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U.S. BKCY. APP. PANEL
OF THE NINTH CIRCUIT

ORDERED PUBLISHED

**UNITED STATES BANKRUPTCY APPELLATE PANEL
OF THE NINTH CIRCUIT**

6	In re:)	BAP No.	CC-06-1135-KMoB
)		
7	STEPHEN LOUIS MEYER,)	Bk. No.	SA 05-16733-JB
)		
8	Debtor.)		
)		
9	_____)		
)		
10	ALL POINTS CAPITAL CORP.,)		
)		
11	Appellant,)		
)		
12	v.)	OPINION	
)		
13	STEPHEN LOUIS MEYER,)		
)		
14	Appellee.)		
)		
15	_____)		

Argued and Submitted on November 15, 2006
at Orange, California

Filed - July 13, 2007

Appeal from the United States Bankruptcy Court
for the Central District of California

Honorable James N. Barr, Bankruptcy Judge, Presiding

Before: KLEIN, MONTALI, and BRANDT, Bankruptcy Judges.

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1 KLEIN, Bankruptcy Judge:

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3 The bankruptcy court avoided two judgment liens under 11
4 U.S.C. § 522(f) as impairing the debtor's exemption in co-owned
5 real estate. Appellant wants the court's order avoiding the
6 senior \$275,000 lien to remain intact on a default theory but
7 wants it reversed as to its own junior lien on the theory the
8 court ignored \$91,497.50 of nonexempt equity to which judgment
9 liens can remain attached after bankruptcy.

10 We agree there is nonexempt equity to which judgment liens
11 may remain attached. Construing § 522(f)(2), which has not been
12 amended since 1994,¹ to avoid an absurd result in the case of co-
13 owned property, we hold that consensual liens against the entire
14 fee must be netted out before computing the value of a debtor's
15 fractional interest for purposes of avoiding judgment liens on
16 which the co-owner is not liable.

17 Appellant's theory for exploiting default to squeeze out the
18 senior lien offends the rule that multiple liens impairing
19 exemptions be avoided in order of reverse priority and offends
20 the rule that default judgments should not be entered when they
21 are not warranted on the merits.

22 As the record is confused by procedural issues and lack of
23 findings, we VACATE and REMAND.

24
25 _____
26 ¹ Section 522(f)(2) was not amended by the Bankruptcy Abuse
27 Prevention and Consumer Protection Act of 2005, Pub. L. 109-8,
119 Stat. 23.

1 The debtor argued that § 522(f)(2) analysis should be done
2 lien by lien in reverse order, beginning with All Points' junior
3 lien. Comparing that lien with the sum of senior liens and the
4 exemption, \$557,005 (= \$232,005 mortgage + \$50,000 exemption +
5 \$275,000 American Capital judicial lien), the \$515,000 value of
6 the property meant that the All Points lien impaired the \$50,000
7 exemption and was avoidable in full.

8 All Points contended that the senior \$275,000 American
9 Capital lien should be first avoided by default and excluded from
10 the analysis. Under its theory, excluding the senior lien and
11 not adjusting equity to reflect the value of the debtor's one-
12 half interest until after the \$232,005 consensual lien is netted
13 out, there would be equity of \$282,995 (= \$515,000 - 232,005) for
14 all owners, the debtor's half of which would be \$141,497.50.
15 Deducting a \$50,000 homestead exemption would yield \$91,497.50
16 that could survive § 522(f)(2) lien avoidance.

17 The court granted the lien avoidance motion in its entirety,
18 without making findings of fact and conclusions of law
19 articulating its reasoning about the statutory formula.

20 The court's conclusion would follow if it read the statute
21 mechanically by focusing on the phrase "value that the debtor's
22 interest would have in the absence of any liens" in § 522(f)(2)
23 and comparing the sum of the \$232,005 consensual lien and the
24 \$50,000 exemption with the \$257,500 value of the debtor's one-
25 half interest in the property, instead of the \$515,000 full value
26 of the property.

27 The avoidance of the senior American Capital lien has an
28 added mystery. No default was entered. Nor did the court

1 indicate that it would enter judgment by default. As there were
2 no findings, we presume that the court was concluding that there
3 was no nonexempt equity for any judicial lien.

4 All Points appealed.

6 JURISDICTION

7 Federal subject-matter jurisdiction over this core
8 proceeding under 28 U.S.C. § 157(b)(2)(K) was founded upon 28
9 U.S.C. § 1334. We have jurisdiction under 28 U.S.C. § 158(a)(1).

11 ISSUES

12 1. Whether a partially-avoidable senior judicial lien may
13 be avoided when the lienholder does not appear in contest of a
14 lien avoidance motion under § 522(f)(1).

15 2. Whether § 522(f)(2) requires that liens against the
16 entire fee be subtracted before computing the value of the
17 debtor's interest in co-owned property.

19 STANDARD OF REVIEW

20 Application of basic rules of procedure and construction of
21 the Bankruptcy Code present questions of law that we review de
22 novo. Ruvacalba v. Munoz (In re Munoz), 287 B.R. 546, 550 (9th
23 Cir. BAP 2002).

25 DISCUSSION

26 Before explaining why the debtor has nonexempt equity in his
27 co-owned residence, we focus on why the senior judicial lien
28 could not be avoided in full on a theory of default.

I

Two procedural flaws infect appellant's theory that the senior judicial lien should remain avoided under the 1994 amendments to § 522(f). Lien avoidance is done on a reverse priority basis as a contested matter in which the default requirements of Federal Rule of Civil Procedure 55 apply. Fed. R. Civ. P. 55, incorporated by Fed. R. Bankr. P. 7055 & 9014. Those default rules do not permit entry of judgments that are not warranted on the merits.

A

Otherwise valid judicial liens that are being avoided under § 522(f) as impairing exemptions are deducted in reverse order of priority. This is law of the circuit. Bank of Am. Nat'l Trust & Sav. Ass'n v. Hanger (In re Hanger), 196 F.3d 1292 (9th Cir. 1999), aff'g & adopting, 217 B.R. 592, 595 (9th Cir. BAP 1997).

