

In the United States Bankruptcy Court

for the Northern District of Iowa

CLIFFORD HOLTHAUS, LOIS HOLTHAUS
Debtors.

Bankruptcy No. 96-61345KW
Chapter 7

ORDER RE OBJECTION TO EXEMPTION

On October 16, 1996, the above-captioned matter came on for hearing pursuant to assignment on an objection to exemption filed by Creditor Citizens State Bank. Debtors appeared in person with Attorney Michael Dunbar. Citizens State Bank appeared by a representative of the Bank and its attorney, John Heckel. Evidence was presented after which the Court took the matter under advisement. This is a core proceeding pursuant to 28 U.S.C. 157(b)(2)(B, K).

STATEMENT OF THE CASE

Debtors were farmers residing near Postville, Iowa. They terminated their farming operation in the fall and winter of 1996. Much of the farm machinery was sold at auction. However, a limited amount of machinery was retained by Debtors to help feed and care for stock cattle which were subsequently sold. After the cattle were sold, Debtors filed this Chapter 7 bankruptcy petition and now claim the items of machinery remaining as exempt property. In addition to the farm machinery, 1500 bushels of corn are listed as exempt. The Bank asserts that the only reason the machinery was not sold at auction was because of a specific arrangement with Debtors that they would be allowed to keep the machinery to provide for the cattle but that upon completion of the sale of the livestock, the machinery would be sold.

Debtors state that they intend to go back into farming. The Bank asserts that Debtors did not intend to go back into the farming operation and this is a recent claim by them. If the Court determines that Mr. Holthaus is a farmer, the Bank stipulates that it is not contesting that Mrs. Holthaus is engaged in farming as a farm wife. The sole issue, therefore, is whether Debtors are farmers who legitimately intend to return to farming in the immediate future.

FINDINGS OF FACT

Mr. Holthaus began farming in 1970 with his father. He is 41 years of age and has a high school education. He married Lois Holthaus in 1975. The Holthaus's have children who are actively engaged in the farming operation and are involved in 4-H. Debtors continued to live on this farm working with Mr. Holthaus's father until 1992 when he took over the farming operation and his father moved to town.

In 1992, Debtors purchased the farm with Citizens State Bank as the lender. Debtors had been using Citizens State Bank as their primary lender since 1982. At the time they commenced dealing with Citizens State Bank, they were still farming with Mr. Holthaus' father in a 50-50 operation. In addition to the farm which they purchased, they also leased two additional farms.

Financial problems began in 1993 with the floods and poor crops. In 1994, there was an acceptable yield on the grain crops though the quality was poor. Much of Debtors' farming operation involved cattle and hog feeding. In 1995, cattle and hog prices were low and did not generate sufficient cash to continue the operation. By late fall of 1995, Debtors prepared the ground for the 1996 crop year. The Bank however did not feel that the operation was providing sufficient cash flow and it would not approve crop financing for 1996. At that time, there were no options remaining for Debtors. Mediation occurred and a mediation release was obtained.

The Bank suggested liquidation and Debtors consented to allow a liquidation of the livestock and most of the machinery. Debtors hoped that a liquidation sale would pay off most of the debt. With the exception of the remaining items which are the subject of this hearing, Debtors sold all of their farm machinery and associated assets. They received approximately \$85,000 through the liquidation sale but had hoped for a larger return. They had estimated revenues of between \$125,000 and \$130,000 at the sale. The farm was also sold and did generate what Debtors considered to be a good sale price for the land. The cattle were sold for \$92,000. Mr. Steve Werner from Citizens State Bank testified that this was a "blood bath" and that the cattle should have brought substantially more.

All machinery except the six items which are now claimed as exempt were sold. Mr. Werner of Citizens State Bank testified that the Bank allowed these items to be kept by Debtors to provide for the remaining cattle. He testified that the Bank consented to these items being reserved by Debtors until the remaining cattle were sold at which time it was anticipated that the remaining items listed now as exempt would also be sold and applied toward the Bank's debt. It is undisputed that a substantial amount of equipment, appliances and associated tools were sold and applied toward the debt. Mr. Werner testified that at the time of these transactions, there was no discussion with Debtors indicating that Debtors would retain these items after the sale of the cattle or that they would want to keep them to commence a new farming operation.

