

**FARM LEGAL SERIES**

**June 2015**

# Rights of Unsecured Creditors

**Phillip L. Kunkel, Jeffrey A. Peterson**  
**Attorneys, Gray Plant Mooty**

## INTRODUCTION

The modern farmer establishes ongoing relationships with many businesses for the purchase and payment of necessary supplies in the normal course of business. These transactions usually do not involve the farmer granting the supplier any special protections to secure the repayment of the debt, such as a security interest. These suppliers are considered unsecured creditors; because the debt that is owed to the supplier is not secured by any property of the farmer. This fact sheet discusses the legal remedies and issues surrounding unsecured creditors.

## CIVIL ACTIONS

Unfortunately, in times of financial distress, a farmer may have trouble paying both his unsecured creditors and his secured creditors. As a result, unsecured creditors may decide to initiate legal action to collect on the debt. An unsecured creditor who resorts to legal action must initiate a lawsuit in the appropriate court to seek payment of the amount owed him.

### Choosing the Court

Subject to legal limitations, the creditor can determine in which court the action is brought. If brought in state court, the action generally will be filed in the county where the debtor farmer (the defendant) resides or in the county the facts involving the lawsuit occurred.

After determining the proper county, the creditor (also known as the plaintiff) must determine in which court to bring the lawsuit. There are two possibilities. The lawsuit may be brought in Conciliation Court, also known as Small Claims Court, if the amount claimed, exclusive of the court filing fee, is \$7,500 or less. The alternative, bringing the lawsuit in District Court, may be used regardless of the amount involved.

In some cases, it may be possible for the creditor to bring a lawsuit in federal court. Federal court is limited by law to allow only those lawsuits that involve the interpretation and application of a federal statute or that involve residents of different states. In either case, the amount in controversy must be greater than \$75,000. Because of these restrictions, most claims by unsecured creditors against farm operators are heard by one of the two state courts.

### Initiating the Lawsuit

If a plaintiff elects to proceed in Conciliation Court, the lawsuit will be handled in an informal manner. Attorneys will not be involved in most cases. To initiate a lawsuit in Conciliation Court the plaintiff must file his claim with the court clerk. The clerk will send a copy of the claim to the defendant and will notify him of the hearing date. At the hearing, each party presents its case and argues its position to the court. The court renders a decision based on the evidence

heard at the hearing. Either party may appeal to the District Court.

### **Summons and Complaint**

The procedures for district court lawsuits are similar. To initiate a lawsuit, the plaintiff must prepare and personally serve upon all defendants a summons and complaint that outlines the claim. In most cases, this complaint need not specify all the facts that gave rise to the claim; rather, it may merely set forth sufficient facts to notify the defendant of the nature of the claim.

### **Answer**

Upon receipt, the defendant has 20 days to respond. The defendant generally responds by serving upon the plaintiff's attorney an answer to the complaint. In his answer, the defendant may assert defenses and/or claims against the plaintiff, other defendants or other third parties that may be responsible to the plaintiff. If the defendant fails to answer within 20 days, the court will grant the plaintiff request though a default judgment.

### **Discovery**

Once the defendant has answered, the parties to the lawsuit may undertake discovery procedures. Court rules allow several procedures that enable the parties to a civil action to identify witnesses, identify documents, develop the facts that gave rise to the lawsuit, limit the contested issues at any trial and foster settlements. Under the court rules, either party may submit a series of written questions to the opposing party. These questions, known as interrogatories, must be answered under oath by the opposing party. The questions may relate to any facts that are or may be in dispute in the lawsuit, to the identity of witnesses that the opposing party will be calling at the trial and to the amount of the plaintiff's claim. The use of interrogatories can be a first step in

developing the facts of the case so that each party is aware of the opposing party's position.

Interrogatories frequently are accompanied by requests for inspecting and copying documents. Under the court rules, both parties may compel the other party to produce any and all documents that may be relevant to the lawsuit.

It is possible for either party to examine any potential witness under oath through a deposition. Witness testimony will be preserved by means of a transcript prepared by a court reporter. It also may be preserved by means of a video tape. Examination of a witness can deal with any facts relevant to the lawsuit.

### **Trial**

Once discovery has been completed, the lawsuit, if not already settled, will be ready for trial. It may be possible, at this point, to obtain a ruling from the court without a full trial. In cases in which there are no disputes of fact and it can be shown that one of the parties is entitled to prevail as a matter of law, a motion for summary judgment may be granted by the court. The effect is to obtain an order from the court that results in a determination for either the plaintiff or the defendant. It is rare for a court to grant such a motion because most cases involve factual disputes.

