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Creditors' Corner

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MINNESOTA IRA EXEMPTION IS NOT LIMITED TO FUNDS CONTRIBUTED THROUGH EMPLOYMENT

The Minnesota Court of Appeals in *Russell's AmericInn LLC, v. Eagle General Contractors, LLC*, App. No. 09-0013, held that a judgment debtor's ability to exempt funds within an IRA is not conditioned on whether the funds in the IRA were contributed through debtor's employment.

In this case, a judgment creditor served a non-earnings garnishment on the custodian of debtor's traditional IRA and Roth IRA. Debtor argued the IRAs were exempt under Section 550.37, Subdivision 24 of the Minnesota Statutes as "a right to receive present or future payments, or payments received ... under a stock bonus, pension, profit sharing, annuity, individual retirement account, Roth IRA, individual retirement annuity, simplified employee pension, or similar plan or contract on account of illness, disability, death, age, or length of service."

The heading of Subdivision 24 classifies the exempt assets listed above as "Employee Benefits."

The evidence showed that the funds in the IRA were contributed personally by debtor and not through his employment. The judgment creditor therefore argued that the IRA funds were not employee benefits received by the debtor, and were not exempt under Subdivision 24.

The Court held that although the statutory heading classified the exempt assets as "employee benefits," the actual statutory language did not expressly require an employment source for the IRA funds. Therefore, Debtor could utilize the exemption.

JUNIOR MORTGAGEE REMAINS FULLY SECURED IN CHAPTER 13 REGARDLESS OF VALUE OF MORTGAGED RESIDENCE

The Bankruptcy Court for the District of Minnesota held in *In re Frame*, BKY No. 09-41010, that a second-position mortgage would be treated as a fully-secured claim in a Chapter 13 bankruptcy, despite the fact that the mortgaged residence had no value in excess of the first-position mortgage.

Typically, a lender's secured claim in a Chapter 13 is limited to the value of its collateral, and a debtor could confirm a repayment plan by paying only that amount. This changes when the collateral is the debtor's principal residence. Section 1322(b)(2) of the Bankruptcy Code provides that a Chapter 13 plan may "modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence."

Nonetheless, Debtor argued that the second-position mortgagee did not have a claim secured by a security interest in the property since the property had no value beyond the amount of the first mortgage. The Court rejected this argument and held that prior decisions have interpreted that the statute does not permit modification to the secured creditor's rights, regardless of any amount of negative equity that the debtor could show in the property.

MERS COMPLIES WITH FORECLOSURE BY ADVERTISEMENT STATUTE

The Minnesota Supreme Court in *Jackson v. MERS*, App. No. 08-397, denied a challenge to the legality of the Mortgage Electronic Registration System under Minnesota's foreclosure by advertisement statute, which is found in Section 580 of the Minnesota Statutes. Specifically, four parties facing foreclosure by advertisement challenged the legality of MERS as the foreclosing party.

MERS is typically identified on the mortgage as the nominal mortgagee. A lender which is a member of MERS will then assign the underlying indebtedness to other parties, but the assignments are not recorded in the public land records, and only appear on MERS. Section 580.02 of the Minnesota Statutes requires public recording of all assignments of the mortgage before a party can commence a foreclosure by advertisement. Plaintiffs argued that the MERS system violates this statute by not recording the assignments of the indebtedness.

The Court rejected Plaintiffs' challenge. MERS complies with Section 580.02 because lenders using MERS name MERS as the mortgagee in the mortgage and grant MERS the power of sale. Lenders using MERS typically only assign the indebtedness, not the actual security instruments. As a result, there was no assignment of the mortgage to record. Minnesota law has long-recognized that the title to the indebtedness and the title to the security instrument do not need to be held by same person. But if that is the arrangement, only the party with title to the security instrument has the power to foreclose, which in this case would be MERS.

DEBTOR WITH 910-DAY LOAN CANNOT BIFURCATE FROM LENDER'S SECURED CLAIM THE AMOUNT OF THE LOAN ATTRIBUTABLE TO SATISFYING A PREVIOUS LOAN ON TRADE-IN VEHICLE

In *In re Mierkowski*, App. No. 08-3866, the Eighth Circuit Court of Appeals affirmed that a Chapter 13 debtor cannot carve-out from a secured claim the amount of a motor vehicle loan that satisfied a prior loan on debtor's trade-in vehicle.

This is another case interpreting the "hanging paragraph" provision found in Section 1325(a) of the Bankruptcy Code. The effect of that provision has been interpreted to prohibit claim bifurcation in a Chapter 13 where the creditor has a purchase-money security interest securing a debt that was incurred to purchase a motor vehicle for personal use within 910 days prior to the bankruptcy. Without the hanging paragraph, a debtor could confirm a Chapter 13 plan by only paying an auto lender's secured claim, which would be the value of the vehicle and would be typically less than the amount of the full debt. The remaining unsecured claim could receive only minimal payment.

In this case, the dealer sold a vehicle to debtor for roughly \$22,000. The dealer accepted a trade-in valued at roughly \$13,000, but the trade-in had a prior unpaid loan of \$21,000. The auto lender paid the negative equity on the trade-in, roughly \$8,000, which was then added to debtor's new loan.

Debtor filed for Chapter 13 bankruptcy within the 910-day period. Debtor argued that even if it is a 910-day loan, the portion of the loan that was used to satisfy the negative equity did not qualify as "purchase money" and therefore could still be bifurcated from the lender's secured claim, notwithstanding the hanging paragraph, because the lender's purchase money security interest did not attach to that amount.

Under the UCC, a purchase money security interest attaches only to those items that are "part of the price" for purchase of a good. Commentary to the UCC lists the following items as part of purchase-money obligations, "sales taxes, duties, finance charges, interest, freight charges, costs of storage in transit, demurrage, administrative charges, expenses of collection, attorneys' fees, and other similar charges." Debtor argued that since this list did not include "negative equity financing" or a similar concept, a lien purporting to secure financing to discharge negative equity did not constitute a purchase money security interest.

The Court rejected this argument held that negative equity financing was "part of the price" of the vehicle under the "other similar charges" provision of the definition, and therefore debtor could not bifurcate the portion of debt representing negative equity financing from the secured claim. The creditor would retain a secured claim in the full amount of the debt.

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