

In re Peters, Case No. 394-36717-elp13

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ELP

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Creditors obtained judgments against the debtor's ex-spouse and judgment liens on the spouse's interest in residential real property to which the spouse held title. Debtor claimed an equitable interest in the residence. Subsequently the spouse conveyed title to the property to the debtor under a separation agreement. Two years later, the debtor filed bankruptcy, claimed the residence as exempt and moved to avoid the creditors' judicial liens.

Relying upon Farrey v. Sanderfoot, 500 U.S. 291 (1991), the court held that the debtor could not avoid the judicial liens because the liens attached to the property prior to the time that the debtor acquired the interest to which the liens attached. Although the debtor may have held an equitable interest in the property at the time the liens attached, the liens did not attach to that interest. The court rejected the debtor's reliance on Owen v. Owen, 500 U.S. 305 (1991), determining that Owen focused upon the meaning of the term impairment and that Owen specifically declined to address Farrey's requirement that the debtor hold the interest to which the lien attached at the time the lien attached.

The court declined to address the questions of whether the liens survived the transfer of the property under state law and whether the debtor could discharge the liens under the procedure set forth in ORS 23.280 - 23.300 because those questions were not properly before the court.

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF OREGON

In Re:) Case No. 394-36717-elp7
)
D. ELIZABETH PETERS,) MEMORANDUM OPINION
)
Debtor.)

The debtor moved under 11 U.S.C. § 522(f)(1)(A) to avoid the judgment liens of Stan Frank and Stephen Martell on the basis that they impaired her homestead exemption. For the reasons set forth below, the motions are denied.

BACKGROUND FACTS

The debtor married Terry L. Peters in 1980. Prior to September of 1992, Terry Peters held title to the family residence. The debtor, however, claims that she held an equitable interest in the residence from the date of her marriage until she acquired a legal interest. On July 2, 1992, Stephen Martell ("Martell") obtained a judgment against Terry Peters in the amount of \$5,500. On September 4, 1992, Stan Frank ("Frank")

obtained a judgment against Terry Peters in the amount of \$40,188. Both Martell and Frank obtained judicial liens on Terry Peters' interest in the property as a result of their judgments. Later in September of 1992, pursuant to a separation agreement, Terry Peters conveyed title to the residence to the debtor.

The debtor filed a Chapter 7 petition on November 9, 1994, and claimed her interest in the residence exempt under ORS 23.240. At that time, the residence was subject to encumbrances in the following order of priority: (1) a deed of trust in favor of Washington Mutual in the amount of \$24,053; (2) a deed of trust in favor of United States National Bank in the amount of \$11,195; (3) two statutory liens in favor of the City of Portland in the amounts of \$1,733 and \$884; (4) Martell's judgment lien in the amount of \$5,500; (5) Frank's judgment lien in the amount of \$40,188. The debtor claims that the residence has a value of \$62,000.

DISCUSSION

With certain inapplicable exceptions, 11 U.S.C. § 522(f)(1)(A) allows a debtor to avoid "the fixing of a [judicial] lien on an interest of the debtor in property to the extent that such lien impairs an exemption to which the debtor would have been entitled to under [section 522(b)]." In defining the concept of impairment, section 522(f)(2)(A) provides as follows:

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 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.

The initial question is whether and to what extent section 522(f) can apply in light of the fact that the liens attached when Terry Peters held record title to the property. The debtor, relies on Owen v. Owen, 500 U.S. 305 (1991) to contend that section 522(f) can be used to avoid a judicial lien that attached before the debtor acquired an interest in the property. Martell and Frank rely on Farrey v. Sanderfoot, 500 U.S. 291 (1991) to contend that section 522(f) cannot apply to avoid the fixing of a judicial lien on property when the lien attached before the debtor acquired her interest in property to which the lien attached.

In Farrey, Farrey and Sanderfoot owned certain real property as joint tenants prior to their divorce with each holding an undivided one-half interest. The divorce decree extinguished these interests, granted Sanderfoot sole title to the real property, ordered Sanderfoot to pay approximately \$29,000 to Farrey and granted Farrey a lien on the real property to secure payment of this amount. Sanderfoot filed bankruptcy and attempted to avoid the lien under section 522(f). The Supreme Court determined that Sanderfoot could not avoid the lien

because Sanderfoot did not own the interest to which the lien attached prior to the time that the lien attached. Rather, Sanderfoot took the interest to which the lien attached and the lien together, as if he had purchased an already encumbered estate.

The Court read the term "the debtor may avoid the 'fixing' of a lien" to require that the lien at issue must have attached to the debtor's interest after the debtor acquired the interest. According to the Court, this language did not allow the avoidance of a lien; rather it allowed the avoidance of the fixing of a lien to a pre-existing interest of the debtor in property. Thus, the debtor could not avoid the fixing of a lien under this section unless the debtor owned the property interest to which the lien attached before the lien attached to that interest. Id. at 296-97. The court also reasoned that the history and purpose of section 522(f) reflect a concern with protecting the debtor's exemptions from creditors who beat the debtor to the courthouse by obtaining judgment liens shortly before the filing of the petition. The section is not concerned with liens that fix on an interest before the debtor acquired that interest. Id. at 298. In such instances, the fixing of the lien is not on the debtor's interest, the race to the courthouse purposes are not implicated and permitting lien avoidance would allow judicial lienholders to be defrauded by the conveyance of an encumbered asset to a

prospective debtor.