If the case must go to trial, the trial may or may not involve a jury. In general, if a person is being sued for the recovery of money, he is entitled to a jury if he so demands. At the trial, the plaintiff must prove that he is entitled to the amount he claims. The plaintiff may introduce all his evidence before the defendant introduces any of his.

## MONEY JUDGMENTS

### Issuance of the Judgment

If the court determines that the plaintiff is entitled to recover a sum of money from the defendant or the defendant failed to answer the complaint, the court will order the clerk of court to issue a judgment in favor of the plaintiff. Once this judgment has been obtained, the plaintiff can file it with the clerk of court by filing an affidavit giving the defendant's name, occupation and address. Once this is completed the judgment is considered "docketed."

### Creation of a Lien

As soon as the judgment has been docketed, it creates a lien to the extent of the unpaid amount of the judgment on all of the defendant's nonexempt real property located in the county in which it is docketed. To get a lien on other real property located in other counties, the plaintiff must transfer the docketed judgment to the other counties. This docketed judgment creates a lien on real property owned by the judgment debtor at the time of the docketing and on all property that he may later acquire. In other words, the judgment lien automatically attaches to any real property later acquired by the debtor. The judgment lien is not on the judgment debtor's personal property or exempt property. For a general discussion of exempt property, see section titled "Exemptions" below.

### Duration of the Lien

This lien is good for 10 years after the judgment is entered, and may be extended for additional 10 year periods. Additional procedures must be followed by the judgment creditor if the judgment debtor owns registered (or "Torrens") property, since the mere docketing of a judgment does not result in the creation of a lien on

registered property. However, a judgment for debt on agricultural property, personal property used in the farm operation, owned by a farm debtor is only good for 3 years. Moreover, in this situation, the judgment does not attach to real or personal property acquired by the farm debtor after the judgment is entered.

### Priority

Once a judgment lien has been docketed, the judgment creditor has priority over other judgment creditors who obtain later judgments against the debtor. This lien prevents the judgment debtor from selling the property because any potential purchaser of the property will not buy the property unless the judgment has been satisfied. A judgment lien will not, however, grant the judgment creditor priority over a prior mortgage or any purchase money mortgage that the judgment debtor grants to a seller of real property in conjunction with the purchase of additional real property. For a more detailed discussion of mortgages and purchase money mortgages, *See Mortgages and Contracts For Deed*.

## COLLECTION OF MONEY JUDGMENTS

A judgment creditor can attempt to collect on the money judgment in two primary ways: 1) through a writ of execution and 2) through garnishment.

### Writ of Execution

In addition to acquiring a lien on real property, a judgment creditor may obtain from the court an order authorizing the sheriff, the creditor, or the creditor's attorney to carry out the court's decision in favor of the judgment creditor. This court order is known as a writ of execution. It allows the judgment creditor to have the

judgment debtor's property seized and sold in satisfaction of the judgment.

Such a writ is issued by the clerk of the court in which the judgment was entered. Usually the sheriff serves the writ, but when the judgment creditor proposes to make an execution of not more than \$10,000 for money owed to judgment debtor by a third party, the execution may be made by the judgment creditor's attorney. However, only one execution per day may be served on a single third party by a judgment creditor. To do so, the attorney must either send a registered or certified letter of execution to the third party or have it served personally. The third party may also be served by registered or certified mail at their regular place of business.

#### **Levy on Earnings**

No notice is required prior to executing with a writ of execution. If, however, the judgment creditor seeks to levy on earnings in the possession of an employer, the creditor must first serve a notice upon the judgment debtor no less than 10 days prior to service of the execution.

#### **Levy on Real and Personal Property**

A writ of execution can be used to collect the judgment from real or personal property, provided that the property is not exempt from levy under Minnesota law. For a general discussion of exempt property, see section titled "Exemptions" below.

The writ of execution will direct the sheriff to satisfy the judgment first out of the judgment debtor's non-exempt personal property. Personal property that can be delivered manually is levied on by the sheriff taking physical custody of it. Other personal property is levied on by leaving with the person holding the property a certified copy of the execution and a notice specifying the

properly levied on. Growing crops may be levied on after they have been planted, but they may not be sold until they mature. Any judgment levy on personal property will be subject to any pre-existing liens or security interests on the property; meaning that any proceeds from the sale of the personal property by the Sheriff will be first applied against any debt secured by the pre-existing liens or security interests on the personal property before the judgment creditor would receive anything.

