NO. 21-134

In the Supreme Court of the United States

JESUS VASQUEZ, JR. AND PENNEY LEIGH VASQUEZ,

Petitioners,

v.

WILMINGTON SAVINGS FUND SOCIETY, FSB,
AS TRUSTEE OF STANWICH MORTGAGE TRUST F,

Respondent.

On Petition for a Writ of Certiorari to the
United States Court of Appeals for the Fourth Circuit

BRIEF OF RESPONDENT IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

In *Dewsnup v. Timm*, 502 U.S. 410 (1992) and *Bank of America, N.A. v. Caulkett*, 575 U.S. 790, 794 (2015) this Court reaffirmed over a century of bankruptcy practice while establishing precedent for a fair resolution of bankruptcy claims. Never has a secured creditor's interest been deemed void and extinguished merely because the lien amount exceeded the value of the secured property. *Dewsnup* and *Caulkett*, passim, therefore reach a fair result by not hindering the rights of contracting parties and simultaneously permitting *in personam* relief for the debtor.

Petitioners seek to overturn this longstanding principle through a tortured reading of the Bankruptcy Code. As such, the sole question presented is whether *Dewsnup v. Timm*, 502 U.S. 410 (1992) should be overturned.

CORPORATE DISCLOSURE STATEMENT

Respondent certifies Wilmington Savings Fund Society FSB ("WSFS") is a subsidiary of WSFS Financial Corporation. No publicly held corporation, other than WSFS Financial Corporation, owns 10% or more of its stock. WSFS Financial Corporation is a publicly-held corporation, does not have any parent corporation and no publicly-held corporation owns 10% or more of its stock.

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REASONS FOR DENYING THE PETITION

Petitioners fail to establish compelling reasons to grant certiorari review, as set forth in Rule 10, as there is no conflict among the circuits or with a relevant decision of this Court.

More than once, this Court has found that the answer to the question presented by Petitioner is no; a Chapter 7 debtor cannot strip an allowed lien down to the value of the collateral. *See Dewsnup v. Timm*, 502 U.S. 410 (1992) and *Bank of America, N.A. v. Caulkett*, 575 U.S. 790 (2015). This is the case both when the collateral is partially under water, as in *Dewsnup*, or when the collateral is entirely underwater, as in *Caulkett*.

Nonetheless, Petitioners again seek to contest the efficacy of the existing precedent. Notably, this Court has reviewed the *Dewsnup* opinion upon similar facts and has not receded from it. In fact, the Supreme Court *expanded* the reasoning in *Dewsnup* when it considered *Caulkett*. If the Supreme Court wished to depart from its holding in *Dewsnup*, it had every opportunity to do so. Petitioners devote a significant portion of their Petition to Justice Scalia's dissenting opinion in *Dewsnup*. However, Justice Scalia joined in the *Caulkett* opinion despite his earlier dissent in *Dewsnup*.

Significantly, the Petitioners are asking this Court to overturn over a century of well-settled bankruptcy practice. At all times, whether pre-Code, post-Code, pre-*Dewsnup*, or post-*Dewsnup*, an allowed secured claim has gone through liquidation proceedings

unimpeded by the bankruptcy courts. While a debtor may obtain *in personam* relief through a discharge of monetary obligations, the Chapter 7 debtor has never been able to extinguish the property interests of its secured creditors save for isolated cases overturned by *Dewsnup* and *Caulkett*.

In sum, for the reasons set forth above and more fully below, the *Dewsnup* and *Caulkett* opinions remain good law. Both are rooted in logic, reason, and practicality, and preserve the rights of contracting parties all without running afoul of the "fresh start" afforded to Chapter 7 debtors. Accordingly, this Court should decline to grant certiorari.

I. THE BANKRUPTCY LANDSCAPE AND *DEWSNUP*

A. The Bankruptcy Code

The Bankruptcy Code specifically addresses secured claims in several sections. Pertinent here, § 506 of the Code sets forth four provisions concerning allowance and valuation of secured claims. The two most relevant subsections of § 506 for purposes of the question presented are § 506(a), dealing with claims allowance, and § 506(d), dealing with lien-voiding.

Section 506(a)(1) states:

> 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 or the amount so subject to setoff is less than the amount of such allowed claim . . . .

