SECTION 506 — SECURED CREDITORS' CLAIMS — LIEN STRIPPING

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INTRODUCTION

Section 506 of the Bankruptcy Code governs secured claims against a debtor's estate, and allows debtors to void a lien to the extent it is unsupported by the value in the collateral. Section 506 provides in relevant part:

> (a)(1) 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.
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> . . .
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> (d) To the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void, unless -
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> (1) such claim was disallowed only under section 502(b)(5) or 502(e) of this title; or
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> (2) such claim is not an allowed secured claim due only to the failure of any entity to file a proof of such claim under section 501 of this title.

The reduction or modification of a creditor's lien pursuant to Section 506 is colloquially referred to as "lien stripping." There are two types of lien stripping. A "strip down" of an undersecured lien reduces the lien to the value of creditor's interest in the collateral. A "strip off" removes an unsecured lien in its entirety.[1] In proceedings under the reorganization chapters of the Bankruptcy Code, the lien "stripping" is a two step process. First, Section 506(a) provides a valuation

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[1]*In re McNeal*, 477 Fed. Appx. 562, 564 (11th Cir. 2012), redesignated as opinion, 735 F.3d 1263 (11th Cir. 2012) (overruled by, In re Waits, 2015 WL 4378369 (11th Cir. 2015)).

procedure and bifurcates the claims into secured and unsecured. Then, the lien stripping is accomplished through the confirmation and performance of the debtor's Chapter 11[2] or Chapter 13 plan,[3] pursuant to Section 1129 or 1322(b) of the Bankruptcy Code. While the Supreme Court held in *Dewsnup v. Timm* that Chapter 7 debtors cannot strip down undersecured liens,[4] a "majority of courts [have held] that Dewsnup's holding should not be imported into Chapter 11 cases."[5]

In Chapter 11 cases, Section 1111(b)(2) allows creditors to elect to have their claims treated as fully secured, and thus "to opt out of the lien-stripping found in § 1129."[6] As the Tenth Circuit observed in *Wade v. Bradford*, "the very existence of this election demonstrates that Chapter 11 permits a debtor to strip a creditor's lien down to the value of the collateral."[7] However, unlike in reorganization proceedings, debtors in Chapter 7 cases are not allowed to strip down partially underwater liens, and the courts were split on whether debtors can strip off wholly unsecured junior liens. On June 1, 2015, the Supreme Court resolved the circuit split and held that wholly unsecured junior liens cannot be stripped off in Chapter 7 cases.

1. *Dewsnup* and Circuit Split.

In 1992, the Supreme Court held in *Dewsnup v. Timm*

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[2]See, e.g., *Wade v. Bradford*, 39 F.3d 1126, 1129, 26 Bankr. Ct. Dec. (CRR) 301, 32 Collier Bankr. Cas. 2d (MB) 568, Bankr. L. Rep. (CCH) P 76186 (10th Cir. 1994).

[3]See, e.g., *In re Davis*, 716 F.3d 331, 335, 57 Bankr. Ct. Dec. (CRR) 266, 69 Collier Bankr. Cas. 2d (MB) 885, Bankr. L. Rep. (CCH) P 82483 (4th Cir. 2013).

[4]502 U.S. 410, 417 (1992).

[5]*In re Heritage Highgate, Inc.*, 679 F.3d 132, 144, 56 Bankr. Ct. Dec. (CRR) 145, Bankr. L. Rep. (CCH) P 82313 (3d Cir. 2012).

[6]*Wade v. Bradford*, 39 F.3d 1126, 1129, 26 Bankr. Ct. Dec. (CRR) 301, 32 Collier Bankr. Cas. 2d (MB) 568, Bankr. L. Rep. (CCH) P 76186 (10th Cir. 1994), *citing In re 680 Fifth Ave. Associates*, 156 B.R. 726, 732, 24 Bankr. Ct. Dec. (CRR) 729, 29 Collier Bankr. Cas. 2d (MB) 491, Bankr. L. Rep. (CCH) P 75363 (Bankr. S.D. N.Y. 1993), decision aff'd, 169 B.R. 22 (S.D. N.Y. 1993), judgment aff'd, 29 F.3d 95, 25 Bankr. Ct. Dec. (CRR) 1445, 31 Collier Bankr. Cas. 2d (MB) 1085, Bankr. L. Rep. (CCH) P 75987, 142 A.L.R. Fed. 789 (2d Cir. 1994).

