

# Lien Avoidance: What You Need to Know



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## Lien Avoidance

Operative Statute,  
Rules, and General  
Orders

- ❖ § 522(f)
- ❖ Federal Rule 4003(d)
- ❖ Federal Rules 9014 and 7004
- ❖ BLR 6008
- ❖ General Order 21-2017

- Lien avoidance protects an individual debtor's right to exempt property.
- A debtor can avoid judicial liens and non-possessory, non-purchase money security interests in household goods ("NPMSIs") to the extent that the lien or NPMSI "impairs" the debtor's exemption in the property.
- Impairment of an exemption essentially means that, after accounting for all of the other liens on the property and the debtor's exemption, there is no equity (fully avoidable) or not enough equity (partially avoidable) to cover the lien.

# How to Do It: Chapter 7



- To avoid a judicial lien or NPMSI in a Chapter 7 case, file a motion pursuant to Rule 4003(d). This initiates a contested matter under Rule 9014, which is subject to most of the rules that apply in adversary proceedings, including the discovery rules. *See Fed. R. Bankr. P. 9014.*
- Under Local Rule 6008-1, you must file a motion, attach the Notice of Requirement of Response (Form 6008-1(B)), and file a Certificate of Service indicating service pursuant to Bankruptcy Rule 9014 and Rule 7004.
- Under Local Rule 6008-2, the respondent has 21 days from the date of service to file and serve a response. If no response is timely filed and served, the motion will be deemed unopposed and the Court may enter an order granting the relief sought. If a response is filed and served, the Court may schedule a hearing .

# How to Do It: Chapter 13



## “Embedded” Motions

- While Chapter 13 debtors have historically avoided judicial liens and NPMSIs by motion, Amended Rule 4003(d), effective December 1, 2017, permits the avoidance of judicial liens and NPMSIs through a Chapter 13 plan (§ 3.4 of the new Form Plan).
- Stand alone motions to avoid judicial liens in Chapter 13 cases are no longer necessary.
- Under Amended Rule 5009, the debtor can request entry of an order declaring that the secured claim has been satisfied and the lien has been released under the terms of a confirmed plan. The request shall be made by motion and shall be served on the holder of the claim and any other entity the court designates in the manner provided by Rule 7004 for service of a summons and complaint. Fed. R. Bankr. P. 5009.

# It's Not a Lien Strip

- Avoidance of a judicial lien or NPMIS is different than “stripping a lien.”
- A debtor can “strip down” or “strip off” a lien from property of the estate by valuing the property under § 506(a). The creditor holds a secured claim to be paid through the plan only to the extent of the value of the property, with the remainder becoming an unsecured claim.
- Lien stripping does not take into account the debtor’s exemption or depend upon the debtor’s ability to exempt the property.

# What liens are avoidable?



- ❖ A judicial lien (unless it secures a domestic support obligation); or
- ❖ A nonpossessory, nonpurchase-money security interest in any--
  - ✦ (i) household furnishings, household goods, wearing apparel, appliances, books, animals, crops, musical instruments, or jewelry that are held primarily for the personal, family, or household use of the debtor or a dependent of the debtor;
  - ✦ (ii) implements, professional books, or tools, of the trade of the debtor or the trade of a dependent of the debtor; or
  - ✦ (iii) professionally prescribed health aids for the debtor or a dependent of the debtor.
- Statutory liens (tax liens, mechanics' liens, *etc.*) are not judicial liens and cannot be avoided under § 522(f), even if the lien holder subsequently went to court and obtained a judgment. *See Hinton v. Internal Revenue Service (In re Hinton)*, BK 07-61497, Doc. #36 09/12/2007. This would include liens that arise by statute in favor of an HOA or COA.
- Remember to check § 522(f)(4) for the definition of a “**household good**” and note the exclusions, such as certain works of art, electronic entertainment equipment, and antiques; motor vehicles (including a tractors or lawn tractors); boats; and motorized recreational devices, conveyances, vehicles, watercraft, and aircraft.