If sufficient non-exempt personal property cannot be found to satisfy the judgment, the sheriff may levy on any non-exempt real property owned by the debtor. Like a levy on personal property, if there is a prior lien against the real property, the judgment creditor would receive any sale proceeds after the satisfaction of the debt secured by the prior lien.

#### **Sheriff's Sale**

Property that is subject to a levy may be sold by the sheriff to satisfy the judgment. If personal property is involved, the sheriff must give 10 days posted notice of the time and place of the sale. If the sale is to be of real property, he must give six weeks posted and published notice.

If the sale is of personal property and the debtor is a resident of the county, prior to posting notice of sale, the officer must serve a copy of the execution and inventory and the notice upon the judgment debtor. If the sale is of real property, a judgment creditor must serve a copy of the notice, at least four weeks before the sale upon the judgment debtor if a resident of the county. The creditor must also service the notice upon any person in possession of the real property other than the judgment debtor and all persons who have recorded a request for notice.

The sale will be held by the sheriff as an auction. If the personal property sold is capable of manual delivery, it must be sold in the view of those at the sale. If the real property sold consists of several known parcels, the parcels must be sold separately and only to the extent necessary to satisfy the execution.

### **Redemption**

Once the sale has occurred, there is no redemption from the sale in the case of personal property. In the case of real property, the judgment debtor may redeem from the sale within one year of the sale date by paying to the purchaser, the sheriff or the clerk of court the sales price, interest, taxes, assessments and payments on prior liens made by the purchaser. Subordinate lien claimants may redeem from the sale, if, within one year, they file a notice of intention to redeem with the clerk of court where the judgment was entered. They are given a five-day period after the expiration of the redemption period of the debtor within which to exercise their redemption rights.

### **Garnishment**

A judgment creditor often looks to money owed to the judgment debtor by a third party as a source of payment for his claim. Such indebtedness can be reached by writ of execution. It also can be reached by a garnishment.

To use a garnishment, the judgment creditor or his attorney prepares and issues a garnishment summons to the third party, often an employer or a bank. This summons, together with appropriate fees, must be personally served on the third party by the judgment creditor. The third party must disclose, within 20 days of service, the amount of indebtedness owed to the judgment debtor. The garnished party also must retain all property disclosed subject to

release or further order of the court. If the third party owes no debt to the judgment debtor, the garnished party will be discharged upon making such a disclosure. If the indebtedness is disclosed, the judgment creditor must collect the property held by the garnished party. This may be done either by obtaining the consent of the judgment debtor or by means of an execution.

### **Wages**

If wages are to be the subject of either an execution or garnishment, an advance notice of 10 days must be given to the judgment debtor. The notice can be served either personally or by first class mail and must inform the debtor that a summons or levy will be served on the debtor's employer in 10 days; that the debtor can serve on the creditor a statement asserting that he is entitled to exemptions from garnishment or execution; that wages are exempt from garnishment in certain cases; that the debtor is entitled to relief if the creditor in bad faith disregards a valid claim of exemption; and that the debtor will be subject to fees and a penalty if he claims an exemption in bad faith or takes any action to frustrate the collection process.

### **FARMER-LENDER MEDIATION**

Where the property to be seized or executed is property used in the farming operation, including equipment, crops and livestock, or where it is serving as collateral on a loan used for farm operations, it is deemed agricultural property and Minnesota's farmer-lender mediation statute generally requires the creditor to offer mediation of the debt to the debtor prior to seizure or execution. The farmer-lender mediation statute began requiring mediation in 1986, with the statute's expiration date being extended in the years following original



passage. Generally, the statute requires, among other things, that a creditor seeking to seize agricultural property first send notice to the debtor and offer the debtor the opportunity to mediate a resolution to the debt prior to beginning such action. If the debtor elects to mediate the debt, the creditor's seizure of the property can be suspended for a period of up to 90 days pending completion of the mediation. Where the debt or obligation involved has been scheduled by the debtor in a bankruptcy or involved in a previous farmer-lender mediation, it is not subject to the farmer-lender mediation statute and the creditor can enforce seek repossession of the property without first offering mediation.