[7]Wade v. Bradford, 39 F.3d at 1129.

that Chapter 7 debtors could not strip down an undersecured lien to the value of the collateral.[8] In that case, the debtors took out a loan for $119,000, which they secured by a first deed of trust on two parcels of farmland in Utah.[9] The property had an approximate value of $39,000, leaving an unsecured deficiency of $81,000.[10] The debtors requested the Bankruptcy Court to strip down the lien to the fair market value of the land, pursuant to the provisions of Section 506(d).[11] The relief sought by debtors was denied by the bankruptcy court and the intermediate courts.[12]

The issue presented to the Supreme Court was whether the primary undersecured mortgage should be considered an "allowed secured claim" under Section 506(d).[13] Based on statutory interpretation and interplay of Sections 506(a) and 506(d), the Supreme Court agreed with the lender's position and held "that § 506(d) does not allow petitioner to 'strip down' a lien because a claim is secured by a lien, which was fully allowed pursuant to § 502."[14] The Court reasoned that the words "allowed secured claim" did not have the same meaning in § 506(d) as in § 506(a).[15] Moreover, the Court was concerned that the practical effect of the debtors' argument would be to "freeze the creditor's secured interest in the judicially determined valuation", which would result in the creditor losing the benefit of any increase in the value of the property and "any increase would accrue to the benefit of the debtor . . . as a 'windfall.' "[16]

However, *Dewsnup* did not explicitly decide whether debtors may strip off entirely underwater junior liens. Following

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[8]502 U.S. 410, 112 S. Ct. 773, 116 L. Ed. 2d 903 (1992).

[9]Dewsnup v. Timm, 502 U.S. at 412.

[10]Dewsnup v. Timm, 502 U.S. at 413.

[11]Dewsnup v. Timm, 502 U.S. at 413.

[12]Dewsnup v. Timm, 502 U.S. at 414.

[13]See Dewsnup v. Timm, 502 U.S. at 415.

[14]Dewsnup v. Timm, 502 U.S. at 417.

[15]Dewsnup v. Timm, 502 U.S. at 417.

[16]Dewsnup v. Timm, 502 U.S. at 417.

Dewsnup, most courts, including the Fourth,[17] Sixth[18] and Seventh[19] Circuits, have extended the *Dewsnup* holding to also prohibit stripping off such junior liens. However, in 2012, the Eleventh Circuit in *McNeal v. GMAC Mortg., LLC,* found that the *Dewsnup* holding does not apply to wholly underwater junior liens.[20] In reaching this conclusion, the *McNeal* Court relied on the pre-*Dewsnup* decision of *Folendore v. U.S. Small Business Administration (In re Folendore),* where the Eleventh Circuit allowed the debtors to strip off wholly unsecured liens, based on the plain language interpretation of Section 506.[21] Most courts in the Eleventh Circuit considered *In re Folendore* as having been abrogated by *Dewsnup*.[22] Even the *McNeal* Court recognized that *Dewsnup* "seems to reject the plain language analysis that [the Court] used in *Folendore*."[23]

However, in *McNeal,* the Eleventh Circuit invoked its "prior panel precedent rule" under which "a later panel may depart from an earlier panel's decision only when the intervening Supreme Court decision is clearly on point."[24] The Eleventh Circuit concluded that *Dewsnup* decision was not clearly on point because it involved a strip down of a partially secured lien rather than the strip off of a wholly unsecured lien at issue in *McNeal*.[25] Thus, the *McNeal* Court held that the debtor can strip off wholly underwater junior lien.[26]

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[17]*Ryan v. Homecomings Financial Network*, 253 F.3d 778, 37 Bankr. Ct. Dec. (CRR) 269, Bankr. L. Rep. (CCH) P 78466 (4th Cir. 2001).

[18]*In re Talbert*, 344 F.3d 555, 41 Bankr. Ct. Dec. (CRR) 276, 50 Collier Bankr. Cas. 2d (MB) 1562, Bankr. L. Rep. (CCH) P 78920, 56 Fed. R. Serv. 3d 1235, 2003 FED App. 0343P (6th Cir. 2003).

