

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF WISCONSIN

In re

SHEVAN C. JOSEPH,

Debtor.

Case No. 98-28086-MDM

Chapter 13

MEMORANDUM DECISION ON JUDICIAL LIEN ON
DEBTOR'S CLAIMED HOMESTEAD EXEMPTION

Background

This matter comes before the court in the context of an objection to a claim. More particularly, it is an objection to the secured status of a claim based on a judgment lien. Fed. R. Bankr. P. 3012. The extent to which the claim is secured determines whether the plan is feasible, as the debtor must pay 100% of a secured claim pursuant to the proposed plan, but only 1% of an unsecured claim. This court has jurisdiction under 28 U.S.C. § 1334(b). This is a core proceeding under 28 U.S.C. § 157(b)(2)(B).

The same creditor has also objected to confirmation of the plan, which is still pending. No motion for lien avoidance under either § 522(f) or § 506(d) has been filed to date.

On November 21, 1996, prior to a previous bankruptcy filing, County Wide Credit Union obtained a judgment in state court against the debtor, and a lien attached to his property at 2579 North Martin Luther King Jr. Drive. At the time the lien attached, the debtor was not using the property as his homestead.

State law provides a procedure to remove judgment liens arising from debts that are subsequently discharged in bankruptcy. *See* Wis. Stat. § 806.19(4). However, on February 3, 1999, in the prior chapter 7 case, Judge James E. Shapiro found the \$13,060.27 judgment obtained by County Wide nondischargeable under 11 U.S.C. § 523(a)(2)(B). *County Wide Credit Union v. Shevan C. Joseph*, Adversary Proceeding No. 98-2141. Since the County Wide debt was not discharged, the judgment lien remained of record. Liens arising from other judgments discharged in the prior chapter 7 were removed pursuant to the state law procedure before the instant case was filed.

The debtor filed this chapter 13 case on August 11, 1998. His completed schedules were filed on August 20, 1998, and an amendment to Schedule C - Property Claimed as Exempt - was filed on March 29, 1999. No objections to the debtor's original or amended schedules were filed, although it appears from the affidavit of service that only the chapter 13 trustee was served with a copy of the amended schedules (docket #50). The debtor claimed the property at 2579 North Martin Luther King Jr. Drive, Milwaukee, as his homestead and claimed the federal exemptions. The original homestead exemption claimed was valued at only \$500. His amended claim of the homestead exemption was valued at \$16,145.

On February 2, 1999, in proceedings related to County Wide's objection to a previous proposed plan, this court made a finding that the Martin Luther King Jr. Drive property was the homestead of the debtor on the date of filing but not when the judgment lien attached. Under state law, the debtor's homestead exemption does not supercede a judgment lien that attached before the property became the debtor's homestead. *Master Lock Credit Union v. Rayford*, 119 Wis. 2d 301, 349 N.W.2d 737 (Ct. App. 1984).

It is uncontested that the property is worth \$27,000. Prepetition outstanding real estate taxes are, according to the city's proof of claim, \$8,244.83. The creditor asserts in its brief that there is an outstanding IRS lien in excess of the value of the property, but the most recent proof of claim filed by the IRS indicates no such lien. The court will take the IRS' word for it. Five hundred dollars was due the land contract vendor at the time of filing.

Arguments

The creditor argues that since a Wisconsin debtor cannot claim a homestead exemption in property that the debtor does not reside in at the time a judgment is obtained, the judgment lien supercedes the debtor's exempt interest at the time of the bankruptcy.

The debtor contends that the creditor is precluded under *Taylor v. Freeland & Kronz*, 503 U.S. 638, 112 S.Ct. 1644 (1992), from objecting to the exemption claimed by the debtor since no timely objection was filed by the creditor or trustee. Thus, under federal law, the exemption must be allowed. Also, pursuant to *Owen v. Owen*, 500 U.S. 305, 111 S.Ct. 1833 (1991), a state law exemption limitation does not preclude the debtor from avoiding the lien to the extent it interferes with his right to claim a federal homestead exemption.

