

## SURVIVAL UNDERWATER: WHOLLY- UNSECURED SECURITY INTERESTS IN BANKRUPTCY

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### I. INTRODUCTION

When I was a boy, I often wished I could just stay underwater at the public swimming pool all the time: the water was cool, gravity seemed no longer much of a factor, and I could hear for miles (or at least to the other end). Ambitious as I was, I eventually realized that it was nearly impossible to speak underwater, that it hurt really badly when I tried to breathe, and that it hurt even worse when my mother figured out what I was trying to do. Survival underwater, therefore, was appealing but dangerously infeasible. Little did I know then, that for a realistic chance to “survive underwater,”<sup>1</sup> all I had to do was to go downtown, lend certain homeowners a few thousand bucks, and have them sign security agreements giving me liens on their homes.

The United States Supreme Court’s decisions in two bankruptcy cases in the early 1990s gave a certain kind of creditor—the creditor with a lien secured by collateral which is worth less than the amount of the lien—the ability to thus “survive underwater.”<sup>2</sup> These decisions continue to divide the lower courts regarding the treatment of secured creditors with so-called “completely underwater” liens.<sup>3</sup> In both decisions, the Court gave many second mortgagees and like creditors hope for an enormous advantage over other completely unsecured creditors, an advantage realized in an alarming number of ensuing lower

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1. That is, to thrive in an otherwise unnatural habitat. As will be explained, bankruptcy is an unnatural habitat for junior mortgagees. The law as it stands now is somewhat like an Aqua-lung—those underwater creditors whose liens are proclaimed unaffected by bankruptcy wear the Aqua-lung of a particular court’s blessing, while those whose liens are modified or eliminated drown in bankruptcy’s dark, deep waters.

2. See generally *Nobelman v. American Savings Bank*, 508 U.S. 324 (1993); *Dewsnup v. Timm*, 502 U.S. 410 (1992). A lien secured by collateral which is worth less than the amount owed on the lien is commonly referred to as being “underwater.” See *Dewsnup*, 502 U.S. at 424.

3. See *In re McDonald*, 205 F.3d 606, 608 n.1 (3d Cir. 2000). An underwater, or undersecured, lien refers to a type of lien where the collateral securing it is worth less than the lienor’s claim. See *id.* A first mortgagee holding an underwater lien can partially satisfy its claim by selling the collateral and seeking the remainder of the claim against the mortgagor personally. See *id.* A “completely underwater” lien, on the other hand, occurs when the underlying collateral yields no value at all for the lienor as, for example, when foreclosure by a senior interest yields nothing for the completely underwater lienor. See *id.*

court decisions.<sup>4</sup> Such completely underwater liens are able to survive extinguishment by bankruptcy, although the potential to realize anything upon eventual foreclosure and sale by senior interests is nil.

Lower courts today are divided over this issue because the Court's decisions generated more questions than answers. Given the increased number of consumer bankruptcy filings<sup>5</sup> and the growth of the secondary mortgage market,<sup>6</sup> there are a significant number of people who have or will have completely underwater debt and, given the current state of division among lower courts, such claims will be treated differently in different jurisdictions. This state of affairs is inconsistent with federal bankruptcy policy. Considering the growing numbers of consumer bankruptcy filings which include completely underwater secured claims,<sup>7</sup> Congress must come to grips with reality and reform that part of the Bankruptcy Code which allows such claims to survive bankruptcy and make a mockery of bankruptcy policy.

Part II of this Note will address two of the most fundamental aspects of bankruptcy policy: the debtors' fresh start and the creditors' equality of treatment. Part III will explain the nature of secured debt and its role in the bankruptcy process, including an overview of the allowed alteration of contract rights between debtors and secured creditors. Part IV will examine the Supreme Court's decisions in *Dewsnup v. Timm*<sup>8</sup> and *Nobelman v. American Savings Bank*,<sup>9</sup> the two decisions which have fostered the controversies under consideration. It will also assess the primary damage these decisions inspire in lower court cases involving completely underwater secured claims. Part V will highlight the growth of home equity lending and examine its role in the judicial division over the application of *Dewsnup* and *Nobelman*. Finally, Part IV will propose legislation to clarify the respective rights of debtors and creditors regarding completely underwater secured claims.

## II. OBJECTIVES OF CONSUMER BANKRUPTCY

Bankruptcy's goal is to provide the honest-but-unfortunate debtor a "fresh start" on life, unleashed by discharge from the manacles of overwhelming debt.<sup>10</sup> The term "fresh start" has engendered much

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4. See generally *Nobelman*, 508 U.S. at 324; *Dewsnup*, 502 U.S. at 410.

5. See David A. Moss & Gibbs A. Johnson, *The Rise of Consumer Bankruptcy: Evolution, Revolution, or Both?*, 73 AM. BANKR. L.J. 311 (1999) (noting that consumer filings reached the one-million mark in 1996, due in part to bankruptcy's fading stigma).

6. See Evan M. Gilreath, *The Entrance of Banks into Subprime Lending: First Union and the Money Store*, 3 N.C. BANKING INST. 149 (1999).

7. See *infra* note 97.

8. 502 U.S. 410 (1992).

9. 508 U.S. 324 (1993).

10. See William E. Callahan, Jr., Note, *Dewsnup v. Timm and Nobelman v. American Savings Bank: The Strip Down of Liens in Chapter 12 and Chapter 13 Bankruptcies*, 50 WASH. & LEE L. REV. 405, 409 n.37 (1993) (citing Charles J. Tabb, *The Scope of the Fresh Start in Bankruptcy: Collateral*

commentary over the years in regard to its role within bankruptcy policy. There can be no question that failure in its myriad forms, including bankruptcy, is no longer deserving of punishment.<sup>11</sup> Rather, forgiveness for failure is much more in tune with modern American life: it promotes self-respect and encourages risk-taking—a hallmark of American culture.<sup>12</sup> Forgiveness also facilitates rehabilitation,<sup>13</sup> as it reinforces in debtors the notion that society wants risk-taking, but also demands responsibility; hence, forgiveness is, and should be, limited in its scope.<sup>14</sup> The goal of bankruptcy, therefore, is to re-introduce debtors into the community as wiser, more reliable individuals who have learned from defeat.

An important component of a debtor's fresh start is retention of property exempt from inclusion in the debtor's bankruptcy estate as well as non-exempt property.<sup>15</sup> Whether property can be exempt or not is provided for in § 522 of the Bankruptcy Code.<sup>16</sup> Debtors usually have most, if not all, their primary assets encumbered at the time of filing.<sup>17</sup> A typical case will present a debtor with a homestead mortgage and one or more motor-vehicle loans.<sup>18</sup> The debtor will want to keep as many assets, or resources, as possible in order to make a success of the fresh start. Since secured debt must be repaid or the collateral surrendered, debtors often renew, or reaffirm, their contracts with secured creditors in order to retain possession of the most desirable assets.<sup>19</sup> Thus, life

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*Conversions and the Dischargeability Debate*, 59 GEO. WASH. L. REV. 56, 56-57 (1990).

11. See KAREN GROSS, FAILURE AND FORGIVENESS: REBALANCING THE BANKRUPTCY SYSTEM 91-93 (1997). Professor Gross contrasts complete condemnation (imprisonment, forced labor) with complete absolution (giving the debtor no incentive to rehabilitate) regarding the treatment of debtors and concludes that a middle-of-the-road approach best serves all affected parties. See *id.*

12. See *id.* at 94.

13. See *Beall v. Pinckney*, 150 F.2d 467, 470 (5th Cir. 1945) (noting that bankruptcy laws are no longer used to punish bankrupts, but to relieve and rehabilitate).

14. See 11 U.S.C. § 727(a)(8) (1994). Debtors can obtain only one Chapter 7 discharge every six years, and only then if obtained in good faith. See *id.* Chapter 13 debtors can obtain only one discharge every six years unless they paid at least seventy percent or more of their debts under their best efforts. See 11 U.S.C. § 727(a)(9) (1994).

15. See CHARLES JORDAN TABB, THE LAW OF BANKRUPTCY 8 (1997). Debtors undergoing a Chapter 7 liquidation do not ordinarily retain unencumbered, non-exempt assets, save for those the trustee finds to be of no value to the estate pursuant to 11 U.S.C. § 554 (1994) (providing that the trustee may abandon any interest in property to the debtor). See *id.* Debtors under a Chapter 13 reorganization, however, do ordinarily keep such assets in order to facilitate the reorganization. See *id.*

16. See 11 U.S.C. § 522 (1994) (stating generally that debtors can exempt property listed under subsection (d) of § 522, or property deemed exempt pursuant to the law of the state in which bankruptcy is declared).

17. See Marianne B. Culhane & Michaela M. White, *Debt After Discharge: An Empirical Study of Reaffirmation*, 73 AM. BANKR. INST. L. REV. 709 (1999).