This reverse priority rule is a corollary to the requirement in the § 522(f)(2)(A) statutory formula that liens be assessed for avoidance on a lien-by-lien basis and has the consequence of giving effect to the priority rules of applicable nonbankruptcy law. 11 U.S.C. § 522(f)(2)(A).³

This reverse priority approach is important because it

³ The statutory exemption-impairment formula is:

(A) For the purposes of this subsection, 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 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.

11 U.S.C. § 522(f)(2)(A) (emphasis supplied).

1 introduces an element of order to the provision of § 522(f)(2)(B)
2 that liens already avoided are excluded from the exemption-
3 impairment calculation with respect to other liens. 11 U.S.C.
4 § 522(f)(2)(B).⁴

5 Without an ordering rule that specifies the order in which
6 judicial liens are to be removed under § 522(f), dysfunction
7 could reign. Junior lienors could plot, perhaps in collusion
8 with debtors who may have an incentive to preserve a junior
9 judicial lien in favor of a friend or relation, to leapfrog or
10 squeeze out senior lienors, applicable nonbankruptcy law
11 notwithstanding. By requiring liens to be attacked in reverse
12 order of priority, the priority rules of applicable nonbankruptcy
13 law are honored and opportunities for gamesmanship are reduced.

14 It is literally impossible for both elements of the
15 operating rule for implementing the § 522(f)(2) equation –
16 reverse priority and ignoring liens previously avoided – to apply
17 if one begins with a lien that is supported by some amount of
18 nonexempt equity. Instead, one must approach lien avoidance from
19 the back of the line, or at least some point far enough back in
20 line that there is no nonexempt equity in sight. As an economist
21 would say, judicial liens are avoided in reverse order until the
22 marginal lien, i.e. the junior lien supported in part by equity,
23 is reached.

24
25 ⁴ The provision is:

26 (B) In the case of a property subject to more than 1 lien, a
27 lien that has been avoided shall not be considered in making
28 the calculation under subparagraph (A) with respect to other
liens.

11 U.S.C. § 522(f)(2)(B).

1 By avoiding both liens, the bankruptcy court implicitly
2 concluded that there was no equity to support any judicial lien.
3 For the reasons we shall explain later, that was error.

4
5 B

6 All Points' contention that American Capital must be
7 eliminated on a default theory is flawed.

8 The record does not reflect that default was entered against
9 American Capital, notwithstanding that it did not respond to the
10 motion. Without an entry of default, it is not permissible to
11 proceed to the second step and enter default judgment.

12 All Points nevertheless would have us assume that a default
13 that does not appear in the record was entered and then equate
14 the phantom default with a default judgment in order to squeeze
15 out American Capital. Although the absence of an entered default
16 ought to end the analysis, we will also (in light of our decision
17 to vacate and remand) explain why the rest of All Points' theory
18 runs afoul of bedrock propositions of default judgment law.

19 First, it is black-letter law that entry of default does not
20 entitle a plaintiff to judgment as a matter of right or as a
21 matter of law. Fed. R. Civ. P. 55(b)(2), incorporated by Fed. R.
22 Bankr. P. 7055 & 9014; 10 JAMES WM. MOORE ET AL., MOORE'S FEDERAL
23 PRACTICE § 55.20[2][b] (3d ed. 2006) ("not entitled to default
24 judgment as a matter of right"); 10A CHARLES ALAN WRIGHT ET AL.,
25 FEDERAL PRACTICE AND PROCEDURE § 2685 (3d ed. 1998) ("not entitled to a
26 default judgment as of right").

27 Settled precedent establishes that default judgment is a
28 matter of discretion in which the court is entitled to consider,

1 among other things, the merits of the substantive claim, the
2 sufficiency of the complaint, the possibility of a dispute
3 regarding material facts, whether the default was due to
4 excusable neglect, and the "strong policy" favoring decisions on
5 the merits. E.g., Eitel v. McCool, 782 F.2d 1470, 1471-72 (9th
6 Cir. 1986) (citing MOORE'S FEDERAL PRACTICE).

7 Default judgments are disfavored because cases should be
8 decided on their merits whenever reasonably possible. Id.; Pena
9 v. Seguros La Comercial, S.A., 770 F.2d 811, 814 (9th Cir. 1985).

10 Our own precedents recognize that default judgments are the
11 result of a two-step process – entry of default and then judgment
12 by default – designed to assure that the plaintiff is entitled to
13 the relief requested. If the plaintiff is not entitled to the
14 relief requested, the court should not enter default judgment and
15 may even enter judgment in favor of the defaulted defendant.
16 Cashco Fin. Servs., Inc. v. McGee (In re McGee), 359 B.R. 764,
17 771-72 (9th Cir. BAP 2006); Wells Fargo Bank v. Beltran (In re
18 Beltran), 182 B.R. 820, 823-24 (9th Cir. BAP 1995). That
19 situation exists here: the debtor is not entitled to a default
20 judgment on the merits.

21 22 II

23 Addressing the problem of how to calculate § 522(f)
24 impairment when property is co-owned begins with the language of
25 the statute.

26 Section 522(f)(1)(A) provides in relevant part: "the debtor
27 may avoid the fixing of a lien on an interest of the debtor in
28 property to the extent that such lien impairs an exemption to

1 which the debtor would have been entitled . . . if such lien is
2 (A) a judicial lien." 11 U.S.C. § 522(f)(1)(A) (emphasis
3 supplied).

4 Section 522(f)(2) prescribes a formula for calculating
5 whether an exemption is impaired:

6 (2)(A) For the purposes of this subsection, a lien shall be
7 considered to impair an exemption to the extent that the sum
of --

8 (i) the lien;

9 (ii) all other liens on the property; and

10 (iii) the amount of the exemption that the debtor could
claim if there were no liens on the property;

11 exceeds the value that the debtor's interest in the property
12 would have in the absence of any liens.

13 (B) In the case of a property subject to more than 1 lien, a
14 lien that has been avoided shall not be considered in making
15 the calculation under subparagraph (A) with respect to other
16 liens.