# Is the lien or NNPMESI avoidable?



- To avoid the lien or NPMSI, the debtor must first establish that the debtor owned an interest in the property at the time the judicial lien or NPMSI attached to the property and on the petition date.
- The debtor must establish that the lien impairs the debtor's exemption, which means the debtor must be entitled to an exemption in the property (*see* O.C.G.A. § 44-13-100).
- The debtor does not need to show that she has equity in the property to avoid a judicial lien or NPMSI because the statute says an exemption to which the “debtor would have been entitled.”
- It is not clear that the debtor must have claimed the exemption on Schedule C, but the best practice is to do so. It provides notice to the judgment lien creditor and avoids questions in the future as to whether the judicial lien or NPMSI was avoided as to that property and the need to reopen and amend Schedule C.



## § 522(f)

[A] lien shall be considered to impair an exemption to the extent that the sum of--

- (i) the lien;
  - (ii) all other liens on the property; and
  - (iii) the amount of the exemption that the debtor could claim if there were no liens on the property;
- exceeds the value that the debtor's interest in the property would have in the absence of any liens.

### How to Tell If the Lien Impairs an Exemption

Example:

- Real Estate with FMV of \$100,000.
- Priority Deed to Secure Debt of \$80,000
- Second DSD of \$10,000
- Judicial lien of \$20,000.
- Debtor is entitled to a \$20,000 exemption.

The lien impairs the debtor's exemption to the extent that the **sum** of:

- (1) the lien the debtor is seeking to avoid (\$20,000);
- (2) all other liens on the property (\$90,000); and
- (3) the debtor's exemption (\$20,000)

which total \$130,000, exceeds the value of the debtor's interest in the property absent any liens (\$100,000) = \$30,000.

In this example, the amount by which the total of the liens and the exemption exceeds the value of the debtor's interest in the property is \$30,000, and this amount exceeds the value of the judicial lien (\$20,000). Accordingly, the entire judicial lien is avoidable.

Check Your Work:

