grounds. At the hearing, the court noted that whether retrospective application of the amendments to Iowa's exemption statute is constitutional had been resolved in this district by the appeal decision in Matter of Reiste, No. 87-153-B (S.D. Iowa, filed May 11, 1987). With respect to the value dispute, the court ordered that the parties resolve the matter by use of a third party appraisal. The FmHA has withdrawn its assertion that it possesses a purchase money security interest in the machinery. The only remaining issue concerns the FmHA's argument that its perfected security interest in the debtors' farm machinery arose prior to the enactment of the 1978 Bankruptcy Code and thus may not be avoided.

FACTUAL BACKGROUND

The debtors seek to avoid the FmHA's liens in the following property.

1. JD 4020 diesel tractor 1964, 14,000 hrs.
2. IHC M tractor, 1946 3. IHC 560 gas tractor, 1960
4. MF 410 gas combine
5. MF corn head
6. Oliver 566 plow 5/16 W. harrow
7. JD AT40 cultivator
8. JD RW 13 10" disc
9. JD 494A planter
10. JD 61 x 12' wagon
11. Westendorf 4 row rotary hoe
12. Caswell loader
13. Hog waterer
14. 3 hog feeders
15. 1 creep feeder
16. 8 farrowing crates
17. Viking elevator
18. Kelly Ryan 41 x 81 feed wagon
19. 1 set of 12" x 38" duals
20. David Bradley hayrake
21. Farmhand grinder mixer
22. Livestock trailer

23. Whestley bale carrier
24. IHC No. 8 4/14 plow
25. Rotary mower (51 blade - broken)

The record reveals that prior to the November 6, 1978 enactment date of the Bankruptcy Code, the debtors executed two promissory notes in favor of the FmHA. Since then, the parties have executed a number of other notes. The nature of the relevant notes are summarized as follows:

NOTES

	Date of Note	Amount	Int.	Disposition
1.	Feb. 13, 1978	$4,800.00	3%	Original note, remortized, not paid.
	Apr. 3, 1981	1,539.71	3%	Rescheduling Feb. 13, 1978 amount.
	May 6, 1984	1,683.72	3%	Rescheduling Apr. 3, 1981 amount.
2.	Feb. 13, 1978	26,400.00	8%	original note, remortized, not paid.
	Apr. 3, 1981	26,114.31	13%	Rescheduling Feb. 13, 1978 amount.
	May 16, 1984	31,539.04	8%	Rescheduling Apr. 3, 1981 amount.
	April 2, 1986	33,139.77	8%	Rescheduling May 16, 1984 amount.

Both original notes dated February 13, 1978 are stamped "REMORTIZED, NOT PAID." All of the subsequent notes listed above contain 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 agreements) (new terms): ....

Shortly before the February 13, 1978 notes were executed, the parties executed a security agreement giving the FmHA a security interest in, among other things, farm machinery. The security agreement is dated January 13, 1978. A number of articles of machinery subject to the present lien avoidance action were acquired after the enactment date and therefore were not listed on the security agreement. These include the IHC 560 gas tractor, the MF 410 gas combine, the MF corn head, the livestock trailer, the Whestley bale carrier and the rotary mower. The security agreement was properly perfected with the Iowa Secretary of State.

DISCUSSION

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 machinery since the lien arose prior to the enactment of the 1978 Bankruptcy Code. The debtors contend that this pre-Code security interest 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. A mere change in the interest rate for the benefit of the lender does not constitute a novation. Matter of Scanlan, Case No. 86-2870-w (Bankr. S.D. Iowa, filed July 30, 1987).

Examination of the pertinent notes in this case reveals that the rewriting of the February 13, 1978 notes does not

constitute a novation of these notes. None of the subsequent notes show that the FmHA advanced new money to pay off the pre-enactment obligations. In fact, the documents show the contrary. The original notes are stamped "REAMORTIZED, NOT PAID." The subsequent notes merely reschedule the original notes. Language in these notes states that "this note is given to...reschedule ... but not in satisfaction of the unpaid principal and interest of the (original] note ....” Further, no additional security agreements were executed and no additional collateral was provided for the subsequent notes.

The debtors argue that, even if a novation has not occurred, lien avoidance is still available for machinery obtained after the enactment date of the Code. They rely on In re Zweibahmer, 25 B.R. 453 (Bankr. N.D. Iowa 1982) wherein the late Bankruptcy Judge William W. Thinnes ruled that liens that attached after the enactment date could be avoided. The undersigned agrees. An "after-acquired property" clause in a pre-enactment security agreement does not in and of itself defeat a motion to avoid liens in after-acquired property. The determinative fact is the date upon which the debtors acquired the property--that is, the date upon which the lien attached. In this case, the IHC 560 gas tractor, the MF 410 gas combine, the MF corn head the livestock trailer, the Whestley bale carrier and the rotary mower were purchased after the enactment date. Accordingly, the debtor may avoid the FmHA's liens on these

articles of machinery.

Finally, the debtors contend that the pre-enactment lien may not exceed $31,200.00, the pre-enactment debt. They maintain that this amount must be reduced by any payments that were applied to the pre-enactment debt. They again rely upon the Zwiebahmer opinion. The undersigned agrees with Judge Thinnes' reasoning. As a general matter, "the secured party's lien equals the value of the collateral or the amount of the underlying indebtedness, whichever is less". Zweibahmer, 25 B.R. at 458. Accordingly, the debt outstanding on the date the Code was enacted is the maximum amount the pre-enactment lien could secure. That amount must be adjusted for payments applied to the pre-enactment debt. Moreover, if the value of the collateral securing the pre-enactment debt is less than the adjusted amount of the pre-enactment debt, then the value of that collateral determines the extent of the non avoidable lien. Id. at 458-459.

The present record does not contain sufficient information to permit the court to determine the extent of the non avoidable lien. If the parties are unable to resolve the remaining factual issue, they will be given an opportunity to submit appropriate evidence regarding the adjusted amount of pre-enactment debt. As indicated earlier, any actual value dispute with respect to the collateral shall be resolved by a third party appraisal.

CONCLUSION AND ORDER

WHEREFORE, based upon the foregoing discussion, the court hereby finds that the FmHA's security interest in machinery arose prior to the enactment of the Bankruptcy Code and was not extinguished by a novation. The court further finds that the FmHA's liens on the machinery acquired after the enactment date of the Bankruptcy Code can be avoided.

THEREFORE, the FmHA's resistance to motion to avoid liens is denied with respect to the IHC 560 gas tractor, the MF 410 gas combine, the MF corn head, the livestock trailer, the Whestley bale carrier and the rotary mower.

With respect to the other machinery, the parties shall submit a supplemental consent order regarding the extent of the non avoidable lien, consistent with this decision, by February 29, 1988. if the parties are unable to stipulate the fact, they may submit their respective evidence and indicate whether further hearing is necessary by the same date. However, any valuation dispute must be resolved by a third party appraisal.

Signed and filed this 25th day of January, 1988.

LEE M. JACKWIG

CHIEF U.S. BANKRUPTCY JUDGE