18. See *id.*

19. See 11 U.S.C. § 524 (1994) (governing reaffirmation agreements). In pertinent part, it reads: (c) An agreement between a holder of a claim and the debtor, the consideration for which, in whole or in part, is based on a debt that is dischargeable in a case under this title is enforceable only to any extent enforceable under applicable nonbankruptcy law, whether or not discharge of such debt is waived, only if:

(1) such agreement was made before the granting of the discharge under section 727,

goes on as though bankruptcy had never occurred; debtors enjoy the use of the assets and creditors get paid.<sup>20</sup>

Creditors, of course, view bankruptcy from an entirely different perspective than debtors. Typically, the respective positions of the parties are reversed in terms of bargaining power during bankruptcy. The characteristically desperate consumer—now a debtor in bankruptcy—essentially has the upper hand in determining which, if any, creditors will be paid and to what extent.<sup>21</sup> Absent a specific statute or rule which would provide otherwise, creditors to be paid are to take a collective, share one/share all approach.<sup>22</sup>

The Bankruptcy Code generally attempts to equalize similar kinds of creditors when participating in distribution upon a debtor's liquidation or reorganization.<sup>23</sup> The Code has a well-structured system

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1141, 1228, or 1328 of this title;

(2)(A) such agreement contains a clear and conspicuous statement which advises the debtor that the agreement may be rescinded at any time prior to discharge or within sixty days after such agreement is filed with the court, whichever occurs later, by giving notice of rescission to the holder of such claim; and

(B) such agreement contains a clear and conspicuous statement which advises the debtor that such agreement is not required under this title, under nonbankruptcy law, or under any agreement not in accordance with the provisions of this subsection;

(3) such agreement has been filed with the court and, if applicable, accompanied by a declaration or an affidavit of the attorney that represented the debtor during the course of negotiating an agreement under this subsection, which states that—

(A) such agreement represents a fully informed and voluntary agreement by the debtor;

(B) such agreement does not impose an undue hardship on the debtor or a dependent of the debtor; and

(C) the attorney fully advised the debtor of the legal effect and consequences of—  
(i) an agreement of the kind specified in this subsection; and  
(ii) any default under such an agreement;

(4) the debtor has not rescinded such agreement at any time prior to discharge or within sixty days after such agreement is filed with the court, whichever occurs later, by giving notice of rescission to the holder of such claim;

(5) the provisions of subsection (d) of this section have been complied with; and

(6)(A) in a case concerning an individual who was not represented by an attorney during the course of negotiating an agreement under this subsection, the court approves such agreement as—

(i) not imposing an undue hardship on the debtor or a dependent of the debtor; and

(ii) in the best interest of the debtor.

*Id.*

20. See TABB, *supra* note 15, at 544. A basic bankruptcy tenet is that the secured creditor is paid at least the value of the collateral. See *id.* Creditors can obtain the collateral itself or proceeds from its sale in several ways: by seeking relief from the stay, through abandonment by the trustee, through redemption by the debtor, or by reaffirmation with the debtor. See *id.* at 544-45. Further, debtors may elect to neither redeem nor reaffirm, but continue to pay on the collateral; the creditors may receive payment through one of the reorganization chapters; or the collateral may simply be surrendered to the creditors. See *id.* See also Scott F. Norberg, *Consumer Bankruptcy's New Clothes: An Empirical Study of Discharge and Debt Collection in Chapter 13*, 7 AM. BANKR. INST. L. REV. 415, 424 nn.18-19 (1999) (providing statistics showing that a majority of Chapter 7 debtors filed intentions to reaffirm, with a smaller percentage actually reaffirming).

21. See Culhane & White, *supra* note 17. Unsecured creditors facing a debtor's so-called "no asset" (no non-exempt assets) Chapter 7 liquidation rarely see payment, while those creditors facing a Chapter 13 reorganization more often than not see at least some payment. See *id.*

22. See GROSS, *supra* note 11, at 137.

23. See Brian A. Blum, *The Goals and Process of Reorganizing Small Businesses in Bankruptcy*,

for dealing with different kinds of creditors, such as secured and unsecured. All general, unsecured creditors are to take a *pro rata* share from the debtor's estate, even those secured creditors whose claims have partially unsecured portions.<sup>24</sup> To ensure that the secured creditor is treated fairly, the creditor is allowed "adequate protection" of its claim.<sup>25</sup> Adequate protection assures the worthiness of the creditor's claim while the collateral is held by the debtor during the pendency of the bankruptcy case.<sup>26</sup>

Creditors often want debtors to reaffirm secured debt so they may reap the benefits of their bargains. More often than not, a debtor will have no meaningful choice other than to reaffirm a homestead mortgage or motor vehicle loan, and creditors are usually more than happy to accommodate such reaffirmation.<sup>27</sup> However, reaffirmation must occur prior to discharge and must meet exacting requirements in order to prevent creditor overreaching.<sup>28</sup> Once reaffirmed, though, the debtor is

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4 J. SMALL & EMERGING BUS. L. 181, n.166 (2000). Creditors seek equal treatment upon distribution-time in bankruptcy. *See id.* Since, under state law, the relationship between debtor and creditor is one-on-one, creditors have less incentive to seek equal treatment of other creditors since they can effectively attach all of a debtor's non-exempt assets in order to satisfy their claims. *See id.* Hence, the mantra "first in time, first in right." *Id.* However, under federal bankruptcy law, creditors are placed in a payment-priority scheme under § 507 and the mantra is largely inapplicable. *See id.* "Bankruptcy—the creditors' collective collection remedy—therefore should treat similarly situated creditors equally or the virtue of collective action may be subverted." C. Scott Pryor, *Revised Uniform Commercial Code Article 9: Impact in Bankruptcy*, 7 AM. BANKR. INST. L. REV. 465, 479 (1999). *See also* Union Bank v. Wolas, 502 U.S. 151, 161 (1991) (acknowledging "the prime bankruptcy policy of equality of distribution among creditors").

24. *See In re Klein Sleep Products, Inc.*, 78 F.3d 18, 20 (2d Cir. 1996). *See also* 11 U.S.C. § 726 (which provides for the order of distribution of the debtor's estate).

25. *See* 11 U.S.C. § 361 (1994) which reads:

When adequate protection is required under section 362, 363, or 364 of this title of an interest of an entity in property, such adequate protection may be provided by-

- (1) requiring the trustee to make a cash payment or periodic cash payments to such entity, to the extent that the stay under section 362 of this title, use, sale, or lease under section 363 of this title, or any grant of a lien under section 364 of this title results in a decrease in the value of such entity's interest in such property;
- (2) providing to such entity an additional or replacement lien to the extent that such stay, use, sale, lease, or grant results in a decrease in the value of such entity's interest in such property; or
- (3) granting such other relief, other than entitling such entity to compensation allowable under section 503(b)(1) of this title as an administrative expense, as will result in the realization by such entity of the indubitable equivalent of such entity's interest in such property.

26. *See* Donald T. Polednak, Note, *Is the Secured Creditor Really "Secure"?: A Survey of Remedies and Sanctions for a Debtor's Unauthorized Use of Cash Collateral in Chapter 11 Bankruptcy*, 31 WASHBURN L.J. 344, 352-53 (1992). A court will not order adequate protection *sua sponte*—creditors must file motions and convince the court that an order for adequate protection is necessary. *See* H.R. REP. NO. 95-595, at 338-40 (1977) (accompanying 11 U.S.C. § 361 (1994)).

27. *See* TABB, *supra* note 15, at 547. Debtors often have no choice but to reaffirm in order to keep an asset; for example, the family car which secures a lien. *See id.* Attending many debtors' lack of choice regarding reaffirmation is acquiescence to creditors' insistence on assuming the full contract value, together with associated interest and other costs. *See id.*

28. *See* 11 U.S.C. § 524(c)(3) (1994) (providing that any reaffirmation agreement must represent a fully-informed, voluntary agreement; that the agreement cannot impose an "undue hardship on the debtor or a dependent of the debtor;" and that a debtor's attorney must advise of the ramifications of entering into or defaulting upon a reaffirmation agreement). *See also* WILLIAM L. NORTON, JR., NORTON BANKRUPTCY LAW AND PRACTICE § 36:10 (2d ed. 1997).

bound to pay on the debt, and is subject to non-bankruptcy remedies, such as foreclosure and a deficiency judgment, in the event of subsequent default.<sup>29</sup>

The reaffirmation of secured debt, therefore, plays a crucial role in bankruptcy's fresh start policy, greatly determining the extent to which a debtor enjoys enabling resources, and the extent to which secured creditors are protected.

### III. TREATMENT OF SECURED DEBT

Secured creditors stand in line ahead of unsecured creditors for payment at distribution time, whether the proceeding is a liquidation or a reorganization.<sup>30</sup> Thus, it will behoove an alert secured creditor to promptly file a proof of claim so that payment can be assured since, ordinarily, secured creditors stand to be paid in full while unsecured creditors do not.<sup>31</sup>

Once a creditor takes a security interest in a debtor's property, the property is then encumbered by a lien which usually survives the bankruptcy process.<sup>32</sup> While the debtor's personal liability thereon is extinguished upon discharge, the lien itself survives and the property is subject to an *in rem* action by the creditor to satisfy the creditor's claim.<sup>33</sup> Although there are three types of liens,<sup>34</sup> this Note will concern

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29. See 11 U.S.C. § 524(c)(4) (1994) (providing that a debtor may rescind a reaffirmation agreement within 60 days of filing it with the court). See also 124 CONG. REC. H11096 (Sept. 28, 1978) (noting when the agreement becomes binding, state law governs and usually requires that—since reaffirmation is essentially a promise to pay a discharged debt—the debtor is morally bound to pay). See also David Gray Carlson, *Redemption and Reinstatement in Chapter 7 Cases*, 4 AM. BANKR. INST. L. REV. 289, 319 n.236 (1996).

30. See Hon. Kathleen P. March & Jennifer Hildebrandt, *Lien Stripping: When You Can and When You Can't*) *The Law Now, and What the Future May Hold*, 24 CAL. BANKR. J. 317 (1999), available at <http://labankruptcyforum.org/articles/lienstrip.htm> at 15-16. Creditors who participate in the bankruptcy distribution by filing proofs of claim must take care to ensure that their liens are not adversely affected by reorganization plans which purport to nullify all liens upon discharge. See *id.* The authors note that 11 U.S.C. § 1327, “vests property ‘free and clear of any claim or interest . . .’” and, hence, has a *res judicata* effect if creditors fail to object to such plans. *Id.* See also Jane Kaufman Winn, *Lien Stripping After Nobelman*, 27 LOY. L.A. L. REV. 541, 554-55 (1994).

31. See 11 U.S.C. §§ 501-502 (1994) (providing for proofs of claims). Under § 502(a), a filed proof of claim is deemed allowed absent objection by a party in interest. It must be noted that secured creditors, pursuant to § 501(a), are not required to file a claim since, according to the Supreme Court, liens survive bankruptcy. See *Long v. Bullard*, 117 U.S. 617 (1886). However, creditors who do not file proofs of claim will not be paid from the debtors' estates and will normally have to wait to collect upon the debtors' discharge. See March & Hildebrandt, at 15. In a Chapter 13 reorganization, creditors may have to wait up to five years. See 11 U.S.C. § 1322(d) (1994) (providing that Chapter 13 plans may extend for up to five years).

