In the United States Bankruptcy Court

for the Northern District of Iowa

LOUIS E. GUYNN
Debtor(s).

Bankruptcy No. L-91-1545C
Chapter 7

ORDER

On July 13, 1993, the above-captioned matter came on for hearing pursuant to assignment. Attorney Joe Peiffer appeared for Debtor. Attorney Ray Terpstra appeared for creditor, Cedar Valley Bank & Trust Company. Attorney Jeff Taylor was present as the Trustee in Bankruptcy. Evidence was submitted and the Court took the matter under advisement.

STATEMENT OF THE CASE

The Trustee and Creditor, Cedar Valley Bank & Trust Company, have filed two objections to exemptions claimed by Debtor Louis Guynn. The first objection addresses Debtor's claim of a homestead exemption to a remainder interest in real estate under 11 U.S.C. § 522(b)(2) and Chapter 561 of the Iowa Code.

Second, Cedar Valley Bank & Trust Company filed an objection to Debtor's exemption claim for tools of the trade. This claim consists of farm machinery and equipment in an amount not to exceed $10,000 pursuant to sec. 627.6(10) of the Iowa Code. More specifically, Creditor asserts that Debtor claimed three separate items of property as exempt in a Chapter 12 Plan of Reorganization previously filed in these proceedings. This Chapter 12 was converted to a Chapter 7 on March 2, 1993. After conversion, Debtor claimed several items of farm machinery as exempt which were different than those claimed as exempt under the Chapter 12. Creditor asserts that Debtor is bound by the exemptions claimed in the Chapter 12 proceeding. Creditor claims that Debtor is not free to modify the claimed exemption. Debtor disagrees and feels that he is free to modify his exemptions after conversion. Creditor also asserts that if the Court finds the Debtor is able to modify the items listed as exempt, Debtor has understated the values of the new exempt property. Creditor asks the Court to properly value the same and to limit the total value of exempt property to $10,000 pursuant to sec. 627.6(10) of the Iowa Code. The Court will address both claims separately.

HOMESTEAD EXEMPTION

Debtor claims as exempt a remainder interest in property located in Benton County, Iowa. The uncontested facts establish a remainder interest bequeathed to Debtor under the Will of his father, Roy Guynn, pursuant to sec. 561.1 and 561.16 of the Iowa Code. Though Debtor's Schedules do not reflect a lease hold on the property subject to the life estate of the Debtor's mother, Clara Guynn; Debtor is, in fact, living on the farmstead previously owned by his father.

The Will of Roy Guynn provides that Louis Guynn and the decedent's other two children shall have an undivided remainder interest in one-half of the real estate owned by the decedent. The other one-half was bequeathed to decedent's wife.

Creditor asserts that it is willing to concede that Debtor is entitled to have his leasehold interest exempted. However, Creditor states that a remainder interest is not subject to the homestead exemption. Creditor concludes, therefore, that Debtor's claim of having this property claimed exempt as a homestead should be denied.

The law is clear that a debtor, in general terms, is allowed a homestead exemption pursuant to 11 U.S.C. § 522(b)(2) and Iowa Code sec. 561.1. A homestead is defined by Iowa Code sec. 561.1 as "embracing the house used as a home by the owner". This definition has been interpreted as mandating that debtor hold a possessory interest in the property. In re Nielsen, No. 84-00352, slip op. at 3 (Bankr. N.D. Iowa Jan. 14, 1986). By definition, a remainder interest does not permit the use of this property as a home until after the death of the life tenant. As such, the remainder interest is future and non-possessory in nature. Therefore, Debtor may not claim his remainder interest exempt as a homestead at this time. However, such a determination does not necessarily preclude Debtor from claiming as exempt, the leasehold interest which he presently holds in the property. Perry v. Adams, 179 Iowa 1215, 1223, 162 N.W. 817, 820 (1917) (this case states that there may be a homestead right in a leasehold); White v. Danforth, 122 Iowa 403, 404, 98 N.W. 136, 137 (1904); Wertz v. Merritt, 74 Iowa 683, 687, 39 N.W. 103, 104 (1888).

Based on the foregoing, Debtor is not authorized to claim the future non-possessory remainder interest as exempt. In re Nielsen, No. 84-00352, slip op. at 3 (Bankr. N.D. Iowa Jan. 14, 1986). However, Debtor is entitled to claim an exemption to the extent of his leasehold estate interest. Perry, 162 N.W. at 820.

AMENDMENT TO EXEMPTION

Debtor claims as exempt tools of the trade. Debtor originally filed a Chapter 12 Farm Reorganization on August 16, 1991. As part of that Reorganization, Debtor claimed two items exempt as tools of the trade; (1) a John Deere A tractor with a value of $500; and (2) a John Deere 7000 planter with a value of $9,500. Debtor retained these exemptions until after the conversion to a Chapter 7 Bankruptcy on March 2, 1993.