17 (C) This paragraph shall not apply with respect to a
18 judgment arising out of a mortgage foreclosure.

19 11 U.S.C. § 522(f)(2) (emphasis supplied). That is, an exemption
20 is impaired if subtracting all of the unavoidable liens and the
21 exemption (totaling \$282,005) from the value of the debtor's half
22 interest (\$257,500) yields zero or less.

23 The difficulty centers around the operation of the phrase
24 "value that the debtor's interest in the property would have in
25 the absence of any liens" in § 522(f)(2)(A)(iii) when the debtor
26 has only a fractional interest in property. In the instance of
27 single-owner property, there is no problem because the phrase
28 refers to the maximum exemption that is available to the debtor
and nothing in excess of that amount.

But in the case of fractionally-owned property, the outcome
depends upon whether one subtracts all liens against the entire
fee before addressing the value in the absence of any liens. If
all consensual liens against the entire fee are netted out first,

1 then the answer is the same as in the single-owner case. If,
2 however, one does not first net out the consensual liens against
3 the entire fee and applies the literal terms of the statutory
4 formula, then the result could be that judicial liens are avoided
5 that do not impair an exemption.

6 Under facts of this appeal, it is the difference between
7 avoiding judicial liens only to the extent that they leave the
8 \$50,000 exemption to the debtor and avoiding an extra \$91,497.50
9 worth of judicial liens.

10 Thus, the strict or mechanical approach to applying the
11 statutory formula, which has the advantage of conforming to the
12 letter of § 522(f)(2)(A)(iii), would result in avoiding more
13 judicial liens than the minimum necessary to assure the debtor
14 the maximum available homestead when the debtor owns only half
15 the property.

16 Such a result appears to be at odds with what Congress
17 intended, which was to overrule judicial decisions that all had
18 the consequence of frustrating a debtor's ability to receive the
19 full exemption authorized by law. H.R. Rep. No. 103-835, 52-54,
20 reprinted in 1994 U.S.C.C.A.N. 3340, 3361-63. In the context of
21 co-owned property, which is not discussed in the House Report,
22 Congress overshot its mark.

23 The alternative common-sense application realigns the
24 application of the statutory formula to conform with unambiguous
25 Congressional intent. Under this approach, one nets out
26 consensual liens against the entire fee in co-owned property
27 before determining the value of a debtor's fractional interest
28 and excludes those liens from the calculation of "all other liens

1 on the property" under § 522(f)(2)(A)(ii). As applied in this
2 instance, it would lead to a conclusion that there is \$91,497.50
3 in nonexempt equity to which judgment liens could remain attached
4 after assuring the debtor of his \$50,000 exemption.

5 Although the latter approach has intuitive appeal because it
6 achieves a result consistent with the notion that the debtor is
7 entitled to no more than the exemption, it must be conceded that
8 it requires a generous interpretation of § 522(f)(2) because the
9 precise language of the statute does not ineluctably yield that
10 conclusion. Nor does this approach answer the question of how to
11 deal with judicial liens against the entire fee.

12 Courts are divided between the strict and the common-sense
13 approaches to the § 522(f) question after the 1994 Amendments.

14 Nationally, the majority position, which includes the First,
15 Third, and Eleventh Circuits, rejects mechanical application of
16 the statutory formula in cases where a debtor co-owns property.
17 All three courts of appeal that have addressed the question have
18 concluded that mechanical application of § 522(f)(2)(A) produces
19 a result at odds with the statutory purpose. Nelson v. Scala,
20 192 F.3d 32, 35 (1st Cir. 1999); Miller v. Sul (In re Miller),
21 299 F.3d 183, 186-87 (3d Cir. 2002); Lehman v. VisionSpan, Inc.
22 (In re Lehman), 205 F.3d 1255, 1257 (11th Cir. 2000). These
23 courts either net the total outstanding secured debt balance owed
24 by both co-owners against the entire fee before calculating the
25 value of the debtor's fractional interest in the property or
26 achieve a result that assures that the debtor does not enjoy more
27 than the amount of the available exemption.

28 Our own precedent under the pre-1994 version of § 522(f)

1 applied the same approach by requiring all encumbrances to be
2 deducted before determining the debtor's fractional interest.
3 Wiget v. Nielsen (In re Nielsen), 197 B.R. 665, 670 (9th Cir. BAP
4 1996), cited with approval, Miller, 299 F.3d at 186.

5 A minority of courts apply the statutory formula literally
6 and mechanically by allowing a debtor to deduct the full amount
7 of liens from the proportional interest in the value of the
8 property. E.g., Zeigler Eng'g Sales, Inc. v. Cozad (In re
9 Cozad), 208 B.R. 495 (10th Cir. BAP 1997); In re White, 337 B.R.
10 686 (Bankr. N.D. Cal. 2005).

11 In concrete terms, the choice between the common-sense and
12 the mechanical applications of the statute in situations where
13 property is co-owned is the difference between protecting only
14 the debtor's \$50,000 California exemption from judicial liens or
15 protecting \$141,497.50.

16 We agree with the three courts of appeals to have considered
17 the question that mechanical application of the statutory formula
18 would lead to an absurd result not intended by Congress. Miller,
19 299 F.3d at 187 ("absurd"); Lehman, 205 F.3d at 1257 ("absurd");
20 Nelson, 192 F.3d at 35 ("outcome at odds with the purpose of
21 Congress"). The goal is to achieve a balance between debtor and
22 creditor by assuring that a debtor receives the full exemption
23 permitted by law and that creditors secured by judicial liens do
24 not lose their secured positions in value that is not exempt.

25 Accordingly, we adhere to our view stated in Nielsen, a case
26 interpreting the pre-1994 version of § 522(f), that "it is common
27 sense in bankruptcy in a lien avoidance context that joint
28 encumbrances be deducted from the joint value of the property."

