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BANKRUPTCY LAW

Beating the Trustee to the Punch

What constitutes good faith effort on the part of a judgment creditor?

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A judgment creditor may lose its rights if its judgment debtor files for bankruptcy before the judgment creditor perfects its judgment under New Jersey law. Under the Bankruptcy Code, a bankruptcy trustee obtains the status of, among others, a hypothetical properly perfected judgment creditor with priority over otherwise senior judgment creditors that have not properly perfected their judgment liens. Judgment creditors in New Jersey should therefore take all necessary steps to perfect their judgment liens.

New Jersey state law imposes a sequence of execution that a judgment creditor must follow prior to levying against a judgment debtor's real property. N.J.S.A. § 2A:17-1 requires a judgment creditor to make a "good faith" attempt to execute against personal property before executing against real property. In 2006, the United States

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Bankruptcy Court for the District of New Jersey decided two cases that required the bankruptcy court to examine whether judgment creditors made good faith efforts to comply with N.J.S.A. § 2A:17-1 to determine whether the bankruptcy trustee could void a judgment creditor's prepetition levy against the judgment debtor's real property.

In March 2006, the New Jersey Bankruptcy Court decided *In re Mariano*, 339 B.R. 344 (Bankr. N.J. 2006). In that case, Continental Casualty Company (CCC) obtained a judgment for nearly \$1 million against the debtor. Prior to the bankruptcy filing dates, CCC issued an information subpoena to the debtor. The debtor's certified responses to the information subpoena indicated, among other things, that she was not receiving money from Social Security benefits, that she did not own the property where she resided, that the present value of her personal property did not exceed \$1,000, that she had no cash on hand, no other personal property, no motor vehicles, and no ownership interest in a business. The debtor did not respond to the question on the information subpoena concerning her ownership interest in any other real estate. CCC's private investigator issued a report that listed the debtor as the record owner of a house in Cherry Hill, New Jersey.

Based on the debtor's response to CCC's information subpoena and the private investigator's report, CCC

obtained a Writ of Execution from the New Jersey Superior Court in March, 2005. The Writ commanded the sheriff to

satisfy the said judgment out of the personal property of the judgment debtor, within your County; and if sufficient personal property cannot be found, then out of the real property in your County belonging to said judgment debtor at the time when the judgment was entered or docketed.

CCC's transmittal letter to the sheriff enclosed the Writ of Execution and requested the sheriff to satisfy CCC's judgment out of the debtor's real property. CCC included with the writ a copy of the debtor's response to CCC's information subpoena, in order to highlight the fact that the debtor "owns no personal property upon which this Writ may be executed." The sheriff levied against the debtor's home in April, 2005.

Thereafter, the debtor filed for Chapter 7 bankruptcy protection. The bankruptcy trustee filed an adversary proceeding against CCC, claiming that the trustee's position as a hypothetical judgment lienholder required CCC to vacate its levy on the debtor's real property. The trustee asserted that CCC failed to follow the sequence of execution prescribed by N.J.S.A. § 2A:17-1.

Specifically, the trustee alleged that CCC did not conduct any additional discovery after receiving the debtor's response to the information subpoena.

Chief Judge Judith H. Wizmur ruled that CCC's actions did constitute reasonable efforts to locate personal property owned by the debtor, and therefore denied the trustee's motion for summary judgment to vacate CCC's levy. Judge Wizmur wrote:

Here, the written interrogatories directed to the debtor and her responses to the questions posed, supplemented by the investigative reports obtained by the judgment creditor about the debtor's assets, constituted the required good faith attempt by CCC to locate personalty owned by the debtor prior to the levy on the debtor's real property.