### STATUTORY LIENS

At times, a seemingly unsecured creditor may acquire priority over other secured creditors based on a statutory provision. For example, a person who furnishes services for materials with respect to goods subject to a security interest receives a lien against the goods by law. That lien will take priority over a perfected security interest. For a more detailed discussion on statutory liens see fact sheet: *Security Interests in Personal Property*.

### EXEMPTIONS

Regardless of the collection procedure used by the judgment creditor, certain property, known as exempt property, remains free from the claims of creditors under Minnesota law (see table 1). Exempt property includes both real and personal property of a debtor that cannot be seized or sold to satisfy the claims of creditors.

The value of the exemptions is determined by the fair market value of the various assets. If otherwise exempt property is subject to a lien, the debtor may claim as exempt the value of the property in excess of the lien

amount (the "equity" in the property). In the case of a joint petition filed by a married couple the value limitations may be doubled. If property is claimed by the debtor as exempt, it generally will remain subject to any voluntary liens that the debtor has granted.

To claim such property as exempt, it must be disclosed to the judgment creditor, who gives the debtor an exemption notice. The homestead may be claimed as exempt by filing with the county recorder a declaration of homestead that includes a legal description of the property claimed as exempt.

### BANKRUPTCY

Unsecured creditors can be adversely affected if the debtor files for protection under the Bankruptcy Code. First of all, if the debtor initiates a Chapter 7, 11, 12, or 13 case this triggers the automatic stay. The automatic stay operates as a court order to halt, at least temporarily, a wide range of conduct for collecting a claim or debt against the debtor. In other words, the filing of any bankruptcy petition stops all collection efforts. The automatic stay is broad in scope. It is intended to prohibit creditors from taking any action against the debtor that disorganizes his efforts to deal with his financial problems or that interferes with his attempt to reorganize his business operation.

Although the provisions of the automatic stay law are broad, they are not absolute or permanent. Creditors, in some instances, may seek court approval to obtain relief from the stay or obtain court approval to continue or initiate collection proceedings against the debtor.

The Bankruptcy Code also establishes a detailed priority system for payment of claims. Unsecured creditors rank lowest in

priority and are generally paid after the secured and other priority unsecured creditors. The following unsecured creditors have the following priority in bankruptcy:

1. Unsecured claim for domestic support obligations;
2. Expenses of the administration of the bankruptcy case, including costs and expenses of preserving the estate taxes incurred by the estate, trustee's fees, and attorney's fees for the trustee;
3. Claims arising in the ordinary course of the debtor's business or financial affairs during the "gap period" between the filing of an involuntary petition and an order for relief;
4. Unsecured claims for wages, salaries, and commissions up to \$12,475 per creditor;
5. Unsecured claims for contributions to employee benefit plans up to \$12,475 per employee, less any amount paid to an employee for wages, salaries, or commissions;
6. In the case of a grain elevator bankruptcy, unsecured claims of farmers against the elevator for grain up to \$6,150 for each creditor;
7. Up to \$2,775 per claim on unsecured claims for money deposited with the debtor for purchase or lease of property or for services contemplated for the personal, household, or family use of the debtor that were not provided;

8. Unsecured claims of governmental units for taxes and penalties;
9. Claims for death or personal injury resulting from the operation of a motor vehicle or vessel if such operation was unlawful because the debtor was intoxicated from using alcohol, a drug, or another substance.

After these priority claims, the next parties in line are general unsecured creditors who filed claims in a timely fashion. If property remains after the general unsecured creditors are paid, all unsecured creditors receive interest at the legal rate from the date the bankruptcy petition was filed. Any funds or property remaining after the payment of interest is paid to the debtor. If the debtor's assets are insufficient to pay in full all of the claims within a particular classification, all creditors share on a pro-rata basis.

## CONCLUSION

Unsecured creditors may initiate legal actions against those who owe them money on accounts. They are at a disadvantage when compared to secured creditors because they must, in most cases, obtain a court determination that they are legally entitled to the amount of money they claim. After obtaining a judgment by the court, an unsecured creditor may then utilize the collection procedures authorized by law.