32. See March & Hildebrandt, *supra* note 30, at 15-16. Creditors who participate in the bankruptcy distribution by filing proofs of claim must take care to ensure that their liens are not adversely affected by reorganization plans which purport to nullify all liens upon discharge. *Id.* (noting that 11 U.S.C. § 1327, “vests property ‘free and clear of any claim or interest . . .’” and, hence, has a *res judicata* effect if creditors fail to object to such plans). See also Winn, *infra* note 106, at 554-55.

33. See *Long*, 117 U.S. at 617, an oft-cited case for the proposition that liens “ride through bankruptcy” unaffected. See also *Dewsnup v. Timm*, 502 U.S. 410, 419 (1992) (discussing *Long*).

34. The three types of liens, defined by the noted sub-parts of 11 U.S.C. § 101 (1994), are: Consensual (51)- an agreed-upon lien; Judicial (36)- lien via a judicial order; Statutory (53)- lien

itself with consensual liens.

Consensual liens are those arising by contract.<sup>35</sup> The amounts of many such consensual liens exceed the value of the collateral securing them; thus, these liens enjoy the dubious distinction of “undersecured” claims.<sup>36</sup> Foreclosure and sale of the collateral will not provide for full payment of the claim. The creditor then usually sues the debtor for the rest of the claim owed (the “deficiency”).<sup>37</sup> Courts divide undersecured liens into two portions: the secured and unsecured portions. The secured portion is that part of the lien supported by the collateral’s value, whereas the unsecured portion is the remainder of the lien.<sup>38</sup>

In bankruptcy proceedings, consensual liens are thus bifurcated pursuant to § 506(a).<sup>39</sup> Under that section, the bankruptcy court will first determine the value of the collateral, then bifurcate the creditor’s claim into its respective secured and unsecured portions.<sup>40</sup>

Prior to 1992, many debtors successfully avoided the unsecured portions of secured liens.<sup>41</sup> Beyond lien avoidance for debtors, bifurcation serves the important function of protecting the pool of assets in which unsecured creditors can share.<sup>42</sup> If a creditor’s two-part claim were allowed to be paid in full from the debtor’s estate, unsecured

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arising solely by virtue of statute. See also TABB, *supra* note 15, at 540.

35. 11 U.S.C. § 101(51) (1994) defines “security interest” as a “lien created by agreement.” Hence, such liens are consensual. See *id.*

36. See 20 AM. JUR. PROOF OF FACTS 3D 521 § 8 (1993). “Undersecured” has been succinctly defined as follows:

A claim is undersecured when the collateral is worth less than the debt owed to the creditor. In the case of an undersecured claim, the claim is secured only to the extent of the collateral’s value, with the remainder constituting an unsecured claim. To the extent a claim exceeds the value of the collateral, the claim is not protected as a property right, the creditor is an unsecured creditor, and the unsecured portion of the debt is dischargeable in the bankruptcy.

*Id.* (footnotes omitted). See also *In re Barteel*, 212 F.3d 277, 280 n.3 (5th Cir. 2000) (“In Bankruptcy Code parlance an ‘undersecured’ claim is one supported by collateral valued at less than the amount of the claim. A ‘wholly undersecured’ claim is one for which the supporting collateral holds no remaining value after satisfaction of senior encumbrances.”).

37. See Margaret Howard, *Stripping Down Liens: Section 506(d) and the Theory of Bankruptcy*, 65 AM. BANKR. L. J. 373, 388 (1991). Section 524(a), however, prevents creditors from seeking deficiency judgments after a debtor’s discharge. See *id.* at 377 n.24.

38. See H.R. REP. NO. 95-595, at 356 (1977). See also Margaret Howard, *Secured Claims in Bankruptcy: An Essay on Missing the Point*, 23 CAP. U. L. REV. 313, 316 (1994).

39. 11 U.S.C. § 506(a) (1994) reads, in pertinent part:

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 . . . and is an unsecured claim to the extent that the value of such creditor’s interest . . . is less than the amount of such allowed claim.

40. See *id.*

41. See *Gaglia v. First Fed. Sav. & Loan Ass’n (In re Gaglia)*, 889 F.2d 1304, 1306 (1990). “The majority of the bankruptcy and district courts that have considered this issue agree that the language of § 506 allows a Chapter 7 debtor to void liens secured by property that is not administered.” *Id.* *Gaglia* was the case noted by the 10th Circuit in *In re Dewsnup*, 908 F.2d 588 (1990), as being in conflict, thus giving the Supreme Court cause to decide the issue of § 506(d) lien-avoidance in Chapter 7 in *Dewsnup v. Timm*, 502 U.S. 410 (1992).

42. See Mary Josephine Newborn, *Undersecured Creditors In Bankruptcy: Dewsnup, Nobelman, and the Decline of Priority*, 25 ARIZ. ST. L.J. 547, 568-69 (1993) (discussing § 57(h), the Bankruptcy Act’s version of the Code’s § 506(a)).

creditors suffer a further restriction on access to available assets.

Lien avoidance and lien stripping, however, are coveted tools for debtors.<sup>43</sup> Several provisions of the Bankruptcy Code allow debtors to avoid liens. Under § 522(f)(1), a debtor may avoid liens on otherwise exempt personal property.<sup>44</sup> Section 722, too, effectively accomplishes the same result by allowing debtors to redeem at the value of the allowed secured claim, normally the value of the collateral.<sup>45</sup> Likewise, a Chapter 13 debtor can propose a reorganization plan that includes lien stripping, except for a claim secured only by the debtor's primary residence.<sup>46</sup>

At first glance, § 506(d) would appear to do the same and more, because it has no language limiting its effect to personal property.<sup>47</sup> A plain reading of the relevant portions of § 506(d) shows that secured claims which have not been allowed are to be avoided, period.<sup>48</sup>

43. See *In re Smith*, 247 B.R. 191, 196 (W.D. Va. 2000). "Lien stripping" consists of two varieties: stripdown and stripoff. See *id.* To strip down a lien is to bifurcate, then avoid the unsecured portion of a lien supported by at least some value in the collateral. See *id.* To strip off a lien is to avoid the lien in its entirety, such as when there is absolutely no supporting value; i.e., a junior mortgage subordinated to a senior mortgage which, upon foreclosure, yields nothing for distribution to the junior. See *id.*

44. See 11 U.S.C. § 522(f)(1) (1994) which reads, in pertinent part:

[T]he debtor may avoid the fixing of a lien on an interest of the debtor in property to the extent that such lien impairs an exemption to which the debtor would have been entitled under subsection (b) of this section, if such lien is-

(A) a judicial lien, other than a [spousal or child support] judicial lien . . . ; or  
 (B) a nonpossessory, nonpurchase-money security interest in any-  
 (i) household furnishings, household goods, wearing apparel, appliances, books, animals, crops, musical instruments, or jewelry that are held primarily for the personal, family, or household use of the debtor or a dependent of the debtor;  
 (ii) implements, professional books, or tools, of the trade of the debtor or the trade of a dependent of the debtor; or  
 (iii) professional prescribed health aids for the debtor or a dependent of the debtor.

(C) This paragraph shall not apply with respect to a judgment arising out of a mortgage foreclosure.

See also Lawrence Ponoroff & F. Stephen Knippenberg, *The Immovable Object Versus the Irresistible Force: Rethinking the Relationship Between Secured Credit and Bankruptcy Policy*, 95 MICH. L. REV. 2234, 2239 (1997).

45. See 11 U.S.C. § 722 (1994) which reads, in pertinent part:

An individual debtor may . . . redeem tangible personal property intended primarily for personal, family, or household use, from a lien securing a dischargeable consumer debt, if such property is exempted under section 522 of this title . . . by paying the holder of such lien the amount of the allowed secured claim of such holder that is secured by such lien.

Since redemption requires lump-sum payment, it is difficult, but perhaps not impossible, to imagine that a newly-christened Chapter 7 debtor would have the requisite funds to pay off a lien in lump-sum fashion for anything but the most trivial of collateral. See Culhane & White, *supra* note 17, at 739, n.107.

46. See 11 U.S.C. § 1322(b)(2) (1994) which reads, in pertinent part:

(b) [T]he plan may-  
 (2) modify the rights of holders of secured claims, other than a claim secured only by a security interest in real property that is the debtor's principal residence, or of holders of unsecured claims, or leave unaffected the rights of holders of any class of claims.

47. See 11 U.S.C. § 506(d) (1994) which reads, in pertinent part: "To the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void . . ."

48. See *id.* The legislative history of 11 U.S.C. § 506(d), too, indicates the same. See H.R. REP. NO. 95-595, at 356-57, (1977) which reads in pertinent part:

[I]f a party in interest requests the court to determine and allow or disallow the claim secured by the

However, § 506(d) has caused much consternation to commentators and courts alike. The Supreme Court, addressing conflicting interpretations of § 506(d) among the circuits, did few a favor by its holding in *Dewsnup v. Timm*.<sup>49</sup>

#### IV. THE DEWSNUP AND NOBELMAN DECISIONS

##### A. *Dewsnup v. Timm*

In early 1992, the Supreme Court handed down a decision in *Dewsnup* which seemingly turned the law of secured credit on its ear. *Dewsnup* has been roundly criticized by academics and reluctantly followed, in many cases, by lower courts. The issue at hand was application of the lien-stripping provision of § 506(d).<sup>50</sup>

The facts in *Dewsnup* were rather uncomplicated. Petitioner Dewsnup<sup>51</sup> borrowed \$119,000.00 in 1978 from the respondents and gave a lien on two pieces of land in Utah.<sup>52</sup> Upon default in 1981, but prior to foreclosure, Petitioner filed a Chapter 7 petition, thus invoking the authority of the automatic stay.<sup>53</sup> In 1987, Petitioner filed an adversary proceeding<sup>54</sup> in which she alleged that the debt owed was more than the fair market value of the properties and that, per § 506(d), the lien, along with her personal responsibility for the debt, should be voided to the extent it was unsecured.<sup>55</sup>

The crux of the case was the parties' interpretations of the term "allowed secured claim."<sup>56</sup> An allowed secured claim is that which passes muster under § 502—if a proof of claim is filed, it is allowed unless a party in interest objects.<sup>57</sup>

Petitioner Dewsnup never objected to the respondents' proof of

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lien under section 502 and the claim is not allowed, then the lien is void to the extent that the claim is not allowed. *See id.*

49. 502 U.S. 410 (1992).