Discussion

The debtor sees the question as whether the exemption must be allowed, as he believes this determines how much of the claim is secured. Pursuant to 11 U.S.C. § 522(l), if no party in interest objects to a claimed exemption, such property is exempt. Bankruptcy Rule 4003 requires the trustee or any creditor to file objections within 30 days after the meeting of creditors or the

filing of any amendment. The amended exemption schedule claiming a homestead exemption of \$16,145 was filed on March 29, 1999 (increasing the original claim of \$500). A copy of that amended exemption schedule was sent to the chapter 13 trustee but apparently not to the creditor holding the judgment lien. No objections to the amended exemption schedule were filed. The Supreme Court and the Seventh Circuit have held that, even where a debtor has no colorable basis for claiming an exemption, once the 30-day period has expired, the property is considered exempt. *Taylor v. Freeland & Kronz*, 503 U.S. 638, 643-44, 112 S.Ct. 1644, 1648-49 (1992); *Matter of Kazi*, 985 F.2d 318 (7th Cir. 1993).

The creditor's lack of notice of the change in the dollar amount of the homestead exemption might give us pause, if this were a question of entitlement to the exemption. *See Preblich v. Battley*, 181 F.3d 1048 (9th Cir. 1999) (thirty day objection period begins when trustee or objecting creditor receives notice of amended exemption schedule). A creditor might not worry about a \$500 exemption that primes its interest, whereas it might have substantial reason to object to a \$16,145 exemption priming its interest. Here, the creditor raised two issues with respect to this property, one of which was already decided; that is, whether the Martin Luther King Jr. Drive property was the debtor's homestead. At a hearing on County Wide's objection to confirmation of a previous plan, this court determined that it was, and the issue was fiercely litigated by County Wide. The determination was made before the amended schedule was filed that increased the value of the exemption. However, when the objection to County Wide's claim was briefed, the creditor was well aware of the amount claimed, but it has not raised the amount or notice of the amendment as an issue. The remaining question is a legal one, and it is independent of the value of the exemption; that is, whether that exemption primes the judgment

holder's lien interest, thereby making the judgment unsecured, at least in part, for the purpose of plan payments in the chapter 13.

The priority of a homestead exemption and a judgment lien usually arises in the context of a motion for lien avoidance under § 522(f). No such motion is pending, and one is not necessary in a chapter 13 case. If the debtor pays the creditor's claim and completes the plan, the remaining debt will be discharged, notwithstanding that it was excepted from the debtor's prior chapter 7 discharge. Once it is discharged, the lien for any unpaid amount can be removed using the state court procedure. Alternatively, § 506(d) voids the lien to the extent it is for an allowed unsecured claim.

Nevertheless, § 522(f) lien avoidance cases are instructive in determining whether the homestead exemption or the judgment lien have priority, as this priority determines to what extent the creditor's claim is secured and unsecured. The Supremacy Clause enables Congress to override state laws if it so intends. Congress exercised this power by enacting national, uniform bankruptcy laws which necessarily exclude or displace any conflicting state regulation. *International Shoe Co. v. Pinkus*, 278 U.S. 261, 265, 49 S.Ct. 108 (1929). A number of courts have found that the Code's lien avoidance provision preempts state exemption law. *E.g.*, *In re Leicht*, 222 B.R. 670, 677 (B.A.P. 1st Cir.1998); *In re Gregory*, 214 B.R. 570 (S.D. Tex. 1997); *In re Farr*, 224 B.R. 438 (Bankr. N.D. Cal. 1998).

In a case similar to this one, the First Circuit held that the Bankruptcy Code preempted the Massachusetts Homestead Act's exceptions for preexisting liens and for prior contract debts. *In re Weinstein*, 164 F.3d 677 (1st Cir. 1999). In *Weinstein*, a judgment lien was recorded on property owned by the debtor two years prior to when the debtor acquired an estate of homestead

on the property. After analyzing *Farrey v. Sanderfoot*, 500 U.S. 291, 111 S.Ct. 1825 (1991), and *Owen v. Owen*, 500 U.S. 305, 111 S.Ct. 1833 (1991), the court of appeals upheld the debtor's homestead exemption. The court noted that the Supreme Court in *Sanderfoot* held that in order to "avoid the fixing of a lien on an interest of the debtor in property" under § 522(f), the debtor must have "possessed the interest to which the lien fixed, before it fixed." *Weinstein*, 164 F.3d at 680 (quoting *Sanderfoot*, 500 U.S. at 299, 111 S.Ct. at 1830). As occurred here, the debtor had an ownership interest before the lien attached, even though it was not his homestead at that time.