11 U.S.C. § 506(a)(1). This provision serves to split an undersecured claim into two distinct parts: (1) a secured claim in the amount of collateral's value, and (2) an unsecured claim for the remaining amount. Secured claims are paid before unsecured claims, and as a result of § 506(a)(1) an undersecured creditor may recover the secured portion of its claim in full, but potentially recovers a reduced amount or even nothing on the unsecured portion.

Section 506(d), the provision discussed in *Dewsnup* and central to the question presented, states that "[t]o the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void." 11 U.S.C. 506(d). The issue addressed by *Dewsnup* was § 506(d)'s use of the phrase "allowed secured claim" and how that phrase should be interpreted in light of the language in § 506(a)(1). In other words, whether § 506(a)(1) acts to reduce the amount of the secured claim to the value of the collateral such that the "allowed secured claim" in § 506(d) was limited to the value of the collateral. If so, under § 506(d), the lien could be deemed void to the extent of the unsecured portion of the claim.

As explained in detail below, this Court has already rejected Petitioners' interpretation of § 506(d), finding that such a reading was "contrary to basic bankruptcy principles." *Dewsnup*, 502 U.S. at 420.

B. Under *Dewsnup*, Only Disallowed Claims May Be Stripped Under § 506(d).

The relationship between § 506(a) and § 506(d) and their respective impacts on voiding a lien is the lynchpin to the question presented. As the seminal case on the issue, an analysis of *Dewsnup* is instructive.

Such an analysis necessarily leads to the conclusion that there is no justification for upsetting how such instances are currently treated in bankruptcy courts throughout the country.

In *Dewsnup*, the creditor lent $119,000 to the debtors, with the debtors' real property serving as security for the loan. *Dewsnup*, 502 U.S. at 412. The debtors defaulted on the loan and filed for bankruptcy under Chapter 7 before the creditor could foreclose. *Id.* at 412-413. The debtors then filed an adversary proceeding claiming that the lien securing the amounts owed should be reduced, or stripped, down to the value of the collateral. *Id.* at 413. At the time of the trial in the adversary proceeding, the value of the collateral was $39,000. *Id.* The debtors argued that application of § 506(a) resulted in the creditor's secured claim being only $39,000, and therefore the remainder of the claim was not an "allowed secured claim" under § 506(d). *Id.* at 413-414. As a result, under the debtors' view, the portion of the lien valued beyond $39,000 should be declared void. *Id.* at 414.

This Court disagreed with the debtors' interpretation of § 506(d) and its interplay with § 506(a). *Id.* at 415. Upon consideration of several potential readings of the two provisions, this Court determined that those provisions, as phrased, were ambiguous. *Id.* at 417, 420. Due to the ambiguity in the text itself, this Court's gaze turned to legislative intent, pre-Code bankruptcy law, the preservation of the rights of contracting parties, and the practical nature of each position supported by the parties. *Id.* at 417-419.

Ultimately, this Court held "§ 506(d) does not allow petitioner to 'strip down' respondents' lien, because

respondents' claim is secured by a lien and has been fully allowed pursuant to § 502." *Id.* at 417. Rather than read § 506(d)'s phrase "secured allowed claim" in conjunction with the similar phrasing in § 506(a), this Court adopted a reading whereby "the words should be read term-by-term to refer to any claim that is, first, allowed, and, second, secured." *Id.* at 415.

Here, the Petitioners filed the underlying adversary proceeding seeking to strip the Respondent's secured lien down to the value of the property, or $220,000. [ROA. 100]. This is roughly a $20,000 reduction from the lien amount. [Pet. App. 4a]. And, as in *Dewsnup*, Petitioners have not raised any issue pertaining to the validity of the Respondent's security interest. Thus, it is an allowed claim. In addition, there is no question that the Respondent's claim is secured. Therefore, under the reasoning of *Dewsnup*, the Respondent's lien is both allowed and secured, and § 506(d) does not permit the Respondent's lien to be reduced to the value of the collateral by declaring it partially void.

