

In the United States Bankruptcy Court

for the Northern District of Iowa

JEFF JAMES NEHL, AMY LYNN NEHL
Debtors

Bankruptcy No. 97-60192-W
Chapter 7

ORDER RE: OBJECTION TO HOMESTEAD EXEMPTION

The matter before the court is Chapter 7 Trustee's Objection to Debtors' Homestead Exemption. The parties have filed a Stipulation of Facts which set out the relevant undisputed facts. They agree that the court may rule on the exemption issue on the basis of the stipulated facts and written arguments. This is a core proceeding pursuant to 28 U.S.C. 157(b)(2)(B).

STATEMENT OF THE CASE

Trustee's objection to Debtors' homestead exemption arises out of the claim of Community Wholesale Company ("Community"). Community provided work and materials which improved Debtors' personal residence pre-petition. Debtors now declare the property which was improved under this home improvement contract exempt as their homestead. Trustee asserts the homestead is not exempt to the extent of the home improvement debt.

Debtors allege Trustee has no authority to assume the position of Community as to any claim against the property as Community has made no filing in connection with this matter. Debtors also state Trustee has no authority to take and sell the property in question to pay Community or other creditors.

FINDINGS OF FACT

The parties stipulate to the facts. Debtors filed jointly for bankruptcy on January 28, 1997. They own the real estate described in the petition as their primary residence. Debtors incurred a debt to Community for improvements to this property. An improvement contract was signed between Debtors and Community and the work was completed prior to filing for bankruptcy. As of the date of filing the bankruptcy petition, the debt owed was \$8,278.00 which is the amount of the asserted homestead exemption to which Trustee has objected. Community did not record the improvement contract, did not file a mechanic's lien, and did not file a proof of claim. Trustee alone filed the Objection to Homestead Exemption.

TRUSTEE'S STANDING TO OBJECT

Debtors initially assert that Trustee has no authority to object to Debtors' homestead exemption claim. Rule 4003(b) provides that an objection to a claim of exemption may be timely filed by the trustee or any creditor. In objecting to exemptions, a trustee acts as the "representative of the estate" under 323,

with the capacity to sue and be sued. First Nat'l Bank v. Norris, 701 F.2d 902, 904 (11th Cir. 1983). As representative of the estate, a trustee has a definite interest in whether property of the estate is exempt and a duty to collect property of the estate. Id. (holding trustee was properly "party in interest" to file objections to exemptions). "A trustee's authority to object to exemptions listed on a debtor's schedules is clear under the Bankruptcy Code, and is integral to every trustee's official duty to marshal and liquidate property of a bankruptcy estate." In re Atlas, 183 B.R. 978, 980 (Bankr. S.D. Fla. 1995). In In re Van Rye, 179 B.R. 375, 378 (Bankr. D. Mass. 1995), aff'd 96 F.3d 1430 (1st Cir. 1996), the court followed Norris to find the trustee had standing to object to the claimed homestead exemption based on pre-homestead debt. 179 B.R. at 378.

The fact that Community filed no claim and did not object to the homestead exemption does not preclude Trustee from exercising his independent statutory authority or performing his duties as trustee. The Court concludes that Trustee has standing to object to the homestead exemption based on the debt owed to Community.

HOMESTEAD EXEMPTION

Iowa Code sec. 561.16 (homestead exemption) provides:

The homestead of every person is exempt from judicial sale where there is no special declaration of statute to the contrary....

Iowa Code sec. 561.21(3) reads as follows:

561.21 Debts for which homestead liable. The homestead may be sold to satisfy debts of each of the following classes:

....

3. Those incurred for work done or material furnished exclusively for the improvement of the homestead.

The first issue is whether Debtors' homestead is vulnerable to the claim of a contractor for improvements to the homestead. Iowa Code sec. 561.21 allows for the sale of otherwise exempt homestead property to satisfy certain specific classes of debt. Debts incurred for "work done or material furnished exclusively for the improvement of the homestead" are specifically indicated in Iowa Code sec. 561.21(3) as debts for which the homestead is liable. This is precisely the class of debt created by the work performed by Community. This debt makes the homestead vulnerable to Trustee's claim. This court held in In re Streeper, 158 B.R. 783, 788 (Bankr. N.D. Iowa 1993), that a homestead subject to a lien under Iowa Code sec. 561.21(3) would not be held exempt. Iowa code sec. 561.21(3) clearly provides the authority to exclude otherwise exempt homestead property from exempt status.