50. *See Dewsnup*, 502 U.S. at 411-12.

51. Petitioner's husband, T. Lamar Dewsnup, evidently died during the pendency of the case. *See id.* at 412.

52. *See id.*

53. *See id.* at 413. Petitioner had filed two Chapter 11 petitions prior to filing her Chapter 7 petition in 1984, but the automatic stay in all the filings prevented foreclosure. *See id.* *See also* 11 U.S.C. § 362 (1994) (providing for the automatic stay).

54. The so-called adversary proceeding is simply a suit brought by an interested party within the bankruptcy case—requiring a formal complaint and service of summons as opposed to the less-formal structure of motion practice—to determine the respective rights and obligations as between the debtor and a particular creditor. *See* Robert M. Lawless, *Legisprudence Through a Bankruptcy Lens: A Study in the Supreme Court's Bankruptcy Cases*, 47 SYRACUSE L. REV. 1, 9 n.21 (1996). *See also In re Loloee*, 241 B.R. 655, 662 (B.A.P. 9th Cir. 1999).

55. *See Dewsnup*, 502 U.S. at 413.

56. *Id.* at 414-15.

57. *See* 11 U.S.C. § 502(a) (1994), which reads:

A claim or interest, proof of which is filed under section 501 of this title, is deemed allowed, unless a party in interest, including a creditor of a general partner in a partnership that is a debtor in a case under chapter 7 of this title, objects.

claim, but proposed that only the secured portion of the lien was an allowed secured claim and that the unsecured portion should be voided pursuant to § 506(d).<sup>58</sup> In essence, she argued that for an allowed secured claim to be viable it must first be allowed pursuant to § 502 and, second, be secured—any unsecured portion, therefore, would not be secured and could not then be understood as part of an allowed secured claim.<sup>59</sup>

The respondents, of course, took a contrary view, advocating that allowed secured claim is to be read as though it were first a secured claim and, second, allowed.<sup>60</sup> Thus, if the claim was secured in any manner, and the debtor then failed to object to it, resulting in an allowed secured claim, then the claim would be amenable neither to bifurcation under § 506(a) nor avoidance under § 506(d).<sup>61</sup>

In a surprising departure from a then-emerging consistency in bankruptcy rulings,<sup>62</sup> the Court held that the plain meaning of § 506(a) and (d) was inapplicable due to its adoption of respondents' interpretation of allowed secured claim.<sup>63</sup> Finding a purported ambiguity in the text as pointed out by the conflicting views of the parties,<sup>64</sup> the Court looked to pre-Code treatment of liens to resolve the doubt in favor of the creditor, rather than the debtor.<sup>65</sup> Since the creditor's entire claim had been allowed pursuant to § 502, no part could then be voided by § 506(d).<sup>66</sup> The Court's ruling meant that while a debtor will not be personally responsible for the debt, a creditor retains its lien and can proceed against the debtor's collateral in an *in rem* proceeding.<sup>67</sup> The Court further noted that any increase in the value of collateral during the pendency of the case should inure to the benefit of the creditor, lest the debtor enjoy a windfall.<sup>68</sup> The Court based its

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58. See Brief for the Petitioner at 9, *Dewsnup v. Timm*, 502 U.S. 410 (1992) (No. 90-741).

59. See *id.* at 19.

60. Brief for the Respondents at 17, 21-22, *Dewsnup v. Timm*, 502 U.S. 410 (1992) (No. 90-741).

61. See *id.*

62. See Newborn, *supra* note 42, at 562 n.76 (citing Allan B. Miller & Jeffrey L. Tanenbaum, *High Court: Two Cases, Two Directions*, NAT'L L.J., May 11, 1992, at 20, 26, for the proposition that *Dewsnup* marks the Court's departure from plain-meaning interpretations of the Bankruptcy Code).

63. See *Dewsnup v. Timm*, 502 U.S. 410, 417 (1992).

64. See *Dewsnup*, 502 U.S. at 416. The Court stated: "The foregoing recital of the contrasting positions of the respective parties and their amici demonstrates that § 506 of the Bankruptcy Code and its relationship to other provisions of that Code do embrace some ambiguities." *Id.*

65. See George M. Ahrend & Randall T. Thomsen, *Tort Claims and Judgments as Debts for "Willful and Malicious Injury" Nondischargeable Under Section 523(A)(6) of the Bankruptcy Code*, 100 COM. L. J. 498, 505 (1995). Even in claims against debtors for nondischargeability, however, much less for resolution of a lien-avoidance issue, doubts are normally resolved in favor of the fresh start policy for debtors. See *id.*

66. See *Dewsnup*, 502 U.S. at 417.

67. See *id.* at 418. The Court thus embraced and reaffirmed its holding in *Long v. Bullard*, 117 U.S. 617 (1886) which was a three-page opinion holding that bankruptcy discharge does not of itself release a lien. See *id.* at 419.

68. See *id.* at 417. Where the value of collateral increased during the pendency of the case, a debtor would enjoy an alleged windfall because creditors would have to accept a court's valuation pursuant to § 506(b); that valuation would be marked as the value of the collateral for all times. See

decision on the rationale that Congress would have specifically referenced a change in the pre-Code practice of preserving liens if, in fact, it intended to effect change.<sup>69</sup>

Justice Scalia, in dissent, placed the majority over his knee and administered a good, old-fashioned spanking.<sup>70</sup> Justice Scalia's well-known penchant for textualism caused him much grief over the majority finding of ambiguity in § 506(a) and (d) merely because the self-interested parties advanced opposing viewpoints.<sup>71</sup>

Given the fact that the Court could not account for all possible variations on the scenario at bench, it proclaimed that its decision was limited to the facts of the case—a Chapter 7 case—and left open its application to other chapters of the Code, thus leaving the lower courts with little guidance.<sup>72</sup> Guidance, however, is the only thing lower courts could hope for after *Dewsnup*, since the reorganization chapters of the Code plainly allow bifurcation and avoidance.<sup>73</sup>

In 1992, the Justices with bankruptcy experience had practiced under the old Bankruptcy Act,<sup>74</sup> not the current Code.<sup>75</sup> While the Act allowed secured creditors to simply avoid participating in a bankruptcy case in order to foreclose on collateral,<sup>76</sup> the Code's automatic stay provision of § 362 requires participation.<sup>77</sup> The old Act, therefore, gave broader *in rem* rights which the 1992 Court appeared to hold dear.<sup>78</sup>

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*id.* Thus, should the collateral's value rise during or after the pendency of the case, the debtor—having either redeemed the collateral or reaffirmed the contract with the creditor, both at the judicially-determined value—enjoys its benefits rather than the creditor, a result most likely not bargained for by the creditor. *See id.*

69. *See Dewsnup*, 502 U.S. at 419. “Furthermore, this Court has been reluctant to accept arguments that would interpret the Code, however vague the particular language under consideration might be, to effect a major change in pre-Code practice that is not the subject of at least some discussion in the legislative history.” *Id.*

70. *See id.* at 420-36 (Scalia J., dissenting).

71. *See id.* at 432. Justice Scalia wrote:

Rather, in Part II of its opinion it merely describes (uncritically) ‘the contrasting positions of the respective parties and their amici’ concerning the meaning of § 506(d), ante, at 777, and concludes, because the positions are contrasting, that there is ‘ambiguity in the text,’ ante, at 778. (This mode of analysis makes every litigated statute ambiguous.)

*Id.*

72. *See Dewsnup*, 502 U.S. at 416-17.

73. *See, e.g.*, 11 U.S.C. § 1123(b)(5) and § 1322(b)(2) (1994) (allowing modification of rights of holders of secured claims other than those holding claims on real estate which is the debtor's principal residence under Chapters 11 and 13).

74. *See* Bankruptcy Act of July 1, 1898, ch. 541, 30 Stat. 544 (1898) (repealed by Bankruptcy Reform Act of 1978, 11 U.S.C. §§ 101-1330).

75. *See* Newborn, *supra* note 42, at 548 n.1 (referencing a 1992 speech to the American Bankruptcy Institute by Chief Justice Rehnquist).

76. *See* Transcript of Oral Argument at 4, *Dewsnup v. Timm*, 502 U.S. 410 (1992) (No. 90-741) (referencing *Long v. Bullard*, 117 U.S. 617 (1886) and *United States Nat'l Bank v. Chase Nat'l Bank*, 331 U.S. 28 (1947)). “[T]he secured creditor could choose to ignore the bankruptcy proceedings entirely and the lien would survive the bankruptcy.” *Id.*

77. *See* 11 U.S.C. § 362(a) (1994) which reads, in pertinent part: “[A] petition filed . . . operates as a stay, applicable to all entities, of—  
(3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate.”

78. *See* Newborn, *supra* note 42, at 581.

Having determined that the phrase allowed secured claim should be read term-by-term as advanced by the respondents,<sup>79</sup> and having determined that allowed secured claim could, in fact, have other meanings elsewhere in the Code,<sup>80</sup> the Court cast considerable doubt on the ability of debtors to truly effect a fresh start in the year 2000.

