

In the United States Bankruptcy Court

for the Northern District of Iowa

CARL M. SIMON and
DIANE L. SIMON

Debtor(s).

Bankruptcy No. 94-21591KD

Chapter 12

MORRIS L. ECKHART JAMES R. Adversary No. 94-
2173KD

KOBY AND BARRY J. HAMMERBACK

Plaintiff(s)

Adversary No. 94-2173KD

vs.

CARL M. SIMON DIANE L. SIMON
ROBERT L. SIMON

Executor of the Estate of

Ralph J. Simon Deceased and

TRI-STATE COMMUNITY CREDIT
CORP.

Defendant(s)

ORDER

On July 21, 1995, the above-captioned matter came on for trial pursuant to assignment. Attorney Peter Riley represented the Debtors/Defendants, Carl M. Simon and Diane L. Simon (individually, "Carl" and "Diane"). Attorney Mike Stapleton represented Defendant, Robert L. Simon, Executor of the Estate of Ralph J. Simon. Attorney Ray Terpstra represented the Plaintiffs, Morris L. Eckhart, James R. Koby and Barry J. Hammerback (collectively, "Plaintiffs"). Tri-State Community Credit Corp. ("Tri-State") is also a named defendant. However, all parties stipulated to Tri-State's interest in this case. As such, neither Tri-State nor its attorney participated in the trial. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A),(K) and (O). Evidence was presented after which the Court took the matter under advisement.

STATEMENT OF THE CASE

Plaintiffs claim a perfected security interest in 300 head of dairy cows, currently located on Carl's farm in Dubuque County, Iowa. Plaintiffs also claim a security interest in the farm products and proceeds from the cattle, pursuant to a security agreement entered into with Carl's brother, Ralph Simon ("Ralph"), on October 26, 1993. Plaintiffs are practicing attorneys and the security agreement was executed contemporaneously with an amended retainer agreement between Plaintiffs and Ralph. The retainer agreement secured Plaintiffs' legal services and expenses for prosecuting a counterclaim which Ralph was asserting against Tri-Veterinary Associates ("Tri-Vets"). Under the security agreement, the cattle were to serve as collateral for the repayment of a promissory note and future advances representing advancements and expenses incurred or to be incurred by Plaintiffs' law firms in representing Ralph in the Tri-Vets counterclaim. A UCC-1 financing statement giving notice of Plaintiffs' security interest was filed with the Iowa Secretary of State on December 30, 1993.

Ralph's counterclaim in the Tri-Vets case was based upon allegations of veterinary malpractice committed by Tri-Vets

in treatment of the cattle. The jury trial lasted twelve weeks between mid-October, 1993 and the end of that year.

Carl, while not a party to the suit, was subpoenaed to give a deposition about one week after the trial had started and subsequently testified in person at trial. Carl gave his deposition under oath on October 21, 1993. One of the primary issues addressed in this deposition was Carl's ownership interest in the cattle. The parties were interested in determining whether Carl's relationship was that of herdsman to or owner of the cattle. Carl testified that he had simply been the herdsman "continuously up until [the day of the deposition]." Upon further questioning, Carl testified that the cattle belonged to Ralph and that Carl had no ownership interest in this herd of cattle. Carl further testified that he had not told anyone that he (Carl) owned the cattle.

On October 31 and November 1, 1992, Carl gave testimony in the Tri-Vets trial. On direct examination by Ralph's attorney, Morris Eckhart, Carl testified that Ralph owned every one of the cows in the Herd. On cross-examination by Tri-Vets' attorney, Carl testified on two separate occasions that the cattle were owned by Ralph and not by him (Carl).

The jury returned a comparative fault verdict in which Ralph received no damage award. Ralph died within a week of the judgment, on January 6, 1994, leaving the promissory note to Plaintiffs unpaid. Plaintiffs now desire to foreclose their security interest in the cattle subject to a security interest held by Tri-State. All parties have stipulated that Tri-State's security interest, obtained on September 10, 1992, is prior and paramount to any held by Plaintiffs. According to Tri-State, the balance on the note, which their security interest is securing repayment of, is \$50,785.25 as of the trial date.

Carl now testifies in this case that, contrary to his prior sworn testimony in the Tri-Vets trial, he is in fact the true owner of the cattle. He further maintains that he was the owner of the cattle on October 26, 1993 when Plaintiffs' security interest in the cattle was obtained from his brother Ralph. Carl claims that, since Ralph had no interest in the cattle at that time or since, Plaintiffs' security interest never attached.

Carl claims to have obtained ownership of the cattle on or shortly after September 1, 1992 by virtue of an agreement between himself and his brother Ralph. Under this alleged agreement, Carl would assume Ralph's farming debt and in return would be compensated by Ralph with a Bill of Sale for one head of cattle for every \$700 of Ralph's debt which he retired. Carl claims that he has taken over sufficient debt (\$218,894.52) so that the entire Herd belongs to him.

