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Can a Lien Exist Without A Debt For It to Secure?

The question of does a lien exist without a debt for it to secure is a complicated issue that unfortunately does not have a universal answer. This post will use two recent cases to explore concerns that counsel should examine if presented with this question.

Commercial lawyers know that a properly constructed consensual mortgage or security interest can secure the debt created by funds loaned after the lien is granted. This is common in commercial revolving loan situations and real estate lines of credit. The lien continues to exist and dates back to its recording or filing for priority purposes even if the amount owed goes to zero and back up again. For an explanation on how this type of lien differs from a lien securing a conventional loan, see 3A Ky. *Prac. Real Estate Transactions* § 22:73 titled Special types of mortgages – Revolving line of credit mortgage.^[i] As discussed in that source, this special type of lien is usually authorized by statute.

What happens in a situation where the lien arguably is not consensual and structured to meet the legal requirements that may permit the lien to continuously exist even when there is no debt to secure? In *In re Terrell*, 2019 WL 7165999 (Bankr. S.D. Ohio July 26, 2019), the bankruptcy court held that a condo association's springing^[ii] lien found in the association's formation documents referred to in the deed to Terrell granted a lien that secured the payment of condo association fees that later went unpaid. In *Terrell*, the issue was whether the Chapter 7 trustee's Strong-Arm Powers of 11 U.S.C. Section 544 permitted the trustee to avoid the condo association's lien? – the answer was “no” if the lien dated to the formation documents.^[iii] The relevant factual question was when the condo association's lien became perfected – before or after the trustee's hypothetical status and avoidance powers arose. Ruling for the condo association, the bankruptcy court said:

Debtor relies heavily on a decision by the Twelfth District Court of Appeals in *Settlers Walk Home Owners Ass'n. v. Phoenix Settlers Walk, Inc.*, 2015 WL 7430296, 2015 Ohio App.

LEXIS 4709 (12th Dist. App. Nov. 23, 2015), which involved a pre-PCA HOA. . . . The [state appellate] court reasoned that “a lien cannot exist in the absence of the debt, the payment of which it secures.” *Id.* at *6, 2015 Ohio App. LEXIS 4709, at *15

Thus, the HOA [lienor] did not perfect an enforceable lien on the property “merely by saying so as part of the recorded Declaration ...” *Id.* . . .

This Court is not persuaded by the decision in *Settler’s Walk*. . . . In the instant case, the [Terrell] Deed Restrictions provide that the Association has a continuing lien on the Property that applies “both prior to and after each yearly assessment, together with the continuing obligation to pay all future”

Stated another way, the Association has a continuing lien on the Property that secures debts that arise from unpaid assessments *and* the obligation to pay future assessments. Thus, the rationale utilized by the court in *Settler’s Walk*, that a “lien cannot exist in the absence of the debt,” does not apply in this case.

The *Terrell* bankruptcy court acknowledged the above-described rule in *Settler’s Walk* but did not need much analysis or supporting authority to decide that legal proposition incorrect thus giving the appearance that the *Settler’s Walk* rule is an outlier. A peek at the *Settler’s Walk* decision, however, reveals this:

However, as the Ohio Supreme Court has stated, “there can be no lien unless there is a debt [.]” *Choteau, Merle & Sandford v. Thompson & Campbell*, 2 Ohio St. 114, 124 (1853).

“Thus, a lien cannot exist in the absence of the debt, the payment of which it secures.” *Westin Hills West Three Townhome Owners Ass’n v. Federal Nat. Mortg. Ass’n*, 283 Neb. 960, 966, 814 N.W.2d 378 (2012), citing *Dean Realty Co. v. City of Kansas City*, 85 S.W.3d 83 (Mo.App.2002). In other words, although there are many types and classes of liens, “all have this characteristic of being secondary to an existing obligation, usually a debt. If there is no debt the lien ceases to have life or existence for its function has vanished[.]” *Hughes Plumbing and Heating, Inc. v. Rhoad*, 3d Dist. Hancock Nos. 5–79–4 and 5–79–5, 1979 WL 207953, *2 (May 22, 1979).

Settler's Walk at para. 18. The *Hughes Plumbing* case cited by the *Settler's Walk* court involves a mechanic's lien dispute and includes this: "Hence where, as here, the underlying debt is set forth in the complaint and denied in the answer, an issue of fact as to the amount of the debt due is created. In the absence of evidence to establish the amount of this debt, either predicated upon contract or quantum merit, there is established no underlying basis for the lien, no matter how procedurally perfect it may be." *Hughes Plumbing* at page 2.

Ohio state appellate courts have stated that a lien could not exist if there was no debt for that lien to support. A similar concept and belief is found in the IRS' doctrine of choateness: that doctrine holds that a later filed IRS lien is superior to a previously filed lien unless the competing lien is choate and, *inter alia*, a choate lien must secure an existing debt.^[iv] See, "IRS Liens, After Acquired Property and the Doctrine of Choateness" (5/4/18) at <https://www.blockchainandbanking.com/irs-liens-after-acquired-property-and-the-doctrine-of-choateness>.

One more thought on this topic, sometimes the lien authorizing statute addresses the question raised by the opposing statements in *Settler's Walk* and *In re Terrell*. The most obvious example is the Uniform Commercial Code alluded to above, wherein Article 9 authorizes security interests that attach when the debt arises but date back in priority to when the UCC filing statement was properly filed. See 4 Ky. *Methods of Prac.* § 11:45 titled Priority issues involving future advances.

Another example of a statutory determination of the extent of a lien is Ohio's real estate judgment lien statute: that lien is obtained by recording notice of the record in the office of the county recorder, but that lien only attaches to real property then owned by the judgment debtor because that is all the statute permits. See O.R.C. Section 2329.02 and syllabus 2 from *Bank of Ohio v. Lawrence*, 161 Ohio St. 542 (1954) which states: "The filing of a certificate of a judgment in the office of the Clerk of the Common Pleas Court in accordance with Section 11656, General Code ([Section 2329.02](#), Revised Code), does not create a lien on after-acquired land of the judgment debtor, unless the certificate is refiled after the

acquisition of such property and before disposition.”

Counsel should exercise care when analyzing the effectiveness and priority of a lien that was procedurally complete and correct but secured no outstanding debt until after the important date (often the date of the competing lien) in your particular facts.

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[i] The reverse of this question is the ability to grant a lien on property you do not yet own. In a sense, this happens all the time when security interests are granted in after-acquired property and the lien on that property arises (or springs in to existence) in favor of the secured party as soon as the lien granting borrower has any rights in that collateral.

[ii] I use the word “springing” in the same sense as that concept is used in estate planning to refer to a future interest in property that arises or “springs” into existence only if a specified event occurs. See, for example Section 647 of 1 Ky. *Practice Series, Probate & Procedure* which includes this: “. . . such language might be interpreted as a springing interest cutting short a resulting estate in fee in the grantor.” In a real sense, that is what happened in *Terrell* since the condo association’s lien was held to attach to the debtor’s fee interest before the trustee’s lien could attach. See also, 1 Ohio Jur. 3d *Abstracts and Land Titles* § 23 titled Outstanding lesser estates, mortgages, liens, and charges.

[iii] The trustee’s Strong-Arm Powers deem the trustee to be a judgment lien creditor as of the day the bankruptcy case was filed and avoid transfers (including the attachment of liens) if a judgment lien creditor could avoid that transfer.

[iv] There are important exceptions to the choate requirements that provide protections for certain liens in competition with the IRS

liens in 26 U.S.C. Section 6323.

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