UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF WISCONSIN

Cite as: [Unpublished]

Paul Eugene Henderson, Debtor
Bankruptcy Case No. 03-12802-13

United States Bankruptcy Court
W.D. Wisconsin, Madison Division

February 27, 2004

Peter E. Grosskopf, Grosskopf & Black, LLC, Eau Claire, WI for Debtor

Robert D. Martin, United States Bankruptcy Judge

DECISION

Paul Eugene Henderson ("Henderson"), the debtor, had a one-third (1/3) tenancy in common in a farm where he resides near Alma, Wisconsin. Alliance Bank ("Alliance") (formerly known as the Bank of Buffalo) received a judgment against Henderson in the amount of $36,932.28 on November 15, 2001 and another judgment in the amount of $17,719.47 on January 17, 2002. On February 4, 2002, Alliance levied execution on Henderson's property. At the execution sale on April 17, 2002, Alliance purchased Henderson's interest in the real estate for $42,632.00.

Henderson filed for Chapter 13 bankruptcy, one year less one day after the execution sale. Henderson claimed a homestead exemption of $1.00 for the property pursuant to 11 U.S.C. §522(d)(1).[1] Henderson proposed to sell a portion of the property to fund his Chapter 13 plan. Alliance objected to confirmation of the Chapter 13 plan, contending that pursuant

[1] 11 U.S.C. §522

(d) The following property may be exempted under subsection (b)(1) of this section:

(1) The debtor's aggregate interest, not to exceed $17,425 in value, in real property or personal property that the debtor or a dependent of the debtor uses as a residence, in a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence, or in a burial plot for the debtor or a dependent of the debtor.

to Wisconsin Statute §815.39[2] Henderson has no interest in the real estate.

Henderson also filed a motion to avoid the judicial liens of Alliance. Alliance objected to that motion.

Prior to and at the time of the execution sale, Henderson did nothing to oppose it. Nor did he formally assert his claim of an exempt homestead. After the sale and before the filing of his Chapter 13 bankruptcy, Henderson claims that he filed a motion with the Buffalo County Circuit Court challenging the execution sale, the Circuit Court declined to hear the motion, and the Circuit Court stated without written ruling or order, that it had no power to hear a post-execution sale argument.

An evidentiary hearing was held on September 16, 2003 on the confirmation of the plan, the motion to avoid the lien of Alliance, and Alliance's objection to the claimed homestead exemption. All issues were taken under advisement.

Alliance argues that Henderson's right to redeem the property was based on Wisconsin Statute §815.40 and that because Henderson failed to redeem the property within one (1) year of the sale, he has no interest in the real estate.

Henderson claimed, but did not prove, that there was an offer by a third party to purchase the vacant one hundred and twenty (120) acres (not including the homestead). He further argued that because Alliance failed to follow statutory procedure in the execution sale (by failing to set aside his exempt homestead), the sale to Alliance should be voided by the Bankruptcy Court and he should be permitted to sell the property to partially fund his plan.

Under Wisconsin law,[3] the person subject to an execution sale may notify an officer "at any time before the sale" that he claims a homestead exemption. Wisconsin Statute §815.21(1). After the sale, there is no requirement of Court confirmation. The Sheriff simply issues a deed upon demand from the execution sale purchaser after the expiration of fifteen (15) months from the date of sale. Wisconsin Statute §815.55.

Henderson admits that he did not claim a homestead exemption on the property before

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[2]Wisconsin Statute §815.39. Execution sale; redemption of real estate. Within one year after an execution sale the real estate sold or any lot, tract or portion that was separately sold may be redeemed by the payment to the purchaser, his personal representatives or assigns, or to the then sheriff of the county where such real estate is situated, for the use of such purchaser, of the sum paid on the sale thereof, together with the interest from the time of the sale.

[3]Wisconsin statutes governing executions, the conduct of execution sales, and rights of redemption have been renumbered (most recently in 1976) but have not been altered since the nineteenth century, although exemptions from execution were revamped in 1985.

the time of the execution sale. He relies, instead on his claim that he did significant business with Alliance Bank during the six (6) years that he occupied the property and that Alliance Bank knew that the property was his homestead. Alliance Bank has stipulated that it knew Henderson resided on the property.