The alleged agreement through which Carl claims ownership of the cattle was never memorialized in a written document. Ralph did eventually execute a Bill of Sale for 300 head of Holstein dairy cattle to Carl on December 30, 1993. However, this was nearly 16 months after the purported cows-for-debt-retirement agreement was entered and just a week before his death. This Bill of Sale was never delivered to Carl but was held in Carl's Tri-State file by Curtis Pint, Ralph and Carl's Tri-State banker. Pint had drafted the Bill of Sale at Ralph's insistence. Carl testified that he was not aware of its existence until it was revealed in this proceeding. On January 12, 1994, the periodic milk check from Wapsie Valley Creamery, Inc. for the Herd's milk production was transferred from Ralph's name to Carl's name, retroactive to January 1, 1994. This transfer was done at the request of Robert Simon (brother to both Ralph and Carl) who was acting as executor for Ralph Simon's recently created probate estate.

Carl asserts that, independent of the ownership issue, the purported security interest in the cattle allegedly conveyed by Ralph to Plaintiffs on October 26, 1993 is void because it was obtained in breach of the confidential, attorney-client relationship between Plaintiffs and Ralph. It is undisputed that the security interest was given in connection with an amendment of the retainer agreement between Plaintiffs and Ralph which was entered into after the attorney-client relationship had been established. The retainer agreement was modified, according to Plaintiffs, during the trial because of tremendous expenses incurred for experts and Ralph's failure to make payments toward advances made by his counsel.

OWNERSHIP OF THE CATTLE

The first issue for the Court's determination is ownership of the cattle at the time of the execution of the security agreement in question as well as ownership at the time of the filing of the present Chapter 11 petition. In making this determination, the Court must evaluate the entire record including the testimony of Carl. Carl presents the Court with

the disturbing proposition that it must evaluate Carl's sworn testimony from two separate trials where Carl testified under oath about the ownership of these cattle in a conflicting and completely irreconcilable manner. In making determinations of credibility, the Court can assess credibility based on the demeanor of the witness, the content of the testimony, and the Court's own experience with the way people act. In re Carrigan, 109 B.R. 167, 170 (Bankr. W.D.N.C. 1989). Evaluating Carl's alternative versions of the truth, the Court finds that his original testimony, in the Tri-Vets' deposition as well as the Tri-Vets trial is the most compelling. The testimony provided in the previous litigation is more compelling to this Court because Carl had no direct financial interest, at that time, in having the jury find, as he then testified, that the cattle did not belong to him. In fact, if he had a possessory interest in the cattle, his testimony would have been against his pecuniary interest.

Carl now asserts that Plaintiffs directed him to present false testimony in the original trial as ownership was at issue and if Ralph were determined not to have an ownership interest in the cattle, judgment would immediately enter against Ralph. The statute of limitations had expired and no second lawsuit could follow. The Court had the opportunity to evaluate this entire evidentiary record. The Court has also had the opportunity to assess the credibility of the various witnesses. There is absolutely no evidence in this record to convince this Court that Plaintiffs induced Carl to give perjured testimony in the Tri-Vets trial. The Court concludes, to the contrary, that Carl was accurately stating the facts as they existed at that time.

Secondly, the evidence reflects no written documentation to support the claims made by Carl that he had ownership of the cattle at the time of the execution of the security agreement. Ralph clearly understood that execution of a Bill of Sale is necessary to perpetuate a sales transaction. The fact that no written Bill of Sale exists at or about the time when Carl claims ownership was transferred and the fact that a Bill of Sale was executed on December 30, 1993, after execution of the security interest, is extremely instructive on the issue of ownership.

In the final analysis, this Court concludes that, based upon the impeachment of Carl's present testimony by his prior contradictory testimony in the Tri-Vets case, Carl's present testimony is nonpersuasive. The Court ultimately concludes that Carl now has a direct financial interest in the issue of ownership of these cattle. His claims are based on allegations completely unsupported by documentary evidence. The Court finds Carl's credibility to be suspect and, therefore, must conclude that the ownership interest on October 26, 1993 belonged solely to Ralph Simon.

The Court must also determine, however, whether the cattle herd belonged to Ralph Simon at the time of the filing of the bankruptcy petition. On December 30, 1993, Ralph met with Tri-State representative, Curtis Pint, and requested that Pint draw up a Bill of Sale transferring ownership of the 300 head of cattle to Carl. At that time, Pint informed Ralph that the Bill of Sale was not necessary for purposes of a Tri-State loan. However, Ralph was adamant about executing this Bill of Sale in favor of Carl. Pint did, in fact, draft the document that day, Ralph signed it, and Pint placed the document in an office file. Pint was also Carl's banker at Tri-State and the executed Bill of Sale was placed in the office file under Carl Simon's name.