[19]*Palomar v. First American Bank*, 722 F.3d 992, 69 Collier Bankr. Cas. 2d (MB) 1555, Bankr. L. Rep. (CCH) P 82510 (7th Cir. 2013).

[20]735 F.3d 1263 (11th Cir. 2012).

[21]862 F.2d 1539 (11th Cir.1989).

[22]McNeal, 735 F.3d at 1265.

[23]McNeal, 735 F.3d at 1265.

[24]McNeal, 735 F.3d at 1265.

[25]McNeal, 735 F.3d at 1265.

[26]McNeal, 735 F.3d at 1266.

2. The Supreme Court Has Granted Certiorari to Resolve the Circuit Split.

On November 17, 2014, the Supreme Court granted certiorari in two Chapter 7 cases challenging the Eleventh Circuit decision in *McNeal*.[27] On June 1, 2015, the Supreme Court issued its decision, which resolved what has been characterized as "the single most important unresolved issue in consumer bankruptcy, effecting every debtor or potential debtor with a second mortgage and every lender who made such loan":[28]

> Whether § 506(d) permits a chapter 7 debtor to 'strip off' a junior mortgage lien in its entirety when the outstanding debt owed to a senior lienholder exceeds the current value of the collateral.[29]

Bank of America's Argument

In its opening brief, Bank of America advanced three main arguments as to why the lien cannot be stripped off the collateral when the creditor is wholly unsecured. First, *Bank of America* argued that the *Dewsnup* Court categorically rejected the construction of Section 506 adopted by the Eleventh Circuit in *In re Folendore*, and by extension in *McNeal*. It argued that Dewsnup did not permit the strip-off of wholly underwater junior liens because Section 506(d) only allows the stripping of liens securing disallowed claims, which are in essence invalid claims under nonbankruptcy law.[30] Bank of America argued that a reading of Section 506 adopted by the Eleventh Circuit would produce an absurd result:

> If the bankruptcy court valued a house (or any other property) at one dollar more than the amount of a senior lien, the debtor could not strip down a junior lien at all, but if the court valued the property at one dollar less than the amount of the senior lien, the debtor could strip off the entire junior lien. That result

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[27] *Bank of Amer. v. Toledo-Cardona*, No. 14-163; *Bank of Amer. v. Caulkett*, No. 13-1421 (petition granted Nov. 17, 2014) (consolidated for argument).

[28] *Bank of America, N.A. v. Toledo-Cardona, Reply Br.*, 2014 WL 5359797 (U.S.), 2 (Oct. 21, 2014).

[29] *Bank of America, N.A. v. Caulkett*, 2015 WL 137523, Petr.'s Br., (U.S.), i (U.S.,2015) (Jan. 9, 2015).

[30] *Bank of America, N.A. v. Caulkett*, 2015 WL 137523 at *19.

> would be particularly anomalous in light of the constantly shifting value of real property — and many other kinds of property subject to liens — and the Bankruptcy Code's general aversion to reliance on judicial valuation.[31]

Next, Bank of America argued that *Dewsnup*'s construction of Section 506(d) does not allow for the distinction between partially and wholly underwater liens.[32] *Dewsnup* interpreted Section 506 in light of a fundamental bankruptcy principle that "liens pass through bankruptcy unaffected," and that principle is equally relevant to a wholly underwater junior lien as to a partially underwater senior lien. Allowing courts to strip-off whole underwater liens would violate that principle.[33]

Finally, Bank of America emphasized, relying on the Court's reasoning in *Dewsnup,* that the practical effect of the Eleventh Circuit's interpretation would be "to freeze the creditor's secured interest at the judicially determined valuation," depriving the creditor of "the benefit of any increase in the value of the property by the time of the foreclosure sale", and providing the debtor a potential "windfall."[34] Bank of America argued that such result would be contrary to the basic bargain of a mortgagee, which is that the creditor's lien stays with the real property until the foreclosure, and any appreciation in the property's value should accrue to the benefit of the creditor, not the debtor.[35]

In essence, Bank of America argued that *Dewsnup* was correctly decided and its holding extends not only to partially underwater liens, but with equal force to liens that are entirely underwater. *Bank of America* also noted that Congress amended the Bankruptcy Code many times since 1992, but never modified Section 506(d) in response to *Dewsnup's* interpretation. Accordingly, *Bank of America* contended

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[31] *Bank of America, N.A. v. Caulkett*, 2015 WL 137523 at *27.