### B. Beyond *Dewsnup*

The highest court in the land had thus spoken: thou shalt not bifurcate and strip down undersecured liens in Chapter 7. Clearly, in such situations lower courts no longer have a say in the matter.<sup>81</sup> The only conceivable way under Chapter 7 for a debtor to strip down a lien—that is, to bifurcate then avoid the unsecured portion—is by redeeming collateral under § 722; however, such redemption applies only to personal property, not real property.<sup>82</sup> Thus, undersecured mortgages are unaffected by a Chapter 7 filing. Conversely, Chapter 13 debtors retain the ability to strip down under § 1322(b)(2) unless the lien secures only the debtor's principal residence.<sup>83</sup>

Given this state of affairs post-*Dewsnup*, many debtors have cleverly found at least one way to effectively circumvent *Dewsnup* by filing under “Chapter 20”<sup>84</sup>: first file under Chapter 13, strip down the lien(s), then convert the case to one under Chapter 7 and enjoy a prompt discharge.<sup>85</sup> This possibility appears to have been codified in 1994 under § 348(f)(1)(B).<sup>86</sup>

79. See *Dewsnup*, 502 U.S. at 410. Justice Scalia entitled the Court's construction as a “one-subsection-at-a-time approach to statutory exegesis.” *Id.* at 423 (Scalia J., dissenting).

80. See *id.* at 417 n.3.

81. See, e.g., *Phoenix Mutual Life Insurance Company v. Greystone III Joint Venture*, 995 F.2d 1274, 1285 (5th Cir. 1992) (Jones, J., dissenting). “I would hope to stand with Galileo, who, rebuffed by a higher temporal authority, muttered under his breath, ‘Eppur si muove.’ (‘And yet it moves.’).” *Id.*

82. See *TABB*, *supra* note 15, at 559. Further, since redemption must be had in a lump-sum fashion, few debtors have the resources following bankruptcy to redeem. See *Ponoroff & Knippenberg*, *supra* note 44, at 2297.

83. See 11 U.S.C. § 1322(b)(2) (1994).

84. See *March & Hildebrandt*, *supra* note 30, at 20 n.24 (citing a host of cases allowing such a procedure). See also Lex A. Coleman, *Individual Consumer “Chapter 20” Cases After Johnson: An Introduction To Nonbusiness Serial Filings Under Chapter 7 And Chapter 13 Of The Bankruptcy Code*, 9 BANKR. DEV. J. 357 (1992).

85. Thirteen plus seven equals, of course, twenty. There is no actual “Chapter 20”- it only exists allegorically. See *March & Hildebrandt*, *supra* note 30, at n.24 (citing a host of cases allowing such a procedure). See also Lex A. Coleman, *Individual Consumer “Chapter 20” Cases After Johnson: An Introduction To Nonbusiness Serial Filings Under Chapter 7 And Chapter 13 Of The Bankruptcy Code*, 9 BANKR. DEV. J. 357 (1992).

86. See 11 U.S.C. § 348(f)(1)(B) (1994) which reads:

(f)(1) Except as provided in paragraph (2), when a case under chapter 13 of this title is converted to a case under another chapter under this title-

(B) valuations of property and of allowed secured claims in the chapter 13 case shall apply in the converted case, with allowed secured claims reduced to the extent that they have been paid in accordance with the chapter 13 plan.

While the same possibility had been available prior to 1994 under Chapter 11, the 1994 amendments to the Code reversed course and passed § 1123(b)(5). See 11 U.S.C. § 1123(b)(5) (1994). That provision, like § 1322(b)(2), currently prohibits lien-stripping on liens secured only by the debtor's

Chapter 13 debtors, though, have not had an easy time coping with the ramifications of *Dewsnup*. *Dewsnup*'s prophesy regarding its application to other chapters of the Code came to life in another controversial case decided shortly thereafter: *Nobelman v. American Savings Bank*.<sup>87</sup> While *Dewsnup* was not directly implicated in *Nobelman*, its influence is readily noted.

### C. *Nobelman*

The facts in *Nobelman* were similar to those in *Dewsnup*; however, *Nobelman* may be distinguished because it was a Chapter 13 case.<sup>88</sup> The debtors in *Nobelman* wanted to strip down the creditor's lien to the value of the collateral, which would have resulted in a loss to the creditor of almost \$48,000.00.<sup>89</sup> The Court essentially reaffirmed the concept espoused in *Dewsnup*—that consensual liens survive bankruptcy unaffected.

However, the Court's decision in *Nobelman* was more developed than that in *Dewsnup*, as *Nobelman* had an arguably less-ambiguous statute at play in the form of § 1322(b)(2).<sup>90</sup> After all, § 1322(b)(2) could not any more plainly state that a debtor cannot modify the rights of a holder of a secured claim which is secured by the debtor's principal residence.<sup>91</sup> Furthermore, the Court in *Dewsnup* found that § 506(a) was not to be read inseparably from § 506(d),<sup>92</sup> whereas the Court in *Nobelman* saw a clearer connection between § 506(a) and § 1322(b)(2), since § 506(a) directly contemplates treatment of secured claims in reorganization plans.<sup>93</sup> The Court ruled that, because the creditor's lien was secured only by the debtor's principal residence, stripdown would impermissibly modify the creditor's rights because it would be paid nothing on its unsecured portion.<sup>94</sup> More significantly, the Court found that the creditor's rights regarding the remaining secured portion would thus necessarily be reduced.<sup>95</sup>

The Court focused on the *rights* of holders of secured claims, rather

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principal residence. *See id.*

87. 508 U.S. 324 (1993).

88. Compare *Dewsnup v. Timm*, 502 U.S. 410 (1992) with *Nobelman*, 508 U.S. 324 (1993).

89. *See Nobelman*, 508 U.S. at 326. American Savings Bank's claim was \$71,335.00, while the debtors, at the time of filing, valued the condominium securing the debt at only \$23,500.00; the condominium's valuation was not in dispute. *See id.* The debtors' Chapter 13 plan expressly provided that unsecured creditors—including American Savings Bank's unsecured portion of its lien—would be paid nothing. *See id.*

90. *See* 11 U.S.C. § 1332(b)(2) (1994).

91. *See id.* I suppose, however, that the fun is in defining what exactly is the debtor's principal residence.

92. *See Dewsnup v. Timm*, 502 U.S. 410, 415 (1992).

93. *See Nobelman*, 508 U.S. at 328-29 (citing 11 U.S.C. § 506(a)).

94. *See id.* at 331.

95. *See id.*

than on *claims*.<sup>96</sup> *Rights* are those state-law, nonbankruptcy, contractual rights for which the claim holder bargained, such as the right to repayment and the right to foreclose upon default.<sup>97</sup> Broadly construing *rights*, together with the anti-modification provisions of § 1322(b)(2), the Court again preserved creditors' abilities to seek *in rem* redress.<sup>98</sup>

#### D. Resulting Treatment of "Completely Underwater" Secured Claims

The Court, in both *Dewsnup* and *Nobelman*, at least by implication, clearly limited its rulings as to what actions a debtor can and cannot take regarding undersecured debt; i.e., the stripdown of liens via § 506(d). Neither case addressed the creditor who has a lien wholly unsupported by value in the underlying collateral (the completely underwater lien). Since there has been a recent increase in lenders taking such security interests,<sup>99</sup> there has been a concomitant increase in debtors seeking to strip off such interests.<sup>100</sup>

96. See *Nobelman*, 508 U.S. at 328. Because § 1322(b)(2) states that a plan may "modify the rights of holders of secured claims," the result reached appears correct, since that statute clearly does not state that a plan may modify the claims of secured creditors. 11 U.S.C. § 1322(b)(2) (1994).

97. See *Nobelman*, 508 U.S. at 329. The term "rights" encompasses nonbankruptcy rights since the Code leaves "rights" undefined. Nonbankruptcy rights include:

[T]he right to repayment of the principal in monthly installments over a fixed term at specified adjustable rates of interest, the right to retain the lien until the debt is paid off, the right to accelerate the loan upon default and to proceed against petitioners' residence by foreclosure and public sale, and the right to bring an action to recover any deficiency remaining after foreclosure.

*Id.*

98. See *id.* at 324. It must be noted that Congress, in 1994, added a new subsection (c) to 11 U.S.C. § 1322 which, by clear and convincing terms (for the less imaginative of us, anyway), abrogates *Nobelman* in part. See 11 U.S.C. § 1322(c) (1994). A straight reading of § 1322(c)(2) allows modification of creditors' rights regarding debtors' principal residences despite the provisions of § 1322(b)(2). See *id.* By including "[n]otwithstanding subsection (b)(2)" in § 1322(c), Congress seemingly made a clear and unequivocal exception to the anti-modification provision of § 1322(b)(2).

*Id.* If the last payment due on the contract comes before the last payment of the debtor's Chapter 13 plan comes due, then the statute provides that the debtor's plan may modify the creditor's claim. See *id.*

99. See *id.* Major players today in such lending are "subprime" lenders, those non-traditional (i.e., other than banks or other financial institutions) sources whose primary clientele includes the poor, the creditless, and the bankrupts-to-be. See *In re Keller Financial Services of Florida, Inc.*, 248 B.R. 859 (Bankr. M.D. Fla. 2000); see also Gilreath, *supra* note 6, at 150-51. Since 1994, the subprime lending business has grown more than five-fold. See *id.* at 153.

100. For cases under Chapter 13, see *In re Mann*, 2000 WL 892833 (B.A.P. 1st Cir.) at 3 n.8 (citing, *inter alia*, *In re Bartee*, 212 F.3d 277 (5th Cir. 2000); *In re McDonald*, 205 F.3d 606 (3d Cir. 2000); *In re Lam*, 211 B.R. 36 (B.A.P. 9th Cir. 1997); *In re Johnson*, 226 B.R. 364 (D. Md. 1998); *In re Edwards*, 245 B.R. 917 (Bankr. S.D. Ga. 2000); *In re Baez*, 244 B.R. 480 (Bankr. S.D. Fla. 2000); *In re McCarron*, 242 B.R. 479 (Bankr. W.D. Mo. 2000); *In re Phillips*, 224 B.R. 871 (Bankr. W.D. Mich. 1998); *In re Cerminaro*, 220 B.R. 518 (Bankr. N.D. N.Y. 1998); *In re Smith*, 215 B.R. 716 (Bankr. W.D. Tenn. 1998); *In re Cervelli*, 213 B.R. 900 (Bankr. D. N.J. 1997); *In re Bivvins*, 216 B.R. 622 (Bankr. E.D. Tenn. 1997); *In re Scheuer*, 213 B.R. 415 (Bankr. N.D. N.Y. 1997); *In re Geyer*, 203 B.R. 726 (Bankr. S.D. Cal. 1996); *In re Sanders*, 202 B.R. 986 (Bankr. D. Neb. 1996); and *In re Libby*, 200 B.R. 562 (Bankr. D. N.J. 1996)).