1 Nielsen, 197 B.R. at 671. Hence, nonavoidable encumbrances on
2 co-owned property must be deducted from the total value of the
3 property before a debtor's fractional interest is determined.
4

5 CONCLUSION

6 Since there are no findings of fact and conclusions of law
7 regarding the underlying substantive questions, we VACATE the
8 order avoiding the liens of American Capital and All Points and
9 REMAND for further proceedings consistent with this decision.
10

11
12 KLEIN, Bankruptcy Judge, concurring:

13
14 I join the majority decision and write separately to note
15 the existence of significant issues that may not be essential to
16 the majority decision but that should not be overlooked. First,
17 whether All Points has appellate standing is uncertain. Second,
18 it would be inappropriate for there to be inconsistent decisions
19 as between All Points and American Capital. Finally, there is a
20 due process notice issue regarding the notice to American Capital
21 that needs to be addressed if, on remand, the bankruptcy court
22 contemplates entry of default.
23

24 I

25 In order to have appellate standing, All Points must be
26 "adversely and pecuniarily affected" by the outcome of the
27 appeal. Gilliam v. Speier (In re KRSM Props., LLC), 318 B.R. 712,
28 716 (9th Cir. BAP 2004).

1 Thus, it is an abuse of discretion to enter default
2 judgments that are inconsistent with decisions as to other
3 defendants. Nielson v. Chang (In re First T.D. & Inv., Inc.),
4 253 F.3d 520, 532 (9th Cir. 2001). Such inconsistencies are
5 regarded as “unseemly and absurd.” 10 MOORE’S FEDERAL PRACTICE
6 § 55.25, quoting Frow v. De La Vega, 82 U.S. 552, 554 (1872);
7 accord 10A FEDERAL PRACTICE AND PROCEDURE § 2690 (quoting Frow).

8 In the words of the Ninth Circuit’s recent invocation of the
9 Frow principle in a bankruptcy appeal, it is “incongruous and
10 unfair” for a bankruptcy court to enter a default judgment
11 inconsistent with the merits decision regarding another
12 defendant. First T.D. & Inv., Inc., 253 F.3d at 532-33 (“We
13 therefore hold that the bankruptcy court violated the Frow
14 principle and abused its discretion by entering final default
15 judgments, pursuant to Fed. R. Civ. P. 54(b), that directly
16 contradict its earlier ruling in the same action.”).

17 In this appeal, the analysis is straightforward. Both
18 American Capital and All Points were in the posture of defendants
19 to the motion to avoid lien. Each of the judicial liens exceeds
20 the amount of the \$91,497.50 equity that is argued to be
21 available to support a judicial lien. As the lienor in senior
22 position, the lien of American Capital could not be avoided to
23 the extent it exceeds \$91,497.50 unless it is determined to be no
24 longer valid on the merits. This result would pertain even if
25 American Capital’s default is entered.

26 A default judgment that avoids the American Capital lien
27 merely because of a default, thereby permitting All Points to
28 step into the shoes of American Capital so as to reap the benefit

1 of the \$91,497.50, plainly would violate the Frow principle, be
2 incongruous and unfair, and amount to a windfall.¹

3
4 III

5 There is also a due process notice issue embedded in the
6 facts. This necessitates clarification of one of our precedents
7 in light of the recent Supreme Court decision in Jones v.
8 Flowers, 126 S.Ct. 1708 (2006), which emphasizes the need for
9 "reasonable additional steps" when a property right would be
10 extinguished and there is reason to doubt the efficacy of notice.

11 The lack of response from American Capital to the motion
12 that would extinguish its judgment lien property right may be
13 attributable to confusion resulting from an asymmetry in the
14 interface between the Federal Rules of Bankruptcy Procedure and
15 California law.

16 We have held that notice of a motion to avoid a judicial
17 lien must be served in the same manner as service of a summons
18 and complaint and when served by mail on a corporation pursuant
19 to Federal Rule of Bankruptcy Procedure 7004(b)(3) must be mailed
20 to the attention of an officer, a managing or general agent, or
21 any other agent authorized by appointment or by law to receive
22 service of process. Beneficial Cal., Inv. v. Villar (In re
23 Villar), 317 B.R. 88, 92-94 (9th Cir. BAP 2004).

24
25 ¹ This is a multiple defendant situation, the lienors being
26 the defendants. The Frow principle, however, is powerful enough
27 to encompass lien avoidances that are presented by the
28 alternative procedure of separate motions because the matters are
so interrelated that they should be treated as the equivalent of
a multiple defendant lienor situation. The point of the Frow
principle, as enforced by the Ninth Circuit in Nielson, is that
inconsistent judgments in such matters are not acceptable.

1 In accordance with Villar, the motion to avoid lien was
2 served by mail under Rule 7004(b)(3) directed to "American
3 Capital Resources Inc, Attn Managing Agent, Three University
4 Plaza, Hackensack, NJ 07601." Thus, service appears to have been
5 accomplished on the judgment creditor, American Capital.

6 The quirk of California law that produces the asymmetry is a
7 provision of the California judgment enforcement statute that
8 notices regarding the judgment are not to be sent to the judgment
9 creditor and, instead, must go to the attorney of record who
10 obtained the judgment or that attorney's successor. California
11 Code of Civil Procedure § 684.010 provides in relevant part:

12 when a notice, order, or other paper is required to be
13 served under this title [Title 9 Enforcement of Judgments]
14 on the judgment creditor, it shall be served on the judgment
creditor's attorney of record rather than on the judgment
creditor if the judgment creditor has an attorney of record.

15 Cal. Code Civ. Pro. § 684.010 (emphasis supplied).²

16
17 ² This provision is complemented by California Code of
18 Civil Procedure §§ 283, 284, and 285 which eliminate ambiguity
19 about counsel's post-judgment authority:

20 An attorney and counselor shall have authority: ... 2. To
21 receive money claimed by his client in an action or
22 proceeding during the pendency thereof, or after judgment,
unless a revocation of this authority is filed, and upon the
payment thereof, and not otherwise, to discharge the claim
or acknowledge satisfaction of the judgment.

