CONSUMER BANKRUPTCY

Some Abstract Companies Don't Know Bankruptcy Law

Non-lien judgments are totally discharged in bankruptcy

By Craig D. Robins

Every other year or so I get a frantic phone call from a former bankruptcy client or their real estate attorney, saying that there is a crisis because they are about to go to closing on the purchase or sale of real estate, and a judgment search yielded an old judgment that must be satisfied, even though the judgment creditor was scheduled in the bankruptcy case.

I just got off the phone with the frantic real estate attorney for one such former Chapter 7 client. He said, "The client inherited some property over a year after the bankruptcy was concluded and we've scheduled a closing to sell it – but the abstract company won't let us close until we remove the judgment of record."

What's wrong with this story? As long as the debt was scheduled in the bankruptcy, no further work is necessary!

Putting this situation into other words, here is the typical scenario. A consumer debtor files for bankruptcy. The debtor has a judgment against him which is properly scheduled in the bankruptcy petition. The debtor does not have any real estate at the time the bankruptcy is filed. The debtor receives a discharge. The debtor acquires property thereafter.

What happens to the judgment? The obligation to pay the judgment is discharged. It is forever eliminated. The fact that the creditor obtained a judgment does not give the creditor any greater rights — even if they recorded the judgment with the County Clerk. Bankruptcy Code § 524 provides that a discharge, "voids any judgment at any time obtained, to the extent that such judgment is a determination of the personal liability of the debtor with respect to any debt discharged..." (Section 524(a)(1)).

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The judgment can never became a lien on property the debtor later acquires because the judgment can only become a lien if it attached to property prior to the bankruptcy. Here, the debtor did not own any property at the time the judgment was entered against her, and she did not own any property at the time she filed for bankruptcy. Thus, the judgment never attached to any real estate.

The judgment nevertheless remains on record with the County Clerk because it is a valid court document. However, it no longer has any effect after the bankruptcy court grants a discharge. Some non-bankruptcy attorneys erroneously believe that an additional step is necessary to remove the judgment from the judgment roll at the County Clerk.

I explained to the client's real estate attorney (an old-timer who admitted he did not know anything about bankruptcy) that the abstract company was incorrect with their position that the judgment lien required attention.

> **"If you are dealing with an abstract company that is giving you a hard time, insist that they clear the matter with the title insurance company."**

It seems that a reader at the Abstract Company inexplicably did not know the law, and told the real estate attorney that the judgment had to be removed. This was grossly incorrect. Since the debt that was the subject of the judgment was discharged at the time the debtor emerged from bankruptcy, the judgment could never attach to any subsequently obtained real estate. Thus, the judgment could not become a judgment lien when the debtor later inherited title to the property.

The real estate attorney, now knowing how bankruptcy law worked after I explained it to him, was able to resolve the problem, although the abstract company did call me to request a copy of the Schedule of Creditors to make sure the debt was listed.

The United States Supreme Court has recognized that judgments which have been discharged in bankruptcy may not be kept "alive for the purpose of permitting the creation of an enforceable lien upon a subject not existent when the bankruptcy became effective." *Local Loan Co. v. Hunt*, 292 U.S. 234, 343 (1934). Put simply, judgment liens do not attach to a defendant's after acquired real property. *Bank of New York v. Nies*, 96 A.D.2d 166; 468 N.Y.S.2d 278; 1983 N.Y.App.Div Lexis 20313.

Please note that dealing with judgment liens as indicated above only applies when the debtor did not own any real estate at the time the debtor filed for bankruptcy relief. If the debtor did own real estate, then the obligation to pay the judgment is discharged, but the lien remains.

Here's why some practitioners are confused about judgments. New York Debtor and Creditor Law § 150 (1) states that "At any time after one year has elapsed since a debtor in bankruptcy was discharged from his debts, the debtor may apply, upon proof of the debtor's discharge, to the court in which a judgment was rendered against him, for an order, directing that a discharge be marked upon the docket of the judgment." [edited for clarity].

Some attorneys think that since a debtor can have a judgment marked "discharged" by the County Clerk pursuant to D&C § 150, doing so is necessary. However, that is not true. Federal bankruptcy law clearly discharges the obligation to pay the judgment. Although a debtor can go to the extraordinary length to have the County Clerk officially mark the judgment as "discharged," this is not necessary, and I have never heard of this ever being done.

D&C § 150 is an antiquated and misunderstood statute that has relatively little application in state court proceedings and can often cause confusion. Any situation requiring removal of a judgment lien in a bankruptcy proceeding, when appropriate, is best done by bringing the application in bankruptcy court pursuant to the Bankruptcy Code, rather than state court, pursuant to D&C § 150. This is because bankruptcy judges are very familiar with the issues involved, and the Bankruptcy Code provisions are relatively straight forward in this area.

In taking a quick look at some New York cases that referenced D&C § 150, I was amazed to see a decision issued just last year from a respected Supreme Court judge who totally misunderstood the application of D&C § 150. In that case, the Supreme Court had issued a judgment against two individuals on a pre-petition debt half a year after they filed their bankruptcy petitions. Thus, the judgment was in violation of the automatic stay pursuant to Bankruptcy Code § 362(a).

The debtors' state court attorney filed a motion to remove the judgment and the court granted that motion citing D&C § 150. The outcome was sort of correct (the judgment should have been removed), but the judge incorrectly supported his decision with a statute that had nothing to do with the situation. Actually, a motion was not even necessary.

When the Supreme Court entered the judgment post-petition, it was an inadvertent violation of the automatic bankruptcy stay. It appears that none of the parties advised the court that the two

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individuals had sought bankruptcy relief. It is a well-settled law that any order entered in violation of the stay is void and not voidable. The attorneys who represented the plaintiff should have advised the court that the judgment was improperly issued against the debtors. No motion was necessary.

Practical Tips: Abstract companies often do not know bankruptcy law. However, the title policies that they prepare are underwritten by the major title insurance companies. These title insurance companies have law departments who do know the law. If you are dealing with an abstract company that is giving you a hard time, insist that they clear the matter with the title insurance company.

To demonstrate that a judgment has been discharged, you need only show a title company proof that the bankruptcy was filed after the judgment was entered and proof that the judgment creditor was scheduled in the petition.

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