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The Unlucky Penny: How $0.01 in Collateral Value Can Limit the Debtor's Ability to Strip Off a Junior Mortgage in a Chapter 7 Bankruptcy Proceeding

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THE UNLUCKY PENNY: HOW $0.01 IN COLLATERAL VALUE CAN LIMIT THE DEBTOR'S ABILITY TO STRIP OFF A JUNIOR MORTGAGE IN A CHAPTER 7 BANKRUPTCY PROCEEDING

Keri Mahoney[*]

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I. INTRODUCTION

The combination of the increased number of underwater mortgages[1] and the increased number of bankruptcy filings[2] has created at least one new issue in bankruptcy law: can a debtor avoid liability on a lien that was fully secured by collateral in his home at the outset of the loan, if a subsequent decrease in the value of the collateral (i.e. his home) has caused the lien to become less than fully secured at the time of the bankruptcy filing? This question can arise in two contexts, each of which follows its own analysis: (1) an attempt to "strip down" the amount of debt owed on a loan to match the current value of the collateral; or (2) an attempt to "strip off" a loan in its entirety, when there is no remaining value on the collateral. Additionally, the analysis varies based on the Chapter of the Bankruptcy Code used for the proceeding.

Individuals filing for bankruptcy typically utilize either Chapter 7 or Chapter 13 of the Bankruptcy Code (the "Code").[3] The Supreme Court has clearly prohibited stripping down a mortgage in both Chapter 7 and Chapter 13 proceedings,[4] but has remained silent as to stripping off a mortgage in either Chapter. So far, the Circuit Courts have agreed that a Chapter 13 debtor may strip off a wholly unse-

[1] Les Christie, *More Than 30% of Mortgage Borrowers Still Underwater*, CNN MONEY (May 24, 2012, 5:23AM), http://money.cnn.com/2012/05/24/real_estate/underwater-mortgages/index.htm (indicating that nearly one-third of borrowers owe more money on their mortgage than their home is worth).

[2] *Compare Business and Nonbusiness Cases Commenced, by Chapter of the Bankruptcy Code, During the 12-Month Period Ending December 31, 2012*, U.S. BANKR. COURTS, http://www.uscourts.gov/uscourts/Statistics/BankruptcyStatistics/BankruptcyFilings/2012/1212_f2.pdf (last visited Mar. 22, 2013) [hereinafter *2012 Bankruptcy Report*] (indicating that approximately 1.2 million bankruptcy proceedings were filed in the federal courts of the United States in 2012), *with Business and Nonbusiness Bankruptcy Cases Commenced, By Chapter of the Bankruptcy Code, During the Twelve Month Period Ended Dec. 31, 2007*, U.S. BANKR. COURTS http://www.uscourts.gov/uscourts/Statistics/BankruptcyStatistics/BankruptcyFilings/2007/1207_f2.pdf (last visited Mar. 22, 2013) (indicating that approximately 850,000 bankruptcy proceedings were filed in 2007).

[3] *2012 Bankruptcy Report*, *supra* note 2 (noting that of the total number of bankruptcy filings in 2012, 843,545 were filed under Chapter 7, while 366,532 were filed under Chapter 13; therefore 99% of all bankruptcy proceedings during 2012 were filed under either Chapter 7 or Chapter 13).

[4] Dewsnup v. Timm, 502 U.S. 410, 417 (1992) (holding that a Chapter 7 debtor cannot strip down a partially unsecured mortgage); Nobelman v. Am. Sav. Bank, 508 U.S. 324, 325-26 (1993) (holding that a Chapter 13 debtor cannot strip down a partially undersecured mortgage).

cured junior mortgage;[5] however, a recent ruling in the Eleventh Circuit created a split as to the issue of whether a Chapter 7 debtor may strip off a wholly unsecured junior mortgage.[6]

This Comment discusses the nuances of underwater mortgages and bankruptcy proceedings. Part II provides an overview of the common types of bankruptcy and the basic terminology related to the concepts discussed in this Comment. Part III summarizes the Supreme Court's interpretation of the Code as applied to stripping down of primary mortgages in both Chapter 7 and Chapter 13 proceedings. Part IV discusses how the Circuit Courts have applied the Supreme Court's jurisprudence to the related concept of stripping off in Chapter 7 proceedings. Part IV ultimately concludes that the minority rule allowing stripping off in Chapter 7 proceedings is the correct view based on the plain text of the Code. Part V describes how the Circuit Courts have applied the Supreme Court's jurisprudence described in Part III to the related concept of stripping off in Chapter 13 proceedings in order to universally hold that stripping off in Chapter 13 is allowed. Finally, Part VI briefly discusses the conclusions reached in the earlier sections of this Comment.

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[5] *See* First Mariner Bank v. Johnson, 411 B.R. 221, 224 (D. Md. 2009), *aff'd sub nom In re* Johnson, 407 Fed. Appx. 713 (4th Cir. 2011) (unpublished, per curium); Lane v. W. Interstate Bancorp (*In re* Lane), 280 F.3d 663, 665 (6th Cir. 2002); Zimmer v. PSB Lending Corp. (*In re* Zimmer), 313 F.3d 1220, 1227 (9th Cir. 2002); Pond v. Farm Specialist Realty (*In re* Pond), 252 F.3d 122, 127 (2d Cir. 2001); Tanner v. FirstPlus Fin., Inc. (*In re* Tanner), 217 F.3d 1357, 1360 (11th Cir. 2000); McDonald v. Master Fin., Inc. (*In re* McDonald), 205 F.3d 606, 615 (3d Cir. 2000); Bartee v. Tara Colony Homeowners Ass'n (*In re* Bartee), 212 F.3d 277, 296 (5th Cir. 2000); Fisette v. Keller (*In re* Fisette), 455 B.R. 177, 187 (B.A.P. 8th Cir. 2011); Domestic Bank v. Mann (*In re* Mann), 249 B.R. 831, 840 (B.A.P. 1st Cir. 2000) (all holding that a Chapter 13 debtor may strip off a wholly unsecured junior mortgage during a bankruptcy proceeding).

[6] *Compare* McNeal v. GMAC Mortg., LLC (*In re* McNeal), 477 F. App'x 562, 564-65 (11th Cir. 2012) (unpublished opinion) (holding that a Chapter 7 debtor may strip off a wholly unsecured junior mortgage), *with, e.g.,* Ryan v. Homecomings Fin. Network, 253 F.3d 778, 783 (4th Cir. 2001) (holding that a Chapter 7 debtor may not strip off a wholly unsecured junior mortgage).

II. OVERVIEW OF RELEVANT BANKRUPTCY LAW

A. Chapter 7 and Chapter 13 Filings in the Wake of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005

Individuals who file for bankruptcy typically do so under either Chapter 7 ("Liquidation Bankruptcy") or Chapter 13 ("Individual Debt Adjustment") of the Code.[7] The Chapter 13 debtor must create a "reorganization plan," which aims to pay off debts with future earnings.[8] The debtor must comply with the reorganization plan, attend educational courses, and fulfill other requirements in order to obtain discharge of his debt.[9]

The Chapter 13 debtor must pay back varying degrees of his debt based on the categorization of the creditor's claim as priority, secured or unsecured.[10] "Priority claims are those granted special status by the bankruptcy law, such as most taxes and the costs of bankruptcy proceedings."[11] These claims must be paid in full, unless the creditor agrees to accept less than full payment.[12] Secured claims are those which are secured by collateral in real property.[13] "If the debtor wants to keep the collateral securing a particular claim, then the plan must provide that the holder of the secured claim receive at least the value of the collateral," or, in some cases, "full payment of the

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[7] *2012 Bankruptcy Report*, *supra* note 2 (99% of all bankruptcy filings during 2012 were filed under either Chapter 7 or Chapter 13); *see also Bankruptcy Basics, Chapter 7: Liquidation Under the Bankruptcy Code*, U.S. COURTS, http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/Chapter7.aspx (last visited Mar. 22, 2013) [hereinafter *Chapter 7 Basics*] (describing Chapter 7 bankruptcy as liquidation); *Bankruptcy Basics, Chapter 13: Individual Debt Adjustment*, U.S. COURTS, http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/Chapter13.aspx (last visited Mar. 22, 2013) [hereinafter *Chapter 13 Basics*] (describing Chapter 13 bankruptcy as individual debt adjustment).

[8] *Chapter 13 Basics*, *supra* note 7.

[9] *Id.*

[10] *Id.*

[11] *Id.*; *see also* 11 U.S.C. § 507 (Supp. IV 2010) (describing the types of claims that are entitled to priority).

[12] *Chapter 13 Basics*, *supra* note 7; *see also* 11 U.S.C. § 1322(a)(2) (Supp. IV 2010) ("The plan . . . shall provide for the full payment . . . of all claims entitled to priority [status] . . . unless the holder of a particular claim agrees to a different treatment of such claim.").

[13] *Chapter 13 Basics*, *supra* note 7.

debt."[14] Unsecured claims are those which are not priority claims and which are not secured by any particular interest in the debtor's property.[15] Unsecured claims do not need to be paid back in full as long as the "debtor will pay all projected 'disposable income' over an 'applicable commitment period,' and as long as unsecured creditors receive at least as much under the plan as they would receive if the debtor's assets were liquidated under Chapter 7."[16] If the debtor complies with all of his obligations throughout the reorganization period, the debtor will receive a discharge from "all debts provided for by the plan."[17]

Conversely, a Chapter 7 debtor must place all of her non-exempt property into the hands of a bankruptcy trustee.[18] The trustee liquidates the debtor's property and distributes the proceeds to creditors in a certain order of priority based on the type of each claim held.[19] Creditors who hold priority claims are paid first and the remaining funds are then distributed through the other classes of claims; the last person paid is the debtor herself.[20] The Chapter 7 debtor's concerns typically center on "retain[ing] exempt property and receiv[ing] a discharge that covers as many debts as possible" because the debtor will not receive any distribution from the liquidation unless and until all other classes of claims have been fully repaid.[21]

In 2005, "Congress enacted the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA") to correct perceived abuses to the bankruptcy system."[22] Congress wanted to ensure that only honest debtors, who utilized bankruptcy as "a last re-

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[14] *Id.*

[15] *Id.*

[16] *Id.*; *see also* 11 U.S.C. § 1325(a)(4) (Supp. IV 2010) ("[T]he court shall confirm a plan if . . . the value . . . of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under chapter 7 . . . .").

[17] *Chapter 13 Basics*, *supra* note 7.

[18] *Chapter 7 Basics*, *supra* note 7.

[19] *Id.* ("Under § 726 of [the Code], there are six classes of claims; and each class must be paid in full before the next lower class is paid anything."); *see also* 11 U.S.C. § 726(a) (Supp. IV 2010) (describing the six classes of claims and the order of priority for distribution in liquidation bankruptcy).

[20] 11 U.S.C. § 726(a).

[21] *Chapter 7 Basics*, *supra* note 7.

