

UNITED STATES BANKRUPTCY COURT FOR THE NORTHERN DISTRICT OF IOWA

IN RE:

ROBERT EDWARD LITWILLER and Chapter 7 CAROLYN KAY LITWILLER,
Debtors.

Bankruptcy No. 01-3520F

ORDER RE: OBJECTIONS TO EXEMPTIONS

The trustee and creditors William and Kristi Wollesen, the William and Kristi Wollesen Revocable Trust, and Byrite Farm Supply Company (collectively the "Wollesens") have objected to the debtors' claims of exemptions in their homestead. Hearing was held May 15, 2002 in Fort Dodge. Larry S. Eide, Chapter 7 trustee, appeared for himself. Terry

L. Gibson appeared for the Wollesens. Jerrold Wanek represented debtors Robert Litwiller and Carolyn Litwiller. The Litwillers and the Wollesens have filed briefs. The trustee relies on the arguments made by the Wollesens. The court now issues its findings and conclusions pursuant to Fed.R.Bankr.P. 7052. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(B).

Findings of Fact

Robert and Carolyn Litwiller filed a joint voluntary Chapter 7 petition on October 16, 2001. They scheduled real estate valued at \$730,000, including a number of parcels of farm ground in Pocahontas County. The Litwillers claimed exempt as their homestead another parcel locally known as 349 Austin Street, Rockwell City, legally described as Lot Two (2), Block Two (2), Cotton's First Addition to Rockwell City, Calhoun County, Iowa.

At hearing on this matter, the parties stipulated to the following facts:

1. From approximately 1965 to October 12, 2000, the Litwillers lived on a parcel of a 450-acre farm in Pocahontas County, which said farm constituted their homestead. There is no evidence of any debt owed in this proceeding by the Litwillers that predated the acquisition of that homestead.

2. The 450-acre farm was subject to mortgages held by First Bank & Trust Company, Lohrville, Iowa (the "Bank"), to secure debt in the approximate amount of \$650,000.

3. On October 12, 2000, the Litwillers purchased a home located at 349 Austin Street, Rockwell City, Iowa, and acquired that residence through financing provided by the Bank, by virtue of an \$81,000 promissory note.

4. The \$81,000 note was secured by the mortgage on the Rockwell City home as well as two mortgages held by the Bank on the 450-acre farm or parcels thereof.

5. The only value or proceeds from the Litwillers' prior homestead on the 450-acre farm that Litwillers say were utilized by them in acquiring their new homestead in Rockwell City was the cross-collateralization or pledge of the farm mortgages as additional security for repayment of the \$81,000 note.

The court makes the following additional findings of fact. The farm was made up of three parcels of approximately 211 acres, 120 acres and 90 acres. The Litwillers' former homestead was located on the 211 acres. The Bank held two farm mortgages dated December 17, 1997 and February 27, 1998. The 1997 mortgage encumbered the 211 acres and another parcel. The 1998 mortgage secured the purchase of the third parcel and covered only that parcel.

Larry Irwin, a loan officer with the Bank, estimated the value of the entire farm at \$1.2 million. He believed the five-acre home site was worth between \$50,000 and \$75,000. He valued the remaining 35 acres of farm ground at \$2,500 to \$2,600 per acre. Using the lower figures, the court finds the value of the 40-acre farm homestead was approximately \$137,500.

The Bank loaned the purchase money for the new homestead with the understanding that the Litwillers would sell the farm. There was no written agreement that they would do so by a certain date. The \$81,000 loan was payable in a single payment of \$83,002.81 due on January 15, 2001. Irwin believed that the loan was for the full purchase price.

The Litwillers defaulted on the notes in early 2001; the Bank foreclosed on the farm. At the sheriff's sale, the Bank bid in approximately \$800,000, representing all the debt owing on the farm notes and the note on the Rockwell City house, including legal fees and interest.

Subordinate liens on the farm existing when the Bank began its foreclosure proceedings included a mortgage to Robert Litwiller's father and a judgment obtained by Pro Cooperative. The William and Kristi Wollesen Revocable Trust, as assignee of Pro Cooperative, filed a claim in the amount of \$223,167.58. There was no evidence showing what parcels were covered by Robert Litwiller's father's mortgage.

In their bankruptcy schedule of secured claims, the Litwillers listed claims totaling \$930,458.74 secured by real property. As of May 14, 2002, creditors had filed claims totaling \$1,255,296.94.

Discussion

The objectors have the burden of proving that the homestead exemption was improperly claimed. Fed.R.Bankr.P. 4003(c).

There is no dispute that Litwillers established a homestead on 40 acres of their farm and that none of their debts as of the date of filing their petition predate the acquisition of the right of homestead.

The Wollesens make two arguments. First, they argue that, in order for a new homestead to be a continuation of the old homestead, a debtor must either sell the old homestead and use proceeds to acquire the new homestead or directly exchange the old homestead for a new homestead. Because the Litwillers did neither, the Wollesens contend that all debts incurred prior to October 12, 2000 are pre-acquisition debts as to the Rockwell City homestead. The Wollesens argue alternatively that the extent of the Litwillers' homestead exemption is limited to the amount, if any, of net proceeds they would have received if they had voluntarily sold their farm homestead. Because both arguments are based on an erroneous reading of Iowa homestead law, the court will overrule the objections.