Wisconsin public policy has long favored a liberal construction of the homestead statutes in favor of the debtor and has preferred a debtor's homestead rights over the rights of creditors. Mogilka v. Jeka, 131 Wis.2d 459, 468 (Ct.App.,1986). The Wisconsin Supreme Court has held that the "fact of occupancy" may be sufficient to indicate one's declaration of the homestead exemption and that "the right to the homestead exemption does not depend upon its formal exercise" Lueptow v. Guptill, 56 Wis.2d 396, 404 (1972). "[U]se and occupancy themselves evidence the selection by the owner of all of such contiguous land as his homestead, and constitute notice to all of its character as his homestead, and of his selection thereof as such, without his giving any other notice." Larson v. State Bank of Ogema, 230 N.W. 132, 134 (Wis. 1930).

Both Alliance Bank, as an execution creditor, and the sheriff as the officer who conducted the sale were presumed to know, at the time of the sale, that Henderson occupied the property as his homestead. "[No] public proclamation or further assertion of his claim for exemption, and no attempt on his part to prevent the sale, was necessary to protect his homestead rights." Larson v. State Bank of Ogema, 230 N.W. 132, 135 (Wis. 1930); *citing* Scofield v. Hopkins, 61 Wis. 370, 372 (1884). "It [was] immaterial that no claim of homestead [had] ever been asserted prior to an action to set aside a sale thereof under execution." Hoppe v. Goldberg, 53 N.W. 17 (Wis. 1892).

Henderson's homestead exemption was effectively claimed by his residing on the property. Whenever a homestead exemption is claimed the remainder alone is subject to sale under a levy, unless the plaintiff in the execution denies the right to the homestead exemption or is dissatisfied with the quantity or value of the land selected. Wisconsin Statute §815.21(1). "A homestead so selected and set apart by such officer shall be the exempt homestead of such person." Wisconsin Statute §815.21(4). There is no evidence that the officer surveyed Henderson's exempt homestead to set it apart or to determine the remainder that would be subject to sale as required by Wisconsin Statute §815.21(3). The failure of the officer to set apart the homestead affects the levy. The levy and the execution sale are clearly flawed and may be voided.

The question then becomes whether Henderson is a party now entitled to avoid the sale. First we must consider whether he is bound by *res judicata*. Even if a prior court is clearly wrong, the finality of its decision may preclude relitigation of the issue or cause that it determined. Henderson claims that he filed a motion with the Buffalo County Circuit Court challenging the execution sale and that his claim was denied by that court. He did not appeal that decision, but rather characterizes it as being informal and not determinative of a final outcome. "Res judicata . . . requires federal courts to give a state court judgment the same

preclusive effect it would have in state court." Long v. Shorebank Development Corp., 182 F.3d 548, 560 (C.A.7 (Ill.),1999); *see also* Wilhelm v. County of Milwaukee, 325 F.3d 843, 846 (C.A.7 (Wis.),2003) "So long as state proceedings satisfy the minimum procedural requirements of the due process clause, [a] state judgment is entitled to full faith and credit in the federal courts, and will be given the same preclusive effect by the federal courts that it would be given by the courts of the rendering state." Jones v. City of Alton, Ill., 757 F.2d 878, 884 (C.A.7 (Ill.),1985). We have little or no evidence of the process employed by the Circuit Court, but what we have suggests an extremely summary proceeding which precluded presentation of evidence and argument. In any event we have no evidence that a formal order of the court was ever entered.

Wisconsin preclusion law is of the common variety. Three elements are required for res judicata: "(1) an identity of the parties or their privies; (2) an identity of the causes of action; and (3) a final judgment on the merits." Barnett v. Stern, 909 F.2d 973, 978 (C.A.7 (Ill.),1990), *citing* Conner v. Reinhard, 847 F.2d 384, 394 (C.A.7 (Wis.),1988). While the parties appear to be identical and the issues substantially similar (at least as to the adequacy of notice of a homestead), this Court has no proof that the avoidance of the execution sale motion was litigated to finality in the Circuit Court. We have only Henderson's recitation of the Circuit Court refusing to consider his claim. There is no other evidence of a final disposition of Henderson's claim. Without evidence of a final judgment in another court, res judicata will not bar this court from reviewing Henderson's right to claim a homestead exemption or to challenge the execution sale.