For cases under Chapter 7, see *In re Mann* at 2 n.4 (citing and comparing *In re Smith*, 247 B.R. 191 (W.D. Va. 2000); *In re Yi*, 219 B.R. 394 (E.D. Va. 1998); *In re Farha*, 246 B.R. 547 (Bankr. E.D. Mich. 2000); *In re Zempel*, 244 B.R. 625 (Bankr. W.D. Ky. 1999); and *In re Howard*, 184 B.R. 644 (Bankr. E.D. N.Y. 1995) (all allowing stripoff), with *In re Laskin*, 222 B.R. 872 (B.A.P. 9th Cir. 1998); *In re Cater*, 240 B.R. 420 (M.D. Ala. 1999); *Crossroads of Hillsville v. Payne*, 179 B.R. 486 (W.D. Va. 1995); *In re Fitzmaurice*, 248 B.R. 356 (Bankr. W.D. Mo. 2000); *In re Cunningham*, 246 B.R. 241

However, many debtors are finding themselves captive to the holdings in *Dewsnup* and *Nobelman*, much to the chagrin of bankruptcy's underlying fresh-start policy. The Court's holdings have spawned divergent views in the lower courts. Some take the Court's holdings unwaveringly and allow completely underwater creditors to maintain their liens, while others read the Court's holdings as applying only to undersecured liens.<sup>101</sup>

The issue has arisen more frequently in Chapter 13 cases, and the majority of courts hold that § 1322(b)(2) does not apply to completely underwater claims.<sup>102</sup> While there is a majority so holding, the split in authority—both judicial and academic—continues to grow.<sup>103</sup> The main thrust of the majority's arguments centers on the coupling of § 506(a) and § 1322(b)(2). Since *Nobelman* instructs courts to value the collateral in order to determine the extent of the creditor's secured claim, "then it follows, even under *Nobelman*, that a wholly unsecured mortgage holder does not have a secured claim."<sup>104</sup>

Almost immediately after *Nobelman* was decided, courts began distinguishing it from cases involving completely underwater liens.<sup>105</sup> In light of the *Dewsnup* court's specific instruction that its holding was limited to the case before it (a Chapter 7 case), these courts were quick to emphasize that *Dewsnup* did not apply to Chapter 13 cases.<sup>106</sup> However, the minority view that completely underwater liens ride through Chapter 13 cases relies distinctly on *Dewsnup*. Thus, while it may well be settled that *Dewsnup* and *Nobelman* apply to undersecured liens in Chapter 13, by no means is the issue settled regarding completely underwater liens.

Until around 1998, the issue had arisen under Chapter 7 only rarely, due largely to the limited applicability of *Dewsnup*.<sup>107</sup> However,

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(Bankr. D. Md. 2000); *In re Virello*, 236 B.R. 199 (Bankr. D. S.C. 1999); *In re Swiatek*, 231 B.R. 26 (Bankr. D. Del. 1999); and *In re Mershman*, 158 B.R. 698 (Bankr. N.D. Ohio 1993) (all following *Dewsnup* and not allowing stripoff).

101. See *infra* notes 109-110 for examples of several cases.

102. See *In re Mann*, 2000 WL 892833 (B.A.P. 1st Cir.) at 2; *In re Miller*, 1999 WL 1052509 (Bankr. E.D. Pa.) at 5.

103. See *In re Bartee*, 212 F.3d 277, 288-89 (5th Cir. 2000).

104. *In re McDonald*, 205 F.3d at 611.

105. See *e.g.*, *In re Lee*, 161 B.R. 271 (Bankr. W.D. Okla. 1993); *In re Hornes*, 160 B.R. 709 (Bankr. D. Conn. 1993); *In re Williams*, 161 B.R. 27 (Bankr. E.D. Ky. 1993); *In re Kidd*, 161 B.R. 769 (Bankr. E.D. N.C. 1993); *In re Moncrief*, 163 B.R. 492 (Bankr. E.D. Ky. 1993).

106. See Jane Kaufman Winn, *Lien Stripping After Nobelman*, 27 LOY. L.A. L. REV. 541, 554-55 (1994). It has been argued that the prevention of lien-stripping in the reorganization Chapters would completely nullify the benefits of reorganization, namely, for example, the benefit proclaimed in 11 U.S.C. § 1327(c) that property vests in the debtor free and clear of liens. See *id.* Furthermore, the reorganization chapters explicitly allow lien-stripping in most instances. See *id.*; see also Lawless, *supra* note 54, at 26 ("If *Dewsnup* applies to chapter 11, then the section 1111(b) election loses its *raison d'être*").

107. See, *e.g.*, *Crossroads of Hillsville v. Payne*, 179 B.R. 486 (W.D. Va. 1995) (denied stripoff); *In re Howard*, 184 B.R. 644 (Bankr. E.D. N.Y. 1995) (allowed stripoff); *In re Mershman*, 158 B.R. 698 (Bankr. N.D. Ohio 1993) (denied stripoff); *In re Wise*, 151 B.R. 116 (Bankr. N.D. Ohio 1992) (denied stripoff).

starting with *In re Yi*<sup>108</sup> in April, 1998, many courts have had occasion to pass on the issue. Several courts held that *Dewsnup* is inapplicable and that completely underwater liens can be stripped off via § 506(d).<sup>109</sup> A majority of courts, however, refuse to entertain such arguments and continue to follow *Dewsnup*.<sup>110</sup> A common rationale advanced by these courts is that, should the collateral increase in value, then the previously completely underwater claim would become a partially-secured claim, thus falling squarely within the ambit of *Dewsnup*.<sup>111</sup> This justification seems rather tenuous given the fact that it is the court that values the collateral under § 506(a) rather than the creditor.<sup>112</sup>

There appear to be many causes for this rather recent spate of Chapter 7 decisions and continued Chapter 13 litigation, not the least of which may be the explosion in the numbers of nonpurchase-money mortgage lenders.<sup>113</sup>

#### V. INFLUENCE OF THE SECONDARY MORTGAGE MARKET

When the Bankruptcy Code was enacted in 1978,<sup>114</sup> Congress did not suspect that the secondary mortgage market of those days would evolve into its present state.<sup>115</sup> Intent on expanding their market reach, today's creditors offer a most appealing form of debt management for the beleaguered: debt-consolidation, or home equity loans.<sup>116</sup>

Debtors can borrow money to pay off credit card, gambling, and most other unsecured debt by giving a creditor a security interest in the debtors' home.<sup>117</sup> Debtors then presumably enjoy one monthly payment

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108. 219 B.R. 394 (E.D. Va. 1998).

109. See, e.g., *In re Smith*, 247 B.R. 191 (W.D. Va. 2000); *In re Yi*, 219 B.R. 394 (E.D. Va. 1998); *In re Farha*, 246 B.R. 547 (Bankr. E.D. Mich. 2000); and *In re Zempel*, 244 B.R. 625 (Bankr. W.D. Ky. 1999).

110. See, e.g., *In re Laskin*, 222 B.R. 872 (B.A.P. 9th Cir. 1998); *In re Cater*, 240 B.R. 420 (M.D. Ala. 1999); *In re Fitzmaurice*, 248 B.R. 356 (Bankr. W.D. Mo. 2000); *In re Cunningham*, 246 B.R. 241 (Bankr. D. Md. 2000); *In re Virello*, 236 B.R. 199 (Bankr. D. S.C. 1999); and *In re Swiatek*, 231 B.R. 26 (Bankr. D. Del. 1999).

111. See *In re Fitzmaurice*, 248 B.R. at 361-62 (quoting *In re Laskin*, 222 B.R. at 876).

112. See H.R. REP. NO. 95-595, 356-57 (1977). While the parties to the case will submit proposals for valuation of collateral, the bankruptcy court decides the valuation per 11 U.S.C. § 506(a). See *id.* The value to be determined is the replacement value of the collateral. See *Associates Commercial Corp. v. Rash*, 520 U.S. 953, 965 (1997); see also Lawless, *supra* note 54, at 25. Presumably, courts carefully value collateral. See *id.*

113. See Gilreath, *supra* note 6, at 149 (noting that the subprime business as a whole—including subprime mortgage lenders take junior mortgages—is rapidly approaching annual revenues of nearly \$200 billion).

114. Bankruptcy Reform Act of 1978, PUB. L. NO. 95-598, 92 Stat. 2549 (codified as amended at 11 U.S.C. §§ 101-1330 (1994)).

115. See *In re Neverla*, 194 B.R. 547, 552 (Bankr. W.D. N.Y. 1996).

116. See Julia Patterson Forrester, *Mortgaging the American Dream: A Critical Evaluation of the Federal Government's Promotion of Home Equity Financing*, 69 TUL. L. REV. 373, 377 (1994). Such home equity loans have been defined as: "[L]oans secured by a homeowner's residence other than loans used solely to purchase or construct the residence, to refinance a purchase money loan, or to make home improvements." *Id.*

117. See Deborah Goldstein, Note, *Protecting Consumers from Predatory Lenders: Defining the Problem and Moving Toward Workable Solutions*, 35 HARV. C.R.-C.L. L. REV. 225, 232 n.35 (2000). Many debtors thus consolidate unsecured loans and transform them into secured loans with the

on debts to one lender, and the worries of keeping the other creditors at bay suddenly disappear. As long as debtors have at least some equity in their homes, lenders are willing to take junior mortgages to help consolidate the debtors' bills.<sup>118</sup> Of course, there is a price to be paid for such lenders' magnanimity. That price often involves inordinately high interest rates and associated fees which are usually exacted from those who can least afford them.<sup>119</sup>

Home equity lenders—also known as subprime lenders<sup>120</sup>—typically seek out those who have home equity but who also have had enough past financial troubles that they are denied conventional financing.<sup>121</sup> In addition to being denied conventional financing, and because of the added advantage of tax deductions on home equity loans, subprime lenders are able to convince many such people to sign up.<sup>122</sup> The high price of home equity loans is a result of the inherent risk associated with these borrowers that conventional lenders would rather avoid.<sup>123</sup> In addition to being financially unstable, many borrowers are naive, elderly and infirm, or otherwise disadvantaged.<sup>124</sup> Generally, it is difficult to imagine such borrowers as having the resources to pay for such financing.