The remaining cattle were liquidated in June of 1996, after the Chapter 7 bankruptcy had been filed. The Chapter 7 Trustee approved the sale of these cattle. Mr. Werner testified that the remaining equipment was sufficient for taking care of the remaining cattle on a short-term basis but is not adequate for setting up or maintaining a cattle operation or tilling the ground. He testified that if the cattle had already been sold, the items which are now claimed as exempt would have been sold along with the other machinery. He testified that, at the present time, there is no feasible manner in which Debtors could return to a farming operation because financing is not available and Debtors' previous landlord was not paid prior rent. He testified that all indications were that Debtors were quitting farming and they intended to make their living with off farm work and it was on this basis that the liquidation occurred.

Debtors testify that they consented to liquidate in an attempt to pay off all creditors though the depressed cattle prices and the limited revenue generated by the sale prevented this from happening. Mr. Holthaus testified that at the time of the sale and subsequently he did not know what the future held though they tried to remain optimistic. Mr. Holthaus testified that he has entered into a lease for 90 acres of farm ground with which he intends to get back into the farming operation. He would like to get back into the cattle operation initially on a limited basis and would raise sufficient crops to feed the cattle. He testified that he would hope to get money from the Bank for a small time livestock operation initially. If financing is unavailable, he could borrow equipment from his father-in-law and brother-in-law who live in the area. Debtor testified that the leased ground has livestock facilities and small buildings. Debtors did indicate that they have an interest in returning to farming, that their children continue to be interested in the farming operation and are involved with 4-H. He stated they would like to get back into farming operation immediately with this leased ground.

MEMORANDUM OF LAW

Under Iowa Code sec. 627.10, an Iowa debtor may only claim state law exemptions. In re Myers, 56 B.R. 423, 425 (Bankr. S.D. Iowa 1985); In re Smith, No. 96-20243KD, slip op. at 3 (Bankr. N.D. Iowa May 7, 1996). State law dictates the availability and scope of exemptions. In re Thompson, 884 F.2d 1100, 1102 (8th Cir. 1989). The debtor has the burden of proof to show that the debtor is engaged in farming. In re Indvik, 118 B.R. 993, 1007 (Bankr. N.D. Iowa 1990).

Each debtor "engaged in farming" may claim as exempt from execution implements and equipment, as well as livestock and feed for the livestock reasonably related to a normal farming operation not to exceed in aggregate a value of

\$10,000.00. Iowa Code sec. 627.6(11)(a), (b). "Engaged in farming" is construed to require the debtor to be engaged in farming at the time the debtor files for bankruptcy, or to intend to return to farming after a temporary cessation of farming operations. Myers, 56 B.R. at 426. If the debtors were not engaged in farming at the time they filed bankruptcy, the essential factor to determine exemptibility of farm equipment is the intention of the debtors to resume their farming operations. In re Ackerman, No. 94-21846KD, slip op. at 5 (Bankr. N.D. Iowa Apr. 12, 1995) (considering intent to continue masonry business); Indvik, 118 B.R. at 1008 (explaining that debtor's intent to return to farming, when credible, allows the court to avoid liens impairing debtor's interest in exempt tools of the farming trade). In Iowa, courts give great weight to the stated intentions of debtors regarding their return to farming. Myers, 56 B.R. at 426.

To determine if debtors are entitled to claim property as exempt because they are engaged in farming, a court may look to several factors. One factor to consider is the intensity of the debtors' past farming activities. In re LaFond, 791 F.2d 623, 626 (8th Cir. 1986). Another factor to be considered is the sincerity of the debtors' intentions to continue farming. Id. A court should also consider whether the items claimed as exempt are regularly used in legitimate farming activities. Id. The reasonable prospects for returning to farming, evidenced by the amount of time since debtors engaged in farming and any other circumstances effecting the debtors' return to farming, should also be examined. In re Richardson, 47 B.R. 113, 119 (Bankr. W.D. Wis. 1985); In re Kleve, No. 95-50141XS, slip op. at 5 (Bankr. N.D. Iowa Oct. 24, 1995). Present uncertainty of the debtors' financial ability to return to farming does not prevent a court from finding that the debtors intend to engage in farming. Smith, slip op. at 4. Even when it is unclear if debtors will be able to resume farm activities or if debtors will have funds to resume farming operations, the Court may find that debtors have the intent to return to farming operations. See Id.