[32] *Bank of America, N.A. v. Caulkett*, 2015 WL 137523 at *25.

[33] *Bank of America, N.A. v. Caulkett*, 2015 WL 137523 at *28.

[34] *Bank of America, N.A. v. Caulkett*, 2015 WL 137523 at *22.

[35] *Bank of America, N.A. v. Caulkett*, 2015 WL 137523 at *27.

that "Congress has acquiesced in Dewsnup's reading of § 506(d)."[36]

Debtors' Argument

The debtors' argument relied heavily on the plain language interpretation of the statute. Under the debtors' view, if a claim is entirely underwater, it is also automatically entirely unsecured claim within the meaning of Section 506(a). Thus, such claim "is not an allowed secured claim" and the corresponding lien should be void under the plain language of Section 506(d).[37] The debtors contended that such statutory interpretation is unaffected by *Dewsnup*'s holding. In fact, the debtors maintained that the *Dewsnup* Court might have been inclined to agree with debtors' interpretation of the statute, however, declined to do so for policy consideration that "persuaded Dewsnup [Court] to deviate from the natural reading of the text."[38]

The debtors argued that those policy considerations are not applicable to fully underwater liens.[39] First, the debtors maintained that the *Dewsnup* Court's primary goal was to prevent windfalls to debtors if property later appreciated in value. The debtors asserted that such rationale is much less applicable to the entirely underwater junior liens than it is to a partially underwater senior lien, which was at issue in *Dewsnup*.[40] If a court voids an entirely underwater junior lien, any future appreciation in value likely would benefit the senior creditor, and not the debtor.[41] The debtors observed that because "foreclosed homes typically sell at deep discounts below fair market value. . . there is usually nothing left over to give debtors a windfall."[42]

Second, the debtors contended that junior mortgagees often use completely underwater junior liens to block

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[36]*Bank of America, N.A. v. Caulkett*, 2015 WL 137523 at *40.

[37]Bank of America, N.A. v. Caulkett, Br. for Resp't, 2015 WL 737956 (U.S.), 12 (Feb. 17, 2015).

[38]Caulkett, 2015 WL 737956 at *23-24.

[39]Caulkett, 2015 WL 737956 at *37.

[40]Caulkett, 2015 WL 737956 at *40.

[41]Caulkett, 2015 WL 737956 at *37.

[42]Caulkett, 2015 WL 737956 at *37.

consensual resolutions of troubled mortgages.[43] The debtors argued that such "hold-up power exercised by second mortgagees can thus clog the housing market, creating a large backlog of homes in foreclosure instead of keeping those homes occupied by homeowners who continue to make payments."[44] Thus, voiding junior liens that are entirely underwater may unclog the housing market by stimulating workouts in lieu of foreclosure.[45]

Moreover, the debtors contended that voiding junior liens does not violate junior mortgagees' bargains, which are reflected in their subordinate position.[46] Given that the loan-to-value ratios on second mortgage loans were so high in comparison to first mortgage loans, frequently reaching 100% of the value of the collateral, junior lender must have anticipated that any drop in home values would impair the loans' value and make them valueless.[47]

The debtors recognized that the *Dewsnup* Court was unwilling to deviate from the century long principle that mortgage liens pass through bankruptcy unaffected. However, the debtors argued that this "maxim's continuing relevance is limited," because the Bankruptcy Code permits liens to be removed in many situations.[48] Thus, the debtors argue that allowing the voiding of second mortgage liens, in contrast to senior liens, would not have a major effect on pre-Code practice.[49]

The Supreme Court's Decision

On June 1, 2015, the Supreme Court unanimously held that debtors may not strip off wholly unsecured junior liens in Chapter 7 cases.[50] n reaching this conclusion, the Supreme Court rejected the textual analysis of Section 506(d) offered

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[43]Caulkett, 2015 WL 737956 at *38.

[44]Caulkett, 2015 WL 737956 at *39-40.

[45]Caulkett, 2015 WL 737956 at *40.

[46]Caulkett, 2015 WL 737956 at *40–41.

[47]Caulkett, 2015 WL 737956 at *41.