---

**For more information:**  
[extension.umn.edu/agriculture/business](http://extension.umn.edu/agriculture/business)

**Table 1: MINNESOTA EXEMPTIONS<sup>1</sup>.**

ITEMS	EXEMPTION AMOUNT
(1) Homestead; rents and proceeds of Homestead	Less than 160 acres; \$390,000 limit if non-ag or \$975,000 limit for ag. whether claimed by one or more debtors
(2) Family bible, library, musical instruments	Unlimited
(3) Church pew and burial lot	Unlimited
(4) (a) Wearing apparel, one (1) watch, utensils, foodstuffs	\$10,350
(b) Household furniture, household appliance, phonographs, radio, and television	\$10,350
(c) Wedding rings or other religious or culturally recognized symbols of marriage exchanged between the debtor and spouse at the time of the marriage	\$2,817.50
(5) Farm machines and implements used in farming by a debtor engaged principally in farming, livestock, farm produce, standing crops, tools, implements (total of (5) and (6) cannot exceed \$13,000)	\$13,000
(6) Tools, implements, machines, instruments, office furniture, stock in trade (total of (5) and (6) cannot exceed \$13,000).	\$11,500
(7) Library and tools of students	Unlimited
(8) All money arising from any claim on account of destruction or damage to exempt property	Unlimited
(9) Life insurance proceeds	\$46,000 plus \$11,500 for each dependent
(10) Police Relief Association, Firemen's Association, or Fraternal Benefit Association Benefits	Unlimited
(11) Manufactured home actually occupied as home	Unlimited
(12) Motor vehicle	\$4,600
(13) Vehicle modified for disability	\$46,000
(14) 75 percent wages	Unlimited
(15) Public assistance benefits	Unlimited
(16) Earnings of a minor child or proceeds by reason of any liability of debtor not for the special benefit of child	Unlimited
(17) Claim for damages recoverable by any person by reason of levy upon or sale under execution of exempt property	Unlimited

<sup>1</sup> In a joint case, these exemptions, other than the homestead exemptions, are available to each spouse. Certain values are adjusted on a biennial basis. The above exemptions are as of July 1, 2014. Certain exemptions will be adjusted again on July 1, 2016.



**Table 1 Continued: MINNESOTA EXEMPTIONS.**

ITEMS	EXEMPTION AMOUNT
(18) Personal injury or wrongful death claim (General Damages)	Unlimited
(19) Loan value, accrued interest on dividends in life insurance policy	\$9,200
(20) Stock bonus, pension, profit sharing benefits, annuity, IRA, employee pension or contract on account of illness, disability, death, age or length of service reasonably necessary for the support of debtor	\$69,000
(21) Veteran's benefits	Unlimited
(22) Disability benefits	Unlimited
(23) Public employee and teachers pension benefits	Unlimited
(24) Unemployment benefits	Unlimited
(25) Workers' Compensation benefits	Unlimited
(26) Money arising from the destruction of exempt property	Unlimited

**Table 2: FEDERAL BANKRUPTCY CODE EXEMPTIONS<sup>2</sup>.**  
11 U.S.C. Section 522(d)

ITEMS	EXEMPTION AMOUNT
Homestead Real or personal property the Debtor uses as a residence; or a burial plat for the Debtor	\$22,975
Motor vehicle	\$3,675
Household furnishings, household goods, wearing apparel, appliances, books, animals, crops or musical instruments held for personal, family, or household use.	\$12,250 total and no more than \$575 in any single item
Jewelry held for personal, family, or household use	\$1,550
Any property—wild card.	\$1,225, <u>plus</u> up to \$11,500 of any unused portion of the homestead exemption
Implements, professional books, or tools of the trade	\$2,300
Unmatured life insurance contract	Unlimited
Loan value, accrued dividends, or interest in life insurance policy	\$12,250
Professional prescribed health aids	Unlimited
Social Security, unemployment, public assistance	Unlimited
Veteran's benefit	Unlimited
Disability, illness, or unemployment benefits	Unlimited
Alimony, support or separate maintenance to the extent reasonably necessary for the support of the Debtor and dependents	Unlimited
Pension, profit-sharing, stock bonus, annuity benefits necessary for support of Debtor and dependents	Unlimited
Crime victim's reparations	Unlimited
Wrongful death claims	Unlimited
Life insurance proceeds necessary for support	Unlimited
Personal injury claims (not including pain and suffering or compensation for actual monetary losses)	\$22,975
A payment in compensation of loss of future earnings of the Debtor necessary for support	Unlimited
Certain retirement funds	Unlimited

<sup>2</sup> In a joint case, these exemptions, other than the homestead exemptions, are available to each spouse. Certain values are adjusted every three years. The above exemptions are as of April 1, 2013. Certain exemptions will be adjusted again on April 1, 2016.