[22] Mark A. Redmiles, *The Supreme Court Interprets the Means Test*, AM. BANKR. INST. J. 18 (Apr. 2011).

sort" to receive a fresh start from "severe financial distress," could file for bankruptcy, and prevent use of the system as "a head start for individuals who could repay some or all of their debts but preferred not to."[23] Additionally, portions of the BAPCPA were designed to limit the availability of Chapter 7 bankruptcy in order to prevent debtors from using Chapter 7 to clear debts which they could afford to repay through a Chapter 13 plan.[24] However, in 2012, Chapter 7 bankruptcy filings were filed at more than double the rate of Chapter 13 filings.[25] Thus, Chapter 7 remains the most common mechanism for an individual to file for bankruptcy.

B. Stripping Off and Stripping Down

Historically, a creditor who held a debt secured by collateral in the debtor's primary residence had a relatively safe investment because home values were typically expected to rise.[26] As long as the value of the collateral (the home) remained greater than the debt owed, the debt remained fully secured by the value of the home. However, as housing prices took a plunge in recent years, some home mortgages became unsecured when the value of the home dropped to an amount less than the amount owed on the mortgage.[27] Consider, for example, a buyer who purchased a home valued at $200,000 by taking a primary mortgage in the amount of $180,000 and a secondary mortgage in the amount of $20,000. Both mortgages were fully secured by the value of the home at the time the home was purchased and the mortgages were created. Assume that shortly after the purchase, the buyer filed for bankruptcy before having owned the home for enough time to make any significant contribution to the principal of the mortgage. If the real estate market had fluctuated such that, at the time of filing for bankruptcy, the buyer's home was only valued

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[23] *Id.*

[24] Jeanne Sahadi, *The New Bankruptcy Law and You*, CNN MONEY (Oct. 17 2005, 12:17 PM) http://money.cnn.com/2005/10/17/pf/debt/bankruptcy_law/index.htm.

[25] *2012 Bankruptcy Report*, *supra* note 2.

[26] *See, e.g.*, GILLETTE EDMUNDS & JIM KEENE, RETIRE ON THE HOUSE: USING REAL ESTATE TO SECURE YOUR RETIREMENT 1 (2006) (discussing an optimistic view of the real estate market, one in which one can possibly expect to retire on home equity alone).

[27] Jake Miller, *Issue Brief: Housing*, CBS NEWS (Oct. 1, 2012, 12:00 PM), http://www.cbsnews.com/8301-505103_162-57523544/issue-brief-housing/ (describing the steady decline in home values in recent years, stating that "[i]n 2008, the bottom fell out, and housing prices plunged nationwide").

at $160,000, then at the time of the bankruptcy filing the amount owed on the primary mortgage alone exceeded the total value of the home. Furthermore, there would be no collateral left to secure any portion of the secondary mortgage. Therefore, at the time of the bankruptcy filing, the primary mortgage would be considered partially unsecured, while the secondary mortgage would be considered wholly unsecured.

The phenomenon discussed above has created the bankruptcy concepts of "stripping off" and "stripping down." *Stripping down* refers to the debtor's attempt to void the unsecured portion of a partially unsecured debt.[28] In the above example, the debtor would try to strip down his primary mortgage from $180,000 to $160,000 because, at the time of bankruptcy filing, the collateral was only valued at $160,000. *Stripping off* refers to voiding a debt (usually a junior lien) that is wholly unsecured at the time of bankruptcy filing.[29] In the above example, the debtor would attempt to strip off the secondary mortgage in its entirety, because the amount owed on the primary mortgage alone ($180,000) exceeds the entire value of the collateral ($160,000), leaving no collateral to secure any portion of the secondary mortgage.

The Supreme Court has disallowed the practice of stripping down in both Chapter 7 and Chapter 13 bankruptcy proceedings,[30] but has remained silent as to the practice of stripping off in both types of proceedings. Until recently, the few circuit courts that ruled on the issue held that a Chapter 7 debtor may not strip off a wholly unsecured junior mortgage.[31] However, the Eleventh Circuit recently

[28] *See, e.g.*, Dewsnup v. Timm, 502 U.S. 410, 412 (1992) (discussing a debtor's attempt to "strip down" a lien when the value of the collateral was less than the amount of the creditor's claim).

[29] *See, e.g.*, Ryan v. Homecomings Fin. Network, 253 F.3d 778, 779 (4th Cir. 2001) (discussing a debtor's attempt to "strip off" a junior lien when the primary mortgage exceeded the value of the home).

[30] *Dewsnup*, 502 U.S. at 417 (holding that a Chapter 7 debtor cannot strip down the value of an outstanding mortgage debt to match the value of the underlying collateral); Nobelman v. Am. Sav. Bank, 508 U.S. 324, 325-26 (1993) (holding that a Chapter 13 debtor cannot strip down the value of a mortgage debt to match the value of the underlying collateral).

[31] Talbert v. City Mortg. Servs. (*In re* Talbert), 344 F.3d 555, 556 (6th Cir. 2003) ("[W]e hold that a Chapter 7 debtor may not use § 506 to 'strip off' an allowed junior lien where the senior lien exceeds the fair market value of the real property in question."); *Ryan*, 253 F.3d at 779 ("[W]e hold that a debtor may not strip off an unsecured but allowed lien pursuant to Section 506(d)."); Laskin v. First Nat'l Bank of Keystone (*In re* Laskin), 222 B.R. 872, 876 (B.A.P. 9th Cir. 1998) ("Section 506 was intended to facilitate valuation and disposition of

broke ranks and created the minority view, being the first Circuit to hold that it is permissible to strip off a wholly unsecured junior mortgage during a Chapter 7 proceeding.[32] Courts have reached the exact opposite conclusion with respect to Chapter 13 proceedings, with a distinct majority of courts holding that a wholly unsecured junior mortgage can be stripped off during a Chapter 13 proceeding.[33] The reasons for the difference in treatment of unsecured junior mortgages in each Chapter will be discussed in Parts IV and V *infra*.

III. STRIPPING DOWN AND THE SUPREME COURT

A. Chapter 7: *Dewsnup v. Timm*[34]

In the early 1990s, a split developed in the circuit courts as to whether a primary mortgage could be stripped down to the value of the underlying collateral in a Chapter 7 bankruptcy proceeding.[35] In 1992, the Supreme Court settled this issue in the case *Dewsnup v. Timm*.[36] In *Dewsnup*, Chapter 7 debtors had an outstanding debt of approximately $120,000—an amount which exceeded the fair market

property in the reorganization chapters of the Code, not to confer an additional avoiding power on a Chapter 7 debtor.").

[32] McNeal v. GMAC Mortg., LLC (*In re* McNeal), 477 F. App'x 562, 564-65 (11th Cir. 2012) (unpublished opinion) (holding that a Chapter 7 debtor may strip off a wholly unsecured junior mortgage).

[33] *See* First Mariner Bank v. Johnson, 411 B.R. 221, 224 (D. Md. 2009), *aff'd sub nom* First Mariner Bank v. Johnson (*In re* Johnson), 407 Fed. App'x 713 (4th Cir. 2011) (unpublished, per curium); Lane v. W. Interstate Bancorp (*In re* Lane), 280 F.3d 663, 665 (6th Cir. 2002); Zimmer v. PSB Lending Corp. (*In re* Zimmer), 313 F.3d 1220, 1227 (9th Cir. 2002); Pond v. Farm Specialist Realty (*In re* Pond), 252 F.3d 122, 127 (2d Cir. 2001); Tanner v. FirstPlus Fin., Inc. (*In re* Tanner), 217 F.3d 1357, 1360 (11th Cir. 2000); McDonald v. Master Fin., Inc. (*In re* McDonald), 205 F.3d 606, 615 (3d Cir. 2000); Bartee v. Tara Colony Homeowners Ass'n (*In re* Bartee), 212 F.3d 277, 296 (5th Cir. 2000); Fisette v. Keller (*In re* Fisette), 455 B.R. 177, 187 (B.A.P. 8th Cir. 2011); Domestic Bank v. Mann (*In re* Mann), 249 B.R. 831, 840 (B.A.P. 1st Cir. 2000) (all holding that a Chapter 13 debtor could strip off a wholly unsecured junior mortgage during a bankruptcy proceeding).

[34] 502 U.S. 410.

[35] *Compare, e.g.*, Dewsnup v. Timm (*In re* Dewsnup), 908 F.2d 588, 593 (10th Cir. 1990) (prohibiting strip down in a Chapter 7 bankruptcy proceeding), *aff'd sub nom.* Dewsnup v. Timm, 502 U.S. 410, *with, e.g.*, Gaglia v. First Fed. Sav. & Loan Ass'n, 889 F.2d 1304, 1308 (3d Cir. 1989) (allowing strip down in a Chapter 7 bankruptcy proceeding) *abrogated by Dewsnup*, 502 U.S. 410.

[36] 502 U.S. 410.

value of the property acting as collateral on the loan.[37] The debtors argued that because the amount of the lien exceeded the value of the collateral, the lien should be reduced such that the outstanding debt would equal the fair market value of the land.[38] The Court stated the issue as whether "a debtor [may] 'strip down' a creditor's lien on real property to the value of the collateral, as judicially determined, when that value is less than the amount of the claim secured by the lien?"[39] The Court held that stripping down under these circumstances was not permissible, based on the plain text of the statute and supported by legislative intent.[40]

1. Statutory Interpretation

Prior to the Supreme Court's holding in *Dewsnup*, Chapter 7 debtors relied on the interplay between § 506(a) and § 506(d) in order to justify stripping down of an undersecured mortgage.[41] Section 506(a) allows a debtor to bifurcate a lien into secured and unsecured components,[42] while section 506(d) allows a debtor to void most claims that are not "allowed secured claims."[43] Therefore, pre-*Dewsnup* debtors argued that the plain text of § 506(a) allowed a debtor to split his mortgage lien into secured and unsecured components and § 506(d) allowed the debtor to void the unsecured portion.[44] This plain text argument was rejected by the Court.[45]

In *Dewsnup*, the debtors carefully crafted their argument in favor of stripping down by reading § 506(a) and (d) of the bankruptcy

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37 *Id.* at 413.

38 *Id.*

39 *Id.* at 412.

40 *Id.* at 417.

41 *E.g.*, Gaglia v. First Fed. Sav. & Loan Ass'n, 889 F.2d 1304, 1306 (3d Cir. 1989), *abrogated by Dewsnup*, 502 U.S. 410.

42 11 U.S.C. § 506(a) (2006) ("An allowed claim of a creditor secured by a lien on property in which the estate has an interest . . . is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property, or to the extent of the amount subject to setoff, as the case may be, and is an unsecured claim to the extent that the value of such creditor's interest or the amount so subject to setoff is less than the amount of such allowed claim.").

43 *Id.* § 506(d) ("To the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void . . . .").

44 *E.g.*, *Gaglia*, 889 F.2d at 1306.