[48]Caulkett, 2015 WL 737956 at *41.

[49]Caulkett, 2015 WL 737956 at *35.

[50]*Bank of America, N.A. v. Caulkett*, 135 S. Ct. 1995, 61 Bankr. Ct. Dec. (CRR) 31 (2015).

by the debtors. Justice Thomas, who delivered the opinion of the Court, explained that "*Dewsnup* defined the term 'secured claim' in § 506(d) to mean a claim supported by a security interest in property, regardless of whether the value of that property would be sufficient to cover the claim."[51] Under such definition, the application of Section 506(d) is reduced to "voiding a lien whenever a claim secured by the lien itself has not been allowed."[52] uch interpretation of Section 506(d) was sufficient to resolve the question presented to the Court. Because the bank's claims were both secured and allowed under Section 502, "they could not be voided under the definition given to the term 'allowed secured claim' by *Dewsnup*."[53]

The Court pointed that the debtors did not ask the Court to overrule *Dewsnup*, but instead asked the Court to limit *Dewsnup's* holding to partially underwater liens. The Court declined to adopt such an "artificial" distinction,[54] and explained that *Dewsnup* does not depend on whether a lien is partially or wholly underwater.[55]The Court also found that the historical and policy arguments advanced by the debtors were "insufficient justification for giving the term 'secured claim' in § 506(d) a different definition depending on the value of the collateral."[56] The Court observed that adopting the debtors' distinction would leave "an odd statutory framework in its place:"

> Under the debtors' approach, if a court valued the collateral at one dollar more than the amount of a senior lien, the debtor could not strip down a junior lien under *Dewsnup*, but if it valued the property at one dollar less, the debtor could strip off the entire junior lien. Given the constantly shifting value of real property, this reading could lead to arbitrary results. To be sure, the Code engages in line-drawing elsewhere, and sometimes a dollar's difference will have a significant impact on bankruptcy proceedings. But these lines were set by Congress, not this Court. There is scant support for the view

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[51]Caulkett, 135 S. Ct. 1995.

[52]Caulkett, 135 S. Ct. 1995 (citation omitted).

[53]Caulkett, 135 S. Ct. 1995.

[54]Caulkett, 135 S. Ct. 1995.

[55]Caulkett, 135 S. Ct. 1995.

[56]Caulkett, 135 S. Ct. 1995.

that § 506(d) applies differently depending on whether a lien was partially or wholly underwater.[57]

3. Timing of Valuation of Property Under Section 506(a) for Lien Striping Purposes.

After *McNeal*, the Courts in the Eleventh Circuit faced a new issue: the proper time to value property for lien stripping purposes in Chapter 7 cases. Often, whether a lien is wholly unsecured or partially unsecured depends on the date of valuation of a senior lien. Section 506(a) provides little guidance on this issue. It merely states, in relevant part, that the value "shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property.[58] Two recent cases may suggested consensus in accepting the petition date as the proper date for valuation of property for lien-stripping purposes in Chapter 7 cases.

In re Meddock

In *In re Meddock*, the debtor reopened his Chapter 7 bankruptcy case and sought to strip off a junior mortgage lien held by SunTrust Bank relying on the Eleventh Circuit's decision in *McNeal*.[59] The bank held both the first and second mortgage on the real property. The debtor owed the bank $158,407 on the first mortgage and about $16,000 on the second mortgage.[60] Each party obtained an appraisal of the property as of the petition date, and both appraisals established that the value of the property as of the petition date was less than the bank's first mortgage.[61] Thus, as of the petition date, the second mortgage was wholly unsecured.[62]

However, between the filing of the petition and filing of the motion to strip the junior lien, the value of the property had increased. The bank submitted a new appraisal, which indicated the property's recent value was $195,000. Thus, as of the date filing of the motion, the second mortgage was

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[57]Caulkett, 135 S. Ct. 1995 (internal citations omitted).

[58]11 U.S.C.A. § 506.

[59]*In re Meddock*, 2014 WL 6968772, *1 (Bankr. M.D. Fla. 2014).

[60]*In re Meddock*, 2014 WL 6968772, *1 (Bankr. M.D. Fla. 2014).

[61]*In re Meddock*, 2014 WL 6968772, *1 (Bankr. M.D. Fla. 2014).

