

Appeal History:

aff'd. No. [2C89-3001](#) (N. D. Iowa Oct. 15, 1990) (O'Brien, J)

In the United States Bankruptcy Court

for the Northern District of Iowa

HAROLD FREDERICK BURMESTER and
MARVEL GWENDOLYN BURMESTER

Bankruptcy No. X85-02282M

Debtor(s).

Chapter 7

Trustee Larry S. Eide

Adversary No. X-87-0370-M

Plaintiff(s)

vs.

FARMERS COOPERATIVE ELEVATOR
CO. Iowa Falls Iowa; HOBSON
CADY & DREW; and HAMPTON
STATE BANK

Defendant(s)

MEMORANDUM OF DECISION AND ORDER

The matter before the court is the trustee's complaint to set aside certain pre-petition transfers of the debtors in real estate. Trial was held October 24, 1988 in Mason City, Iowa.

The court now issues its memorandum of decision and order which contains findings of fact and conclusions of law pursuant to Bankr. R. 7052.

This is a core proceeding under 28 U.S.C. § 157(b)(2)(H).

Challenges as to certain conveyances by the debtors as to the real property in question were resolved by stipulations of settlement and prior orders of the court. Settlements have also resolved the trustee's request that the court determine secured party statuses of the various defendants as to the real property. These resolutions leave at issue only the continuing validity of a real estate mortgage held by defendant Farmers Cooperative Elevator Co. (COOP).

STIPULATED FACTS

At the commencement of the trial, trustee and Coop stipulated to the following facts which the court now adopts as a part of its findings:

1. Defendant Farmers Cooperative Elevator Co. was a creditor of the Debtors at the time of execution, delivery and recording of the mortgage in question (hereinafter referred to as the "transfer").
2. The transfer was made on account of antecedent debt owed by the Debtors to Defendant Farmers Cooperative Elevator Co. before such transfer was made.
3. The transfer purportedly secured Defendant Farmers Cooperative Elevator Co. to the real estate in question and would now entitle said Defendant to receive a greater portion of its claim that it would receive but for the transfer.
4. The lien, claim or encumbrance of Defendant Farmers Cooperative Elevator Co. would, if not set aside, be a first lien against the real estate in question.
5. The real estate in question has been sold by the Trustee for the sum of \$144,000.00.
6. There would exist insufficient assets in this estate to pay all secured and unsecured creditors in full.
7. The transfer to Defendant Farmers Cooperative Elevator Co., if valid, would permit said Defendant to receive payment of all of its claim.
8. In making said transfer, the Debtors intended or desired to prefer Defendant Farmers Cooperative Elevator Co. in the payment of its debt.
9. Debtors were indebted to Defendant Farmers Cooperative Elevator Co. in the approximate amount of \$9,952 on the date of filing this Bankruptcy.
10. Debtors executed and delivered to Defendant Farmers Cooperative Elevator Co. a Mortgage dated July 29, 1985, encumbering approximately 120 acres of Franklin County farmland. This Mortgage was filed on August 1, 1985 in the office of the Recorder of Franklin County, Iowa as Instrument No. 851565.
11. The debt for which this Mortgage was given was carryover debt due by the Debtors for crop expense purchases for crop years including 1985 and prior.
12. At the time of execution, delivery and recording of the Mortgage to Defendant Farmers Cooperative Elevator Co., Debtors were indebted to numerous other parties for substantial sums of money and said debts exceed the then value of their assets by more than \$300,000.
13. At the time of the execution, delivery and recording of the Mortgage to Defendant Farmers Cooperative Elevator Co., Debtors were Defendants in a mortgage foreclosure action brought by Defendant Hampton State Bank. The Debtors asserted in that mortgage foreclosure action that the mortgage lien to Defendant Hampton State Bank was not valid and could not be foreclosed. A Motion for Summary Judgment had been filed by Defendant Hampton State Bank in that mortgage foreclosure proceeding and was shortly to be heard by the Franklin County District Court.
14. At or about the time of execution, delivery and recording of the Mortgage to Defendant Farmers Cooperative Elevator Co., Debtors executed and delivered Mortgages

to Sietsema-Vogel Funeral Home, Alvina Burmester Bohn and Defendant Hobson, Cady & Drew.

