

In the United States Bankruptcy Court

for the Northern District of Iowa

JERRY KENNETH FRANK and
AGNES MARIE BECKER FRANK
Debtor(s).

Bankruptcy No. X89-00039M

Chapter 7
Contested No. 2135

RULING RE: DEBTORS' MOTION FOR RELIEF FROM STAY

The matter before the court is debtors' Motion for Relief from Stay. The motion is resisted by Federal Land Bank of Omaha (FLB) and case trustee Larry S. Eide. Final hearing on the motion was held October 24, 1990 in Cedar Rapids, Iowa. Debtors and FLB have filed briefs in support of their positions. A brief has also been filed by the U. S. Trustee. He supports the debtors' motion.

FINDINGS OF FACT

In April, 1987, FLB filed a foreclosure action in Iowa District Court in Hancock County; it sought to enforce a note and mortgage executed by the Franks. Franks answered alleging fraud as a defense and asserting a counterclaim against FLB. The Iowa District Court bifurcated trial. Franks' counterclaim against FLB was tried first to a jury. The jury returned a verdict in favor of Franks in the amount of \$36,800.00. The district court granted FLB's Motion for Judgment Notwithstanding the Verdict. The district court's decision was based on the bar of the statute of limitations. The district court also granted FLB judgment against Franks on the note and foreclosed FLB's mortgage. The mortgaged property contained 80 acres. Forty of the acres were debtors' homestead. A sheriff's sale took place with the sheriff selling the 80 acres in two parcels; one parcel included the 40-acre homestead. FLB was the successful bidder as to each parcel.

Franks filed a chapter 12 bankruptcy on January 8, 1990. it was converted to a chapter 7 case on May 15, 1990. Franks claimed their 40 acres homestead as exempt.

The case trustee, Larry S. Eide, attempted to sell for a single purchase price the debtors' rights of redemption in the two parcels. These rights of redemption became property of the estate upon the filing of the bankruptcy case. The court did not approve the sale because it found impermissible the trustee's attempt to transfer the debtors' right of redemption in the homestead. The court also ruled that the trustee may not sell debtors' "appeal rights" insofar as the pending appeal allowed debtors to raise a fraud defense to the foreclosure of the homestead. The court has ruled, however, that the trustee may sell the counterclaim insofar as it is a right of the estate to an affirmative recovery from FLB.

On October 29, 1990, the trustee filed his Notice of Public Sale. He proposes to sell the estate's counterclaim against FLB. He also proposes to sell the estate's right of redemption to the non-homestead 40 acres. The trustee's notice of sale distinguishes his ability to sell the counterclaim from

his inability to sell any fraud defense Franks may have to the foreclosure on the homestead. This is in compliance with the court's prior orders.

DISCUSSION

Franks seek relief from the automatic stay of 11 U.S.C. § 362 in order to proceed with the appeal in the Iowa Supreme court. Franks concede that any affirmative recovery on the counterclaim against FLB would belong to the estate or to its assignee. Franks also concede the authority of the trustee to transfer the right of redemption to the non-homestead 40 acres. Franks ask for relief in order to proceed with the appeal only so far as it relates to the homestead. They believe that FLB's alleged fraud is a defense to the foreclosure proceeding. FLB that all of the debtors' interests at the time of the bankruptcy filing became property of the estate and are transferable by the trustee. FLB's position ignores the very nature of the homestead right provided under Iowa Code § 561.16. Although Franks may have waived their homestead defenses against FLB, this does not mean the trustee in bankruptcy may invade the homestead for the purpose of a distribution to unsecured creditors. Debtors are presently in possession of the 40-acre homestead. Until the redemption period expires, they have the legal opportunity to redeem their home from the sheriff's sale. To permit the trustee to sell the right to redeem the homestead would be to allow the trustee to impermissibly invade the homestead right. To permit the trustee to sell a claim in defense of that right is also impermissible.

The interrelationship of state and federal law in bankruptcy cases often creates difficult questions. Prior to the filing of the bankruptcy case, the relationship of the parties to the appeal and the appellate issues was simple. The filing of Franks' bankruptcy case had the effect of dividing the ownership of the claims pending on appeal. As this court sees it, Franks should be able to use fraud as a defense to FLB's foreclosure. Franks should also retain the right to redeem their homestead. The trustee of the Franks' bankruptcy estate may now pursue the appeal as it relates to the \$36,800.00 counterclaim. Now, instead of two parties to the appeal, there are three. The trustee's sale of the counterclaim and the right to redeem the non-homestead property may effect an assignment of the trustee's right to be heard on appeal. But even if the trustee determines not to pursue the pending appeal, this should not affect the Franks' rights to continue to protect their homestead. Franks should be granted the requested relief. In the interest of judicial economy, this court will also grant relief to FLB so that it also may participate in the appeal before the Iowa Supreme Court. The trustee needs no such relief as the trustee is not stayed. Should the trustee assign the estate's rights to the counterclaim to a third party, the third party would not be stayed from prosecuting his or her portion of the appeal.

CONCLUSIONS OF LAW

Debtors Jerry and Agnes Frank have shown cause within the meaning of 11 U.S.C. § 362(d)(1) for modification of the automatic stay. Sufficient cause exists to provide similar relief to FLB.

ORDER

IT IS ORDERED that debtors' Motion for Relief from the Automatic Stay is granted. Jerry and Agnes Frank may proceed before the Iowa Supreme Court in defense of FLB's foreclosure on their homestead.

IT IS FURTHER ORDERED that Federal Land Bank of Omaha may proceed before the Iowa Supreme Court in the pending appeal.

SO ORDERED ON THIS 7th DAY OF NOVEMBER, 1990.

William L. Edmonds
Chief Bankruptcy Judge