[62]*In re Meddock*, 2014 WL 6968772, *1 (Bankr. M.D. Fla. 2014).

wholly secured.[63] The bank argued that the Court should use the date of the filing of the debtor's motion to strip off a junior lien for purposes of the valuation.[64] The bank's argument followed the Supreme Court reasoning in *Dewsnup* that any increase in value of property during the pendency of the bankruptcy case should inure to the benefit of the creditor.[65]

The Court recognized that in *Dewsnup* the Supreme Court stated that "any increase over the judicially determined valuation during bankruptcy rightly accrues to the benefit of the creditor, not to the benefit of the debtor and not to the benefit of other unsecured creditors whose claims have been allowed and who had nothing to do with the mortgagor-mortgagee bargain."[66] However, relying on *McNeal*, the Court rejected the argument as inapplicable to cases involving stripping off entirely underwater liens.[67] In essence the Court declined to extend *Dewsnup's* reasoning beyond its narrow holding that the debtor cannot strip down a partially unsecured lien in a Chapter 7 case. Finding little guidance in Section 506(a) of the Bankruptcy Code, the Court observed that the only decision on the issue, *In re Sroka,* discussed *infra*, decided by another judge in the same District, held that the petition date was the proper valuation date. The Court found the court's reasoning in *In re Sroka* persuasive, and stripped off the junior mortgage.[68]

In re Sroka

In *In re Sroka*, similar to the debtor *In re Meddock*, the debtor sought valuation of the senior lien to strip off an entirely underwater lien of a junior lien holder.[69] The debtor asserted that the appropriate valuation date in Chapter 7

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[63]*In re Meddock*, 2014 WL 6968772, *1 (Bankr. M.D. Fla. 2014).

[64]*In re Meddock*, 2014 WL 6968772, *2 (Bankr. M.D. Fla. 2014).

[65]*In re Meddock*, 2014 WL 6968772, *2 (Bankr. M.D. Fla. 2014).

[66]*In re Meddock*, 2014 WL 6968772, *2 (Bankr. M.D. Fla. 2014) citing *Dewsnup v. Timm*, 502 U.S. 410, 112 S. Ct. 773, 116 L. Ed. 2d 903, 22 Bankr. Ct. Dec. (CRR) 750, 25 Collier Bankr. Cas. 2d (MB) 1297, Bankr. L. Rep. (CCH) P 74361A (1992).

[67]*In re Meddock*, 2014 WL 6968772, *2 (Bankr. M.D. Fla. 2014).

[68]*In re Meddock*, 2014 WL 6968772, *3 (Bankr. M.D. Fla. 2014).

[69]*In re Sroka*, 2014 WL 2808101 (Bankr. M.D. Fla. 2014).

cases is the petition date.[70] The junior lien holder argued that the Court should adopt a more flexible approach and utilize the date of the filing of the debtor's motion to determine the amount of the senior lien.[71] The Court surveyed cases decided under different chapters of the Code and came to the following conclusion:

> In Chapter 11 cases, the valuation date appears fluid, with courts generally opting for one of four dates: the petition date, valuation hearing date, confirmation date, or plan's effective date. Conversely, in Chapter 7 and 13 cases, courts overwhelmingly use the petition date as the benchmark for valuation.[72]

Relying on the majority view, the Court held that in Chapter 7 cases the petition date is the appropriate date for valuation purposes"[73]

4. Is Lien Stripping on Abandoned Property Permitted?

In two recent decisions, the District Court and the Bankruptcy Court for the Southern District of Florida clashed on the issue of whether abandonment removes a property from the jurisdiction of the bankruptcy court for the purposes of lien stripping. First, the District Court in *La Paz at Boca Pointe Phase II Condo. Ass'n, Inc. v. Bandy,* held that abandonment removes property from the jurisdiction of the bankruptcy court for the purposes of lien-stripping.[74] In reaching such conclusion, the District Court relied on the Tenth Circuit's decision in *In re Dewsnup*,[75] which considered the exact issue, and held that the removal of property from the estate precluded the lien stripping. In 1989, the Third Circuit reached the opposite conclusion in *Gaglia v. First*

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[70]*In re Sroka*, 2014 WL 2808101, *3 (Bankr. M.D. Fla. 2014).