Next we must answer whether Henderson as a Chapter 13 debtor in this bankruptcy is authorized to seek avoidance of the sale under bankruptcy law. Despite a judgment of execution, Henderson still had an interest in the homestead property at the time he filed bankruptcy, such that the property was part of the estate under 11 U.S.C §541(a)(1)[4].

The Bankruptcy Code authorizes Chapter 13 debtors to assert the trustee's strong-arm powers to protect an exemption.[5] 11 U.S.C. §522(h)[6] provides that "the debtor may avoid a

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[4]11 U.S.C. §541. Property of the estate.
(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such an estate is comprised of all the following property, wherever located and by whomever held:
(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

[5]11 U.S.C. §1303 grants a Chapter 13 debtor "exclusive of the trustee, the rights and powers of a trustee under 11 U.S.C. §363(b), 11 U.S.C. §363(d), 11 U.S.C. §363(f), and 11 U.S.C. §363(l)."

[6]11 U.S.C. §522. Exemptions.
(h) The debtor may avoid a transfer of property of the debtor or recover a setoff to the extent that the debtor could have exempted such property under subsection (g)(1) of this section if the trustee had avoided such transfer, if -

transfer of property of the debtor or recover a setoff to the extent that the debtor could have exempted such property." The execution sale was not a voluntary transfer of property. Henderson did not conceal the property. Because a Chapter 13 trustee is primarily a disbursing agent for plan payments he has no reason to seek avoidance of pre-petition transfers of exempt property. Henderson, thus, is able to exercise an avoidance power normally assigned to the trustee and listed under 11 U.S.C. §522(h). The homestead property is of a kind that the debtor would have been able to exempt from the estate if the trustee had avoided the transfer under one of the provisions in 11 U.S.C. §522(g)[7].

While Henderson is entitled to exempt this homestead from the execution sale, he has claimed only a de minimus exemption valued at $1.00 in his bankruptcy schedules. Does this small toe hold let Henderson undo the sale? The answer must certainly be "yes." While the exemption claimed in the bankruptcy may sometimes differ from the maximum exemption permitted by state law, it is the failure to recognize the state exemption that constituted the defect in the execution sale. So, any claim of exemption under 11 U.S.C. §522(d) would support use of 11 U.S.C. §522(h). Furthermore, the exemptions claimed on the bankruptcy schedules are subject to virtually unlimited amendment during the bankruptcy case.

But the question remains as to whether the powers given to the trustee provide any relief for Henderson. 11 U.S.C. §544 "strong arm" power is the most likely to be of use, but it provides the trustee only the rights of a hypothetical or real judgment creditor, execution lien holder or bona fide purchaser as of the date of bankruptcy, and none of those parties would necessarily have been able to upset Alliance's execution sale in a state court. At least no case has been found under Wisconsin law that goes as far as conferring on a third party the right to contest an execution sale in which the only defect was a failure to set aside and recognize a homestead exemption. So, it is far from clear that the trustee's avoiding powers aid Henderson at all.

Even if it could not be avoided by a trustee, the execution sale did not deprive Henderson of all his interest in the property. At the time the case was filed, Henderson retained a right to redeem the property sold at execution, but also brought to the bankruptcy

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(1) such transfer is avoided by the trustee under section 544, 545, 547, 548, 549, or 724(a) of this title or recoverable by the trustee under section 553 of this title; and
(2) the trustee does not attempt to avoid such transfer.