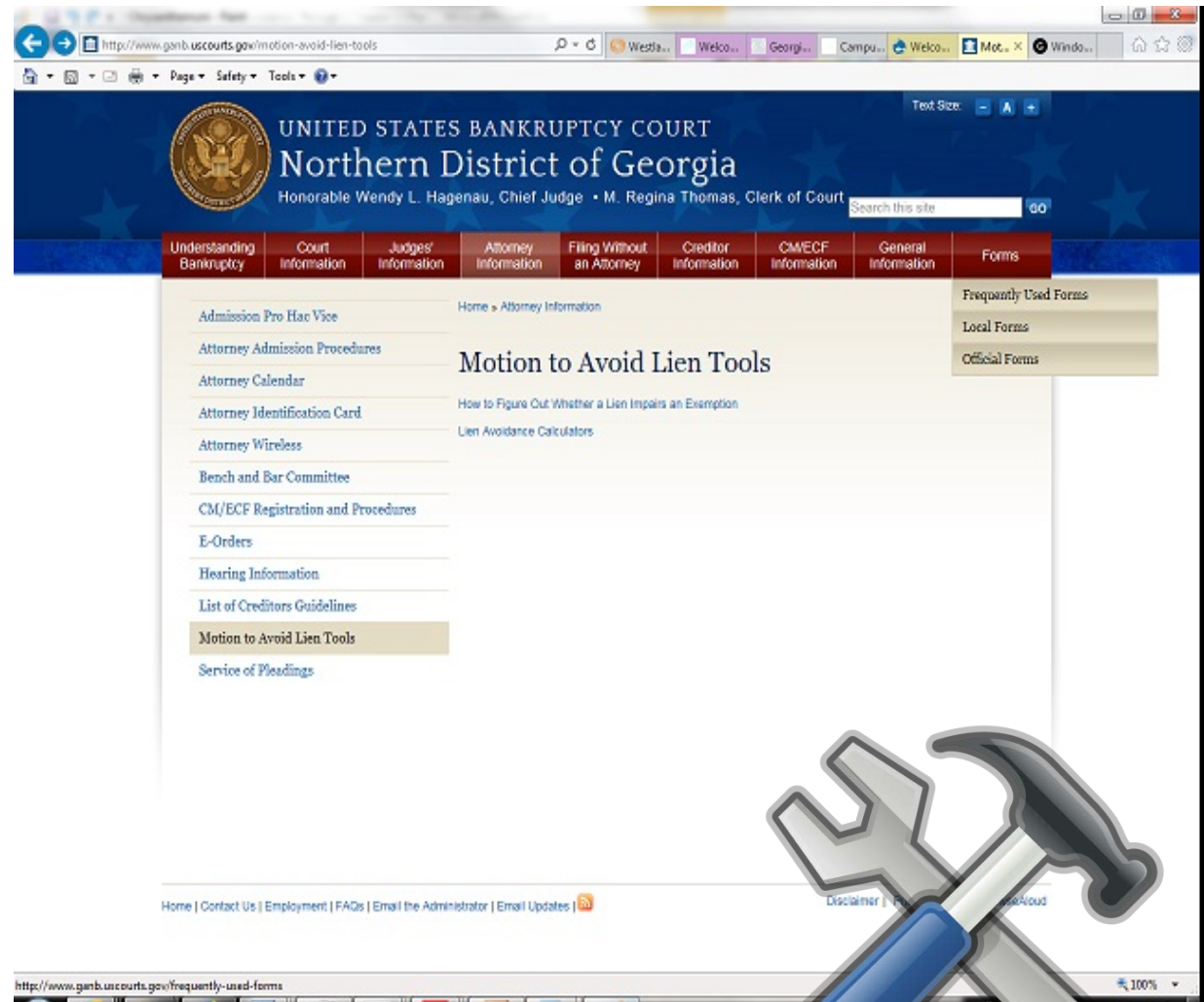
FMV \$100,000 – \$80,000 (1<sup>st</sup> DSD) – \$10,000 (2<sup>nd</sup> DSD) – \$20,000 (Exemption) = NEGATIVE \$10,000



# Lien Avoidance Tools

The Court's website has some very helpful tools for attorneys to use to determine whether a lien is avoidable.

You can find Judge Massey's Lien Avoidance Calculator under Attorney Information – Motion to Avoid Lien Tools.



The screenshot shows a web browser displaying the website for the United States Bankruptcy Court, Northern District of Georgia. The page title is "Motion to Avoid Lien Tools". The navigation menu includes: Understanding Bankruptcy, Court Information, Judges' Information, Attorney Information, Filing Without an Attorney, Creditor Information, CMECF Information, General Information, and Forms. The "Attorney Information" menu is expanded, showing options like Admission Pro Hac Vice, Attorney Admission Procedures, Attorney Calendar, Attorney Identification Card, Attorney Wireless, Bench and Bar Committee, CM/ECF Registration and Procedures, E-Orders, Hearing Information, List of Creditors Guidelines, Motion to Avoid Lien Tools (highlighted), and Service of Pleadings. The main content area includes a breadcrumb trail "Home > Attorney Information", the title "Motion to Avoid Lien Tools", and links for "How to Figure Out Whether a Lien Impairs an Exemption" and "Lien Avoidance Calculators". A search bar is located in the top right corner. At the bottom of the page, there are links for Home, Contact Us, Employment, FAQs, Email the Administrator, and Email Updates. A watermark of a hammer and wrench is visible in the bottom right corner of the screenshot.

# Joint Debtors and Fractional Property Interests



- ❖ With joint debtors, consider which spouse is liable for the judgment and which spouse owns the property. If one spouse owns the property and the judgment is against the other spouse only, the lien cannot attach to the other spouse's property.
- ❖ If the debtor who is liable on the judgment owns only a fractional interest in the property, the majority view is that the calculation is based on the debtor's fractional interest. For example, if the debtor owns a one-half interest in the property, the lien avoidance calculation includes only one half of the debts encumbering the property and one half of the value of the property. *See In re Lehman*, 205 F.3d 1255 (11th Cir. 2000).