Iowa's exemption statute is construed liberally in favor of debtors. Allison-Bristow Comm. School Dist. v. Iowa Civil Rights Comm'n, 461 N.W.2d 456, 458 (Iowa 1990); In re Eby, 76 B.R. 140, 141 (Bankr. S.D. Iowa 1987) (construing Iowa Code sec. 627.6(11)(a)). A liberal construction gives a court some latitude in making the determination as to whether Debtors' desire and intent to continue farming are credible. Smith, slip op. at 4. Obtaining off-farm jobs does not necessarily preclude the debtors from claiming an exemption for farm equipment. Id.; In re Fink, No. 95-51926XS, slip op. at 5 (Bankr. N.D. Iowa Feb. 8, 1996).

To determine whether a tool or implement is exempt to a farmer, the court must inquire if the items claimed as exempt are the "proper implements in the reasonable conduct of the debtor's trade or profession." Indvik, 118 B.R. at 1005. In order for an item to qualify as an implement, it must be reasonably fitted or employed as a means of making labor more effective. In re Eby, 76 B.R. at 141. In an analogous case, this Court decided that brick and block do not constitute tools of the trade of a masonry company. In re Ackerman, No. 94-21846KD, slip op. at 7 (Bankr. N.D. Iowa April 12, 1995). After looking to general industry standards, this Court concluded that items which may be categorized as general inventory are not exempt tools of the trade. Id. General inventory as defined under Iowa Code sec. 554.9109(4) includes goods held by a person for sale or lease or to be furnished under contracts of service, or raw materials, or materials used or consumed in a business. Id. Items used only once constitute inventory and not tools of the trade. Id.

Iowa Code sec. 627.6(11)(b) allows a debtor to claim livestock and feed for the livestock reasonably related to a normal farming operation as exempt, subject to the limitation that the aggregate amount of this claimed exemption and the exemption for implements and equipment of the farmer not exceed \$10,000.00. In seeking lien avoidance under 522(f)(2)(A), the debtor may avoid liens on livestock and feed for that livestock only if it is to be held for personal, family or household use. In re Simmons, 86 B.R. 160, 163 (Bankr. S.D. Iowa 1988).

Debtors' stated intention to return to farming must be given great weight by this Court. Myers, 56 B.R. at 426. Debtors have shown intensity in their past farming operations, evidenced by over 20 years of farming activities. They have demonstrated the sincerity of their intentions to continue farming by executing a lease for 90 acres to begin their farming operations again next year. The items which Debtors claim are exempt, are regularly used in legitimate farming activities. The reasonable prospect of Debtors returning to farming is evidenced by the short time period between their cessation of farming activities due to bankruptcy and obtaining a lease to begin farming next year. Present uncertainty of

Debtors' financial capability to return to farming does not dissuade this Court from finding that Debtors intend to engage in farming. Smith, slip op. at 4. Construing Iowa's exemption statute liberally, the Court finds that Debtors intend to engage in farming in the future and may claim exemptions under Iowa Code sec. 627.6(11).

The corn claimed exempt by Debtors is not exempt under sec. 627.6(11)(a). Only implements and equipment are exempt under 627.6(11)(a). As in In re Ackerman, the corn constituted inventory and may not be claimed exempt as a tool of the trade, because it is only used once and will be consumed in the business. The corn is not exempt under sec. 627.6(11)(b), because Debtors no longer have livestock to feed. Debtors would not be able to avoid the lien on the corn because 1500 Bu. corn would not be used for personal, family or household use.

Debtors designated corn and farming equipment valued at \$21,375.00 as exempt on their schedules. Iowa Code sec. 627.6(11) limits the exemption to \$10,000.00 each for implements and equipment. Both parties stipulate that if Debtor Clifford Holthaus may claim exemptions as a farmer, Debtor Lois Holthaus may do so also. As the 1500 Bu. corn is not exempt, Debtors may claim the rest of the disputed implements and equipment totaling \$14,950.00 as exempt.

WHEREFORE, Debtors' Motion to Avoid Lien is GRANTED as to the following items:

- a. 642 Bobcat unloader;
- b. 751 New Holland manure spreader;
- c. 856 International tractor;
- d. Two bale spears.

FURTHER, Debtors' Motion to Avoid Lien is DENIED and the objection by Citizen's State Bank is SUSTAINED as to the 1,500 bushels of corn.

SO ORDERED this 4th day of November, 1996.

Paul J. Kilburg
U.S. Bankruptcy Judge