ADDITIONAL FINDINGS OF FACT BY THE COURT

15. Harold Burmester (HAROLD) began farming in 1950. Burmesters filed their Chapter 7 case on November 1, 1985. In the 12 to 15 years prior to his filing bankruptcy, Burmester was a borrower and customer of Hampton State Bank (HAMPTON). Loans with the bank included real estate loans and operating loans.

16. By the time Burmesters filed their Chapter 7 case, they were indebted to Hampton in excess of \$260,000.

17. In addition to having a security interest in personal property of the Debtors, Hampton also held a real estate mortgage on property legally described as follows:

The West Half (W- $\frac{1}{2}$) of The Southeast Quarter (SE- $\frac{1}{4}$) except the West 230 Feet of The South 574 Feet thereof in Section Eleven (11), Township Ninety-two (92) North, Range Twenty-one (21) West of the 5th P.M., Franklin County, Iowa; and

The Northeast Quarter (NE- $\frac{1}{4}$) of Section Fourteen (14), Township Ninety-two (92) North, Range Twenty-one (21) West of the 5th P.M., Franklin County, Iowa.

18. Hampton began a foreclosure proceeding on this property in May of 1986. Burmesters defended the foreclosure action and challenged the validity of the bank's mortgage.

19. By early February, 1985, Burmesters had become indebted to Coop for the purchase of farm supplies. This included purchases of items which enabled Burmesters to plant a crop in 1985.

20. On February 8, 1985, the attorney for Coop contacted Harold Burmester requesting information from him as to satisfaction of a promissory note in the amount of \$6,322.60 plus interest. This promissory note represented indebtedness of Burmesters to Coop for prior purchases. At the time of the February 8, 1985 letter, Burmesters were also indebted to Coop for purchases on open account. On July 1, 1985, the balance due on the note including interest was \$7,431.95. The balance due on the open account as of July 1, 1985 was \$8,095.56.

21. On July 1, 1985, Burmesters executed a promissory note to Coop in the amount of \$15,747.51 which combined the prior note and the open account indebtedness. The July 1, 1985 note was a demand note and required interest at 15% per annum. The open account had been accruing interest at the rate of 24% per annum.

22. Coop had determined not to sue Burmester because of his difficult financial position and the low likelihood of collection. It desired not to make financial matters more difficult on Burmesters or to waste its own money on collection and intended to rely on Burmesters' good faith efforts to pay.

23. Although Coop had not requested security for the promissory note, Harold Burmester later contacted Coop and offered it a mortgage on the following property:

The Northeast Quarter (NE- $\frac{1}{4}$) of Section Fourteen (14), Township Ninety-two (92) North, Range Twenty-one (21) West of the 5th P.M., except a tract commencing (legal

description omitted). Said excepted tract containing approximately Forty (40) acres more or less. The foregoing description is located in Franklin County, State of Iowa.

According to Harold, Coop had requested the execution of the July 1 note. Harold, however, brought up the granting of the mortgage to Coop to secure the note. When he signed the note, Harold did not tell Coop that he would give them a mortgage. When the mortgage was later executed, the terms of the note were not changed.

24. Coop accepted the mortgage proposal. At the time of the execution of the mortgage on July 29, 1985 and at the time of its recording on August 1, 1985, Burmesters were insolvent in that the sum of their debts was greater than all of their property at fair valuation (including exempt property). Further, at the time Burmesters gave the mortgage to the Coop on the 120-acre parcel, they had no other assets with which to pay debts.