Debtor then filed new Schedules and filed a new claim of exemptions for tools of the trade under § 627.6(11). He claimed as exempt; (1) a Chevy C20 truck with a value of $200.00; (2) a John Deere 7000 planter with a value of $6,500; and (3) a John Deere 4320 tractor with a value of $3,250. The John Deere 7000 planter is the same as was claimed exempt under the Chapter 12 proceeding.

The value of these items only becomes relevant if the Court makes a determination that Debtor is able to modify the exemptions after conversion from a Chapter 12 to a Chapter 7 Bankruptcy. Creditor presented Mr. Duane F. Johnson on the issue of value. Mr. Johnson is an auctioneer, a real estate agent, and an appraiser with 15 years experience. He has sold used farm machinery and equipment on numerous occasions during that time. He has previously testified as an expert on valuation. He testified that he examined this equipment personally and in his opinion, the John Deere planter has a value of $6,500; the Chevy C20 truck has a value of $250; and the John Deere 4230 has a value of $5,500. The main controversy involves valuation of the John Deere tractor. Debtor questions whether this is a John Deere 4230 or a John Deere 4320 which the Debtor argues would have a significantly lesser value. Mr. Johnson testified that he personally examined this tractor and compared the serial

numbers from the tractor with John Deere manuals. He stated that he is satisfied that this is a series 4230 tractor. Considering defects in the tractor by personal observation, and by comments made by Debtor, he placed the fair market value at $5,500. Debtor testified that this tractor was part of his father's estate. He testified that it is a series 4320. He testified that his father purchased this tractor used in the late 1970's. It has transmission problems and jumps out of gear periodically. It also has hydraulic problems. All of these problems require a substantial investment to correct. Based on these considerations, he places the value at $3,250. Debtor valued this tractor at $7,500 in the Chapter 12 Schedules. It was listed in the Chapter 12 bankruptcy as a John Deere series 4230 and not a John Deere 4320.

The Court has considered the evidence of value. Mr. Johnson has considerable experience in appraising farm machinery. Based upon the prior bankruptcy schedules, as well as the serial numbers from the tractor, it is the finding of this Court that this is a John Deere 4230 series tractor. Based upon its condition, as testified by Mr. Johnson, the fair market value is considerably higher than that placed upon the tractor by the Debtor. It is the conclusion of this Court that the value of this tractor is $5,500. The value of the Chevy C20 truck is $200 and the value of the John Deere 7000 planter is $6,500.

The precise issue for determination is whether Debtor may change his exemption election with regard to tools of the trade following conversion of the Bankruptcy from Chapter 12 to Chapter 7. Bankruptcy Rule 1009(a) provides that the Court may order an amendment to any schedule, including Schedule C - Property Claimed As Exempt - as a matter of course, at any time before the case is closed. Fed. R. Bankr. P. 1009(a). Courts have interpreted Rule 1009 in different ways. Some Courts feel that they have considerable discretion in allowing Debtors to amend freely. Some Courts have allowed amendment of exemptions even in the face of assertions of bad faith or prejudice to creditors. Redmond v. Tuttle, 698 F.2d 414, 417 (10th Cir. 1983). Similarly, some Courts have held that amendments to exemptions must be granted under Rule 110 simply because the amendment was proposed prior to the close of the case. These Courts conclude that the Court's only function under Rule 110 is to ascertain what parties should be given notice, rather than requiring an additional showing of good faith. In re Gershenbaum, 598 F.2d 779, 781 (3d Cir. 1979).

However, a substantial number of courts also conclude that prejudice to creditors or bad faith by Debtor are elements which may be considered in evaluating a motion to amend. In re Doan, 672 F.2d 831, 833 (11th Cir. 1982); see also In re Williamson, 804 F.2d 1355 (5th Cir. 1986); Lucius v. McLemore, 741 F.2d 125 (6th Cir. 1984); In re Andermahr, 30 B.R. 532 (Bankr. 9th Cir. 1983). One Bankruptcy Court has also incorporated concepts of prejudice and bad faith into a four part test for determining when to allow amendments to exemption schedules. A significant element of this test is an inquiry into whether an adverse party will be prejudiced if the amendment is granted and whether an undue hardship would befall a good faith creditor if the amendment were granted. In re Kochell, 23 B.R. 191, 192 (Bankr. W.D. Wis. 1982).

Iowa Bankruptcy Courts have utilized analysis incorporating concepts of prejudice and bad faith. The District Court for the Southern District of Iowa affirmed a Bankruptcy Court decision which overruled an objection to debtor's amendment to exemptions where prejudice to creditors and bad faith on the part of debtor was not shown. In re Pettit, 57 B.R. 362, 363 (S.D. Iowa 1985); see also In re Lawrence, No. 81-00370, slip op. at 3 (Bankr. N.D. Iowa Apr. 10, 1984) (approving an exemption amendment where objector cited no prejudice flowing from such an amendment). It is the conclusion of this Court that consideration of prejudice to creditors or bad faith on the part of the Debtor are appropriate considerations for the Court prior to granting a Motion to Amend Exemptions.