MECHANIC'S LIEN

Debtors' resistance suggests that Community was required to file a mechanic's lien to make its claim enforceable against the homestead. Even after the time for obtaining a mechanic's lien has run, a creditor may enforce a judgment against the homestead for home improvement costs. Moffitt v. Denniston & Partridge Co., 294 N.W. 731, 734 (Iowa, 1940). This Court concludes that, as

Community could have pursued a judgment against Debtors prior to filing which would be enforceable against Debtors' homestead under Iowa Code sec. 561.21(3), the Trustee, acting in the place of Community, has the authority to pursue this remedy.

EXTENT OF INVASION OF HOMESTEAD EXEMPTION

Trustee has objected only to the extent of the debt due to the home improvement creditor, Community. The question is presented whether the homestead, having been found non-exempt to some extent, is therefore fully liable to the claims of other creditors. Iowa Code sec. 561.21(3) is specific in its reference to work or material furnished exclusively for improvement of the homestead. The statute supports satisfaction of debts only to the specified classes of creditors detailed under Iowa Code sec. 561.21. See In re Thompson, No. 95-32455XF, slip op. at 6 (Bankr. N.D. Iowa July 29, 1996) (holding trustee may reach homestead only to the extent of pre-acquisition debt). The court in In re Schuldt, 91 B.R. 501 (Bankr. S.D. Iowa, 1988) held that a homestead was liable, and therefore not exempt, only "to the extent" of pre-acquisition debts. Pre-acquisition debts are covered under Iowa Code sec. 561.21(1), just as home improvement debts are covered under Iowa Code sec. 561.21(3). The invasion of the homestead exemption in this case is, therefore, limited to the amount of the debt for the home improvement.

DISTRIBUTION OF PROCEEDS

The Trustee's Objection does not discuss how proceeds of the execution against the non-exempt portion of the homestead should be distributed. The home improvement creditor, Community, is responsible for its unsecured status. Community had the opportunity to file a mechanic's lien or obtain a judgment against Debtors prior to their bankruptcy petition. While it is the nature of the debt to Community which allows Trustee to recover against the homestead, Trustee represents all unsecured creditors. Discharge was issued on May 8, 1997.

A similar issue was discussed in In re Nehring, 84 B.R. 571 (Bankr. S.D. Iowa 1988), which involved pre-acquisition debt, another class of debt specifically identified under Iowa Code sec. 561.21 as one for which the homestead is liable. "[Creditor] did not reduce the antecedent debt to judgment before bankruptcy was filed....[D]ischarge will forever bar [creditor] from obtaining a judicial sale of the homestead. [Creditor] will, of course, share pro rata in any distribution to unsecured creditors." Id. at 577. The court goes on to provide that: "To allow one unsecured creditor to enhance its post discharge position over that of the other unsecured creditors would be inequitable and contrary to Congressional intent." Id. at 578.

A more recent case, In re Wrigley, 195 B.R. 915 (Bankr. E.D. Ark. 1996), emphasizes the divergent perspectives which control the collection and distribution of assets of the estate in bankruptcy. "Although the nature of a creditor's claim is determined under state law, Butner v. United States, 440 U.S. 48, 54-55 (1979), the Bankruptcy Code establishes the priorities claims receive when the trustee distributes the assets of the estate." Wrigley 195 B.R. at 915.

In In re Van Rye, 179 B.R. 375, 378 (Bankr. D. Mass. 1995), aff'd 96 F.3d 1430 (1st Cir. 1996), the court stated that proceeds recovered representing pre-homestead debt should be distributed ratably among both pre- and post-homestead creditors. "The pre-homestead creditors are not lien creditors; their claims would not survive a bankruptcy discharge but for the actions of the Trustee [in objecting to homestead exemption]." Id. at 379. The court concluded that the homestead equity representing the pre-homestead debt inures to the benefit of all creditors of the estate. Id.

The claim of Trustee against the homestead is initially triggered by the debt owed Community. However, once these proceeds are collected and made part of the estate they are distributable pro rata among all unsecured creditors, with Community's status equal to that of the other unsecured creditors.

WHEREFORE, Trustee has standing to object to Debtors' claim of homestead exemption.

FURTHER, Debtors' homestead is not exempt to the extent necessary to satisfy the home improvement debt.

FURTHER, the pursuit of the non-exempt homestead is not dependent on any pre-bankruptcy lien filed by Community Wholesale Company.

FURTHER, Trustee may sell the homestead to the extent necessary to satisfy the home improvement debt to Community Wholesale Company, in the amount of \$ 8,278.00.

FURTHER, the proceeds shall be distributed pro rata among all unsecured creditors.

FURTHER, judgment shall enter accordingly.

SO ORDERED this 4th day of June, 1997.

Paul J. Kilburg
U.S. Bankruptcy Judge