45 *Dewsnup*, 502 U.S. 410.

code as complementary provisions.[46] The debtors argued that § 506(a) could be used to bifurcate allowed claims into secured and unsecured claims; then § 506(d) could be used to void any claim which was not an allowed, secured claim under § 506(a).[47] On the other hand, the creditor argued that within § 506(d), "the words [allowed and secured] should be read term-by-term to refer to any claim that is first, allowed, and second secured."[48] Therefore, the creditor concluded that § 506(d) could not be used to void any amount of the lien, because the lien itself was, " 'allowed' pursuant to §502 of the Code and [was] secured by a lien with recourse to the underlying collateral . . . ."[49]

The Court adopted the interpretation of the creditor, reasoning that "§ 506(d) does not allow [debtors] to 'strip down' [a creditor's] lien, because [a creditor's] claim is secured by a lien and has been fully allowed pursuant to § 502."[50] The Court observed that the statutory text is ambiguous on this point, but looked to legislative intent to adopt the interpretation that § 506(a) should be read separately from § 506(d).[51] The Court favored the creditor's interpretation of the ambiguity, as this interpretation was most consistent with pre-Code treatment of these types of liens.[52]

2. Legislative Intent

The creditor argued that prior to the enactment of the present-day versions of § 506(a) and (d), liens of the type in question passed through bankruptcy unaffected; therefore, absent clear legislative intent to the contrary, this long-standing practice should not be disturbed.[53] The Court agreed with this argument, pointing to earlier jurisprudence of the Court indicating that a bankruptcy discharge destroys only *in personam* liability against the debtor, while leaving

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[46] Brief for Petitioner at *14 Dewsnup v. Timm, 502 U.S. 410 (1992) (No. 90-741); *see also* 11 U.S.C. § 506.

[47] Brief for Petitioner at *14 Dewsnup v. Timm, 502 U.S. 410 (1992) (No. 90-741).

[48] *Dewsnup*, 502 U.S. at 415.

[49] *Id.*

[50] *Id.* at 417.

[51] *Id.*

[52] *Id.*

[53] Brief for Respondent at *27 Dewsnup v. Timm, 502 U.S. 410 (1992) (No. 90-741).

in rem liability intact.[54] The Court seemingly adopted the creditor's observation that "there [was] nothing in the Code's legislative history that reflect[ed] any intent to alter that law."[55] The ambiguity in the text itself, combined with the lack of language within the legislative history indicating intent to depart from the pre-Code treatment of these types of liens, caused the Court to conclude that it was "not convinced that Congress intended to depart from the pre-Code rule that liens pass through bankruptcy unaffected."[56]

3. *Implications for Similar Scenarios*

While the *Dewsnup* court was clear in its holding with respect to an undersecured primary mortgage in a Chapter 7 proceeding, it is difficult to determine the breadth of its holding with respect to similar, but not identical, fact situations. The Court carefully limited its holding to the case before it, expressly stating that:

> Hypothetical applications that come to mind and those advanced at oral argument illustrate the difficulty of interpreting the statute in a single opinion that would apply to all possible fact situations. We therefore focus upon the case before us and allow other facts to await their legal resolution on another day.[57]

These two sentences provide significant support for the minority of courts that have held that *Dewsnup* does not apply to the similar, but not identical, issue of stripping off a wholly unsecured junior mortgage.[58] The Court was careful to expressly limit the holding to a very specific fact pattern; the express language of the opinion indicates that courts need not overturn other contrary rules in similar situations based on the *Dewsnup* holding.[59] Nonetheless, a majority of courts have found *Dewsnup* to be controlling precedent when

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54 *Dewsnup*, 502 U.S. at 418 (discussing Johnson v. Home State Bank, 501 U.S. 78, 84 (1991)).

55 *Id.* at 416.

56 *Id.* at 417.

57 *Id.* at 416-17.

58 *E.g.*, *In re* Lavelle, No. 09-72389-478, 2009 WL 4043089 at *4 (Bankr. E.D.N.Y. Nov. 19, 2009) (quoting above two sentences from *Dewsnup* in reaching the conclusion that *Dewsnup* is not controlling in similar, but not identical, factual situations such as stripping off), *overruled by* Wachovia Mortg. v. Smoot, 478 B.R. 555 (E.D.N.Y. 2012).

59 *Dewsnup*, 502 U.S. at 416-17.

faced with the issue of stripping off a wholly unsecured junior mortgage, as discussed in Part IV.A. *infra*.

B. Chapter 13: *Nobelman v. American Savings Bank*[60]

When filing for bankruptcy under Chapter 13 of the Code, the debtor must create a reorganization plan with the goal of repayment of certain debts with "future earnings or other future income."[61] Section 1322(b) of the Code describes the parameters of a reorganization plan and provides that the debtor's plan may "modify the rights of holders of secured claims."[62] Therefore, the issue of stripping down an undersecured mortgage, follows an entirely different analysis in a Chapter 13 case than in a Chapter 7 case, because § 1322 is available as a mechanism to modify the rights of certain secured creditors for Chapter 13 debtors but not for Chapter 7 debtors.[63]

Section 1322(b)(2) sets out a general rule that the rights of secured creditors *may be* modified as part of a debt reorganization plan.[64] However, immediately following this rule is the antimodification exception, which prohibits modifications of rights of claimants who hold a debt secured only by the debtor's primary residence.[65] The question in a Chapter 13 proceeding, therefore, is not only whether the claim is an "allowed secured claim" under § 506, but also whether such a claim falls within the antimodification exception stated in § 1322(b)(2).[66]

In *Nobelman*, the facts were similar to *Dewsnup*; however in *Nobelman*, the debtors filed their petition under Chapter 13 and requested stripping down of the mortgage as part of a reorganization plan created pursuant to § 1322,[67] while in *Dewsnup*, the debtors had filed their petition under Chapter 7 and requested stripping down of

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[60] 508 U.S. 324 (1993).

[61] 11 U.S.C. § 1322(a)(1) (Supp. IV 2010).

[62] *Id.* § 1322(b)(2).

[63] *Compare, e.g.*, *Dewsnup*, 502 U.S. at 411-13 (determining whether § 506 allows strip down in Chapter 7 proceeding), *with, e.g.*, *Nobelman*, 508 U.S. at 325-26 (determining whether § 1322 allows strip down in Chapter 13 proceedings).

[64] 11. U.S.C. § 1322(b)(2).

[65] *Id.*

[66] *E.g.*, *Nobelman*, 508 U.S. at 332 (finding that debtor could not strip down mortgage because antimodification exception applied).

[67] *Id.* at 326.

the mortgage pursuant to § 506(d).[68] In *Nobelman*, the debtors argued that the antimodification protection of 1322(b)(2) applied "only to the extent the mortgagee holds a 'secured claim' in the debtor's residence and that [the court] must first look to § 506(a) to determine the value of the mortgagee's 'secured claim.' "[69] The debtors further argued that "[u]nder this view, the bank is the holder of a 'secured claim' only in the amount of . . . the value of the collateral property."[70] Therefore, the debtors concluded that § 1322(b)(2) should allow a debtor to strip down an undersecured mortgage in a Chapter 13 proceeding.[71]

The Court disagreed with the debtors' arguments, and instead determined that § 1322 did not allow a debtor to strip down an undersecured mortgage.[72] The Court focused heavily on the precise terminology used in the statute, and noted that § 1322 speaks to modification of "rights" of the creditor, rather than modification of "claims" of the creditor.[73] Absent a definition of the term "rights" in the Code, the Court determined that "Congress ha[d] 'left the determination of property rights in the assets of a bankrupt's estate to state law,' since such '[p]roperty interests are created and defined by state law.' "[74] The rights of the mortgagee, therefore, were deemed to be those rights set out in the mortgage instrument, which, as the Court noted, typically include "the right to repayment of the principal in monthly installments over a fixed term at specified adjustable rates of interest . . . ."[75] Therefore, in *Nobelman*, the creditor's *rights* were protected by the antimodification exception, because the creditor still held a claim secured by collateral in the debtors' primary residence, regardless of the fact that the value of the collateral was less than the amount of the creditor's claim.[76] The Court concluded that stripping down was not allowed, because modification of the amount of the

68 *Dewsnup*, 502 U.S. at 411-412, 413.

69 *Nobelman*, 502 U.S. at 328.

70 *Id.*

71 *Id.*

72 *Id.* at 332.

73 *Id.* at 328.

74 *Nobelman*, 502 U.S. at 329 (second alteration in original) (quoting Butner v. United States, 440 U.S. 48, 54-55 (1979)).

75 *Id.* ("These are the rights that were 'bargained for by the mortgagor and the mortgagee,' and are rights protected from modification by § 1322(b)(2).").

76 *Id.* at 331.

mortgage principal would be a modification of a right of a creditor holding a claim secured by an interest in the debtors' principal residence—precisely the type of modification disallowed by § 1322(b)(2).[77]

Although the majority focused purely on the language of § 1322 in reaching its holding, Justice Stevens discussed the policy supporting the majority opinion in his concurring opinion.[78] Stevens questioned why Congress would provide more protection for a mortgagee holding a lien secured by collateral in a debtor's primary residence than for any other creditor holding a lien secured by collateral in other real or personal property.[79] Stevens noted that Congress likely provided more protection to mortgagees of primary residences in order to "encourage the flow of capital into the home lending market."[80]

Therefore, *Nobelman* provides two major rationales for prohibiting stripping down of a mortgage on a debtor's primary residence in a Chapter 13 proceeding. First, the plain text of § 1322 speaks to protection of creditor's "rights" as to a claim secured by a debtor's primary mortgage.[81] Modification of the amount of the principal is a modification of the "right" of the creditor and therefore is prohibited by the antimodificaiton exception at § 1322(b)(2).[82] Second, Congress intended to protect mortgagees from modification under Chapter 13 in order to encourage more lending in the residential real estate market.[83] The result of *Nobelman* is that the antimodification exception found within § 1322(b)(2) prohibits a debtor from modifying the *rights* of a creditor with respect to a lien that is partially or wholly secured by the debtor's primary residence.[84]

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[77] *Id.* (noting that the terms of the mortgage instrument include the amount of the principal, the term of the loan, the interest rate and the monthly payment, and that modification of any of these terms would be an impermissible modification of creditor's rights).

[78] *Id.* at 332 (Stevens, J., concurring).

[79] *Nobelman*, 508 U.S. at 332 (Stevens, J., concurring).

[80] *Id.*

[81] *Id.* at 328 (majority opinion).

[82] *Id.* at 332.

[83] *Id.* (Stevens, J., concurring).

[84] *Nobelman*, 508 U.S. at 332 (majority opinion).