In Owen, the creditor obtained and recorded a judgment against the debtor in 1976. Although the debtor did not, at that time, own any property that was subject to the judgment, under state law the judgment lien would attach to any after-acquired property. The debtor purchased a condominium which became subject to the judgment lien in 1984 and which, because of a change in the state homestead law, qualified as a homestead one year later. Under state law, however, the homestead exemption remained subject to pre-existing liens. The debtor filed a Chapter 7 petition in 1986 and the debtor sought to avoid the judgment lien under section 522(f). The Supreme Court reversed an order denying the avoidance of the lien, rejecting the argument that the lien did not impair the homestead exemption because the state homestead exemption was not assertable against a pre-existing judicial lien.

In reaching this holding, the court focused on the term impairment and indicated that the question is not whether the lien impairs the exemption, but whether the lien impairs an exemption to which the debtor would have been entitled in the absence of the lien. The fact that state law may have excepted certain pre-existing liens from the protection of the homestead exemption did not mean that such liens did not impair the exemption under this standard. The court further noted, however,

that its conclusion that impairment may exist under these circumstances did not resolve the motion to avoid the liens because the lower courts had not yet determined whether the lien fixed on an interest of the debtor. The court declined to address this question. Owen, 500 U.S. at 314. On remand, the Eleventh Circuit determined that the lien did not fix on an interest of the debtor in property because the lien fixed at the same time that the debtor acquired an interest in the property and the debtor had no property interest prior to the fixing of the lien. In re Owen, 961 F.2d 170 (11th Cir.), cert. denied, 113 S.Ct. 659 (1992).

The debtor's reliance on Owen, 500 U.S. 305 (1991), under the facts of this case is misplaced. The Supreme Court's opinion in Owen does not establish, as the debtor contends, that section 522(f) can be used to avoid a lien that attached before the debtor acquired an interest in the property. Rather, the Supreme Court's opinion in Owen dealt with the term impairment and whether impairment can exist when state law defines an exemption so that it is subject to a judicial lien. In Owen the Supreme Court specifically declined to address whether section 522(f) can be used to avoid a lien that attached to an interest in property before the debtor acquired the interest. Farrey addressed this question and held that section 522(f) cannot be used to avoid such liens.

Turning to the application of the rule of Farrey, at the time that the judicial liens in question arose, Terry Peters held record title to the property. The debtor claims that she held some sort of equitable interest in the residence, which neither Martell nor Frank dispute and which I will assume to be true for purposes of this motion. The Martell and Frank judgments were against Terry Peters, but not against the debtor. The judgments, therefore, became liens against Terry Peters' interest in the residence. See ORS 18.350. The judgment liens did not attach to any equitable interest of the debtor in the residence because she was not the judgment debtor. In addition, a judgment lien will not attach to an equitable interest that was hostile to the interest of the judgment debtor and that was in existence at the time the judgment was rendered. See Meier v. Kelly, 22 Or. 136, 29 P. 265, 267 (1892).

Because the judgment lien attached to the interest of Terry Peters in the residence but not to any equitable interest of the debtor, the judgment lien attached before the debtor acquired the interest in property to which the lien attached. The debtor took the interest to which the lien attached and the lien together, as if she had purchased encumbered property. Under the rule of Farrey, the debtor cannot avoid the fixing of these judicial liens under section 522(f) because the judicial liens fixed on the interest before the debtor acquired the

pertinent interest in the property. That the debtor may have had some equitable interest in the property at the time the judicial liens attached does not change this result because the liens did not attach to that equitable interest.

The debtor also asserts that the judgment liens should be avoided under state law because the grantee of a homestead takes the homestead free of a judgment lien on the property unless the homestead owner has lost his homestead through abandonment or otherwise. In support of this argument, the debtor relies on Smith v. Popham, 266 Or. 625, 513 P.2d 1172 (1973). This argument is unpersuasive for several reasons.

First, the argument concerns whether and to what extent a judgment lien survives the transfer of property under state law and has no bearing on the question before the court -- whether the fixing of the judgment lien may be avoided because it impairs the debtor's right to an exemption.

Second, Smith was decided before the enactment of ORS 23.280 - 23.300, which provides a procedure by which the seller or purchaser of homestead property can provide notice and obtain a discharge of the judgment liens against the property. If debtor wants to discharge the judgment liens utilizing state law, she must provide the notice and comply with the procedure set forth in ORS 23.280 - 23.300. My decision that the liens are not avoidable under § 522(f) should not be construed to limit the

debtor's ability to discharge the liens under state law in an appropriate state court proceeding.

CONCLUSION

For the reasons set forth above, the debtor's motion to avoid the judicial liens of Martell and Frank are denied.

This Memorandum Opinion shall constitute Findings of Fact and Conclusions of Law as required by Fed. R. Bankr. P. 7052 and they shall not be separately stated.

ELIZABETH L. PERRIS
Bankruptcy Judge