25. Although it is unclear and disputed as to when, debtors received a check or checks arising out of their farming operation either relating to a seed corn payment or the sale of grain. The check or checks were multiple payee check(s) payable to Hampton, the debtors, Coop and perhaps others. A dispute arose among the creditors named as payees, and particularly Coop and Hampton, as to the disposition of the proceeds. The funds were ultimately distributed among the named creditors, and although Burmesters were unsure as to exactly how the money was distributed, they felt that Coop did not receive as much as it should have from the checks and the bank perhaps received more. Coop should have received more, Burmesters thought, because Coop had funded 1985 crop inputs while the bank had not.

The parties believe it important to obtain a determination as to when this dispute arose. The plaintiff believes it arose prior to the transfer of the mortgage to Coop and therefore circumstantially shows debtors' intent to hinder, delay or defraud, whereas Coop argues that the dispute over the grain checks occurred after the transfer of the mortgages and is therefore irrelevant to the issue of motive. The court finds that the mortgage transfer took place after the dispute.

26. The transfer of the mortgage to Coop was suggested to Harold Burmester by his attorney, Art Cady. At the time of the transfer, Burmesters were contemplating bankruptcy. Also at the time of the debtors' execution of the mortgage, debtors were aware of the challenge to the bank's "first mortgage" and had made Coop aware of this challenge.

27. Debtors hoped that if the bank mortgage were invalidated, Coop could be paid from the value of the property. Burmesters were told by their attorney that there was a "good chance" that the bank's mortgage was invalid. Cady had told Harold Burmester that if the bank's mortgage were invalidated and in the absence of the debtor granting mortgages to other creditors, the bank would still get most of the 160 acres covered by the mortgage. This was Harold Burmester's understanding because the bank was suing him also on the underlying debt.

Burmesters testified that the reason for granting the mortgage to Coop was because they wanted to see Coop get paid. They had no other assets with which to pay Coop and if they did not give the mortgage to Coop, the bank would still receive all the benefit from the real property even if bank's mortgage were invalidated. Burmesters understood that they had insufficient assets to pay all their creditors in full and that if Coop were paid from the 120 acres because of the mortgage, it would mean that the bank would get less from that real property. In other words, as Harold Burmester testified, the effect of the granting of the mortgage to Coop, if bank's mortgage were invalidated, was to lessen the total amount bank would be paid from the property. This was not only his understanding but also his intent

so Coop could get paid. Burmester further testified that he understood his granting of the mortgage to Coop would have the effect of hindering bank in the event bank's mortgage was invalidated. Harold Burmester understood that if the Burmesters' challenge to bank's mortgage was unsuccessful, the second mortgage they were giving Coop would be worthless. Coop also understood this. Coop, in taking the mortgage, had no great expectations as to its value.

28. In August, 1986, the Iowa District Court for Franklin County invalidated Hampton's mortgage.

29. The bank later obtained a judgment lien against the subject property when it obtained a judgment against Burmesters in state court on September 6, 1985.

30. Post-mortgage payments on the note had reduced its balance to \$9,952 by the date of bankruptcy.

DISCUSSION

Trustee seeks to set aside the transfer of the mortgage to Coop on three grounds:

(1) Burmesters granted Coop the mortgage with intent to hinder, delay or defraud bank and therefore the mortgage should be set aside under 11 U.S.C. § 548(a)(1);

(2) Burmesters transfer of the mortgage to Coop was a fraudulent conveyance under Iowa law and therefore should be set aside under 11 U.S.C. § 544(b); and

(3) the transfer of the mortgage is avoidable under 11 U.S.C. § 548(a)(2)(A) and (B)(i) in that at the time of the transfer debtors were insolvent and received less than a reasonably equivalent value in exchange for the mortgage.

TRANSFER WITH INTENT TO HINDER, DELAY OR DEFRAUD UNDER 11 U.S.C. § 548 (a)(1)

Trustee argues that the evidence shows, as he alleges, that Burmesters gave the mortgage to Coop in order to hinder the collection efforts of Hampton State Bank.

The burden of proof with regard to these allegations is on the plaintiff. This court believes that the trustee has failed to meet this burden.