23 Cal. Code Civ. Pro. § 283 (emphasis supplied).

24 The attorney in an action or special proceeding may be
25 changed at any time before or after judgment or final
26 determination, as follows: 1. Upon the consent of both
27 client and attorney, filed with the clerk, or entered upon
28 the minutes; 2. Upon the order of the court, upon the
application of either client or attorney, after notice from
one to the other.

Cal. Code Civ. Pro. § 284 (emphasis supplied).

(continued...)

1 Thus, service regarding California judgment enforcement
2 matters must be directed to the counsel who obtained the judgment
3 and not to the judgment creditor. It follows, that a California
4 judgment creditor who receives a notice that must be sent to
5 counsel may reasonably think that the notice can be ignored as
6 either redundant of service on counsel or ineffective.

7 To be sure, the avoidance of a judgment lien pursuant to the
8 Bankruptcy Code is not a state enforcement of judgment matter,
9 even though it implicates the ultimate enforceability of the
10 judgment. That is, however, a fine distinction that invites
11 confusion and could operate as a trap for the unwary.³

12 In Jones, the Supreme Court reiterated that due process
13 requires "notice reasonably calculated under all the
14 circumstances, to apprise interested parties of the pendency of
15 the action and afford them an opportunity to present their
16 objections." Jones, 126 S.Ct. at 1713-14, quoting Mullane v.
17 Cent. Hanover Bank & Trust Co., 339 U.S. 306, 314 (1950). The

18
19 ²(...continued)

20 When an attorney is changed, as provided in the last
21 section, written notice of the change and of the
22 substitution of a new attorney, or of the appearance of the
party in person, must be given to the adverse party. Until
then he must recognize the former attorney.

23 Cal. Code Civ. Pro. § 285.

24 ³ Villar did not address Cal. Code of Civ. Proc. § 684.010
25 and did not consider whether service in accordance with it would
26 qualify as service under Fed. R. Bankr. P. 7004(a) by virtue of
27 its incorporation of Fed. R. Civ. P. 4(h), which recognizes (by
cross-reference to Rule 4(e)(1)) service "pursuant to the law of
28 the state in which the district court is located, or in which
service is effected." Fed. R. Civ. P. 4(e)(1) & (h),
incorporated by Fed. R. Bankr. P. 7004(a)(1). We need not reach
the question because there was no service in this case on
American Capital that purported to comply with § 684.010.

1 notice that is required "will vary with the circumstances and
2 conditions." Jones, 126 S.Ct. at 1714, quoting Walker v. City of
3 Hutchinson, 352 U.S. 112, 115 (1956).

4 If there is reason to think that notice may not have been
5 effective, then "additional reasonable steps" may be needed "if
6 practicable to do so." Jones, 126 S.Ct. at 1718.

7 In the face of the confusion that results from the seemingly
8 contradictory requirements of Villar and of § 684.010, the
9 solution is to require the "additional reasonable step" of giving
10 notice of a motion to avoid a California judgment lien to the
11 attorney of record who is responsible for enforcing the judgment.
12 The reality is that, in view of the attorney of record's
13 continuing obligations under California statute with respect to
14 recorded judgments, notice to the attorney may be more likely to
15 elicit response than service on the judgment creditor.

16 This reality is confirmed by the fact that the actual
17 contest of the lien avoidance motion came from All Points, which
18 was not served in the manner required by Villar. Rather, the
19 debtor's counsel served All Points' attorney of record in the
20 manner of § 684.010.

21 It is odd that the debtor's bankruptcy counsel, having
22 served the lien avoidance motion on All Points' counsel in the
23 manner of § 684.010, but not on All Points separately in the
24 manner of Villar,⁴ would not also have served American Capital's
25
26

27 ⁴ The service address, taken from the All Points Abstract
28 of Judgment, was: "All Points Capital, c/o Scott Schutzman,
Esq., 3700 S Susan Street #120, Santa Ana, CA 92704)."

1 counsel in the same manner.⁵ Excluding American Capital's
2 counsel from the loop is even odder because debtor's bankruptcy
3 counsel is named as the judgment debtor's counsel of record on
4 the face of American Capital's Abstract of Judgment; he knew the
5 identity of American Capital's counsel and, as demonstrated by
6 the manner in which he served All Points, he believed it was
7 appropriate to serve counsel. Oddities like these cause me to
8 worry about sandbags.

9 It is apparent that the better practice for bankruptcy
10 judicial lien avoidance motions in any state is to serve both the
11 judgment creditor and the attorney of record. In California, the
12 apparent asymmetry created by § 684.010 warrants requiring that
13 the attorney of record be served as an "additional reasonable
14 step" that is "practicable" within the meaning of Jones in order
15 to assure that the essential principle of notice reasonably
16 calculated to come to the attention of the target is honored.

17 In short, on remand, the bankruptcy court should assure
18 itself that notice consistent with due process in light of Jones
19 was provided to American Capital before proceeding.
20
21
22
23
24

25 ⁵ The address on American Capital's Abstract of Judgment
26 is: "American Capital Resources, Inc., a subsidiary of Unicapital
27 Corporation, a Delaware corporation, c/o Ivanjack & Lambirth,
28 LLP, 500 S. Grand Ave., 21st Fl., Los Angeles, CA 90071-0904."
And it shows the counsel who prepared document as: "Thomas B.
Shuck - SBN 116228, Ivanjack & Lambirth, LLP, 500 S. Grand Ave.,
21st Floor, Los Angeles, CA 90071-0904."

1 MONTALI, Bankruptcy Judge, concurring and dissenting:
2

3 I concur with the opinion's analysis in Part II regarding
4 the proper way to apply § 522(f)(2),¹ when a debtor seeks to
5 avoid a judicial lien impairing an exemption in partially owned
6 property. This analysis responds to a situation crying out for
7 resolution in our circuit, namely, how to protect a debtor's
8 exemption, and no more, in the all-too-common joint ownership
9 single debtor situation. However, I believe remand should be a
10 mere formality, as I believe the law compels, and we should
11 direct, entry of an order avoiding the two judicial liens except
12 to the extent of \$91,497.50 in favor of All Points. I also
13 concur with something unspoken by the majority, but questioned by
14 Judge Klein in his concurrence: the notion that All Points has
15 standing to prosecute this appeal.

