

## **December 1, 2017 Rules Changes**

### **Part IV**

#### **No Math Required? Avoiding Liens Under § 522(f)**

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*The Rules of Bankruptcy Procedure are being amended this year in ways that will significantly affect chapter 13 trustees and practitioners. In this series, scheduled to run before the December 1 effective date, Larry Ahern and Beverly Burden will explain these changes. In this fourth part of the series, the authors describe a nifty tool in the “national plan” that can be used as a part of any local plan or motion to calculate the amount of lien avoidance available under section 522(f).*

#### **Summary**

[In Part III of this series](#), we described the available procedures by which a request to avoid a lien under section 522(f) may be made and the method by which such a request must be served in accordance with the amended rules. There, we pointed out that under amended Rule 4003(d), a lien may be avoided either by motion (under Rule 9014), or by the terms of a confirmed chapter 13 plan.<sup>1</sup> That is the *how*. This article looks further at *what* – the amount of judicial liens that may be avoided – and the mechanics of making that computation under section 522(f), utilizing a feature in the so-called “national plan” to determine the amount.<sup>2</sup>

#### **Avoiding Judicial Liens Under § 522(f)**

11 U.S.C. § 522(f) permits a debtor to avoid a judicial lien to the extent the lien “impairs” an exemption to which the debtor would have been entitled in the absence of the lien.<sup>3</sup> A lien impairs an exemption to the extent that the sum of the amounts secured by that lien and all other liens on the property, plus 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.<sup>4</sup>

Unlike “stripping off” an underwater junior mortgage on the debtor’s residence,<sup>5</sup> the avoidance of a judicial lien is not an all-or-nothing process. It requires performing a

mathematical calculation – often not a lawyer’s strongest skill. Any tool that can transform a statutory formula from a narrative into a table or spreadsheet format is a boon to the math-challenged.

The “National Plan”

As a part of the process of promulgating the rules that are scheduled to become effective on December 1, 2017, the Rules Committee proposed the adoption of a uniform chapter 13 plan, which is colloquially referred to as the “national plan.”<sup>6</sup> Although most jurisdictions have rejected the national plan in favor of local form plans, section 3.4 of the national plan provides a useful tool and can be readily incorporated into any local plan or motion to effectuate a lien avoidance. Section 3.4 of the plan contains a calculation device as follows:

The judicial liens or nonpossessory, nonpurchase money security interests securing the claims listed below impair exemptions to which the debtor(s) would have been entitled under 11 U.S.C. § 522(b). Unless otherwise ordered by the court, a judicial lien or security interest securing a claim listed below will be avoided to the extent that it impairs such exemptions upon entry of the order confirming the plan. The amount of the judicial lien or security interest that is avoided will be treated as an unsecured claim in Part 5 to the extent allowed. The amount, if any, of the judicial lien or security interest that is not avoided will be paid in full as a secured claim under the plan. See 11 U.S.C. § 522(f) and Bankruptcy Rule 4003(d). *If more than one lien is to be avoided, provide the information separately for each lien*