The evidence shows that Burmesters intended, if possible and in the event that the bank's mortgage were invalidated in state court, to prefer Coop over other creditors and more particularly bank. Burmesters understood that the mortgage would have that effect on the contingency that bank's mortgage was invalidated under state law.

This court must distinguish, however, the knowledge or perception of debtors that the preferential treatment would have a hindering effect, from an intent to hinder, delay or defraud bank by the transfer.

The court believes that the evidence shows that the motive of debtors in giving Coop the mortgage was to enable, if possible, Coop to be paid because of its cooperation with debtors in providing input supplies for their farming operation.

There is no question that Burmesters deliberately and knowingly gave what they believed might result in a preferential payment on what was then unsecured debt. Harold even intended that in order for Coop to be paid, the Bank would receive less from his assets. He apparently had the same type of intent in the dispute on the farm products checks.

However, the intent which a trustee must prove under § 548(a) must be more than the simple intent to prefer creditor. Roelmeyer v. Intercontinental Bank (In re Lucar Enterprises), 49 B.R. 717, 718 (Bankr. S.D. Fla. 1985); see Coder v. Arts, 213 U.S. 223, 241-244 (1908).

It is the finding and conclusion of this court that the trustee has failed to prove that the intent of debtors was to hinder, delay or defraud bank as opposed to preferring Coop, although debtors understood that preference would have a hindering effect.

FRAUDULENT CONVEYANCE UNDER STATE LAW

Trustee argues that the transfer of the mortgage to Coop is avoidable under 11 U.S.C. § 544(b) as a fraudulent conveyance under state law. Plaintiff must show a fraudulent conveyance under state law by clear and satisfactory evidence. Rouse v. Rouse, 174 N.W.2d 660, 668 (Iowa 1970). Trustee argues that the transfer was made without consideration while the debtors were insolvent.

The debtors at the time of the transfer were insolvent under state law. First National Bank in Fairfield v. Frescoln Farms, Ltd., Robert Frescoln, and Charles Randall Frescoln, No. 218 87-750 slip op. at 12-13, Iowa, October 19, 1988.

The court cannot agree that there was no consideration for the transfer.

While there was no new consideration, there was a pre-existing debt to support the mortgage.

[A] valid pre-existing debt is ordinarily deemed sufficient consideration for any conveyance or giving of security by debtors to creditors, provided the amount of that antecedent debt is not materially less than a fair and reasonable value of the property conveyed or encumbered.

Rouse v. Rouse, 174 N.W.2d 660, 669 (Iowa 1970).

Debtors conveyed and Coop accepted a mortgage on real property to the extent of \$18,000.00. The indebtedness at the time was slightly under \$16,000.00.

The court finds and concludes that the amount of the antecedent debt was not materially less than the fair and reasonable value of the interest in property conveyed. Or in other words, the court does not find that the consideration for the mortgage interest was grossly inadequate.

Since there was consideration for the transfer, trustee may only avoid the transfer if he can show that Coop participated in an intent to hinder, delay or defraud Hampton. Hatheway v. Hanson, 230 Iowa 386, 297 N.W. 824, 827 (1941).

A creditor may take security for the debt due him, even though he is aware that the purpose of the debtor in giving it is to hinder, delay, and defeat, and thus to defraud, other creditors. (Citations omitted.) But if the creditor know of the fraudulent purpose of the debtor, and accept the mortgage wholly or in part to aid in accomplishing it, he

participates in the wrong, and the mortgage is fraudulent against creditors, although it was only on a reasonable amount of property to secure a valid debt.

Richards v. Schreiber, Conchar & Westphal Co., 98 Iowa 422, 67 N.W. 569, 571 (1896).

This court found no fraudulent intent on the part of Burmesters and likewise finds none on the part of Coop. Coop did not harbor an intent to hinder, delay or defraud Hampton State Bank. It sought instead to obtain payment of its own debt on the likelihood that the bank's mortgage would be disallowed.

It is therefore concluded that Burmesters' mortgage to Coop was not a fraudulent conveyance under Iowa law.