Of course, not all home equity lenders are “bad.”<sup>125</sup> Much like pawnbrokers, they have found and filled a niche in the current market system.<sup>126</sup> The so-called “predatory” home equity lenders are, however, bad in every sense of the word.<sup>127</sup> Stories abound how these lenders victimize the unwary with high-pressure tactics to coerce them into

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potential to survive bankruptcy. *See id.* at 249.

118. *See* Forrester, *supra* note 116, at 388. Some lenders are advertising that they are even willing to lend to borrowers who have *no* equity. *CBS Evening News* (ditech.com advertisement during CBS television broadcast, July 20, 2000).

119. *See* Richard R. Daugherty, *Will North Carolina's Predatory Home Lending Act Protect Borrowers from the Vulnerability Caused by the Inadequacy of Federal Law?*, 4 N.C. BANKING INST. 569, 570 (2000).

120. *See* Gilreath, *supra* note 6, at 150 n.9. “Mortgage and home equity loans account for 60% of the subprime market.” *Id.*

121. *See id.* at 150.

122. *See* Forrester, *supra* note 116, at 376-77. Professor Forrester would much rather see the federal government refrain from its practice of actively promoting home equity financing through tax incentives. *See id.* at 378.

123. *See* Gilreath, *supra* note 6, at 151-52 (noting also that such borrowers are brought to the lenders out of necessity, thus having to pay whatever the market dictates, and that servicing the loans is costlier because avoiding default demands close supervision of borrower activity).

124. *See* Daugherty, *supra* note 119, at 569-70. *See also* Forrester, *supra* note 116, at 389 (noting that the elderly are especially vulnerable, many having substantial home equity but are on fixed incomes).

125. *See* Gilreath, *supra* note 6, at 149 (suggesting in the title that banks are waking up to the potential for profits in home-equity lending as practiced by non-traditional consumer financing companies, although it is not inconceivable that there are those who might view banks themselves as a necessary evil).

126. *See* A. Darby Dickerson, Note, *Bailor Beware: Limitations and Exclusions of Liability in Commercial Bailments*, 41 VAND. L. REV. 129, 135 n.32 (1988). Pawnbrokers have been around since at least the time of the ancient Romans. *See id.*

127. *See* Winn, *supra* note 106, at 584 (noting targeting of minorities, the unscrupulous pressuring for several liens on homes, etc.). *See also* Forrester, *supra* note 115, at 387.

agreeing to pay for loans with exorbitant rates and fees. Ultimately, these loans overwhelm debtors more than the unsecured debts the home equity loans are alleged to alleviate.<sup>128</sup> Relying on such rates and fees, the goal of these lenders is to eventually take the home from the borrower upon an inevitable default and sell the home at a profit.<sup>129</sup> Thus, in reality, there is little risk of loss for lenders and an enormous risk of foreclosure for borrowers.<sup>130</sup>

While attempts at policing such practices have helped to a degree, federal law overall tends to promote rather than discourage predatory home lending.<sup>131</sup> In response to failed lobbying efforts in Congress, some states are beginning to act to curtail predatory lending.<sup>132</sup> Federal bankruptcy law generally disfavors such predatory practices, however, and will not permit them under § 547 and § 548 of the Bankruptcy Code; under those sections, debtors can avoid preferential or fraudulent transfers, under which predatory lending can easily qualify.<sup>133</sup>

128. See, e.g., Forrester, *supra* note 116, at 389 n.81 (describing a nearly-blind woman who, shortly after the 1989 San Francisco earthquake, was conned into agreeing to a home-repair loan by two men. Instead of paying off her first mortgage, the men allegedly sold the loan to her purchase-mortgage company, the result of which caused her monthly payment to more than triple from an already-high rate of \$619.00 per month. She was bringing in only \$1,100.00 per month).

129. See *id.* at 390-91 (noting that many such loans require monthly payments exceeding two-thirds of the borrowers' incomes and that the lenders rely on home equity rather than ability to repay).

130. See *id.* Professor Forrester notes that these lenders:

[M]ay misrepresent loan terms, promise to refinance on less onerous terms after the borrower has made payments for some period, pressure a borrower to sign loan documents without taking time to read them, physically obscure key terms, have a borrower sign documents with key terms left blank, or forge a borrower's signature. Using these unscrupulous and often illegal tactics, lenders may induce unsophisticated borrowers to enter into loan transactions with payments larger than their incomes can support. When a borrower has difficulty making payments, the lender may encourage refinancing of the debt with a larger loan carrying a higher interest rate and requiring higher monthly payments and payment of additional points and closing costs.

*Id.* Thus, predatory lenders can be said to merely "use" their customers to acquire their homes for resale at a profit. See *id.*

131. See *id.* "As the law currently stands, the federal government encourages homeowners to choose home equity financing [by providing tax-deduction incentives] over other types of consumer credit but eliminates the protection that bankruptcy law would offer had the homeowner chosen another type of financing." *Id.* at 435.

132. See Daugherty, *supra* note 119, at 584 (citing North Carolina and New York as two such states).

133. 11 U.S.C. § 547(b) (1994) reads, in pertinent part:

- (b) Except as provided in subsection (c) of this section, the trustee may avoid any transfer of an interest of the debtor in property-
- (1) to or for the benefit of a creditor;
  - (2) for or on account of an antecedent debt owed by the debtor before such transfer was made;
  - (3) made while the debtor was insolvent;
  - (4) made-
    - (A) on or within 90 days before the date of the filing of the petition; or
    - (B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and
  - (5) that enables such creditor to receive more than such creditor would receive if-
    - (A) the case were a case under chapter 7 of this title;
    - (B) the transfer had not been made; and
    - (C) such creditor received payment of such debt to the extent provided by the provisions of this title.

Nevertheless, proving overreaching or fraud is never easy;<sup>134</sup> only truly shocking fees or rates make overreaching or fraud easier for debtors to prove.

The completely underwater liens of home equity lenders, including predatory lenders, would clearly come within the contemplated scope of the lien avoidance provisions of § 506(d) but for *Dewsnup* and *Nobelman*.<sup>135</sup> While, as Justice Stevens pointed out in his concurring opinion in *Nobelman*, statutes such as § 1322(b)(2) were enacted to encourage home lending,<sup>136</sup> the result in both *Dewsnup* and *Nobelman* is to provide home-equity lenders with completely underwater liens the preferred status of secured creditors due to be paid in full. Such result-oriented decisions would perhaps be better made now with the bigger picture of the current state of home-equity lending in mind.<sup>137</sup>

On a number of levels, the fallout inherent in the foregoing overview of home equity lending smacks of inequity. First and foremost, affected debtors are denied a fresh start.<sup>138</sup> They may well be ripe for bankruptcy's forgiveness but, instead, are only plucked and eaten by such lenders. Since many are already on the verge of bankruptcy upon taking out such loans, the last-ditch hope that these loans provide all too often turns to gloom as debtors are forced by necessity to either give up their homes or enter into further-oppressive reaffirmation agreements.<sup>139</sup>

Beyond obliteration of debtors' fresh starts, the *Dewsnup/Nobelman* approach also makes other unsecured creditors feel the pain. Like the cellular phone-holding driver of the eight feet-tall S.U.V. who passes a mile-long line of others at highway construction zones to brazenly cut in front, completely underwater home-equity

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11 U.S.C. § 548(a) (1994) reads, in pertinent part:

(a)(1) The trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor, that was made or incurred on or within one year before the date of the filing of the petition, if the debtor voluntarily or involuntarily-

(B)(i) received less than a reasonably equivalent value in exchange for such transfer or obligation; and

(ii)(I) was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation;

(II) was engaged in business or a transaction, or was about to engage in business or a transaction, for which any property remaining with the debtor was an unreasonably small capital; or

(III) intended to incur, or believed that the debtor would incur, debts that would be beyond the debtor's ability to pay as such debts matured.

134. See W. PAGE KEETON, ET AL., PROSSER AND KEETON ON THE LAW OF TORTS Section 105, p. 728 (5th ed. 1984).

135. "Allowed secured claim" would, of course, not describe a claim obtained by misrepresentation, if proved.

136. See *Nobelman v. American Savings Bank*, 508 U.S. 324, 332 (1993).

137. See Lawless, *supra* note 54, at 24.

138. See Forrester, *supra* note 116, at 429-30.

139. See 11 U.S.C. § 361 (1994). It will be emphasized that, as the debtor may be desperate to keep a home, an attorney may well file an affidavit stating that reaffirmation would be in the debtor's best interest. See Forrester, *supra* note 116, at 431.

lenders who retain their liens butt in line ahead of other equally-unsecured creditors to enjoy secured status.<sup>140</sup> Thus, the concept of equal treatment of creditors has turned out to be, in practice, essentially a myth.

As stated, a majority of courts in Chapter 13 cases are in favor of stripping off such liens.<sup>141</sup> Courts previously skittish about doubting *Dewsnup* are now coming forward to limit its protection in Chapter 7.<sup>142</sup> The soothsayers' predictions as to the ramifications of *Dewsnup* and *Nobelman* are coming to fruition,<sup>143</sup> and a resolution is now needed in order to protect the American institution of bankruptcy.

## VI. POTENTIAL SOLUTIONS

While there are potential procedural safeguards against untoward results obtained by *Dewsnup* and *Nobelman*,<sup>144</sup> the answers to this dilemma should ultimately come from Congress. Congress was seemingly lax in its efforts to convey its intent in passing statutes like § 506(d) and § 1322(b)(2),<sup>145</sup> but enough has occurred in the last two

140. See Winn, *supra* note 106, at 584. The author of this Note urges motorists to exercise extreme caution when approached by any such S.U.V. driver. Above all, do not attempt to pet or feed it, and always wear appropriate safety restraints.