Iowa homestead law authorizes a homeowner to change homesteads. Iowa Code § 561.7. The effect of changing homesteads is that homestead rights are transferred to the new property.

Where there has been a change in the limits of the homestead, or a new homestead has been acquired with the proceeds of the old, the new homestead, to the extent in value of the old, is exempt from execution in all cases where the old or former one would have been.

Iowa Code § 561.20. "The new homestead is a continuance of the old and the exemption dates from the acquisition and occupancy as a home of the old."

American Savings Bank of

Marengo v. Willenbrock, 209 Iowa 250, 228 N.W. 295, 298

(1929). Thus, debts that are incurred after acquisition of an old homestead and prior to acquisition of a new homestead do not become pre-acquisition debts as to the new homestead. In

re Streeper, 158 B.R. 783, 788 (Bankr. N.D. Iowa 1993). The

extent to which the new homestead is exempt, as measured by the "value of the old," is determined without regard to encumbrances on the old homestead. Millsap v. Faulkes, 236

Iowa 848, 20 N.W.2d 40, 41 (1945); Willenbrock, 228 N.W. at

300.

The Wollesens contend that a change of homesteads pursuant to § 561.20 requires direct use of the old homestead to acquire the new. Iowa law is not so limited.

The owner may, from time to time, change the limits of the homestead by changing the metes and bounds, as well as the record of the plat and description, or vacate it.

Such changes shall not prejudice conveyances or liens made or created previously thereto.

No such change of the entire homestead, made without the concurrence of the other spouse, shall affect that spouse's rights, or those of the children.

Iowa Code § 561.7. Former § 2000, from which § 561.7 was derived, "authorized the owner to change the limits of the homestead, or to 'change it entirely.'" Blue v. Heilprin, 105

Iowa 608, 75 N.W. 642, 643 (1898). See also Furman v. Dewell,

35 Iowa 170, 171 (1872) (the owner may "change the homestead entirely," quoting former § 2288). The court in Blue v. Heilprin stated:

There are two ways in which plaintiffs could acquire a right of homestead in these premises, namely, by purchase, or by change of homestead. By purchase, as where the purchaser, having no other homestead, purchases and occupies as a homestead, or purchases with funds not derived from another homestead, and occupies as his homestead. By change of homestead, under section 2000, by changing the old for a new homestead, or purchasing the new with the proceeds of the old. The purpose of the law is to preserve to the family the home which it may have.

Blue v. Heilprin, 75 N.W. at 644 (emphasis added).

An owner need not have equity in the first homestead to preserve homestead rights in a new homestead; nor need there be any transfer of the old homestead, by proceeds or otherwise, into the new. In re Whyte, No. 96-31970XF (Bankr. N.D. Iowa Nov. 26, 1996) (citing Willenbrock).

In Furman v. Dewell, 35 Iowa 170 (1872), the debtor established a homestead in the town of Magnolia in 1865. In 1867, he purchased 35 acres of land. He eventually improved the land and built a house on it. In 1869, a creditor obtained judgment on a note. The lien attached to the 35 acres. In 1871, the debtor moved with his family to the house on the 35 acres and established a new homestead there. The court was unconcerned with the manner in which the debtor had acquired his new homestead. The change of homesteads was not to the prejudice of the prior lien. Although the new homestead became exempt when the debtor occupied it as such, the judgment lien then attached to the physical property of the old homestead, which the debtor still owned. Id. at 172. Moreover, the new homestead was of lesser value than the old homestead; the creditor's security was improved.

Similarly, Litwillers owned other real property in addition to their homestead. Judgment liens attached to the non-homestead property. When Litwillers changed homesteads, those liens attached to the property that had been the old homestead. Litwillers' change of homesteads allowed judgment liens to attach to additional property of a value exceeding that of the new homestead.

The Wollesens' alternative argument is that the Litwillers' homestead is

limited to the amount they would have received as net proceeds from voluntary sale of their farm homestead. The argument is without merit.

The extent of Litwillers' new homestead is limited by the "extent in value of the old" homestead, calculated without regard to encumbrances. American Savings v. Willenbrock, 228

N.W. at 300. The value of Litwillers' farm homestead was approximately \$137,500. The transfer to the Rockwell City homestead valued at approximately \$81,000 did not exceed that limitation. The case Millsap v. Faulkes, 20 N.W.2d 40 (Iowa 1945), cited by Wollesens, did not disturb the rule of Willenbrock. In Millsap v. Faulkes, the debtor had sold his homestead for \$8,450. He planned to pay off his mortgage and invest the balance of the proceeds in a new homestead valued at \$4,950. Creditor argued that proceeds above \$4,950 were liable for payment of his judgment, without regard to the mortgage. The court, unsurprisingly, ruled for the debtor. The case is not on point.

IT IS ORDERED that the objections to the debtors' claims of exemptions in their homestead filed by the trustee and creditors William and Kristi Wollesen, the William and Kristi Wollesen Revocable Trust, and Byrite Farm Supply Company are overruled.

SO ORDERED THIS 2nd DAY OF JULY 2002.

William L. Edmonds, Bankruptcy Judge