The First Circuit further observed that the Supreme Court in *Owen* held that to determine whether a lien "impairs an exemption to which the debtor would have been entitled" under § 522(f), the proper question to ask is not whether the lien impairs an exemption to which the debtor is in fact entitled, but rather whether the lien impairs a state or federal exemption to which the debtor would have been entitled but for the lien. *Id.* (citing *Owen*, 500 U.S. at 310-13, 111 S.Ct. at 1836-38). The *Owen* Court expressly rejected the notion that because the Code's opt-out policy allows states to define their own exemptions, those exemptions must be applied with all their built-in limitations. *Owen*, 500 U.S. at 313, 111 S.Ct. at 1838. *Owen* also stated that § 522(f) was clearly applicable to federal exemptions, as this debtor has claimed, although the debtor in *Owen* had used the state exemptions. *Id.* at 312-13, 111 S.Ct. at 1837. Because the state exemption limitation conflicted with § 522(c), which protects exempt property from recovery for all prepetition debts except for certain types of debts not applicable here and unavoidable liens, the First Circuit held that the state exemption limitation was invalid in bankruptcy. *Weinstein*, 164 F.3d at 682.

Thus, Wisconsin's rule, that a debtor does not have the right to claim a homestead exemption on property that the debtor does not reside in at the time a judgment is obtained, is preempted by the Bankruptcy Code.

This holding is not inconsistent with *Matter of Davis*, 170 F.3d 475 (5th Cir. 1999), wherein the court held that the Code did not preempt Texas exemption law, which protected the debtors' homestead from seizure and sale. The creditor had a nondischargeable support claim under § 523(a)(5), and exempt assets are subject to recovery for such claims under § 522(c)(1). However, under state law, an exempt homestead was not subject to seizure, even for support debts. The court held that § 522(c) did not create a liability that did not otherwise exist under state law; it merely provides that bankruptcy protection does not extend to exempt property for certain purposes. Section 522(c) does not protect exempt property from recovery for support and certain tax debts, but it does not eliminate bankruptcy protection of exempt property for other nondischargeable debts, such as the debt at issue in this case.

A debtor's available exemptions are determined at the time of filing the bankruptcy petition. *In re Patterson*, 64 B.R. 120 (W.D. Wis. 1986). The homestead exemption available at the time of the petition, August 11, 1998, was \$16,145. The debtor's homestead exemption supercedes the judgment lien of the creditor, and so do real estate taxes and the balance due the land contract vendor. Under § 506(a), a claim is an allowed secured claim to the extent of the "creditor's interest in the estate's interest" in property, and is an allowed unsecured claim for the balance. Therefore, the secured portion of County Wide's claim can be calculated as follows:

Value of property:	\$27,000.00
Less:	
Real estate taxes	8,244.83
Land contract	500.00
Homestead exemption	<u>16,145.00</u>
Secured claim	\$2,110.17

The balance of the creditor's claim, \$10,950.10, is unsecured.

Conclusion

Based on the foregoing, the claim of County Wide Credit Union is allowed as secured in the amount of \$2,110.17, and unsecured in the amount of \$10,950.10. A separate order will be entered accordingly.

This memorandum represents the court's findings of fact and conclusions of law under Fed. R. Bankr. P. 7052.

Dated at Milwaukee, Wisconsin, September 14, 1999.

BY THE COURT:

_____/s/_____
Honorable Margaret Dee McGarity
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF WISCONSIN

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SHEVAN C. JOSEPH,

Debtor.

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ORDER

For the reasons set forth in the court's memorandum decision entered on this date, IT IS ORDERED that the claim of County Wide Credit Union is allowed as secured in the amount of \$2,110.17, and unsecured in the amount of \$10,950.10.

Dated at Milwaukee, Wisconsin, September 14, 1999.

BY THE COURT:

_____/s/_____
Honorable Margaret Dee McGarity
United States Bankruptcy Judge

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