<div style="border: 1px solid black; padding: 2px; margin-bottom: 5px;"><b>Information regarding judicial lien or security interest</b></div> <p><b>Name of creditor</b></p> <p>_____</p> <p><b>Collateral</b></p> <p>_____</p> <p><b>Lien identification</b> (such as judgment date, date of lien recording, book and page number)</p> <p>_____</p> <p>_____</p>	<div style="border: 1px solid black; padding: 2px; margin-bottom: 5px;"><b>Calculation of lien avoidance</b></div> <table border="1" style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 70%;">a. Amount of lien</td> <td style="width: 30%; text-align: right;">\$ _____</td> </tr> <tr> <td>b. Amount of all other liens</td> <td style="text-align: right;">\$ _____</td> </tr> <tr> <td>c. Value of claimed exemptions</td> <td style="text-align: right;">+ \$ _____</td> </tr> <tr> <td>d. Total of adding lines a, b, and c</td> <td style="text-align: right;">\$ _____</td> </tr> <tr> <td>e. Value of debtor(s)' interest in property</td> <td style="text-align: right;">- \$ _____</td> </tr> <tr> <td>f. Subtract line e from line d.</td> <td style="text-align: right;">\$ _____</td> </tr> </table> <p>Extent of exemption impairment (Check applicable box):</p> <p><input type="checkbox"/> <b>Line f is equal to or greater than line a.</b></p> <p>The entire lien is avoided. (Do not complete the next column.)</p> <p><input type="checkbox"/> <b>Line f is less than line a.</b></p> <p>A portion of the lien is avoided. (Complete the next column.)</p>	a. Amount of lien	\$ _____	b. Amount of all other liens	\$ _____	c. Value of claimed exemptions	+ \$ _____	d. Total of adding lines a, b, and c	\$ _____	e. Value of debtor(s)' interest in property	- \$ _____	f. Subtract line e from line d.	\$ _____	<div style="border: 1px solid black; padding: 2px; margin-bottom: 5px;"><b>Treatment of remaining secured claim</b></div> <p><b>Amount of secured claim after avoidance (line a minus line f)</b></p> <p>\$ _____</p> <p><b>Interest rate</b> (if applicable)</p> <p>_____ %</p> <p><b>Monthly payment on secured claim</b></p> <p>\$ _____</p> <p><b>Estimated total payments on secured claim</b></p> <p>\$ _____</p>
a. Amount of lien	\$ _____													
b. Amount of all other liens	\$ _____													
c. Value of claimed exemptions	+ \$ _____													
d. Total of adding lines a, b, and c	\$ _____													
e. Value of debtor(s)' interest in property	- \$ _____													
f. Subtract line e from line d.	\$ _____													

Mechanics of Avoiding a Judicial Lien Under § 522(f)

Consider an example based on the following facts:

Property value <sup>7</sup>	\$280,000
1st mortgage	\$180,000
Judgment lien	\$112,400
2nd mortgage	\$ 80,300
Exemption	\$ 6,000

The calculation using the table from the national plan would be as follows:

<p><b>Information regarding judicial lien or security interest</b></p> <p><b>Name of creditor</b> <u>Collections-R-U</u></p> <p><b>Collateral</b> <u>House and Lot at 100 Main St, Small Town, KY (Residence)</u></p> <p><b>Lien identification</b> (such as judgment date, date of lien recording, book and page number) <u>Judgment Lien Recorded in Small County, KY</u></p> <p><u>MB 100 page 50</u></p>	<p align="center"><b>Calculation of lien avoidance</b></p> <table border="1"> <tr> <td>a. Amount of lien</td> <td align="right">\$112,400</td> </tr> <tr> <td>b. Amount of all other liens (\$180,000 (1st) + \$80,300 (2nd))</td> <td align="right">\$260,300</td> </tr> <tr> <td>c. Value of claimed exemptions</td> <td align="right">+ \$ 6,000</td> </tr> <tr> <td>d. Total of adding lines a, b, and c</td> <td align="right">\$378,700</td> </tr> <tr> <td>e. Value of debtor(s)' interest in property</td> <td align="right">- \$280,000</td> </tr> <tr> <td>f. Subtract line e from line d.</td> <td align="right">\$ 98,700</td> </tr> </table> <p>Extent of exemption impairment (Check applicable box):</p> <p><input type="checkbox"/> <b>Line f is equal to or greater than line a.</b> The entire lien is avoided. (Do not complete the next column.)</p> <p><input checked="" type="checkbox"/> <b>Line f is less than line a.</b> A portion of the lien is avoided. (Complete the next column.)</p>	a. Amount of lien	\$112,400	b. Amount of all other liens (\$180,000 (1st) + \$80,300 (2nd))	\$260,300	c. Value of claimed exemptions	+ \$ 6,000	d. Total of adding lines a, b, and c	\$378,700	e. Value of debtor(s)' interest in property	- \$280,000	f. Subtract line e from line d.	\$ 98,700	<p><b>Treatment of remaining secured claim</b></p> <p><b>Amount of secured claim after avoidance (line a minus line f)</b> \$ <u>13,700</u> (\$112,400 minus \$98,700)</p> <p><b>Interest rate</b> (if applicable) (intentionally left blank)%</p> <p><b>Monthly payment on secured claim</b> \$(intentionally left blank)</p> <p><b>Estimated total payments on secured claim</b> \$(intentionally left blank)</p>
a. Amount of lien	\$112,400													
b. Amount of all other liens (\$180,000 (1st) + \$80,300 (2nd))	\$260,300													
c. Value of claimed exemptions	+ \$ 6,000													
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e. Value of debtor(s)' interest in property	- \$280,000													
f. Subtract line e from line d.	\$ 98,700													