**Example:** A judicial lien of \$20,000

Debtor owns  $\frac{1}{2}$  interest in real estate worth \$200,000 with a DSD of \$100,000 (joint) and Debtor is entitled to a \$20,000 exemption.

Value of Debtor's interest in property (\$100,000) minus Debtor's share of the DSD (\$50,000) minus Debtor's exemption (\$20,000) = \$30,000 (Lien is not avoidable)

# Multiple judicial liens



- When there are multiple judicial liens on the property, you must avoid the liens one at a time.
- Start with the judicial lien that would have the lowest priority under applicable non-bankruptcy law.
- Under Georgia law, the oldest judicial lien has the highest priority. *In re DotMD, LLC*, 303 B.R. 519, 525 (Bankr. N.D. Ga. 2003), aff'd *In re Dot MD, LLC*, 145 F. App'x 326 (11th Cir. 2005). All judgments rendered at the same term of court are considered to be of equal date. *Id.*; O.C.G.A. § 9-12-87.

- Once you have avoided the most recent judicial lien (taking into account all of the other liens), move to the next most recent lien.
- Do not include avoided liens when calculating the avoidance for the remaining liens.
- Note that nonavoidable liens, such as tax liens, are included in the calculation, even if they are lower priority than the lien you are trying to avoid. *See In re Taras*, 131 F. App'x 167, 170 (11th Cir. 2005).



# Judicial Liens on Multiple Properties



- You must analyze each property separately because § 522(f) refers to impairment of “an exemption” and not to impairment of the total of all exemptions.
- For purposes of the Chapter 13 plan, generally, if there is no non-exempt equity in any of the debtor’s property, treating the lien once in the Plan’s § 3.4 will be appropriate.
- However, if there is non-exempt equity in one of the properties (for example real estate) that will cause the lien to not be fully avoidable as to that property, you cannot lump together all of the property and will need to do a separate § 3.4 for the property against which the lien is not avoidable.

# Multiple Properties Example



Debtors have:

- **Real Property with FMV \$206,400 and Exemption of \$43,000**
  - 1<sup>st</sup> DSD \$131,716
  - Judicial Lien \$39,879 Real Property
- **Vehicles**
  - Vehicle 1 - FMV \$9,800 and Exemption of \$0
    - Lien \$24,642
  - Vehicle 2- FMV \$3,950 and Exemption \$0
- **Misc. Personal Property- FMV \$8,265 and Exemption \$8,265**
- **Furniture with FMV \$500**
  - Lien \$2,422

# A Right Way, and a Wrong Way

- If you lump the value of all of the Debtors' property together, add up all of the "other liens" on all of the property, and add up the exemptions on all of the property, the judicial lien on the real estate is partially avoidable, leaving a secured claim of **\$26,865**.



- If you treat the real property separately from the personal property, the judicial lien on the real estate is partially avoidable, leaving a secured claim of **\$31,684**.

# Lumping Makes a Difference



+	Information regarding judicial lien or security interest	Calculation of lien avoidance	Treatment of remaining secured claim
-	Name of creditor DDR Southeast Snellville, LLC	a. Amount of lien \$39,879.00	Amount of secured claim after avoidance (line a minus line f) \$31,684.00
	Collateral Real estate	b. Amount of all other liens \$131,716.00	
		c. Value of claimed exemptions \$43,000.00	Interest rate (if applicable)
		d. Total of lines a, b, and c \$214,595.00	%
		e. Value of debtor(s) interest in property \$206,400.00	Monthly payment on secured claim
	Lien identification (such as judgment date, date of lien recording) Judicial	f. Subtract line e from line d \$8,195.00	
	Extent of exemption impairment (Check applicable box).		
	<input type="checkbox"/> Line f is equal to or greater than line a. The entire lien is avoided. (Do not complete the next column.)		
	<input type="checkbox"/> Line f is less than line a. A portion of the lien is avoided. (Complete the next column.)		