C. Conclusions of *Dewsnup* and *Nobelman*

The Supreme Court has, therefore, banned the practice of stripping down undersecured mortgages in both Chapter 7 and Chapter 13 proceedings.[85] This means that if there is any amount of value in the home that is acting as collateral for the mortgage, even just one penny, the mortgage may not be stripped down to match the value of the home. In order to reach this conclusion, the Court's primary consideration was the precise textual meaning of the applicable statutes within the Code.[86] The Court also turned to legislative intent to aid in its interpretation and to provide support for its plain text conclusions.[87] These same principles of interpretation will be applied to the related concept of mortgage strip off in Parts IV and V *infra*.

IV. STRIPPING OFF AND CHAPTER 7

A. Majority View: Stripping Off Is Not Allowed

Courts have struggled to determine whether *Dewsnup* applies in full force when a debtor attempts to strip off a junior lien that has become wholly unsecured by virtue of depreciation of the value of the home.[88] In such cases, the debtor's residence is typically subject to two liens: (1) a primary mortgage which, by itself, exceeds the value of the home; and (2) a secondary mortgage (the junior lien), for which there is no remaining value on the home to act as collateral once the primary mortgage is satisfied.[89] While courts are split, a distinct majority of courts have found that *Dewsnup* prohibits stripping

[85] *Id.* at 325-26 (holding that §1322(b)(2) disallows strip down of a mortgage in Chapter 13 proceeding); Dewsnup v. Timm, 502 U.S. 410, 417 (1992) (disallowing strip down of a mortgage in Chapter 7 proceeding).

[86] *Nobelman*, 508 U.S. at 328 (focusing on the use of the term "rights" in the plain text of the statute); *Dewsnup*, 502 U.S. at 415, 417 (concluding that "the better of the several approaches" to interpretation involves reading each term in the statute separately).

[87] *Nobelman*, 508 U.S. at 332 (Stevens, J., concurring) (reconciling plain text interpretation with legislative intent to increase flow of lending into home market); *Dewsnup*, 502 U.S. at 417 (considering Congressional intent in light of historical treatment of similar liens).

[88] *See generally, e.g.*, Laskin v. First Nat'l Bank of Keystone (*In re* Laskin), 222 B.R. 872 (B.A.P. 9th Cir. 1998) (court considers application of *Dewsnup* when Chapter 7 debtor seeks to strip off wholly unsecured junior lien).

[89] *E.g.*, *id.* at 873 (debtors' residence subject to two mortgages, the primary mortgage alone exceeds the value of the home).

off a wholly unsecured junior mortgage, just as it prohibits stripping down a partially unsecured primary mortgage.[90]

1. *Ninth Circuit Bankruptcy Appellate Panel:* Laskin v. First National Bank of Keystone (In re *Laskin*)[91]

The Ninth Circuit Bankruptcy Appellate Panel[92] was the first post-*Dewsnup* appellate court to interpret § 506(d) in the context of stripping off a lien attached to real property.[93] In *Laskin*, the debtors held property that was subject to two liens: (1) an undersecured primary mortgage; and (2) a wholly unsecured junior lien.[94] The debtors sought to strip off the wholly unsecured junior lien during their Chapter 7 bankruptcy proceeding.[95]

In order to escape *Dewsnup's* prohibition on lien stripping, the debtors argued that their lien was entirely unlike the lien at issue in *Dewsnup* because their lien was wholly, rather than partially, unsecured at the time of the bankruptcy filing.[96] The debtors reasoned that the *Dewsnup* holding was a narrow holding; one that applied only to a debtor's attempt to strip down a partially secured lien.[97] The debtors concluded that the *Dewsnup* holding, therefore, had no bearing on their attempt to strip off their junior mortgage, because their

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[90] *E.g.*, Talbert v. City Mortg. Servs. (*In re* Talbert), 344 F.3d 555, 556 (6th Cir. 2003) ("Because the Supreme Court's reasoning in *Dewsnup* . . . applies with equal force and logic to the issue at hand, we hold that a Chapter 7 debtor may not use § 506 to 'strip off' an allowed junior lien . . . ."); Ryan v. Homecomings Fin. Network, 253 F.3d 778, 779 (4th Cir. 2001) ("Because we find that the Supreme Court's reasoning in *Dewsnup* . . . is equally applicable to 'strip offs' as to 'strip downs', [sic] we hold that a debtor may not strip off an unsecured but allowed lien . . . ."); *Laskin*, 222 B.R. at 875 ("[W]e conclude that *Dewsnup* nevertheless bars the relief debtors seek.").

[91] 222 B.R. 872.

[92] To date, five circuits have established Bankruptcy Appellate Panels (BAPs) which are "unit[s] of the federal courts of appeals" having jurisdiction over "[a]ppeals from dispositive orders of bankruptcy judges . . . with further appeal as of right to the court of appeals for the circuit." *Courts of Appeals: Bankruptcy Appellate Panels*, UNITED STATES COURTS, http://www.uscourts.gov/FederalCourts/UnderstandingtheFederalCourts/CourtofAppeals/BankruptcyAppellatePanels.aspx (last visited Mar. 22, 2013).

[93] *Laskin*, 222 B.R. 872.

[94] *Id.* at 873.

[95] *Id.* at 874.

[96] *Id.*

[97] *Id.*

junior mortgage was wholly unsecured.[98] Instead, the debtors equated their case with numerous other cases where a debtor sought to strip off a wholly unsecured junior mortgage.[99] The debtors cited numerous cases in which other courts had allowed a *Chapter 13* debtor to strip off a wholly unsecured junior lien, and urged the court to adopt the view of these courts in their *Chapter 7* proceeding.[100] However, this argument was fatally flawed because of the debtors' exclusive reliance on Chapter 13 cases for support.[101] These cases were easily distinguished because in each Chapter 13 case the strip off had been allowed pursuant to § 1322(b)(2)—a provision of the Code which does not apply to a Chapter 7 debtor.[102] Therefore, the debtors had failed to provide any legal support for their contention that a debtor should be allowed to strip off a wholly unsecured junior lien during a Chapter 7 bankruptcy proceeding.[103]

Additionally, the court noted (although the debtors had neglected to) that there were at least two post-*Dewsnup* bankruptcy courts that had allowed a Chapter 7 debtor to strip off a wholly unsecured junior lien.[104] However, the court declined to follow these courts, reasoning that the analysis used by these courts, "reverse[d] the statutory process," as § 506(d) could not, by itself, void a lien which was otherwise allowed and secured.[105] The court found that the same three policy rationales that provided support for *Dewsnup's* prohibition on stripping down similarly provided support for a prohibition on stripping off: (1) consistency with the historical practice of allowing these types of liens to pass through bankruptcy unaffected; (2) respect for the agreement between the mortgagor and mortgagee which allows the lien to remain with the property until foreclosure; and (3) prevention of a windfall for the debtor by allowing any increase in the value of the property prior to the time of foreclosure to accrue in the favor of the creditor.[106] Therefore, the court concluded that the debtors could not strip off their junior lien because *Dewsnup*

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98 *Laskin*, 222 B.R. at 875.

99 *Id.*

100 *Id.*

101 *Id.*

102 *Id.*

103 *Laskin*, 222 B.R. at 873 (affirming denial of debtors' motion for lack of case law).

104 *Id.* at 876.

105 *Id.*

106 *Id.*

prevented a debtor from stripping down or off any lien attached to the debtor's residence, regardless of whether the lien was partially or wholly unsecured.[107]

2. Fourth Circuit: **Ryan v. Homecomings Financial Network**[108]

In *Ryan*, the debtors sought to strip off a wholly unsecured junior mortgage during their Chapter 7 bankruptcy proceeding.[109] The debtors argued that *Dewsnup* did not prevent them from stripping off their unsecured junior lien because *Dewsnup* prohibited the practice of lien stripping only where the lien in question was at least partially secured by equity in the debtor's residence.[110] Alternatively, the debtors argued that *Nobelman* provided support for their contention that a wholly unsecured junior lien could be stripped off during a Chapter 7 proceeding.[111]

The Fourth Circuit disagreed with both of the debtors' arguments.[112] First, the court determined that *Dewsnup* was indistinguishable from *Ryan*, stating:

> [W]e discern no principled distinction to be made between the case *sub judice* and that decided in *Dewsnup*. The Court's reasoning in *Dewsnup* is equally relevant and convincing in a case like ours where a debtor attempts to strip off, rather than merely strip down, an approved but unsecured lien.[113]

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107 *Id.*

108 253 F.3d 778 (4th Cir. 2001).

109 *Id.* at 779.

110 *Id.* at 781.

111 *Id.* at 782. Specifically, the debtors argued that Nobelman prohibited lien stripping under § 1322 only when the claim was "secured by equity in a debtor's principal residence." Brief for Appellants at *11 Ryan v. Homecomings Fin. Network, 253 F.3d 778 (4th Cir. 2001) (No. 00-2137). This argument is barely addressed by the court, however as noted by the creditors, it is clearly misguided, because § 1322 has no bearing on a Chapter 7 case; rather a Chapter 7 debtor needs to find a basis in § 506 to justify voiding any portion of the lien. Brief for Appellee at *20-21 Ryan v. Homecomings Fin. Network, 253 F.3d 778 (4th Cir. 2001) (No. 00-2137) ("Consequently, Nobelman does not stand for the proposition espoused by the Appellants that a Chapter 7 debtor merely has to show lack of equity to strip off a wholly unsecured lien against property, nor is it evidence of a judicial evolution in the interpretation of Section 506 as it applies to Chapter 7 bankruptcies.").

112 *Ryan*, 253 F.3d at 781-82.

113 *Id.* at 782.