The issue for the Court's determination is whether this executed Bill of Sale effectively transferred title to the cattle to Carl. It is clear that the Bill of Sale was either a transfer for consideration or an inter vivos gift. It is the conclusion of this Court that the transfer is valid under either theory. In that regard, it is noted that no party has challenged the validity of this Bill of Sale. Absent a challenge to the sale or whether it was a sale for valid consideration, the Court concludes that the same is properly considered to be a transfer for valid consideration even if the Court does not know or cannot determine the extent or nature of that consideration.

Secondly, even if the Bill of Sale were not considered to be an arms length sale, the same can constitute an inter vivos gift of the cattle from Ralph to Carl effective December 30, 1993. Even though delivery of the Bill of Sale was not made to Carl, the donee, during the life of Ralph, it is well settled that for the purposes of an inter vivos gift, delivery may be made to a third party as agent or trustee of the donee. In re Fenton's Estate, 165 N.S. 463, 465 (Iowa 1917). It is the conclusion of this Court that the execution and delivery of the Bill of Sale to Pint was done in such a way and under such circumstances as to indicate that Ralph Simon relinquished control over the cattle and intended to vest title in Carl at that time, thus making the transaction a valid delivery of an inter vivos gift.

The existence of the intent of Ralph Simon to make a transfer and further to make it effective on December 30, 1993 is

evidenced by the subsequent transfer of the Wapsie Valley Creamery milk check into Carl's name. This transfer was done at the request of Robert Simon, the executor of Ralph's estate, shortly after Ralph's death. The change was made retroactive to January 1, 1994, the day following the transfer of ownership of the cattle. Had Carl not had title to the cattle herd as of January 1, Robert Simon would have had no legal obligation to transfer the milk check into Carl's name. In fact, Robert, as executor of Ralph's estate, would have been under a legal obligation to retain such income for the benefit of the estate. Iowa Code sec. 633.175 and sec. 633.160 (1995).

In summary, it is the conclusion of this Court, for the reasons set forth herein, that on October 26, 1993, the date of creation of the security agreement between Ralph Simon and the Plaintiffs, ownership of the cattle in question resided in Ralph Simon and not Carl Simon. Subsequent to that time, however, on December 30, 1993, Ralph Simon effectively transferred title to Carl Simon by means of the Bill of Sale executed by Ralph Simon in favor of Carl Simon. As such, on the date of the filing of the petition in this case, the ownership of the cattle resided with Carl Simon as an asset of this estate.

ATTACHMENT OF THE SECURITY INTEREST TO THE CATTLE

Under applicable Iowa law, a security interest attaches to the collateral securing a debtor's repayment of a debt obligation and becomes enforceable against the debtor when (1) the debtor signs a security agreement which contains a description of the collateral; (2) value is given by the secured party to the debtor; and (3) the debtor has rights in the collateral. Iowa Code sec. 554.9203(1)(a)-(c)(1995).

There is no dispute that Ralph signed a security agreement with Plaintiffs on October 26, 1993 which described the collateral subject to the security interest as all of the debtor's farm products now owed or hereafter acquired, as well as specifically, 300 Holstein cows together with the proceeds, products, increase, replacements and substitutes of, to and from the cows.

A person gives "value" to a debtor if he accepts a security agreement as security for repayment of a pre-existing claim or obligation. Iowa Code sec. 554.1201(44)(b). The security agreement of October 26, 1993 was accepted by Plaintiffs as security for the repayment of the promissory note which Ralph executed contemporaneously with the security agreement. The promissory note represented an existing debt which Ralph owed to Plaintiffs for repayment of expenses incurred by Plaintiffs in representing Ralph in the Tri-Vets matter. Therefore, Plaintiffs gave Ralph the requisite value.

The ultimate issue in this case is whether Ralph had sufficient interest in the collateral on October 26, 1993, for the Plaintiffs' security interest to attach. While total legal ownership is not required to have "sufficient rights in the collateral" under 554.902(1)(c), the Court's factual finding that Ralph was the owner of the Herd on the date in question, forecloses the necessity for any further analysis of this issue. Ralph, as owner of the Herd on the date in question had the requisite rights in the collateral for the security interest to attach. Swets Motor Sales v. Pruisner, 236 N.W.2d 299 (Iowa 1975).

VALIDITY OF SECURITY AGREEMENT/AMENDED RETAINER AGREEMENT

Carl asserts that, even if Ralph was the owner of the cattle when the security interest was given, the security interest is ineffective because it was entered into as part of an amendment to a retainer agreement between Ralph and Plaintiffs which was clearly made after the attorney-client relationship had been established. Carl asserts that Ralph was pressured into signing the amended agreement as well as the promissory note and security agreement which were executed contemporaneously with the amended agreement.