[71]*In re Sroka*, 2014 WL 2808101, *3 (Bankr. M.D. Fla. 2014).

[72]*In re Sroka*, 2014 WL 2808101, *4 (Bankr. M.D. Fla. 2014).

[73]*In re Sroka*, 2014 WL 2808101, *4 (Bankr. M.D. Fla. 2014).

[74]*La Paz at Boca Pointe Phase II Condominium Ass'n, Inc. v. Bandy*, 523 B.R. 267 (S.D. Fla. 2014).

[75]*In re Dewsnup*, 908 F.2d 588, 590–91, 21 Bankr. Ct. Dec. (CRR) 539, 23 Collier Bankr. Cas. 2d (MB) 1110, Bankr. L. Rep. (CCH) P 73533 (10th Cir. 1990), judgment aff'd, 502 U.S. 410, 112 S. Ct. 773, 116 L. Ed. 2d 903, 22 Bankr. Ct. Dec. (CRR) 750, 25 Collier Bankr. Cas. 2d (MB) 1297, Bankr. L. Rep. (CCH) P 74361A (1992).

Fed. Sav. & Loan Ass'n,[76] and the Supreme Court granted certiorari in *Dewsnup* to resolve the Circuit split on this issue. However, the Supreme Court decided the case on another issue, and held that the strip down of a lien was impermissible under the Bankruptcy Code.[77] The majority's decision did not address the jurisdictional issues raised by the Tenth Circuit.

The District Court in *La Paz at Boca* found that the Tenth Circuit's decision in *Dewsnup* was controlling. The District Court stated:

> After reviewing the Eleventh Circuit's decision in *McNeal*, the Court finds that the Bankruptcy Court's application of that case was in error. *McNeal* did not address abandonment and it did not address jurisdiction in the context of abandonment. In the event property remains within the jurisdiction of a bankruptcy court in the Eleventh Circuit, *McNeal* is certainly binding authority that stands for the proposition that unsecured liens may be stripped off. With respect to jurisdiction and abandoned property, however, the Court finds that *Dewsnup*—not *McNeal*—controls. Although the Supreme Court's decision in *Dewsnup* decision is silent on the issue of abandonment, it nonetheless affirmed the Tenth Circuit's decision which in turn clearly held that abandonment removes property, for the purposes of lien stripping, from the jurisdiction of the bankruptcy court.[78]

A month later, on January 9, 2015, the Bankruptcy Court in the same judicial district, in *In re Bodensiek*, reached the opposite conclusion.[79] The Bankruptcy Court was fully cognizant of the prior decision of the District Court on the issue. However, the Court noted that the order of the District Court had no precedential effect, and held that the "[c]ourt

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[76]*Gaglia v. First Federal Sav. & Loan Ass'n*, 889 F.2d 1304, 19 Bankr. Ct. Dec. (CRR) 1697, 22 Collier Bankr. Cas. 2d (MB) 91, Bankr. L. Rep. (CCH) P 73099 (3d Cir. 1989) (rejected by, Hargrove v. Edwards Co., Inc., 133 B.R. 765 (E.D. Va. 1991)) and (abrogated by, Dewsnup v. Timm, 502 U.S. 410, 112 S. Ct. 773, 116 L. Ed. 2d 903, 22 Bankr. Ct. Dec. (CRR) 750, 25 Collier Bankr. Cas. 2d (MB) 1297, Bankr. L. Rep. (CCH) P 74361A (1992)).

[77]*Dewsnup v. Timm*, 502 U.S. 410, 112 S. Ct. 773, 116 L. Ed. 2d 903, 22 Bankr. Ct. Dec. (CRR) 750, 25 Collier Bankr. Cas. 2d (MB) 1297, Bankr. L. Rep. (CCH) P 74361A (1992).

[78]La Paz, 523 B.R. at 272.