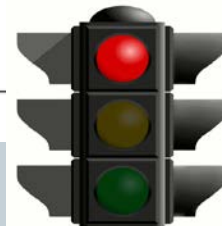
1.5 Surrender of collateral.



**Right Way**

	Information regarding judicial lien or security interest	Calculation of lien avoidance	Treatment of remaining secured claim
	Name of creditor DDR Southeast Snellville, LLC	a. Amount of lien \$39,879.00	Amount of secured claim after avoidance (line a minus line f) \$26,865.00
	Collateral unexempt equity in property	b. Amount of all other liens \$175,622.00	
		c. Value of claimed exemptions \$48,478.00	Interest rate (if applicable)
		d. Total of lines a, b, and c \$263,979.00	4%
		e. Value of debtor(s) interest in property \$250,965.00	Monthly payment on secured claim
		f. Subtract line e from line d \$13,014.00	\$15.00 step to \$500.00 in October, 2018
	Lien identification (such as judgment date, date of lien recording) Judicial	Extent of exemption impairment (Check applicable box).	
		<input type="checkbox"/> Line f is equal to or greater than line a. The entire lien is avoided. (Do not complete the next column.)	
		<input checked="" type="checkbox"/> Line f is less than line a. A portion of the lien is avoided. (Complete the next column.)	

§ 3.5 Surrender of collateral.



**Wrong Way**

# Is Avoiding the Lien Worth It?



- **Does the debtor own property in the state and/or county where the lien is? There must be something to secure the lien in order to make avoiding the lien worth while.**
- **Does the debtor still have the collateral pledged as NPMSI?**
  - If not, avoiding the lien may not be necessary, as there is nothing securing the loan any longer.
- **In a Chapter 13 case, is the NPMSI loan more than a year old?**
  - If no, avoid and treat as a general unsecured claim.
  - If yes, then pay back at reduced principal based on the fair market value of the collateral.
- **If you want to err on the side of making sure that a clean and complete discharge issues for your client.... Avoid the lien!**



# Serving the Chapter 13 Plan



- If the plan contains a provision avoiding a judicial lien or NPMSI, Debtor is responsible for serving the plan on the affected creditor in accordance with Rule 7004. *See General Order 21-2017, ¶ 2.2.*
- Debtor must promptly file a Certificate of Manner of Service of Plan (“CMOS”) indicating: the date and method of service for each creditor served under Rule 7004 and the name of each creditor served. *See General Order 21-2017, ¶ 2.3.1.*
- When completing the CMOS, it is best practice to identify clearly the person being served. For example, when serving the registered agent, indicate XYZ Corporation, Registered Agent for Creditor, Inc., or when serving an officer, indicate John Doe, President.

# Serving a Pre-Confirmation Modification

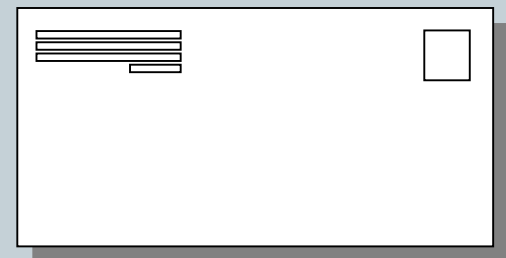


- If the debtor files a pre-confirmation modification of the plan, the same service requirements are applicable, unless the modified plan does not materially and adversely affect the lien creditor. General Order No. 21-2017, ¶ 4.2.3. If an attorney has appeared in the case for the creditor, the debtor must also serve the attorney.
- As with the original plan, the debtor must file promptly a CMOS. *Id.* ¶ 4.4.
- If the modified plan materially and adversely affects the lien creditor, the debtor must also serve notice of the reset confirmation hearing in accordance with Rule 7004 and provide not less than 28 days' notice of the hearing. *Id.* ¶ 4.3.1. The CMOS must be separate docket entry from the notice of rescheduled confirmation. *Id.*

# Tips on Rule 7004 Service



- See Judge Massey's helpful monograph regarding proper service, available on the Court's website under the Attorney Information tab.
- If the creditor is an individual (not a corporation, LLC, *etc.*), do not serve the creditor at a post office box. *See* Rule 7004(b)(1). *In re Tyler*, 493 B.R. 905 (Bankr. N.D. Ga. 2013); *In re CEP Holdings v. Zavala*, AP 07-6498, Doc. #25 05/07/2008.