The calculation strictly follows the statutory formula of counting “all other liens,” including consensual liens that are junior to the judicial lien.<sup>8</sup>

### Example

To better comprehend the power of section 522(f), compare how proceeds from a hypothetical sale of the property would be distributed under nonbankruptcy law in a “first-in-time, first-in-right” jurisdiction with the distribution scheme after avoiding a judicial lien under § 522(f):

	<b>Distribution of sales proceeds (\$280,000)</b>	
	<b><u>Without § 522(f)</u></b>	<b><u>With § 522(f)</u></b>
1st mortgage (\$180,000)	\$180,000	\$180,000
Judgment lien (\$112,400)	\$100,000	\$ 13,700
2nd mortgage (\$80,300)	\$ 0	\$ 80,300
Debtor (\$6,000 exemption)	\$ 0	\$ 6,000

Section 522(f) thus allows the debtor to carve his/her exemption out of the judicial lien while leaving intact the consensual liens against the property. The tool provided by the national plan enables the debtor's attorney to do the carving without requiring much math.

*The authors understand that the calculator found in section 3.4 of the national plan was the creation of John Rao, of the National Consumer Law Center, and we gratefully acknowledge his contribution.*

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<sup>1</sup> Fed. R. Bankr. P. 4003(d) (amended, eff. Dec. 1, 2017).

<sup>2</sup> The § 522(f) tool may also be used in determining the extent to which a nonpossessory, nonpurchase money security interest in household goods impairs an exemption and is avoidable, but it is more beneficial in the avoidance of judicial liens on property subject to other liens as well.

<sup>3</sup> 11 U.S.C. § 522(f)(1)(A); *see generally* Brown, Ahern, and MacLean, West’s Bankruptcy Exemption Manual §§ 6.1-6.2 (Thompson Reuters 2017).

<sup>4</sup> 11 U.S.C. § 522(f)(2)(A).

<sup>5</sup> [See Part III of this series](#), in which we discussed the procedure established by amended Rule 3012 for the determination of the value of a secured claim under section 506 of the Code, which requires only a motion, an objection, or (for non-governmental creditors) a plan. As we discussed, whether this amendment will resolve the debate over whether a complaint is required to strip off a lien is unclear.

<sup>6</sup> The Official Form for chapter 13 plans, the requirements in new Rule 3015.1 for local form chapter 13 plans, and the amended rules relating to confirmation will be discussed in a future article in this series.

<sup>7</sup> Assume the debtor is the sole owner of the property in fee simple. The avoidance of liens on jointly owned property may involve an analysis of the extent of the debtor’s property rights under state law. *See, e.g., In re Brinley*, 403 F.3d 415 (6th Cir. 2005) (holding full value of property is used in § 522(f) analysis, where debtor owned property jointly with non-filing spouse as tenants by entirety).

<sup>8</sup> *See In re Kolich*, 328 F.3d 406 (8th Cir. 2003); *In re Brinley*, 403 F.3d 415 (6th Cir. 2005).