Judge Wizmur distinguished this case from other decisions in which the New Jersey state courts determined that the judgment creditor did not make reasonable efforts to locate personal property before executing against real property. (*Raniere v. I & M Investments, Inc.*, 159 N.J. Super. 329 (Ch.Div.1978)) (invalidating judgment creditor's levy on real estate owned by judgment debtor because judgment creditor conducted no supplementary proceedings and obtained no information concerning personal property owned by the judgment debtor before instructing sheriff to proceed first against judgment debtor's real property); (*In re Italiano*, 66 B.R. 468 (Bankr.D.N.J.1986) (invalidated judgment creditor's levy on real estate owned by debtor because creditor knew of debtor's personal property but did not share knowledge of personal property with the sheriff, advising sheriff to execute generically against personal and real property at the same time).

Judge Wizmur based her decision by

analyzing the *Raniere* decision and the New Jersey Supreme Court's decision in *Pojanowski v. Loscalzo*, 127 N.J. 240 (1992). In *Pojanowski*, the Court examined the effort required by a judgment creditor under Rule 4:59-1(e) (allowing for supplementary discovery to aid a judgment creditor in executing against property owned by a judgment debtor). The judgment creditor in *Pojanowski* conducted a post-judgment deposition of the debtor in which the debtor "responded negatively or evasively" to the creditor's inquiries regarding the debtor's personal property. Following the deposition, the judgment creditor obtained an order authorizing the sale of the debtor's real estate. The New Jersey Supreme Court affirmed the lower court's decision that the judgment creditor's deposition constituted "reasonable efforts" to locate personal property owned by the judgment debtor. The Court noted that additional inquiries by the judgment creditor, or instructions by the judgment creditor to enforce against personal assets first, would have been futile.

Relying on *Pojanowski*, Judge Wizmur noted that "the trustee does not suggest that any personal assets of the debtor would have been found if an additional inquiry had been conducted, or if the sheriff had been directed to levy first upon personalty."

Judge Wizmur also examined the *Raniere* court's comment that the sheriff must return a writ of nulla bona prior to executing against a judgment debtor's real estate, which writ would certify that the sheriff made a "strict and diligent search and has been unable to locate any personalty of the debtor within the county." Judge Wizmur concluded that the "requirement" for the return of a writ of nulla bona was an anachronism from an 1877 District Court Act that is no longer applicable, and determined that "where reasonable efforts to locate debtor's personalty are made by the judgment credi-

tor, a writ of nulla bona is not required to be returned by the sheriff as a prerequisite to the validation of an execution against real estate."

In October 2006, the Honorable Donald H. Steckroth, U.S.B.J., decided *In re Martini*, 2006 WL 2471617 (Bankr. N.J. 2006), a post-*Mariano* interpretation of the interrelationship between a judgment creditor's ability to defeat a bankruptcy trustee's attempt to void the judgment creditor's real property lien, based on the strength of the judgment creditor's "good faith" attempt to meet the requirements of N.J.S.A. § 2A:17-1 prior to executing against a judgment debtor's real property. The question presented in *Martini* was whether the judgment creditor could be said to have made reasonable efforts at compliance by merely serving the debtor with an Order of Discovery under Rule 4:59-1(e), and subsequently obtaining an Order to Enforce Litigant's Rights after the judgment debtor failed to respond to the Order of Discovery. Judge Steckroth found that the judgment creditor in *Martini* did not do enough to effect a real property levy that would defeat the bankruptcy trustee. Judge Steckroth noted that the judgment creditor did not serve a copy of the signed Order to Enforce Litigant's Rights on the judgment debtor, did not seek a warrant for the judgment debtor's arrest following noncompliance with the Order to Enforce Litigant's Rights, and did not issue a Writ of Execution to the sheriff to execute against personal and real property of the judgment debtor.

Together, the *Mariano* and *Martini* decisions provide helpful guidelines for representing both the judgment creditor and the bankruptcy trustee regarding the bankruptcy court's interpretation of what constitutes a good faith effort on the part of a judgment creditor to comply with N.J.S.A. § 2A:17-1 such that the judgment creditor will be found to have taken priority over the trustee. ■