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CONSUMER BANKRUPTCY

Voiding Pre-2005 Judgment Liens

Debtors May Use Post-2005 Homestead Exemption

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On August 30, 2005, just weeks before the Bankruptcy Code was radically overhauled by the Bankruptcy Amendment Act, the New York Legislature, with absolutely no advance warning, boosted the homestead exemption from \$10,000 to \$50,000 per person.

This was a boon to debtors as it enabled a typical husband and wife filing for bankruptcy relief to protect \$100,000 worth of equity in their home. However, it was the bane of judgment creditors, many of whom stood to lose the total value of their judgment liens.

How Judgment Liens Are Created. If a creditor obtains a judgment in a New York State

Supreme Court proceeding, the judgment automatically becomes a lien on any property held by that judgment debtor in the county where the Supreme Court was located. If a creditor obtains a judgment in a District Court, then in order for that judgment to act as a lien, the creditor must file a transcript of judgment (and pay a filing fee) with the county clerk in the county where the real estate is located.

Judgment Liens Can Be Removed. If a judgment lien impairs a bankruptcy debtor's homestead exemption, the debtor can bring a motion under Bankruptcy Code section 522 (f) to void that part of the judgment that impairs the homestead exemption.

This is a motion commonly brought in bankruptcy proceedings. Usually, creditors do not even oppose such motions.

The Homestead Amendment Causes Judgment Creditors to Develop Novel Defenses. Last year I brought a typical motion to void a judgment lien, relying on the \$50,000 per person homestead exemption created by the 2005 change to the New York Exemption statute. The judgment was about five years old and predated the exemption change.

I was surprised when the creditor sought to object to the motion, claiming that the debtor should only be entitled to use the old

\$10,000 exemption, rather than the newer \$50,000 exemption. (If this was the permitted result, then the judgment would not have impaired the homestead exemption and the lien would have remained.)

The creditor argued an interesting theory that it had a vested property right which could not be altered by the amendment to the law. Fortunately for my client, the Court decided for the debtor and didn't even address this novel defense because the creditor's motion reply papers were improperly submitted.

The Recent *Trudell* Case Prevents Judgment Creditors from Subverting the Exemption Increase on Constitutional Grounds. Just last month, Judge Michael J. Kaplan, sitting in the Bankruptcy Court for the Western District of New York, entertained the exact same argument. *In re Trudell*, W.L. 141775 (Bankr. W.D.N.Y., Jan. 14, 2008.)

The Judge recognized that the increased homestead exemption retroactively applied to debts incurred prior to the 2005 change in the exemption statute. However, the Judge believed that there was still a valid issue to be resolved concerning whether the lien is a "vested property right" that cannot constitutionally be taken away by the August 30, 2005 amendment without addressing concerns under the "takings clause" of the Constitution.

The Judge discussed the concept of retroactivity and commented that "although retroactive statutes are not specifically prohibited by either the Federal or the New York State Constitution, a retroactive statute may nevertheless be held to violate constitutional provisions of general applicability, such as the proscription of legislation impairing vested rights without due process, or the obligation of contracts."

The Judge continued with his discussion by suggesting that it was not necessary for him to even address such elusive concepts of when "rights" and "interests" become vested because New York's highest Court addressed the question of when a "judgment lien" upon real estate becomes vested, citing a case from 1872.

The Judge concluded that "what the Legislature gave to holders of judgment liens, the Legislature may take away prior to sale or other satisfaction of the judgment lien."

Accordingly, the Court held that the fact that the judgment lien was filed before the enactment of the increase in homestead exemption from \$10,000 to \$50,000 does not affect the Debtor's right to claim the \$50,000 exemption in order to accomplish the avoidance of the judgment lien. Victory for the debtor.

Editor's Note: (revised 2008):
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