The court also noted two distinct rationales stated by the *Dewsnup* court which it believed to be equally applicable to debtors' attempt to strip off the unsecured junior lien: (1) that the mortgagor and mortgagee bargained for the lien to remain with the real property until foreclosure, and therefore "[a]ny increase over the judicially determined valuation during bankruptcy rightly accrues to the benefit of the creditor," and (2) absent clear Congressional intent to the contrary, it would not be proper to create such a "broad new remedy against allowed claims to the extent that they become 'unsecured,' " when traditionally, liens of this kind passed through bankruptcy unaffected.[114]

The court was equally unimpressed by debtors' attempt to use *Nobelman* to support their argument.[115] As the court noted, *Nobelman* hinges on the interpretation of § 1322—a provision of the Code that was inapplicable to the Chapter 7 debtors before the court in *Ryan*.[116] Therefore it was *Dewsnup's* interpretation of § 506(d) that was relevant to *Ryan*.[117] Accordingly, the court determined that *Dewsnup* was controlling; therefore, the Chapter 7 debtors were prohibited from stripping off the wholly unsecured junior lien attached to their residence.[118]

3. *Sixth Circuit:* **Talbert v. City Mortgage Services *(*In re *Talbert)***[119]

In *Talbert*, the debtors attempted to strip off a wholly unsecured junior lien attached to their residence during a Chapter 7 bankruptcy proceeding.[120] The debtors relied on similar arguments as those seen in *Ryan* and *Laskin*.[121] Interestingly, in this case, the creditors chose not to file an answer or other response in the bankruptcy court—the lower court raised the lien stripping issue *sua sponte*.[122] Continuing this strategy, the creditors also chose not to file an appel-

114 *Id.* (quoting Dewsnup v. Timm, 502 U.S. 410, 420 (1992)).
115 *Id.*
116 *Id.*
117 *Ryan*, 253 F.3d at 782.
118 *Id.* at 783.
119 344 F.3d 555 (6th Cir. 2003).
120 *Id.* at 556.
121 *Id.* at 558.
122 *Id.* at 556.

late brief when the case reached the Sixth Circuit.[123] Nonetheless, the court found that *Dewsnup* prohibited the debtors' attempt to strip off the unsecured junior lien for many of the same reasons as those articulated by the courts in *Ryan* and *Laskin*: (1) adherence to the "pre-Code rule that real property liens emerge from bankruptcy unaffected;" (2) honoring the terms of the loan agreement by keeping the lien with the property until foreclosure; and (3) allowing any increase in the value of the property prior to the foreclosure sale to accrue to the benefit of the creditor in order to prevent the debtor from achieving a windfall.[124]

4. Summary of Rationale for the Majority View

The Fourth, Sixth, and Ninth circuits have all followed reasoning similar to that seen in *Dewsnup* in order to create the majority view which prohibits the practice of stripping off during a Chapter 7 proceeding.[125] First, these courts looked for any indicator that Congress intended to alter the longstanding practice of allowing real property liens to pass through bankruptcy unaffected.[126] These courts concluded that Congress did not intend to alter this longstanding rule, as there was no clear language indicating otherwise.[127] This conclusion is supported by a broader principle, also noted in *Dewsnup*, that bankruptcy serves to give the honest debtor a fresh start by destroying *in personam* claims against the debtor, while leaving *in rem*

[123] *Id.* at 557 ("First, we must determine what consequences, if any, City Mortgage faces for not filing a brief in this appeal. Although not a situation we confront often, on a previous occasion, we have addressed the effects of this unhelpful and highly risky form of appellate advocacy . . . .")

[124] *Talbert*, 344 F.3d at 560-61 ("The Supreme Court's reasoning for not permitting 'strip downs' in the Chapter 7 context applies with equal validity to a debtor's attempt to effectuate a Chapter 7 'strip off.' ").

[125] *Id.* at 556 ("Because the Supreme Court's reasoning in *Dewsnup* . . . applies with equal force and logic to the issue at hand, we hold that a Chapter 7 debtor may not use § 506 to 'strip off' an allowed junior lien . . . ."); Ryan v. Homecomings Fin. Network, 253 F.3d 778, 779 (4th Cir. 2001) ("Because we find that the Supreme Court's reasoning in *Dewsnup* . . . is equally applicable to 'strip offs' as to 'strip downs', [sic] we hold that a debtor may not strip off an unsecured but allowed lien . . . ."); Laskin v. First Nat'l Bank of Keystone (*In re* Laskin), 222 B.R. 872, 875 (B.A.P. 9th Cir. 1998) ("[W]e conclude that *Dewsnup* nevertheless bars the relief debtors seek.").

[126] *E.g.*, *Ryan*, 253 F.3d at 782 (quoting *Dewsnup* for the proposition that Congress did not intend to alter the pre-Code rule allowing real property liens to pass through bankruptcy unaffected).

[127] *E.g.*, *id.*

claims against the same debtor intact.[128] Second, these courts looked to contract law for support, reasoning that at the time the mortgage contract was created, both the creditor and the debtor bargained for the lien to remain with the property until foreclosure.[129] These courts refrained from altering this agreement because these terms were what the parties bargained for when they entered into their agreement.[130] Third, these courts expressed a policy concern about the potential for an unfair outcome if the value of the property were to increase following the bankruptcy discharge.[131] These courts reasoned that any increase in the value of the property should accrue to the benefit of the creditor in order to avoid a windfall to the debtor.[132] This result could not be achieved if the debtor were allowed to strip off the lien during the bankruptcy proceeding.[133]

B. Minority View: Strip Off is Allowed

In the years immediately following *Dewsnup*, a number of district courts and bankruptcy courts had adopted the view that *Dewsnup* applied *only* when the debtor attempted to strip down an undersecured mortgage.[134] In this view, *Dewsnup* did not prevent a debtor from striping off a wholly unsecured junior mortgage.[135] In-

[128] Dewsnup v. Timm, 502 U.S. 410, 418 (1992) (discussing Johnson v. Home State Bank, 501 U.S. 78, 84 (1991)).

[129] *E.g.*, *Talbert*, 344 F.3d at 561 ("Also, as in the case of a 'strip down,' a 'strip off' would rob the mortgagee of the bargain it struck with the mortgagor, i.e., that the consensual lien would remain with the property until foreclosure.").

[130] *E.g.*, *id.*

[131] *E.g.*, *id.* ("Finally, as was true in the context of 'strip downs,' Chapter 7 'strip offs' also carry the risk of a 'windfall' to the debtors should the value of the encumbered property increase by the time of the foreclosure sale.").

[132] *E.g.*, *id.*

[133] *E.g.*, *id.*

[134] Warthen v. Smith (*In re* Smith), 1 F. App'x 178, 181 (4th Cir. 2001) (unpublished opinion); Yi v. Citibank (*In re* Yi), 219 B.R. 394, 397 (E.D. Va. 1998); Smoot v. Wachovia Mortg. (*In re* Smoot), 465 B.R. 730, 733 (Bankr. E.D.N.Y. 2011), *rev'd sub nom.*, Wachovia Mortg. v. Smoot, 478 B.R. 555 (E.D.N.Y. 2012); *In re* Lavelle, No. 09-72389-478, 2009 WL 4043089 at *6 (Bankr. E.D.N.Y. Nov. 19, 2009); Farha v. First Am. Title Ins. (*In re* Farha), 246 B.R. 547, 550 (Bankr. E.D. Mich. 2000); Zempel v. Household Fin. Corp. (*In re* Zempel), 244 B.R. 625, 629 (Bankr. W.D. Ky. 1999); Howard v. Nat'l Westminster Bank, U.S.A. (*In re* Howard), 184 B.R. 644, 647 (Bankr. E.D.N.Y. 1995) (all finding that *Dewsnup* does not apply to a debtor's attempt to strip off a wholly unsecured junior lien).

[135] *Smith*, 1 F. App'x at 181; *Yi*, 219 B.R. at 399; *Smoot*, 465 B.R. at 736; *Lavelle*, 2009 WL 4043089 at *6; *Zempel*, 244 B.R. at 630; *Howard*, 184 B.R. at 647 (all allowing Chapter 7 debtor to strip off wholly unsecured junior lien).

terestingly, the split was so contested that even within the same bankruptcy court in New York the judges had adopted varying views.[136] As the issue evolved, each court that had adopted the minority view was subsequently abrogated when a higher court in the jurisdiction adopted the majority view.[137] However, in an unpublished opinion[138] the Eleventh Circuit recently became the first circuit court to adopt the minority view—specifically that § 506(d) allows a debtor to strip off a wholly unsecured junior lien during a Chapter 7 bankruptcy proceeding.[139]

In the minority view, the paradox of the unlucky penny arises—if, at the time of the bankruptcy filing, the home is valued at *one penny more* than the amount of the primary mortgage, the junior mortgage passes through bankruptcy unaffected.[140] On the other hand, if, at the time of the bankruptcy filing, the home is valued at *one penny less* than the amount owed on the primary mortgage, the debtor can void the junior lien in its entirety.[141] This view provides

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[136] *Compare, e.g.*, *Howard*, 184 B.R. 644 (opinion by Judge Eisenberg from bankruptcy court in the eastern district of New York allowing Chapter 7 debtor to strip off wholly unsecured junior lien), *with e.g.*, Pomilio v. Mers (*In re* Pomilio), 425 B.R. 11 (Bankr. E.D.N.Y. 2010) (opinion by Judge Grossman, also from bankruptcy court in the Eastern District of New York, prohibiting a Chapter 7 debtor from stripping off a wholly unsecured junior lien). The split in this courthouse was recently resolved in favor of the majority view. *See* Wachovia Mortg. v. Smoot, 478 B.R. 555, 570 (E.D.N.Y. 2012) (holding that *Dewsnup* is applicable and binding as to stripping off of wholly unsecured junior liens).

[137] For example, courts in Kentucky and Michigan had adopted the minority view, s*ee Farha*, 246 B.R. 547 and *Zempel*, 244 B.R. 625; however, these cases were abrogated when the Sixth Circuit adopted the majority view, Talbert v. City Mortg. Servs. (*In re* Talbert), 344 F.3d 555 (6th Cir. 2003). Similarly, the Fourth Circuit and a district court in Virginia initially adopted the minority view, *see Smith*, 1 F. App'x 178 *and Yi*, 219 B.R. 394, but were abrogated when the Fourth Circuit changed course and adopted the majority view, Ryan v. Homecomings Fin. Network, 253 F.3d 778, 779 (4th Cir. 2001). A keen eye will note that all of the opinions adopting the minority view, cited *supra* note 134, were subsequently abrogated by either *Talbert*, *Ryan*, or *Smoot*. This means that at the time of this article, the minority view is only used within the Eleventh Circuit as a result of *McNeal*, discussed *infra* Part IV.B.1.

[138] "An opinion shall be unpublished unless a majority of the panel decides to publish it. Unpublished opinions are not considered binding precedent, but they may be cited as persuasive authority." 11TH CIR. R. 36-2.

[139] McNeal v. GMAC Mortg., LLC (*In re* McNeal), 477 F. App'x 562, 564-65 (11th Cir. 2012) (unpublished opinion).

[140] *E.g.*, Dewsnup v. Timm, 502 U.S. 410 (1992) (not allowing debtor to avoid any portion of lien despite the fact that value of collateral was less than the amount of the secured creditor's claim).

[141] *E.g.*, *McNeal*, 477 F. App'x 562 (allowing debtor to avoid entire junior lien when primary lien exceeded value of property attached to both liens).