The background of this case establishes that Debtor filed an amended and substituted Chapter 12 Plan of Reorganization, which, in relevant part, was the product of negotiation and settlement of an adversary proceeding against the Bank. It provided that the Bank's lien in the two items claimed exempt (1948 John Deere A Tractor and John Deere 7000 Planter) would be avoided. This plan was confirmed by Bankruptcy Judge Michael Melloy on February 13, 1992 at which time the liens were avoided. The facts establish that upon conversion of the bankruptcy to a Chapter 7, Debtor wishes to substitute the 1948 John Deere A Tractor exemption, which no longer has a lien because of the approved lien avoidance, for two other items, which continue to have liens.

It is readily apparent that if an amendment to exemptions is granted, the Debtor will be free to seek lien avoidance in the two substituted items pursuant to 11 U.S.C. § 522(f)(2)(B) as tools of the trade. It is the conclusion of this Court that this potentiality creates creditor prejudice. It allows the Debtor to benefit unfairly from the protection extended under the Bankruptcy Code. It allows the Debtor to seek lien avoidance on exempt property on two separate occasions. When the liens were avoided in the first instance, the Creditor Bank experienced a diminished capacity to protect its financial position. Allowing Debtor to seek a second lien avoidance under the present circumstances, would further erode the Creditor Bank's position. No extraordinary circumstances are shown by the Debtor why this should be allowed in this case.

Secondly, the liens were avoided on the original two exemptions because of a settlement reached in an adversary proceeding against the Bank. As part of a stipulation of settlement, the Bank agreed not to object to Plan Confirmation and also agreed to the lien avoidance. The Stipulation of Settlement did not include any reference to Debtor subsequently claiming additional property as exempt and subject to potential lien avoidance. The decision to accept or reject any settlement is not made in a vacuum, and the fact that other liens might later be avoided can safely be assumed to have affected the Bank's negotiation and settlement process. To allow the Debtor to modify his exemptions at this time, would have the practical effect of allowing the Debtor to circumvent the effect of the original Stipulation of Settlement.

A somewhat similar situation was addressed by the Bankruptcy Court of the Western District of Oklahoma. In re Gilbert, 147 B.R. 801 (Bankr. W.D. Okla. 1992). Debtors and Creditor Bank negotiated and agreed that in exchange for the use of cash collateral and a promise not to object to Plan Confirmation, debtors would grant the bank a replacement lien in all of their farm equipment. Upon conversion of the case to a Chapter 7, debtors sought to avoid the lien in several pieces of the equipment. The Bankruptcy Court held that in the interest of fairness and equity, provisions of debtors' Chapter 12 Plan when effectuated prior to the conversion to a Chapter 7, remained binding upon the parties after conversion. The Court felt that upon conversion the effective date of the filing of the converted case, is the effective date of the original case, as controlled by 11 U.S.C. § 348(a). As such, the provisions of the debtors' confirmed plan were negotiated, post-petition agreements, entered into subsequent to the effective date of the debtors' Chapter 7 bankruptcy. The act of conversion does not render these agreements vulnerable to attack in the subsequent proceedings. In other words, the Court found that it was contrary to principles of equity and fairness to permit these debtors to reap the full benefit of their bargain but then deny the creditor the benefit of its bargain. Because of this, the Court did not allow the debtors to avoid the bank's lien in the converted case. In re Gilbert, 147 B.R. 801 (Bankr. W.D. Okla. 1992).

It is the conclusion of this Court that the reasoning found in Gilbert is applicable in the present case. This Court concludes that concepts of prejudice and bad faith are appropriate in determining whether a Motion to Amend Exemption Schedules should be allowed. In the present case, it is the conclusion of this Court that the Creditors would suffer prejudice by allowing amendments to the exemption

schedules, for the reasons set forth in this opinion. Therefore, it is the ultimate conclusion of this Court that Debtor's Application to Amend the Exemption Schedules should be denied and the Debtor is bound by those exemptions previously claimed in these bankruptcy proceedings.

WHEREFORE, it is the ruling of this Court that the Debtor may not claim his remainder interest as a homestead exemption.

FURTHER, it is the finding of this Court that the Debtor is entitled to claim his leasehold interest as exempt.

FURTHER, the Debtor's Motion to Amend Exemption Schedules is DENIED for the reasons set forth in this opinion.

FURTHER, as the Court has denied Debtor's Motion to Amend Exemption Schedules, the Court need not address valuation of those items of property claimed as exempt.

SO ORDERED this 17th day of August, 1993.

Paul J. Kilburg
U.S. Bankruptcy Judge