

WFG Underwriting Bulletin



To: All WFG Policy Issuing Agents; All WFG Title Examiners and Officers
From: WFG Underwriting
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Subject: Bankruptcy Discharge Does Not Eliminate Liens

We continue to see confusion in closings involving sellers or borrowers who previously went through bankruptcy. It is important to remember:

- A bankruptcy discharge wipes out the debtor's personal obligation to pay most debts, but it does not automatically eliminate liens that had already attached to the debtor's property.
- Mortgage liens, judgment liens, association liens, tax liens, and other encumbrances are not removed from the property unless specifically dealt with in the bankruptcy proceeding.
- This limitation is expressly stated in the standard form of bankruptcy discharge order (often on the back page or in the fine print).

How Liens Can Be Stripped or Removed in Bankruptcy

If a debtor wishes to eliminate or reduce liens through bankruptcy, this requires a **separate court process**. Common mechanisms include:

- **Lien Avoidance – 11 U.S.C. § 522(f):**
Permits a debtor to avoid (remove) certain judgment liens that impair the debtor's exemptions (under bankruptcy or state law). This type of stripping may appear either in a court order or by claiming the exemption in the bankruptcy petition and the passage of time after the creditor meeting. If relying on the claim of exemption in the petition, there are technical requirements, so the stripping should be discussed with and reviewed by your WFG underwriter.
- **Lien Stripping in Chapter 7 –**
An unsecured junior mortgage may not be "stripped off" in a Chapter 7 proceeding, even when the value of the senior mortgage(s) exceeds the value of the property. *Bank of America v. Caulkett*, 135 S.Ct. 1995 (SC 2015). Such mortgages may however be invalidated under other bankruptcy provisions.
- **Lien Stripping in Chapter 11 --11 U.S.C. §§ 506(a), (d).** Stripping of liens in Chapter 11 cases is generally permitted by court order.
- **Lien Stripping in Chapter 13 – 11 U.S.C. §§ 506(a), 1322(b)(2):**
A debtor may "strip off" a wholly unsecured junior mortgage (for example, a second mortgage when the property value is less than the first mortgage) in Chapter 13. This requires a motion

and order from the bankruptcy court. The orders may be very nuanced, so consult your WFG Underwriter.

“Cramdown” in Chapter 13 – 11 U.S.C. § 506(a), § 1325(a)(5):

The secured portion of a lien (often on personal property or non-residential real estate) may be reduced to the collateral’s fair market value, with the remainder treated as unsecured. *Note:* This cannot be used to modify a first mortgage on the debtor’s principal residence.

- **Adversary Proceedings – Fed. R. Bankr. P. 7001:**
Certain lien disputes, including validity, priority, or extent of a lien, may be brought and resolved as a separate lawsuit within the bankruptcy case.
- **Consent Orders / Settlements:**
Lienholders and debtors sometimes resolve lien issues through negotiated agreements approved by the bankruptcy court.

Confirming that a lien has been properly removed in the course of a bankruptcy can be tricky. You are urged to consult your WFG underwriter and to review any orders found with them.

Practical Takeaway for Title and Escrow

- Do not assume that a bankruptcy discharge means all liens against the property are gone.
- Always review the bankruptcy docket if lien issues are raised. If a lien was avoided, stripped, or otherwise addressed, look for a **specific order of the bankruptcy court** authorizing its removal. If it is based on a claimed exemption, seek guidance from WFG underwriting.
- In the absence of such an order, the lien remains against the property and must be satisfied or otherwise dealt with at closing.
- Be kind to the next examiner. Record copies of the orders stripping liens as part of your closing.

WFG Underwriting Standard

Our agents must:

- Confirm whether any liens were affected by a bankruptcy through a specific court order, not just by the discharge.
- Require recordable evidence of lien removal before insuring free of the lien.
- Contact WFG underwriting for guidance if there is uncertainty or if the bankruptcy record is incomplete.

Remember: A discharge clears the debtor’s personal liability (**11 U.S.C. § 524**), but liens stay with the property unless a bankruptcy judge orders otherwise.

NOTE: This Bulletin should not be interpreted as reflecting negatively upon the character of an individual or entity mentioned herein and is for the sole purpose of establishing underwriting positions and policies reflecting WFG National Title Insurance Company’s best business judgment. The information contained in this Bulletin is intended solely for the use of employees of WFG National Title Insurance Company, its title insurance agents and approved attorneys. Disclosure to any other person is expressly prohibited unless approved in writing by the WFG National Title Insurance Company’s Underwriting Department.

The Agent may be held responsible for any loss sustained as a result of the failure to follow the standards set forth above.