"a strong incentive for borrowers with wholly unsecured mortgages to file for chapter 7 [sic] [because] [t]hey will be able to remove these mortgages from their properties and discharge the underlying debt, an option that is not available elsewhere."[142]

1. Eleventh Circuit: McNeal v. GMAC Mortgage, LLC *(*In re *McNeal)*[143]

In *McNeal*, the debtor voluntarily filed for Chapter 7 bankruptcy.[144] At that time, her house was valued at $141,416 and was subject to two mortgages: (1) a primary mortgage of $176,413; and (2) a junior lien in the amount of $44,444.[145] Thus, the value of the primary mortgage alone exceeded the fair market value of the house, leaving absolutely no collateral to secure the junior lien.[146] Accordingly, the debtor attempted to strip off the junior lien pursuant to § 506 of the Code.[147] The bankruptcy court and the district court determined that *Dewsnup* prohibited all lien stripping pursuant to § 506(d); therefore the debtor could not rely on this provision to strip off her wholly unsecured junior lien.[148]

On appeal, the Eleventh Circuit determined that *Dewsnup* was not on point; therefore the lower courts were not free to depart from earlier circuit precedent clearly allowing a debtor strip off of an unsecured junior mortgage during a Chapter 7 bankruptcy proceeding.[149] The court noted that "the Supreme Court's reasoning in *Dewsnup* seem[ed] to reject the plain language analysis" that formed the basis for the circuit's earlier precedent, but nonetheless required the lower courts to follow its earlier plain text analysis because of the "im-

[142] *Bankruptcy: Eleventh Circuit Endorses "Strip Off" of Junior Liens*, 42-NOV REAL EST. L. REP., at 6. Indeed, debtors in the lower courts within the jurisdiction of the Eleventh Circuit have already started to benefit from the *McNeal* holding. *See, e.g.*, *In re* Bertan, No. 11–27057, 2013 WL 216231 at *2 (Bankr. S.D. Fla. Jan. 18, 2013) (noting the wisdom of *McNeal* and thereby allowing a debtor to strip off an unsecured junior lien during Chapter 7 proceeding).

[143] 477 F. App'x 562.

[144] *Id.* at 563.

[145] *Id.*

[146] *Id.* (stating that the amount of the primary lien was approximately $175,000, while the value of the home was only approximately $140,000).

[147] *Id.*

[148] *McNeal*, 477 F. App'x at 563.

[149] *Id.* at 564-65.

portant difference between the holding in a case and the reasoning that supports that holding."[150] Following this logic, the Eleventh Circuit reversed the decision of the bankruptcy and district courts, and allowed the debtor in *McNeal* to strip off her wholly unsecured junior lien.[151]

It is interesting to note what *McNeal* did not hold. It did not determine whether, in the wake of *Dewsnup*, it may be necessary to re-visit earlier precedent or whether the rationales underpinning *Dewsnup* provided sufficient justifications to overrule earlier precedent. *McNeal* merely held that *Dewsnup* was not on point; therefore the lower courts could not use *McNeal* to depart from contrary earlier circuit precedent.[152] The court's substantive reasons for allowing strip off are not restated in *McNeal*, but the court states that courts should continue to adhere to the prior precedent set by the Eleventh Circuit.[153]

2. *The Eleventh Circuit's Pre-*Dewsnup *Precedent:* Folendore v. U.S. Small Business Administration *(*In re *Folendore)*[154]

In *Folendore*, the Small Business Administration ("SBA") had provided a loan to the debtors, which was secured by collateral in certain real and personal property belonging to the debtors.[155] The SBA loan was subject to a Subordination Agreement, which gave priority to two other liens that were secured by the same property securing the SBA loan.[156] At the time of the bankruptcy filing, the value of the two priority liens exceeded the value of the collateral property; therefore the SBA loan was not backed by any collateral value in the real property.[157] Accordingly, the debtors sought to strip off the SBA lien pursuant to § 506(d).[158] The court noted that the parties agreed "that the SBA [did] not have an allowed secured claim," and

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[150] *Id.* at 564.
[151] *Id.* at 564-65.
[152] *Id.* at 564.
[153] *McNeal*, 477 F. App'x at 564.
[154] 862 F.2d 1537 (11th Cir. 1989).
[155] *Id.* at 1538.
[156] *Id.*
[157] *Id.*
[158] *Id.*

that the plain text of 506(d) rendered this type of lien as void.[159] Therefore, the court expressly adopted the view that § 506(d) allowed the debtors to void the wholly unsecured junior lien because the plain text of § 506(d) voids any claim that is not both allowed and secured.[160]

3. Reconciling **Folendore** *and* **Dewsnup**

Although the *McNeal* court declined to take the opportunity to reconcile the reasoning of *Dewsnup* with the reasoning supporting the precedent set by *Folendore* this is the next logical step in the analysis. In order to determine whether *Dewsnup* defeats the logic of *Folendore*, the Eleventh Circuit would likely look to the two factors that formed the basis for the Court's holding in *Dewsnup*: (1) the plain text of the statute; and (2) legislative history.[161] *Dewnsnup* actually provides significant support for *Folendore's* plain text analysis because *Dewsnup* resolves the ambiguity in § 506(d) in favor of reading the terms "allowed" and "secured" as two separate requirements.[162] Applying *Dewsnup's* interpretation of § 506(d), a claim that is not *both* allowed and secured can be voided using § 506(d)—a result that is consistent with *Folendore's* plain text interpretation of § 506(d).[163]

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[159] *Folendore*, 862 F.2d at 1538.

[160] *Id.* at 1539.

[161] *See* Dewsnup v. Timm, 502 U.S. 410, 415, 417 (providing plain text interpretation of the term "allowed, secured claim" as used in § 506(d), and supporting this interpretation based on Congressional intent to not alter pre-Code treatment of real property liens).

[162] *Id.* The Court states that "respondents' alternative position, espoused also by the United States . . . generally is the better of the several approaches." *Id.* at 417. The Court states the respondents' alternative position, the position the Court ultimately adopts, to be as follows:

> In the alternative, respondents, joined by the United States as *amicus curiae*, argue more broadly that the words "allowed secured claim" in § 506(d) need not be read as an indivisible term of art by reference to § 506(a), which by its terms is not a definitional provision. Rather, the words should be read term-by-term to refer to any claim that is, first, allowed, and, second, secured.

Id. at 415.

[163] *Folendore*, 862 F.2d at 1538 (voiding a lien when the claim is allowed but not secured).

C. Which Viewpoint is Correct?

The route by which the Eleventh Circuit creates the minority viewpoint, splits the issue into two subissues. The first subissue is whether, procedurally speaking, lower courts may rely on *Dewsnup* to reverse circuit precedent with respect to stripping off. The second subissue is whether, substantively speaking, § 506(d) allows a Chapter 7 debtor to strip off a wholly unsecured junior lien.

1. *Procedurally Speaking: Is* **Dewsnup** *on Point?*

At the current time, the minority view is only in existence within the Eleventh Circuit, and it is only because of the procedure-based rationale stated in *McNeal*.[164] The rationale of *McNeal* is only that *Dewsnup* is not on point; therefore, the lower courts are bound by *Folendore*.[165] The Eleventh Circuit follows a prior panel precedent rule which provides that "a prior panel's holding is binding on all subsequent panels unless and until it is overruled or undermined to the point of abrogation by the Supreme Court or by this court sitting *en banc*."[166] Therefore, even if the panel writing the *McNeal* opinion felt that the time was ripe to abrogate or overrule *Folendore*, the panel was bound by principles of *stare decisis*.[167] Without an en banc review, the panel simply could not depart from the earlier circuit precedent unless *Dewsnup* sufficiently undermined the earlier circuit precedent set by *Folendore*.[168]

Looking carefully at the precise holding of *Dewsnup*, it becomes clear that the Eleventh Circuit was correct in observing that the *Dewsnup* holding was not entirely on point with respect to the strip off line of cases. The lien at issue in *Dewsnup* was secured by some collateral; therefore, the Court spoke only as to the inability to

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[164] *See supra* notes 134-137 (indicating the abrogation of the minority view in all but the Eleventh Circuit); McNeal v. GMAC Mortg., LLC (*In re* McNeal), 477 F. App'x 562 (11th Cir. 2012) (adopting the minority view in the Eleventh Circuit).

[165] *McNeal*, 477 F. App'x at 564.

[166] United States v. Archer, 531 F.3d 1347, 1352 (11th Cir. 2008).

[167] *See id.* (acknowledging the strength of the Eleventh Circuit's prior precedent rule).

[168] *See, e.g.*, United States v. Steele, 147 F.3d 1316, 1317-18 (11th Cir. 1998) ("Under our prior precedent rule, a panel cannot overrule a prior one's holding even though it is convinced it is wrong.").

void a claim that is both *allowed* and *secured*.[169] On the other hand, the strip off cases are entirely distinguishable due to the fact that these cases deal with liens that are wholly unsecured.[170] The plain text interpretation used by the Court in *Dewsnup* indicates that § 506(d) speaks only of claims that are not both allowed and secured, but contains no mention of treatment of unsecured liens under § 506(d).[171] Therefore, *Dewsnup's* holding that § 506(d) cannot void a lien that is both allowed and at least partially secured, does not speak directly to the case where the lien is allowed but *unsecured*. This, coupled with the statement of the *Dewsnup* court expressly narrowing its holding to the specific facts of *Dewsnup*, supports the Eleventh Circuit's viewpoint that *Dewsnup* should not be blindly applied as binding precedent to the strip off line of cases.[172]

This observation is significant due to the fact that there are currently lower courts within seven different circuit jurisdictions, where the circuit court has remained silent on the issue, but the lower courts have applied *Dewsnup* as controlling precedent in order to hold that a debtor may not use § 506(d) to strip off a wholly unsecured junior lien during a Chapter 7 bankruptcy proceeding.[173] Six of these circuits follow rules similar to the Eleventh Circuit's prior precedent rule, meaning that prior panel precedent can only be reversed by an intervening Supreme Court decision that is on point, or by an

[169] Dewsnup v. Timm, 502 U.S. 410, 417 (1992) ("Therefore, we hold that § 506(d) does not allow petitioner to 'strip down' respondents' lien, because respondents' claim *is secured by a lien* . . . ." (emphasis added)).

[170] *E.g.*, *In re* Bertan, No. 11–27057, 2013 WL 216231 at *1, *2 (Bankr. S.D. Fla. Jan. 18, 2013) (allowing strip off of junior lien when there was "no equity securing the Creditor's obligation . . . .").

[171] *Dewsnup*, 502 U.S. at 417.

[172] *Id.* at 416-17 ("We therefore focus upon the case before us and allow other facts to await their legal resolution on another day.").

[173] *See, e.g.*, Wachovia Mortg. v. Smoot (*In re* Smoot), 478 B.R. 555 (E.D.N.Y. 2012) (district court within the jurisdiction of the Second Circuit relying on *Dewsnup*); Richins v. Bank of Am. Home Loans (*In re* Richins), 469 B.R. 375 (Bankr. D. Utah 2012) (bankruptcy court within the jurisdiction of the Tenth Circuit relying on *Dewsnup*); *In re* Immel, 436 B.R. 538 (Bankr. N.D. Ill. 2010) (bankruptcy court in the jurisdiction of the Seventh Circuit relying on *Dewsnup*); Janssen v. Citifinancial Servs. (*In re* Janssen), 311 B.R. 518 (Bankr. E.D. Mo. 2004) (bankruptcy court within the jurisdiction of the Eight Circuit relying on *Dewsnup*); Bowman v. Ocwen Fed. Bank (*In re* Bowman), 304 B.R. 166 (Bankr. M.D. Penn. 2003) (bankruptcy court within the jurisdiction of the Third Circuit relying on *Dewsnup*); *In re* Virello, 236 B.R. 199 (Bankr. D.S.C. 1999) (bankruptcy court within the D.C. Circuit relying on *Dewsnup*); *In re* Madjerac, 157 B.R. 499 (Bankr. D. Me. 1993) (bankruptcy court within jurisdiction of First Circuit relying on *Dewsnup*).

en banc review.[174] This means that the reasoning of these lower courts was not procedurally sound, particularly if the holding was inconsistent with pre-*Dewsnup* circuit precedent. These lower court decisions applying *Dewsnup* to stripping off may be easily reversed at the appellate level, particularly if the circuit courts were to find that prior precedent within the circuit would require a different result.