When a contract for compensation is entered into between an attorney and a client after the attorney-client relationship is established, there is a presumption of unfairness or invalidity which attaches to the contract. The burden is then on the attorney to show that it was fairly and openly entered into, that is, that the client was informed concerning the contract and understood its effect. Lawrence v. Tschirgi, 57 N.W.2d 46, 48 (Iowa 1953). The court in Tschirgi found that an attorney, seeking to obtain a judgment against a client based upon an unusual contingency fee agreement entered into after the attorney-client relationship had been established, had not sustained his burden of showing that the client had been fully informed concerning the agreement and understood its effect. Id. at 50-53. As a result the court reversed the

lower court's judgment in favor of the attorney. Id. at 53.

The Court finds this attack on the validity of the security interest unpersuasive for several reasons. The law in Iowa states that: "... a privity of contract must exist between the parties to an action upon a contract. One whom the law regards as a stranger to the contract cannot maintain an action thereon." Olney v. Hutt, 105 N.W.2d 515, 519 (Iowa 1960)(quoting, Davis v. Clinton Water Works Co., 6 N.W. 126, 127 (Iowa 1880)). The Court finds that Carl was not in privity to the agreement and as such may not maintain a challenge its validity. The court notes that Robert Simon, executor of the Estate of Ralph Simon, did raise this issue in his answer to Plaintiff's complaint, however, Ralph's estate made no direct assertion of this issue at trial and counsel for Ralph's estate did not actively participate in the proceeding. While Carl made an attempt to assert this defense at the proceeding, a party may not raise the rights or interests of a third party unless, there is some hindrance to the third party's ability to protect his own interests. United States v. De Gross, 960 F.2d 1433, 1437 (9th Cir. 1992). There is no showing that there is any hindrance to the Estate of Ralph Simon to assert this claim regarding the validity of Plaintiffs' security agreement.

Even if the Court feels the foregoing may constitute an overly technical interpretation of standing, Defendant cannot prevail on the merits. Plaintiffs offered testimony that plaintiff Barry Hammerback had advised Ralph that amending the retainer agreement created a conflict of interest for Plaintiffs and it would be appropriate for him to seek independent legal counsel to review the agreement. It is clear Ralph understood secured financing as well as the effect of granting a security interest in his personal property. He previously granted a security interest in the very same Herd to Tri-State. In the absence of any evidence to rebut Plaintiffs' testimony that Ralph had been informed about the effect of the security agreement and advised to seek independent legal advise, the Court finds that Plaintiffs have sustained their burden regarding the showing that the amended retainer agreement, security agreement and promissory note were entered into fairly and openly.

Finally, even assuming it could be shown that the October 26, 1993 transaction between Plaintiffs and Carl is susceptible to invalidation under Tschirgi, such a conclusion would not aid Defendant in this case. The only part of the transaction which would be subject to invalidation is the increase in the contingency fee percentage payable to Plaintiffs had Ralph received any damage award in the Tri-Vets case. That is the only part of the transaction in which Ralph would be potentially economically disadvantaged. Ralph was not economically disadvantaged by the granting of the security interest in the cattle. It merely served to secure repayment of his obligation to reimburse Plaintiffs for expenses which they had expended on Ralph's behalf in prosecuting the Tri-Vets case. The obligation to reimburse the Plaintiffs for these expenses was neither altered nor increased under the amended retainer agreement. Therefore, the granting of the security interest, standing on its own, would not be invalidated even if given contemporaneously with an invalid adjustment to the contingency fee percentage.

SUMMARY

The security interest which Ralph conveyed to Plaintiffs under the security agreement executed by the parties on October 26, 1993 is valid and attached to the cattle as collateral as of that date, subject to Tri-States' prior security interest. Ownership of the cattle was subsequently transferred to Carl who took ownership subject to both Tri-State's and Plaintiffs' perfected security interests. Thus, the cattle herd is property of Carl Simon's bankruptcy estate, subject to the foregoing perfect security interests.

ORDER

WHEREFORE, Plaintiffs' hold a valid security interest in the cattle, subject to the prior and paramount lien of Tri-State.

FURTHER, the cattle are presently the property of Carl Simon's bankruptcy estate and are subject to both the Tri-State security interest and Plaintiffs' security interest.

FURTHER, Plaintiffs' request for an order directing that the milk proceeds realized from the cattle be paid over to and become property of the estate of Ralph J. Simon subject to the lien of Plaintiffs is denied.

SO ORDERED this 26th day of September, 1995.

Paul J. Kilburg
U.S. Bankruptcy Judge