[79]*In re Bodensiek*, 522 B.R. 737, 741 (Bankr. S.D. Fla. 2015).

may grant a motion to value and strip liens under section 506 without regard to whether the collateral was, or might be, abandoned by the estate."[80]

In reaching this opposite conclusion, the Bankruptcy Court reasoned that the "fact that the Supreme Court affirmed the judgment of the Tenth Circuit gives no weight to the logic applied by the Tenth Circuit in its own ruling as the Supreme Court took another path to its conclusion."[81] Instead, the Bankruptcy Court relied on the dissent in *Dewsnup* by Judge Scalia, and joined by Justice Souter.[82] The dissent addressed the issue originally presented to the court, "whether section 506 applies to property abandoned by the bankruptcy trustee under section 554."[83] There, after criticizing the majority interpretation, Judge Scalia wrote:

> The fallacy in this is the assumption that the application of § 506(a) (and hence § 506(d)) can be undone if and when the estate ceases to "have an interest" in property in which it "had an interest" at the outset of the bankruptcy proceeding. The text does not read that way. Section 506 automatically operates upon all property in which the estate has an interest at the time the bankruptcy petition is filed. Once § 506(a)'s grant of secured-creditor rights, and § 506(d)'s elimination of the right to "underwater" liens and liens securing unallowed claims have occurred, they cannot be undone by later abandonment of the property. Nothing in the statute expressly permits such an unraveling, and it would be absurd to imagine it.
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> Respondents' variation on the Tenth Circuit's holding avoids these alternative absurdities only by embracing yet another textual irrationality—asserting that, even though the language that is the basis for the "abandonment" theory (the phrase "in which the estate has an interest") is contained in § 506(a), and only applies to § 506(d) *through* § 506(a), nonetheless only the effects of § 506(d) and *not* the effects of § 506(a) are undone by abandonment. This hardly deserves the name of a theory.[84]

The Bankruptcy Court found this logic to be

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[80]Bodensiek, 522 B.R. at 741.

[81]Bodensiek, 522 B.R. at 739.

[82]Bodensiek, 522 B.R. at 739–740.

[83]Bodensiek, 522 B.R. at 739–740 quoting Dewsnup, 502 U.S. at 431–32.

[84]Bodensiek, 522 B.R. at 739–740.

"unassailable."[85] It reasoned that "the only reasonable interpretation of section 506(a) is that it is effective as of the petition date, and so the use of the present tense—'in which the estate has an interest'—means the petition date and not some later date when the court considers a motion to value. Any other interpretation would lead to a series of untenable results."[86]

CONCLUSION

After the Eleventh Circuit's decision in *McNeal*, many debtors sought to have their cases reopened in an effort to have wholly underwater junior liens stripped off from their properties. The Supreme Court's decision in *Bank of Am., N.A. v. Caulkett* will most likely end this practice. Given this holding, debtors will likely continue to resort to so-called "Chapter 20" filings, which allow debtors to strip off underwater junior liens in Chapter 13, shortly after debtor receives a discharge in Chapter 7 case.[87] While the court are split on this issue, two recent decisions of the Eleventh Circuit in *In re Scantling*,[88] and of the United States Bankruptcy Panel for the Sixth Circuit in *In re Cain*[89] indicate that there is a growing consensus among the courts that Chapter 20 debtors can strip junior liens regardless of the unavailability of the discharge in Chapter 13.[90]

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[85]Bodensiek, 522 B.R. at 740.

[86]Bodensiek, 522 B.R. at 740.

[87]Chapter 20 in the bankruptcy jargon refers to Chapter 13 petition filed shortly after debtor receives a discharge in Chapter 7 case. "This strip off is accomplished, first, through a determination under § 506(a) that the creditor does not hold a secured claim and, second, by modifying the creditor's 'rights' under § 1322(b)(2), by avoiding the lien that the creditor would otherwise be entitled to under nonbankruptcy law." *In re Scantling*, 754 F.3d 1323, 1325, Bankr. L. Rep. (CCH) P 82652 (11th Cir. 2014).

[88]*In re Scantling*, 754 F.3d 1323, Bankr. L. Rep. (CCH) P 82652 (11th Cir. 2014).

[89]*In re Cain*, 513 B.R. 316, 71 Collier Bankr. Cas. 2d (MB) 1720, Bankr. L. Rep. (CCH) P 82656 (B.A.P. 6th Cir. 2014).

[90]See Cain, 513 B.R. at 320–22 (B.A.P. 6th Cir. 2014) (discussing a split of authority on the issue of whether ability of the debtor to strip off valueless liens depends on debtor's eligibility for discharge, and recognizing a growing consensus among the courts to allow lien stripping in Chapter 20 cases).