2. Substantively Speaking: Can a Debtor Use § 506(d) to Strip Off a Junior Lien?

The minority view is not only the better view as a matter of procedure, it is also the better view in terms of substance. The majority view is based heavily on concerns other than the plain text of the statute; it reaches the conclusion that *Dewsnup* bans both stripping off an stripping down by extrapolating the policy and historical concerns surrounding stripping down and assuming that those same concerns apply equally to stripping off.[175] In *Dewsnup*, the Court only turned to related policy, such as the historical treatment of similar liens, in order to resolve the ambiguity in the text of § 506(d).[176] The Court stated that these considerations would not have been controlling but for the ambiguity in the statutory text.[177]

As a result of *Dewsnup*, the text of § 506(d) is now unambiguously interpreted in a manner that requires courts to read the phrase "allowed secured claim" term-by-term, to refer to a claim that is both allowed *and* secured.[178] In *Dewsnup*, the Court stated that the factors

[174] Adams v. Zarnel (*In re* Zarnel), 619 F.3d 156, 168 (2d Cir. 2010) ("This panel is 'bound by the decisions of prior panels until such time as they are overruled either by an en banc panel of our Court or by the Supreme Court.' " (citation omitted)); United States v. Betcher, 534 F.3d 820, 823-24 (8th Cir. 2008) ("However, '[i]t is a cardinal rule in our circuit that one panel is bound by the decision of a prior panel.' " (alteration in original) (citation omitted)); United States v. Holloway, 499 F.3d 114, 118 (1st Cir. 2007) ("Only the Supreme Court or an *en banc* court can overturn prior panel precedent in ordinary circumstances . . . ."); Citizens Exposing Truth About Casinos v. Kempthorne, 492 F.3d 460, 464 (D.C. Cir. 2007) ("The court is bound by its precedent absent en banc review."); *In re* Smith, 10 F.3d 723, 724 (10th Cir. 1993) ("We are bound by the precedent of prior panels absent en banc reconsideration or a superseding contrary decision by the Supreme Court."); O. Hommel Co. v. Ferro Corp., 659 F.2d 340, 354 (3d Cir. 1981) ("[A] panel of this court cannot overrule a prior panel precedent.").

[175] *See* discussion *supra* Part IV.A.

[176] *Dewsnup*, 502 U.S. at 419-20.

[177] *Id.* ("Of course, where the language is unambiguous, silence in the legislative history cannot be controlling.").

[178] *Id.* at 415, 417.

it found controlling would not have been controlling if the statute were not ambiguous.[179] The statute is no longer ambiguous by virtue of *Dewsnup's* interpretation; therefore courts are wrong to consider the *Dewsnup* factors rather than the clear and unambiguous text of the statute in applying § 506(d) to stripping off.

As Justice Douglas once stated, "[The courts] do not sit as super-legislature to determine the wisdom, need, and propriety of laws that touch economic problems, business affairs, or social conditions."[180] Therefore, it is not enough that policy would support reading the statute in a manner different than Congress intended, for it is Congress who has the Constitutional authority to stipulate, through the process of legislation, the precise nature of the rights and obligations of a creditor and debtor throughout the bankruptcy process.[181] Accordingly, in addressing which interpretation is correct, the courts must suppress the desire to pick an interpretation based on its wisdom, but rather must adhere to the law as unambiguously expressed by Congress.

Bearing this in mind, the plain text interpretation of the *Folendore* court,[182] read in conjunction with the plain text interpretation of the *Dewsnup* court,[183] favors the notion that the plain text of the statute expressly allows a debtor to strip off an unsecured junior mortgage. As the *Dewsnup* court noted, the term "allowed secured lien" as utilized in § 506(d) is not a term of art defined by § 506(a), but rather is reference to a claim that is both allowed *and secured*.[184] Section 506(d) states, "To the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such a lien is void . . . ."[185] In the stripping off line of cases, there is no question that the creditor's claim is not secured.[186] By the plain text of § 506(d), the creditor's claim is not both allowed and secured; therefore

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[179] *Id.* at 419-20.

[180] Griswold v. Connecticut, 381 U.S. 479, 482 (1965).

[181] U.S. CONST. art. I, § 8, cl. 4 (giving Congress the authority to establish Bankruptcy laws).

[182] Folendore v. U.S. Small Bus. Admin. (*In re* Folendore), 862 F.2d 1537, 1539 (11th Cir. 1989).

[183] *Dewsnup*, 502 U.S. at 415, 417.

[184] *Id.*

[185] 11 U.S.C. § 506(d) (2006).

[186] *E.g.*, Ryan v. Homecomings Fin. Network, 253 F.3d 778, 779 (4th Cir. 2001) ("The parties agree that the second deed of trust is a fully allowed claim, but wholly unsecured as to the property.").

the associated lien is void.[187] Given the role of the court as an interpreter of the law, rather than a maker of the law, all of the important policy concerns leading to the majority view are simply not enough to overcome the plain text of the statute, which becomes wholly unambiguous as a result of the *Dewsnup* Court's reading of the terms "allowed secured claim" as used in § 506(d).

Additionally, the minority view does not frustrate the legislative intent embraced by the *Dewsnup* court. The *Dewsnup* court construed the statute in a manner favorable to maintaining consistency with prior treatment of debts of the kind at issue in order to resolve the ambiguous legislative text.[188] The *Dewsnup* court determined that, absent clear legislative intent to the contrary, Congress did not intend to alter the well-entrenched principle of bankruptcy law that debts secured by interests in real property should pass through bankruptcy unaffected.[189] However, while it is true that claims that were at least partially secured by collateral in real property have historically passed through bankruptcy unaffected, the question remains as to whether the same can be said for claims that were not secured by any collateral value in real property at the time of bankruptcy filing. Both of the cases relied on by the *Dewsnup* court in embracing the existence of the pre-Code allowance of real property liens to pass through bankruptcy unaffected either specifically acknowledged a distinction between a secured and unsecured creditors, or preserved the lien based on outdated requirements of the Code that are not applicable today.[190] Furthermore, the foundation of this viewpoint can be found within the creditors' appellate brief, which advocated for the majority view banning stripping down, but nonetheless limited its discussion to secured claims.[191]

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[187] 11 U.S.C. § 506(d).

[188] *Dewsnup*, 502 U.S. at 417.

[189] *Id.*

[190] *See* Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555, 588 (1935) ("It is true that the position of a secured creditor, who has rights in specific property, differs fundamentally from that of an unsecured creditor, who has none . . . ."); Long v. Bullard, 117 U.S. 617, 620-21 (1886) (allowing creditor's lien on real property to survive bankruptcy discharge because the creditor did not prove his debt or release the lien).

[191] Brief for Respondent at *27 Dewsnup v. Timm, 502 U.S. 410 (1992) (No. 90-741) ("[The Bankruptcy Code] recognized the right of a *secured creditor* to pay itself from its security . . . ." (emphasis added) (citation omitted)); *Id.* at *27-28 ("Thus, Section 57(h) permitted a *secured creditor* to participate in the distribution of the estate . . . ." (emphasis added)); *Id.* at *28 ("The 1898 Act contained no express provisions relating to . . . the effect of

Finally, a careful reading of the legislative history indicates Congressional desire to treat secured claims differently than unsecured claims. The House Report states, in relevant part:

> One of the more significant changes from current law in proposed Title 11 is the treatment of secured creditors and secured claims. Unlike current law, H.R. 8200 distinguishes between secured and unsecured claims, rather than between secured and unsecured creditors. The distinction becomes important in the handling of creditors with a lien on property that is worth less than the amount of their claim, that is, those creditors that are undersecured. Current law is ambiguous and vague, especially under Chapter XIII, on whether an undersecured creditor is to be treated as a secured creditor, or as a partially secured and partially unsecured creditor. By addressing the problem in terms of claims, the bill makes clear that an unsecured creditor is to be treated as having a secured claim to the extent of the value of the collateral, and an unsecured claim for the balance of his claim against the debtor.[192]

This portion of the House Report clearly acknowledges that secured claims are to be treated differently than unsecured claims. This would seem to indicate that, regardless of the pre-Code rule as to real property liens in general, in the post-Code world, Congress intended unsecured claims to be treated differently than fully or partially secured claims.

V. STRIPPING OFF AND CHAPTER 13

For the purpose of analyzing the proper treatment of a lien that is less than fully secured during bankruptcy, the fundamental difference between Chapter 7 and Chapter 13 is the impact of § 1322.[193]

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the bankruptcy case on the lien of a *secured creditor*." (alteration in original) (emphasis added) (citation omitted)).

192 H.R. REP. NO. 95-595, at 180-81 (1977).

193 *Compare, e.g.*, Nobelman v. Am. Sav. Bank, 508 U.S. 324 (1993) (analyzing whether § 1322(b)(2) allowed a Chapter 13 debtor to strip down a lien), *with, e.g.*, *Dewsnup*, 502 U.S. 410 (analyzing whether § 506 allowed a Chapter 7 debtor to strip down a lien, without

A Chapter 13 debtor can rely on § 1322—a provision of the Code that is unavailable to a Chapter 7 debtor—in order to modify some of his obligations towards certain creditors.[194] Section 1322(b)(2) sets out a general rule allowing the debtor to "modify the rights of holders of secured claims."[195] The statute then immediately creates an exception to the general rule (often referred to as the "antimodification exception") which disallows modification of a "claim [that is] secured only by a security interest in real property that is the debtor's principal residence . . . ."[196] Therefore, § 1322 allows a debtor to modify the rights of a holder of a secured claim, unless the claim is secured by an interest in the debtor's principle residence.[197]

Accordingly, the legal issue central to the question of stripping off and Chapter 13 is whether the claim relating to the unsecured junior lien is subject to modification under § 1322(b)(2), or whether it is protected by the antimodification exception.[198] Put simply, the question is whether the junior lien is secured by an interest in the debtor's principal residence. If the junior lien is not secured by an interest in the debtor's principal residence then the general rule set out in § 1322(b)(2) allows the debtor to strip off the lien.

A. Majority View: § 1322 Allows a Debtor to Strip Off an Unsecured Junior Mortgage

The overwhelming majority of courts have concluded that a debtor can use § 1322(b)(2) to strip off a wholly unsecured junior lien.[199] These courts view the junior lien as falling within §

mention to § 1322(b)(2)).