16 Otherwise I dissent from the opinion and feel obliged to
17 respond to Judge Klein's observations in his concurrence about
18 what he calls inconsistent outcomes and his views about
19 California procedural law. The opinion takes judicial activism
20 to a new level - judicial advocacy - by rewarding American
21 Capital, an absentee litigant who has had not one, but several
22 bites of the apple, and hands it an undeserved partial victory.
23 In doing so it misstates controlling precedent on how courts
24 should deal with multiple liens impairing exemption. Further,
25

26 ¹ Unless otherwise indicated, all chapter, section and rule
27 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1330, and
28 to the Federal Rules of Bankruptcy Procedure, Rules 1001-9036, as
enacted and promulgated prior to the effective date of The
Bankruptcy Abuse Prevention and Consumer Protection Act of 2005,
Pub. L. 109-8, 119 Stat. 23 (Apr. 20, 2005).

1 the concurrence invokes an inapplicable doctrine prohibiting
2 inconsistent outcomes when no one else has. Then it suggests an
3 improper mandatory state-federal service procedure that can only
4 confuse bankruptcy practitioners and bankruptcy judges who are
5 used to well-established and unequivocal federal procedures.

6 **1. Standing**

7 All Points held a judicial lien which the record suggests
8 was valid but for the powerful weapon individual debtors have to
9 avoid judicial liens to the extent that they impair exemptions
10 under Section 522(f)(1).

11 Debtor moved (the "Motion") to avoid All Points' and
12 American Capital's judicial liens because they impaired his
13 claimed exemption in his residence. For reasons known only to
14 American Capital, it did not oppose Debtor's Motion. Maybe the
15 lien had been satisfied by a third party. Maybe American
16 Capital's judgment also created a lien on other property with
17 sufficient value. Maybe American Capital feared the outcome the
18 bankruptcy court reached here and had no economic incentive to
19 fight. Maybe American Capital had little hope for a third
20 position lien on a fractional interest of a debtor in Chapter 7
21 bankruptcy. It really does not matter. Regardless of American
22 Capital's reasons, its non-opposition to the Motion left All
23 Points "in the money" to the extent of \$91,497.50 but for the
24 bankruptcy court's ruling. By that ruling All Points' economic
25 interest was adversely and pecuniarily affected. See Fondiller
26 v. Robertson (In re Fondiller), 707 F.2d 441, 443 (9th Cir.
27 1983). A "person aggrieved" is one who is "directly and
28 adversely affected pecuniarily by an order of the bankruptcy

1 court." Id. at 442. The order "must diminish the appellant's
2 property, increase its burdens, or detrimentally affects its
3 rights." Duckor Spradling & Metzger v. Baum Trust (In re
4 P.R.T.C., Inc.), 177 F.3d 774, 777 (9th Cir. 1999). The order
5 stripped both judicial liens and American Capital did not appeal.
6 All Points had standing to defend the Motion and to prosecute
7 this appeal.²

8 **2. Rewarding The Absent Party**

9 The law of the Ninth Circuit prescribes that when
10 calculating exemption impairment, liens are to be "subtracted in
11 order of reverse priority and that those which are avoided not be
12 included in the calculation."³ Bank of Am. Nat'l Trust & Sav.
13 Ass'n v. Hanger (In re Hanger), 217 B.R. 592, 595 (9th Cir. BAP
14 1997), aff'd, 196 F.3d 1292 (9th Cir. 1999) (emphasis added).
15 This approach is consistent with section 522(f)(2)(B), which
16 provides that liens that have been avoided are not included in
17 the calculation of other liens. Id.; 11 U.S.C. § 522(f)(2)(B).

18 Ordinarily, when a debtor seeks to avoid more than one
19 judicial lien at the same time under section 522(f), the liens
20 are to be "subtracted in order of reverse priority." Id. Thus,
21 if American Capital had opposed Debtor's Motion, the court would
22 have avoided any junior liens (viz. the lien of All Points)

24 ² The opinion's concerns about dysfunction reigning and
25 debtors colluding with junior lienors is nothing more than
26 speculation. The bankruptcy court has many tools in its toolbox
27 of remedies to deal with such nefarious conduct. No such conduct
is present here.

28 ³ The opinion cites this same phrase from Hanger;
regrettably, it does not address the critical words after "and".

1 before determining whether the American Capital lien impaired the
2 Debtor's exemption.

3 Here American Capital, properly served, did not oppose
4 Debtor's Motion and its lien was effectively avoided by default
5 at the same time the court was considering whether to avoid All
6 Points' lien over its objection.⁴ That the order was actually
7 entered later is of no consequence; the court was obligated not
8 to consider the avoided lien under section 522(f)(2)(B). That
9 portion of the order is final as to American Capital, and should
10 not be disturbed on appeal. Thus, under Hanger, the avoided
11 American Capital lien should not be included in the section
12 522(f)(2) calculation vis-a-vis All Points.

13 As that case points out the purpose of section 522(f) is not
14 to avoid all liens, but simply to protect a debtor's exemption.
15 Simply avoiding the lien of the American Capital and deleting it
16 from the All Points' calculation would protect Debtor's exemption
17 in full. It is inaccurate to characterize All Points as
18 "stepping into the shoes" of American Capital. That is a
19 subrogation concept. Here the statute and Hanger instruct that
20 the avoided lien not be counted. We should follow that
21

22
23 ⁴ This is the same result that would follow had Debtor
24 filed two separate, but similar, motions. Had he done so, with
25 the motion directed at American Capital set earlier, there is
26 little doubt that the court would have defaulted American Capital
27 and avoided its lien. See discussion of Local Bankruptcy Rule
28 9013-1 ("LBR 9013-1") of the Central District of California,
infra. When the motion directed at All Points came before the
court, there would be no justification to consider American
Capital's then avoided lien. To reject this same result when
Debtor's counsel filed the Motion directed at two respondents
elevates form over substance and punishes effective and efficient
lawyering.