[7]11 U.S.C. §522. Exemptions.
(g) Notwithstanding sections 550 and 551 of this title, the debtor may exempt under subsection (b) of this section property that the trustee recovers under section 510(c)(2), 542, 543, 550, 551, or 553 of this title, to the extent that the debtor could have exempted such property under subsection (b) of this section if such property had not been transferred, if -
(1)(A) such transfer was not a voluntary transfer of such property by the debtor; and
(B) the debtor did not conceal such property; or
(2) the debtor could have avoided such transfer under subsection (f)(2) of this section.

estate a personal cause of action to undo the defective execution sale. "An execution sale of land in disregard of the law . . . is not void, but only voidable at the insistence of the party aggrieved." Raymond v. Pauli, 1867 WL 3258, 2 (Wis. 1867). The right to redeem was scheduled to expire in one (1) day and was only extended an additional sixty (60) days by 11 U.S.C. §108[8]. The cause of action to set aside the sale would appear to be governed by the general Wisconsin statute of limitations for civil action (although presumably subject to laches or other equitable relief if the sale were fully consummated and relied upon). The action to set aside the sale is what is being prosecuted as a part of these motion hearings. On that cause Henderson is entitled to relief.

11 U.S.C. §522(f)(1) permits a "debtor [to] avoid the fixing of a lien on an interest of the debtor in property to the extent that such lien impairs an exemption to which the debtor would have been entitled." In In re Desrosiers, 49 B.R. 132 (Bkrtcy.D.N.H.,1985), Judge Yacos held that the rights which a judgment creditor obtained by virtue of a pre-petition execution sale and United States Marshall's deed were subject to being nullified upon redemption by the debtor and were, therefore, within the definition of a lien as defined in 11 U.S.C. §101(37). Judicial liens are avoidable by the debtor pursuant to 11 U.S.C. §522(f) to the extent they impair the exemptions. The creditor's contention that it had obtained a real property interest in the debtor's land at the sale and had moved past the point of holding a lien was specifically rejected.

"A lien shall be considered to impair an exemption to the extent that the sum of the lien, all other liens on the property, and 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). Where the value of the liened property exceeds the value of the exemption claimed, the lien in question may be avoided only to the extent of the exemption, the remaining value of the property remains subject to the lien. In re Sherbahn, 170 B.R. 137 (Bkrtcy.N.D.Ind.,1994). Henderson claimed a homestead exemption on his bankruptcy schedules in the amount of $1.00. The liens of Alliance appear to exhaust any claimed value of the subject property. Therefore, the exemption which Henderson claimed has been impaired by the lien, and the lien must be reduced by the amount of the claimed exemption of $1.00. Bankruptcy Rule 1009(a), however, provides that the debtor may amend an exemptions claim at any time before the case is closed.[9]

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[8]*see* Moody v. Amoco Oil Co., 734 F.2d 1200, 1213 (C.A.7 (Wis.),1984).

[9]Bankruptcy Rule 1009.
Amendments of Voluntary Petitions, Lists, Schedules and Statements.
(a) General Right to Amend. A voluntary petition, list, schedule, or statement may be amended by the debtor as a matter of course at any time before the case is closed. The debtor shall give notice of the amendment to the trustee and to any entity affected thereby. On motion of a party in interest, after notice and a hearing, the court may order any voluntary petition, list,

Thus, the execution sale is voided. But voiding the execution sale does not destroy Alliance's entire lien in the property. The lien is avoided only to the extent that the property to which it attaches is exempt. To the extent that lien is not avoided it must be honored in the plan. The current plan proposes to sell only one hundred and twenty (120) acres (Wisconsin permits a maximum homestead of forty (40) acres). The lien of Alliance would attach to at least one hundred and fifty (150) acres. The debtor has not met his burden of showing that the proceeds of the proposed sale would compensate Alliance for the full value of its lien, a lien required by 11 U.S.C. §1325(a)(5). The lien of Alliance is only reduced by the $1.00 claimed exemption. The proposed plan does not offer Alliance the full value of its lien minus the available exemption. The plan cannot be confirmed. Debtor may have twenty (20) days to amend.

POST SCRIPT:

Alliance has moved for relief from stay. Debtor has not claimed to have equity in the property subject to Alliance's lien. Because the proposed plan cannot be confirmed, the property is not necessary to debtor's effective reorganization. Furthermore, the debtor has not provided adequate protection of Alliance's interest in the subject property. Cause having thus been shown, the stay against Alliance's efforts to obtain debtor's real property may be lifted to conduct a new execution sale or otherwise pursue its lien consistent with this memorandum decision.

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schedule, or statement to be amended and the clerk shall give notice of the amendment to entities designated by the court.