[194] 11 U.S.C. § 1322(b)(2) (Supp. IV 2010).

[195] *Id.*

[196] *Id.*

[197] *Id.*

[198] *See, e.g.*, Lane v. Western Interstate Bancorp (*In re* Lane), 280 F.3d 663, 665 (6th Cir. 2002) (determining whether a debtor could modify "the rights of a totally unsecured homestead mortgagee" by using § 1322(b)(2)).

[199] *E.g.*, First Mariner Bank v. Johnson (*In re* Johnson), 407 F. App'x 713, 713 (4th Cir. 2011) (unpublished per curiam opinion); *Lane*, 280 F.3d at 665; Zimmer v. PSB Lending Corp. (*In re* Zimmer), 313 F.3d 1220, 1221 (9th Cir. 2002); Pond v. Farm Specialist Realty (*In re* Pond), 252 F.3d 122, 123 (2d Cir. 2001); Bartee v. Tara Colony Homeowners Assoc. (*In re* Bartee), 212 F.3d 277, 280 (5th Cir. 2000); Am. Gen. Fin., Inc. v. Dickerson (*In re* Dickerson), 222 F.3d 924, 926 (11th Cir. 2000); McDonald v. Master Fin., Inc. (*In re* McDonald), 205 F.3d 606, 608 (3d Cir. 2000); Fisette v. Keller (*In re* Fisette), 455 B.R. 177, 187 (B.A.P. 8th Cir. 2011); Domestic Bank v. Mann (*In re* Mann), 249 B.R. 831, 832

1322(b)(2)'s general rule allowing modification; not within the antimodification exception for liens secured by a debtor's primary residence.[200] These courts reconcile this viewpoint with *Nobelman* by reasoning that *Nobelman* protects only the rights of creditors who are first deemed to have a secured debt within the meaning of § 506(a).[201] The debt is secured if the creditor's "interest in the collateral has economic value."[202] A creditor's lien on the debtor's real property has no economic value if there is a primary lien on the same property which exceeds the value of the property.[203] Accordingly, a wholly unsecured junior lien is unsecured within the meaning of § 506(a) (although it is "secured by a lien on the debtor's principal residence") because the junior lien has no economic value; therefore the debtor is free to modify the loan as he could any other unsecured debt.[204]

Interestingly, as a procedural matter, courts that adopt the majority view are inherently acknowledging that stripping off is not precisely analogous to stripping down. If it were true that stripping off and stripping down were the same, then the lower courts would not be allowed to deviate from the Court's precedent stated in *Nobelman*. Although the courts do not expressly discuss this, by adopting the view that a Chapter 13 debtor can strip off a wholly unsecured junior lien, these courts are inherently stating that *Nobelman's* precedent prohibiting strip down does not act as precedent to prohibit strip off.

(B.A.P. 1st Cir. 2000) (all allowing Chapter 13 debtor to strip off wholly unsecured junior lien).

200 *See* cases cited *supra* note 199.

201 *E.g.*, *Lane*, 280 F.3d at 667 ("But the majority of courts . . . have declined to read *Nobelman* as placing such [unsecured] lienholders in the class of claimants whose rights are entitled to special protection under the antimodification clause of § 1322(b)(2).").

202 *Id.* at 664; *see also* 11 U.S.C. § 506(a) (2006) (defining secured claim).

203 *See, e.g.*, *Zimmer*, 313 F.3d at 1221-22 (describing a junior lien as unsecured when the primary lien attached to the same property exceeded the value of the property).

204 First Mariner Bank v. Johnson, 411 B.R. 221, 224-25 (D. Md. 2009) ("Without first demonstrating that it has an allowed secured claim, a creditor cannot invoke the antimodification protection in § 1322(b)(2)."), *aff'd sub nom*, *Johnson*, 407 F. App'x at 713 ("Accordingly, we affirm for the reasons stated by the district court.") (unpublished per curium opinion).

B. Minority View: *Nobelman* is Controlling; Therefore a Debtor May not Strip Off an Unsecured Junior Mortgage

So far, only one lower court has adopted the view that *Nobelman* prohibits not only stripping down pursuant to § 1322, but also stripping off.[205] To support this view, the court points to the fact that *Nobelman* stood for the protection of the *rights* of the creditor, and that these rights are equally entitled to protection in the case of an undersecured primary mortgage as they are in the case of a completely unsecured junior mortgage.[206] The court reasoned that *Nobelman* protects the rights of a creditor whose debt is secured by a lien on the debtor's primary residence, regardless of the amount, if any, of the "equity protecting the secured creditors."[207] The court concluded that based on the language of § 1322(b)(2) and the *Nobelman* opinion, there was no reason to treat unsecured junior liens differently than partially secured primary mortgages.[208]

C. Which Viewpoint is Correct?

The correct view is that of the overwhelming majority of courts—that is, stripping off pursuant to § 1322(b) is fully allowable, because a lien without any equity, even if on the debtor's primary residence, does not fall within the antimodification exception of § 1322(b)(2).[209] This view focuses heavily on the plain text definition

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[205] Barnes v. Am. Gen. Fin. (*In re* Barnes), 207 B.R. 588, 593 (Bankr. N.D. Ill. 1997) ("The Debtors' attempt to strip off the Creditor's security interest in the Debtors' principal residence finds no support in either § 1322(b)(2) or *Nobelman*."). Additionally, at least two cases exist where a court has disallowed a strip off in a Chapter 13 proceeding; however, these cases were based on procedural or substantive matters that did not address the issue of whether § 1322(b)(2) allowed the modification of the lien. Woolsey v. Citibank, N.A. (*In re* Woolsey), 696 F.3d 1266, 1279 (10th Cir. 2012) (holding that Chapter 13 debtor could not strip off junior lien pursuant to § 506(d), but acknowledging result may have been different had debtors' asked for strip off pursuant to § 1322(b)(2)); *In re* Thompson, No. 10-00530, 2010 WL 3719943 at *1 (Bankr. D.C. Sept. 17, 2010) (dismissing motion to strip off for failure to file as adversary claim).

[206] *Barnes*, 207 B.R. at 592 (discussing with approval the view that "the proper reading of [*Nobelman*] was an endorsement of creditor rights, where 'rights' were defined by state law and the underlying contract.").

[207] *Id.* at 593.

[208] *Id.*

[209] *E.g.*, Lane v. Western Interstate Bancorp (*In re* Lane), 280 F.3d 663, 665 (6th Cir. 2002).

of "secured" as set forth in § 506(a) of the Code.[210] The minority view, on the other hand, attempts to embrace the policy behind *Nobelman* and expand that policy to reach the similar situation of stripping off of junior liens.[211] However, courts should not allow policy to negate the plain text of the statute because Congress has the authority to legislate, even if unwisely, provided that the legislation remains within Constitutional bounds.[212] The plain text of § 1322(b)(2) allows modification of secured claims, other than those claims that are "secured only by a security interest in . . . the debtor's principal residence."[213] Section 506(a) clearly indicates that a junior mortgage lacking in any equity is not a secured claim;[214] therefore, by the plain text of these two sections, Congress did not intend to protect this type of claim from modification as part of a Chapter 13 plan.

Additionally, recall that Justice Stevens noted that Congress likely created the antimodification exception in order to encourage lending in the home market.[215] However, it does not necessarily follow that Congress would have wanted to entice creditors into offering higher risk second mortgages. The recent financial crisis, which was precipitated, in part, by the collapse of the subprime mortgage market,[216] highlights the fact that not all lending in the home market is equal; therefore Stevens's observation about Congressional intent for creating the antimodification exception should not be extrapolated to mean that Congress intended to encourage banks to give high-risk loans secured by little, if any, collateral in the debtor's home.

VI. CONCLUSION

The comparison between the two majority viewpoints, that strip off is not allowed pursuant to § 506(d) in Chapter 7 bankruptcy, but is allowed pursuant to § 1322(b) in Chapter 13 bankruptcy, is rid-

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[210] *See supra* notes 199-204, and accompanying text.

[211] *See supra* notes 205-208, and accompanying text.

[212] *See supra* notes 180-181, and accompanying text.

[213] 11 U.S.C. § 1322(b)(2) (Supp. IV 2010).

[214] 11 U.S.C. § 506(a) (2006).

[215] Nobelman v. Am. Sav. Bank, 508 U.S. 324, 332 (1993) (Stevens, J., concurring).

[216] Robin Harding & Claire Jones, *Fed Red-Faced as Notes Reveal Officials Failed to Grasp Dangers of 2007 Crisis*, FINANCIAL TIMES, Jan. 19, 2013, at 1, *available at* GALE, Doc. No. GALE|A315424351 (stating that the crisis occurred "on the back of problems in the market for subprime mortgage loans . . . .").

dled with contradictions and inconsistences. First, as a matter of procedure, courts treat *Dewsnup* as binding with respect to stripping off, while failing to treat *Nobelman* as binding with respect to stripping off. The majority view with respect to Chapter 7 is premised on the notion that Court's prohibition on stripping down is precisely on point to the similar situation of stripping off; therefore *Dewsnup* prohibits both stripping down and stripping off in Chapter 7 proceedings.[217] Conversely, the majority view with respect to Chapter 13 is premised on the notion that the Court's prohibition on stripping down is not precisely on point to the similar situation of stripping off; therefore *Nobelman* prevents only stripping down of junior mortgages while leaving open the question of stripping off.[218]

Furthermore, as a matter of substance, the two majority viewpoints treat the Code's definition of "secured" in a conflicting fashion. The majority view in Chapter 13 carefully reads the plain text of § 506(a) to mean a junior lien with no economic value is to be treated as unsecured for the purposes of § 1322(b).[219] Conversely, the majority view in Chapter 7 carefully reads the plain text of § 506(a) to indicate that a junior lien with no economic value should be treated as a claim that is secured for the purposes of § 506(d).[220]

In order to reconcile these procedural and substantive conflicts, courts should focus first and foremost on the plain text of the Code, as interpreted by *Dewsnup* and *Nobelman*. This analysis would lead to the conclusion that a junior lien that is secured by collateral lacking in any economic value is unsecured within the meaning of § 506(a). Following this, the plain text of § 506(d), as interpreted by *Dewsnup*, allows the debtor to void a lien that is not both allowed and secured. Similarly, the unsecured lien is not a debt secured by collateral in the debtor's primary residence; therefore this lien can be modified by the debtor as part of a Chapter 13 plan. Although certain policy implications certainly support the other viewpoints adopted by the courts, the courts are interpreters, rather than creators, of law. As such, courts should adhere to the plain text of the statute set forth by Congress as the first step in interpreting these complex areas of Code. Therefore, the proper viewpoint is that strip-

217 *See supra* Part IV.A.
218 *See supra* Part V.A.
219 *See supra* Part V.A.
220 *See supra* Part IV.A.

ping off should be allowed, both in Chapter 7 and in Chapter 13 proceedings, as this is the view that is consistent with the plain text of the Code.