1 instruction here. The opinion's result rewards American Capital
2 for its silence at the bankruptcy court and before us by
3 restoring its lien position ahead of All Points. The suggestion
4 that All Points can acquire American Capital's position is hardly
5 a comfort to it.

6 **3. The Default**

7 Part I-B of the opinion suggests that the two-step process
8 for entry of default judgments in adversary proceedings under
9 Rule 7055 (incorporating Fed. R. Civ. P. 55) applies to the
10 Motion. I disagree. Rule 9014 provides that "unless the court
11 directs otherwise," Rule 7055 applies in contested matters. In
12 other words, if a bankruptcy court has established local rules
13 for obtaining an order by default in a contested matter, those
14 rules (and not the "black-letter" law two-step default process of
15 Rule 7055) govern.

16 Here, LBR 9013-1 establishes the procedure for obtaining
17 defaults in contested matters and those procedures do not involve
18 a two-step process. Subsection (g)(1)(F) of LBR 9013-1
19 specifically provides that an order granting a motion to avoid a
20 lien under section 522(f) may be obtained without a hearing
21 unless one is "specifically requested by filing and serving a
22 written response" complying with subsection (a)(7) within fifteen
23 days of service of the notice.⁵ In addition, if the movant wants
24 to set the matter for hearing, LBR 9013-1(a) requires all
25 opposition papers to be filed no later than fourteen days prior
26 to the hearing date and provides that papers "not timely filed

27
28 ⁵ LBR 9013-1(i) reiterates that a section 522(f) motion is
a contested matter and describes what information should be set
forth in the motion and supporting papers.

1 and served may be deemed by the court to be consent to the
2 granting or denial of the motion, as the case may be." LBR 9013-
3 1(a)(7) and (11) (emphasis added). "Failure of any counsel to
4 appear [at the hearing], unless excused by the court in advance,
5 may be deemed consent to a ruling upon the motion adverse to that
6 counsel's position." LBR 9013-1(a)(14).

7 The bankruptcy court, through its local rules, directed a
8 procedure for obtaining default relief on motions to avoid
9 judicial liens pursuant to section 522(f). Consequently, under
10 the language of Rule 9014 itself ("unless the court directs
11 otherwise"), the two-step default procedures of Rule 7055 are
12 inapplicable here. In addition, with one exception in favor of
13 the United States only, I could locate no case involving a
14 contested matter where a preliminary default was entered pursuant
15 to Rule 7055 and followed by a default judgment or order.⁶

16 I therefore believe the opinion is incorrect in intimating,
17 if not outright holding, that unopposed contested matter motions
18 must be disposed of by Rule 7055's two step process, especially
19 where that process is inconsistent with local rules. Such an
20 approach would create an unnecessary step in what is a tried and
21 true well-designed, efficient and expedient system for disposing
22 of routine contested matter motions. Debtor's Motion was one of
23 those routine motions.

24
25 ⁶ Fed. R. Civ. P. 55(e) (and thus Rule 7055) prohibits
26 default judgments against the United States unless the claimant
27 establishes a claim or right to relief by evidence satisfactory
28 to the court. In Gadoury v. United States (In re Gadoury), 187
B.R. 816 (D.R.I. 1995), the court upheld the two-step process on
a debtor's motion against the United States to determine tax
liability.

1 **4. No Inconsistency In Outcomes**

2 The concurrence cites a very old Supreme Court case, Frow v.
3 De la Vega, 82 U.S. 552 (1872), for the unremarkable proposition
4 that a decree of a court sustaining a charge of joint fraud
5 committed by defendants is inconsistent with another decree
6 disaffirming that charge and declaring it to be unfounded. The
7 Supreme Court said "such a result would be unseemly and absurd,
8 as well as unauthorized by law." 82 U.S. at 554. Moving to a
9 more current time, the concurrence cites an application of the
10 Frow doctrine in a bankruptcy setting in Neilson v. Chang (First
11 T.D. & Investment, Inc.), 253 F.3d 520 (9th Cir. 2001). There
12 the Ninth Circuit required that a pure point of law, viz. whether
13 a provision of California law providing a safe harbor for an
14 otherwise unperfected security interest, be applied consistently
15 as to certain answering defendants and other defendants whose
16 defaults had been entered.

17 It is important to note that the parties who invoked the
18 Frow rule were themselves appellants, complaining about the
19 default judgments against them because they were inconsistent
20 with the court's earlier summary judgment in favor of the
21 defendants who invoked the statutory safe harbor.

22 Here, American Capital (not before us) is the beneficiary of
23 the Frow rule. But as the Bankruptcy Court's analysis and the
24 opinion's interpretation of the applicable substantive law both
25 demonstrate, the relative positions of American Capital and All
26 Points versus the Debtor here involved mixed questions of law and
27 fact, turning on specific valuations and interests and unsettled
28 principles of law dealing with lien avoidance on fractional

1 interests in jointly owned property. More importantly, the
2 bankruptcy court here was completely consistent in its
3 disposition, avoiding both judicial liens for the same reason.
4 Thus, not only does the Frow doctrine not apply, but the
5 invocation of it in favor of a nonparty to this appeal is
6 unjustified. There is no intimation anywhere that an incorrect
7 decision such as the Bankruptcy Court made in T&D Investment was
8 void ab initio requiring an appellate court to examine the
9 propriety of the outcome sua sponte. It is for American Capital,
10 and no one else, to raise this issue; otherwise it has been
11 waived and should not be raised now.

12 **5. Inapplicable California Rules of Procedure**

13 I also disagree with the concurrence's inference that
14 American Capital could obtain relief from its default based upon
15 an expectation that its California attorney would be served in
16 accordance with inapplicable state law procedures that have
17 nothing to do with avoidance of liens that impair homestead
18 exemptions. We have nothing but speculation as to whether or how
19 American Capital was misled. Where is this expectation in the
20 record?