# More Tips on Rule 7004 Service



- ❖ If the creditor is a corporation or other entity, such as a limited liability company, you must serve an officer, registered agent, or other agent authorized to receive service of process. FRBP 7004(b)(3). This rule requires that the corporate officer or agent be identified by name, rather than simply ATTN: President. *In re Faulknor*, No. 04-43921-PWB, 2005 WL 102970, \*2 (Bankr. N.D. Ga. Jan. 18, 2005).
- ❖ Generally, serving only the attorney who obtained the judgment on behalf of the creditor is not sufficient unless it is clear that the attorney continues to be authorized to receive service of process for the creditor.
- ❖ Serving the Secretary of State may not always be appropriate and is more complicated than simply mailing the plan to the Secretary of State. See O.C.G.A. 9-11-4(e)(1); *In re Dobbs*, Case No. 18-50813-PWB, 2018 WL 1363450 (Bankr. N.D. Ga. Mar. 15, 2018).

# More Tips of Rule 7004 Service



- If the creditor is an FDIC-insured depository institution (you can check at [www.fdic.gov](http://www.fdic.gov) to be sure), read Rule **7004(h)** carefully.
  - Generally, you must served an **officer by certified mail** unless the Court orders otherwise, the creditor has waived that benefit in writing, or an attorney has appeared for the creditor.



- Service on a registered agent for an FDIC-insured depository institution is never sufficient, even if you send it by certified mail.



# And Still More Tips on Rule 7004 Service



- If the creditor is the federal government or a federal agency, serve the U.S. attorney in Atlanta and the U.S. Attorney General at Washington, D.C, and the specific agency. FRBP 7004(b)(4), (b)(5).
- If the creditor is a state or municipality, serve the person or office that would be required for service under state law. FRBP 7004(b)(6); *see also* O.C.G.A. § 9-11-4(e)(5) (service upon a county, municipality, city, or town, to the chairman of the board of commissioners, mayor or city manager, or an agent authorized by appointment to receive service of process; if against any other public body or organization, to the chief executive officer or clerk thereof).

# When is the Lien Avoidance Effective?



- There is a split of authority as to whether an order avoiding a judicial lien is effective upon entry of the order or payment completion/discharge. *Compare In re Harris*, 482 B.R. 899, 902 (Bankr. N.D. Ill. 2012) (holding that a lien avoidance is not effective until debtor completes the Chapter 13 plan payments and receives a discharge), *In re Prince*, 236 B.R. 746, 750–51 (Bankr. N.D. Okla. 1999), and *In re Stroud*, 219 B.R. 388, 390 (Bankr. M.D.N.C. 1997) (holding that § 522(f) lien avoidance is not effective until plan completion/discharge), with *In re Mulder*, 2010 WL 4286174, at \*2–3 (Bankr. E.D.N.Y. Oct. 26, 2010) (holding that the lien is avoided immediately upon entry of the order) and *In re Ferrante*, 2009 WL 2971306, at \*4 (Bankr. D.N.J. Sept. 10, 2009) (same).

# What if the case is dismissed or converted?



- Section 349(b)(1)(B) provides that “[u]nless the court, for cause, orders otherwise, a dismissal of a case . . . reinstates . . . any transfer avoided under section 522. . . .” 11 U.S.C. § 349(b)(1)(B).
- For authority that “conversion of a case from Chapter 13 to Chapter 7 does not affect the validity of an order entered upon a motion to avoid a judicial lien under 11 U.S.C. § 522(f),” see *In re Phillips*, 553 B.R. 536, 548 (Bankr. E.D.N.C. 2016).