FRAUDULENT CONVEYANCE UNDER 11 U.S.C. §§ 548(a)(2)(A) AND (B)(i)

Trustee argues that at the time of the mortgage transfer, debtors were insolvent and received less than reasonably equivalent value in exchange for the mortgage.

There is no doubt that at the time of the transfer the debtors were insolvent within the meaning of 11 U.S.C. § 101(31). However, as indicated in the previous section of this memorandum, the court believes that the pre-existing debt of nearly \$16,000.00 was reasonably equivalent value in exchange for the mortgage interest in the property which Coop received.

CONCLUSIONS OF LAW

The transfer of the mortgage interest in debtors' real property to Coop to secure antecedent debt in the approximate amount of \$16,000.00 was not a fraudulent conveyance under 11 U.S.C. § 548(a)(1) and § 544(b) as it incorporates the Iowa law of fraudulent conveyances; or under § 548(a)(2)(A) and (B)(i), and therefore should not be set aside.

ORDER

IT IS THEREFORE ORDERED that the trustee's complaint against Farmers Cooperative Elevator Co. be dismissed. Judgment shall enter accordingly.

SO ORDERED ON THIS 16th DAY OF NOVEMBER, 1988.

William L. Edmonds
Chief Bankruptcy Judge

In the United States District Court

for the Northern District of Iowa

Central Division

HAROLD FREDERICK BURMESTER and
MARVEL GWENDOLYN BURMESTER

Bankruptcy No. X85-02282M

Debtors.

Larry S. Eide

Adversary No. X-87-0370-M

Appellant

vs.

FARMERS COOPERATIVE ELEVATOR
CO. Iowa Falls Iowa; HOBSON
CADY & DREW; and HAMPTON
STATE BANK

Appellee

ORDER No. 2C 89-3001

This matter is before the court on an appeal by Larry S. Eide, Trustee, in the bankruptcy of Harold and Marvel Burmester from a bankruptcy order following trial of a core proceedings. The bankruptcy court denied the Trustee's request to set aside as a fraudulent conveyance a pre-petition mortgage of the debtors to the appellee, Farmers Cooperative. A hearing was held before this court. After careful consideration of the briefs of both parties, the Trustee's appeal is denied.

A bankruptcy court's findings of fact are subject to the clearly erroneous standard of review. Bankr. R. 8013. Its conclusions of law are subject to de novo review. Stevens v. Pike County Bank, 829 F.2d 693 (Sth Cir. 1987).

There is no question but that the briefs of the appellant raise probing questions that gave this court reason to further ponder this decision. However, the bottom line is even if Mr. Burmester knew that the giving of the mortgage was going to hinder the bank, but his primary reason was a preference for the Coop, and the bankruptcy court is persuaded that the contrary has not been proven, then this court should not, under this record, change that decision. Further, the bankruptcy court found that there was adequate antecedent consideration for the mortgage and that said consideration need not be simultaneous or nearly so to the transaction. This court has not been able to find persuasive precedent to the contrary.

Based on the arguments presented in the appellee's brief and the reasoned opinion of the bankruptcy court, the judgment of said court is affirmed and the appeal is denied.

IT IS THEREFORE ORDERED that the November 16, 1988 order of the bankruptcy court is affirmed.

October 15, 1990.

Donald E. O'Brien, Chief Judge
UNITED STATES DISTRICT COURT

United States Court of Appeals

for the Eighth Circuit

No. 90-2921NIFD

Harold Frederick Burmester; Marvel Gwendolyn
Burmester

Appeal from the United States District Court for
the District of Northern Iowa

Debtors

Larry S. Eide, Trustee

Appellant

vs.

Farmers Cooperative Elevator

Appellee.

JUDGMENT

Appellant's motion to dismiss the appeal is granted. The appeal is hereby dismissed in accordance with Rule 42(b), Federal Rules of Appellate Procedure.

Mandate to issue forthwith.

December 12, 1990

Order Entered Under Rule 27B(a)

Clerk, U. S. Court of Appeals, Eighth Circuit.

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