21 The concurrence reluctantly acknowledges that Debtor's
22 counsel properly served the Motion on American Capital in
23 accordance with Rule 7004(b)(3) and Beneficial Cal. Inv. v.
24 Villar (In re Villar), 317 B.R. 88 (9th Cir. 2004).⁷ It then
25 presumes, without support, both confusion by state court
26

27
28 ⁷ The record before us reflects that American Capital was properly served with Debtor's Motion, All Points' Response and Objections to Evidence, the Order on Appeal, All Points' Notice of Appeal, and Debtor's Motion for Leave to Appeal.

1 attorneys and American Capital's reasonable ignoring of a federal
2 bankruptcy court motion not served in accordance with state law.
3 Then playing the "due process card" the concurrence infers that
4 there has been a lack of due process to American Capital and
5 argues for a rule that requires compliance with a state rule of
6 procedure notwithstanding Hanna v. Plumer, 380 U.S. 460 (1965)⁸.
7 This is not only misguided based upon the inapplicability of
8 those state court rules, but amounts to a "slippery slope" which
9 can only confuse the issue further about where and when
10 bankruptcy practitioners should follow state law even when they
11 comply with applicable bankruptcy rules.

12 California Code of Civil Procedure § 684.010 requires
13 service of papers under Title 9, Enforcement of Judgments, on the
14 judgment creditors' attorneys of record. Title 9 covers a
15 multitude of subjects, including enforcement of money judgments,
16 enforcement of non-money judgments, third party claims and
17 related procedures, and satisfaction of judgments. There is
18 nothing in Title 9 (or as far as I know anywhere in California
19

20
21 ⁸ In Hanna the Supreme Court upheld the adoption of Federal
22 Rule of Civil Procedure 4(d)(1) to control service of process in
23 diversity cases notwithstanding a state law that required a
24 different method. It noted that to hold that a federal service
25 rule ceases to function when it alters the mode of enforcing
26 state created rights would be to

27
28 "... disembowel either the Constitution's grant of power
29 over federal procedure or Congress' attempt to exercise that
30 power in the Enabling Act." Hanna, 380 U.S. at 473-74
31 (footnote omitted).

32 While the concurrence does not purport to replace Rule 7004 with
33 California Code of Civil Procedure § 684.010, its reliance on
34 California law certainly is inconsistent with Hanna and should be
35 disregarded.

1 law) permitting a judgment debtor to eliminate all or a portion
2 of a judgment lien to the extent it impairs the judgment debtor's
3 exemption. Yet the concurrence urges that federal lien avoidance
4 practice comply with state law service rules that do not
5 encompass lien avoidance. In fact, enforcement of judgments
6 necessarily occurs after an action has been commenced and has
7 gone to judgment. The idea that counsel of record on a judgment
8 must be served is quite sensible, given the state of any
9 particular lawsuit and post-judgment activity. The procedural
10 rule imposed by the California legislature appears to be more a
11 matter of convenience than of fundamental due process. Thus,
12 while a great number of state court procedures embraced within
13 Title 9 require service of papers on counsel, there is no hint
14 that California law must be complied with when a party avails
15 itself of a right found exclusively within the Bankruptcy Code.

16 As previously noted, avoidance of a lien that impairs an
17 exemption is accomplished by the initiation of a contested matter
18 and is governed by Rule 9014. See Rule 4003(d).⁹ Service of
19 motions initiating contested matters is governed by Rule 9014(b),
20 which requires service in accordance with Rule 7004. Effectively
21 it is the commencement of a new matter, called a contested
22 matter, but functionally no different from the initiation of
23 process. While under certain circumstances service in accordance
24 with state rules of procedure is permitted (See Rule 7004(a),
25

26 ⁹ Rule 4003(d) provides as follows:

27 Avoidance by Debtor of Transfers of Exempt Property. A
28 proceeding by the debtor to avoid a lien or other transfer
of property exempt under § 522(f) of the Code shall be by
motion in accordance with Rule 9014.

1 incorporating Federal Rule of Civil Procedure 4(h)), nowhere in
2 federal practice (except in the concurrence) is it required.

3 Apart from the debate of whether inapplicable state rules of
4 procedure are necessary to graft onto well developed federal
5 rules, here the concurrence on its own has decided to render an
6 advisory opinion that somehow under Supreme Court precedent, due
7 process requires compliance with inapplicable state rule of
8 procedure. This is so notwithstanding the fact that no party has
9 raised this matter on appeal, and only American Capital can
10 possibly benefit by this outcome. By no means is this view the
11 holding of this decision.

12 In conclusion, it is error to remand and relieve American
13 Capital of its inattention and punish All Points for its
14 diligence. Neither party asked us to do that, and doing so is
15 gratuitous. We should avoid the anomaly of an aggrieved creditor
16 versus a successful debtor on an appeal resulting in not the
17 creditor winning and the debtor losing (as I would rule) but
18 rather the debtor losing and American Capital winning by being
19 invited back into the battle to have the benefit of All Points'
20 advocacy, perhaps to assure it the benefit of a lien being
21 brought back from the dead. This result is not in response to a
22 Federal Rule of Civil Procedure 60(b) motion but rather this
23 panel's decision that American Capital should be returned to an
24 approximately \$91,000 lien position already avoided by an order
25 that is final as to it. This is inconsistent with Ninth Circuit

1 precedent and is inappropriate.¹⁰ In the highly unlikely event
2 American Capital someday could convince the bankruptcy court that
3 it is entitled to some post-judgment relief, that court would
4 need to address just how to fashion an appropriate remedy. That
5 is not our concern now.

6 We should REVERSE and REMAND in favor of All Points in
7 accordance with the foregoing.

23 ¹⁰ As we observed in another, similar bankruptcy appeal,
24 '[f]ederal courts are not run like a casino game in
25 Investors Thrift v. Lam (In re Lam), 192 F.3d 1309,
26 1311 (9th Cir. 1999). The Bank has forfeited its right
27 to challenge value of the collateral as determined by
28 the bankruptcy court.

Enewally v. Washington Mutual Bank (In re Enewally), 368 F.3d
1165, 1173 (9th Cir. 2004).