141. See *In re Mann*, 2000 WL 892833 (B.A.P. 1st Cir.) at 2; *In re Miller*, 1999 WL 1052509 (Bankr. E.D. Pa.) at 5. See also *supra* text accompanying note 103.

142. See *In re Mann* at 2 n.4 (citing *In re Smith*, 247 B.R. 191 (W.D. Va. 2000); *In re Yi*, 219 B.R. 394 (E.D. Va. 1998); *In re Farha*, 246 B.R. 547 (Bankr. E.D. Mich. 2000); *In re Zempel*, 244 B.R. 625 (Bankr. W.D. Ky. 1999); and *In re Howard*, 184 B.R. 644 (Bankr. E.D. N.Y. 1995) (all allowing stripoff)). See also *supra* text accompanying note 101.

143. See generally Newborn, *supra* note 42.

144. See Forrester, *supra* note 116, at 453 n.423. Under Chapter 13, for instance, debtors could modify the terms of home equity loans to provide for extended, lower monthly payments at market interest rates without violating creditors' rights under *Nobelman*. See *id.* However, this would appear to only mitigate, rather than eliminate, home equity loan problems. See *id.*

145. See *In re Neverla*, 194 B.R. 547, 552 (Bankr. W.D. N.Y. 1996). The court in *In re Neverla* made cogent observations of Congressional intent regarding these statutes:

In 1977, when Section 1322(b)(2) was finally enacted, it may have been true that: (1) there was a general anticipation that real estate values would not decline but would always continue to increase, even if at differing rates; (2) it was not anticipated that the income tax laws would change to allow consumers to deduct non-business interest only if paid on Homestead Mortgages; and (3) it was not predictable that there would develop an active and extensive secondary mortgage market and that financial institutions would develop and aggressively market numerous subordinate Homestead Mortgage products. However, by the time of the enactment of the Bankruptcy Reform Act of 1994, Congress was aware that: (1) all of the foregoing had happened; (2) the United States Supreme Court had decided *Nobelman v. American Savings Bank*, essentially overturning the interpretation of the majority of the Circuit Courts which had construed Section 1322(b)(2); and (3) numerous discussions and law review articles had addressed the problem of Chapter 13 cases with wholly unsecured Homestead Mortgages, many of which were wholly unsecured at the time they came into existence. Nevertheless, Congress did not redraft Section 1322(b)(2), even though it did make changes to Subsections 1322(b)(3) and 1322(b)(5).

It is difficult, given the legislative history of Section 1322(b)(2) and the decision of the United States Supreme Court in *Nobelman v. American Savings Bank*, to assume that Congress believed it was unnecessary to further clarify Section 1322(b)(2) because the legislative history and *Nobelman* could only result in Bankruptcy Courts determining that fully secured Homestead Mortgages were to be paid in full, undersecured Homestead Mortgages, even if supported by only one dollar in collateral value, were to be paid in full because the rights of the holders of such undersecured Homestead Mortgages were to be

decades to give Congress the impetus needed to effect change.

Since the issue of stripping off is one of lien avoidance, § 506(d) is the culprit needing reform. One commentator has proposed the following reform for § 506(d): "Except as provided in section 1111(b) of this title, a trustee, subject to court approval, may void a lien to the extent that it secures a claim against the debtor that is an allowed unsecured claim, if such avoidance would benefit the estate."<sup>146</sup>

Of particular appeal in this proposal is the substitution in the current version of "not an allowed secured claim" with "allowed unsecured claim,"<sup>147</sup> which should easily defeat claims of ambiguity regarding classification of the claim.<sup>148</sup> A debtor can be fairly certain to receive a fresh start once the *Dewsnup* cloud of doubt is removed, and the last clause ensures equal treatment of other, equally unsecured creditors.

For further clarity, I would propose the following reform of § 506(d):

To the extent that a lien secured by collateral, any portion of which lien is unsecured regardless of whether such lien secures a claim which is allowed or disallowed under section 502, such unsecured portion of such lien is void and the value thereof is preserved for the benefit of all unsecured creditors pursuant to section 551.

This proposal puts creditors on notice that they will immediately lose the unsecured portions of their liens if their customers file for bankruptcy relief; thus, creditors will be expected to think twice when advancing funds for what they know or suspect will be effectively unsecured security interests. This proposal also provides incentives for counsel to more fully cooperate in arriving at accurate estimates of the value of collateral so that courts can make more deliberate determinations.<sup>149</sup> Further, much like Professor Newborn's,<sup>150</sup> this proposal gives general, unsecured creditors hope for payment in those cases where such creditors are generally unpaid. At its core, this proposal is both pro-debtor and pro-creditor as it paves a clear path for

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fully protected, and wholly unsecured Homestead Mortgages were to be modified, treated as unsecured, and the underlying mortgage liens avoided, even if they were determined to be unsecured after the application of Section 506(a) because prior liens on the residence exceeded its fair market value by a mere one dollar.

*Id.*

146. Newborn, *supra* note 41, at 593.

147. *Id.*

148. *But see* Lawless, *supra* note 54, at 21-22. Professor Lawless would be skeptical of the Court's abilities to easily hold bankruptcy statutes unambiguous after *Dewsnup*. *See id.*

149. *See Dewsnup v. Timm*, 502 U.S. 410, 417 (1992). *See also supra* text accompanying note 68 (regarding potential increases in the value of collateral).

150. *See* Newborn, *supra* note 42, at 593. Unlike Professor Newborn's proposal, however, this proposal does not confer exclusive authority to seek lien avoidance on the trustee. While the trustee essentially is the guardian of assets for creditors, he/she will typically not be as motivated to seek avoidance as debtors, since debtors faced with losing their homes will more likely be willing to fight tooth-and-nail to keep them.

the debtor's fresh start and for the equal treatment of creditors.

Given the somewhat surprising recent Chapter 7 cases readily distinguishing *Dewsnup*,<sup>151</sup> the Supreme Court may well reinterpret § 506(d) before Congress gets around to reforming it. Moreover, Congress has already shown that it is easily amenable to the lobbying of mortgage lenders<sup>152</sup> and, considering recent proposals for further bankruptcy reform, it now appears to be even more so.<sup>153</sup> When the Court speaks, people listen.<sup>154</sup> However, Congress makes the laws which the Court interprets, so if Congress speaks to these issues in no uncertain terms, the courts, debtors, and creditors will stand on firmer ground.

## VII. CONCLUSION

Courts that are willing to distinguish *Dewsnup* and *Nobelman* regarding completely underwater security interests are seeing such interests for what they really are—unsecured interests undeserving of secured status. As predicted, the Supreme Court's *in rem* view of secured debt under the old Bankruptcy Act is giving way to the Code's more expansive "priority" view.<sup>155</sup> The evolution of debtor/creditor relations evidently escaped the grasp of the 1978 Congress; however, Congress today can survey the landscape and address what such evolution has wrought.

The fresh start for debtors and equal treatment of creditors are two fundamental principles of bankruptcy law. *Dewsnup* and *Nobelman*

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151. See *In re Mann*, 2000 WL 892833 (B.A.P. 1st Cir.) at 2 n.4 (citing *In re Smith*, 247 B.R. 191 (W.D. Va. 2000); *In re Yi*, 219 B.R. 394 (E.D. Va. 1998); *In re Farha*, 246 B.R. 547 (Bankr. E.D. Mich. 2000); *In re Zempel*, 244 B.R. 625 (Bankr. W.D. Ky. 1999); and *In re Howard*, 184 B.R. 644 (Bankr. E.D. N.Y. 1995) (all allowing stripoff)).

152. See, e.g., 11 U.S.C. § 1322(b)(2), which gives only home-mortgage lenders protection against lien-stripping. Since most such institutional lenders are organized, have specific objectives in mind regarding the effects of bankruptcy, and have the resources to pursue lobbying efforts in Congress, they frequently succeed in realizing legislative goals. See Lawless, *supra* note 54, at 116. Consumers, on the other hand, have little interest in inquiring into bankruptcy issues until faced with having to file a petition for relief; hence, organized lobbying on their behalf pales in comparison to that of home-mortgage lenders. See *id.*

153. See The Bankruptcy Reform Act of 2000, H.R. 833, 106<sup>th</sup> Cong. 2000 (providing, *inter alia*, that § 506 will not apply to debts secured by motor vehicles if acquired within 5 years of filing a petition for bankruptcy relief, or secured by any personal property acquired within 6 months thereof—thus, institutional creditors and Congress are apparently not satisfied with protection merely for debtors' residences).

154. Unlike Professor Lawless and despite the troubling rulings under examination, I have no doubt that the Supreme Court should remain the ultimate interpreter of the laws of the United States, including bankruptcy laws. See Lawless, *supra* note 54, at 119 (positing that perhaps the Court's role "at the top of the bankruptcy system should be reconsidered. . ."). Under 28 U.S.C. § 157(a), Article III courts have original jurisdiction over bankruptcy matters despite routinely referring them to bankruptcy courts. Therefore, the likelihood that Congress or the Court would, or should, ever provide that there be some other supreme interpreter of bankruptcy laws is nil. The Constitution's provision that there be one Supreme Court works well, no matter how "specialized" any particular area of law may be.

155. Newborn, *supra* note 42, at 574-81 (with "priority" referring to the relative priority-for-payment status of secured and unsecured creditors).

2000]

*Note*

109

generally wreak havoc on these principles, and whether courts follow the majority or minority view makes a huge difference to individual debtors and creditors in different jurisdictions. Administration and interpretation of federal law should be consistent throughout the country,<sup>156</sup> and it is up to both Congress and the Court to continue to strive for the justice they proclaim to effect.

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156. See *Gasperini v. Center for Humanities, Inc.*, 518 U.S. 415, 416 (1996) (noting “the twin aims of the *Erie* rule [are] discouragement of forum-shopping and avoidance of inequitable administration of the laws” (citing *Hanna v. Plumer*, 380 U.S. 460, 468 (1965))).