II. *DEWSNUP*'S HOLDING REFLECTS PRE-CODE BANKRUPTCY LAW

Although the *Dewsnup* opinion has been met with scholarly criticism, as many opinions from this Court are, its critics often overlook that *Dewsnup* did little more than fall in line with time-honored bankruptcy practice. *Dewsnup* itself explains that its holding "appears to have been clearly established before the passage of the 1978 Act. Under the Bankruptcy Act of 1898, a lien on real property passed through bankruptcy unaffected." *Dewsnup*, 502 U.S. at 418, citing *Farrey v. Sanderfoot*, 500 U.S. 291, 297, 111 S. Ct. 1825, 1829 (1991), and *Johnson v. Home State Bank*,

501 U.S. 78, 84, 111 S.Ct. 2150, 2154 (1991); *see also Stock Land Bank v. Radford*, 295 U.S. 555, 579 (1935). *Long v. Bullard*, 117 U.S. 617, 620-621 (1886). Petitioners cite instances where liens *are* affected by the bankruptcy process, including where liens are unperfected or disallowed. [Pet. p. 17-18]. These instances are noticeably inapposite to the question presented before this Court as the Respondents' lien is perfected and is allowed-Petitioners have not contested otherwise.

In context, allowing a perfected, allowed lien to ride through a Chapter 7 bankruptcy unaffected reaches the most equitable result. By permitting the lien to remain on the property until foreclosure or satisfaction, the contract between the mortgagor and mortgagee is upheld. *Dewsnup*, 502 U.S. at 417. *See also United States v. Security Indus. Bank*, 459 U.S. 70, 75 (1982) (acknowledging the difference between a creditor's right to secure repayment versus the constitutional impact of property rights in interpreting the Code so as to not modify liens retroactively due to constitutional concerns); *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 543-545 (1994) (holding that the Code should not limit state-law property rights absent a clear contrary intention); Bankruptcy alters state-law rights only if needed to achieve a bankruptcy objective. *Butner v. United States*, 440 U.S. 48, 54, 55 (1979).

With the interpretation of § 506(d) advocated by the Petitioners, a creditor's secured interest would remain at the judicially determined valuation. *See Dewsnup*, 502 U.S. at 417. In turn, should the collateral increase in value, "the creditor would lose the benefit of any increase in the value of the

property by the time of the foreclosure sale." *Id*. Instead, any such increase in the value of the property beyond the judicially determined valuation would benefit the debtor. *Id*. Any increase in the value of the collateral "rightly accrues to the benefit of the creditor" rather than to the benefit of the debtor or unsecured creditors. *Id*.

The Supreme Court has repeatedly held that the Code should not be read in a manner that departs from pre-Code bankruptcy practice unless Congress clearly intended that result. *Dewsnup*, 502 U.S. at 419-410; *Midlantic Nat'l Bank v. New Jersey Dept' of Evnt'l Prot.*, 474 U.S. 494, 500-501 (1986); *Cohen v. de la Cruz*, 523 U.S. 213, 221, 118 S. Ct. 1212, 1218 (1998). Although advanced by the Petitioners, there is no reasonable argument that pre-Code bankruptcy practice permitted a Chapter 7 debtor to strip a first mortgage down to the value of the collateral – it unequivocally did not. This Court explicitly recognized this principle in *Dewsnup* and justifiably upheld what was standard practice, further supported by a reasonable, fair reading of § 506(d). *Dewsnup* merely reinforced pre-Code practice in holding that allowed liens passed through liquidation proceedings unaffected.

III. THE CODE ITSELF PRECLUDES HOLDING THAT § 506(D) PERMITS LIEN STRIPPING ON ALLOWED CLAIMS.

In addition to historical, pre-Code bankruptcy practice, the Code itself supports *Dewsnup*'s holding that lien stripping on allowed claims is precluded. As reflected in the amount of debate surrounding the *Dewsnup* opinion, the language of § 506(a) and (d), when construed together, is ambiguous. *See Dewsnup*, 502 U.S. at 417. This Court did not err when it found

the Code's language to be ambiguous, and similarly did not err when reviewing the Code in the context of pre-Code practice. Moreover, additional support is found in the legislative history of the Code, specifically as to § 506. The Code itself, coupled with its legislative history, demonstrates an effort to preserve state law rights.

Subchapter I of Chapter 5 of the Code, where § 506 is found, establishes a framework governing claims against the estate and distribution priorities. Section 502 addresses allowed claims versus disallowed claims. Meanwhile, § 506 zeroes in on the treatment of secured claims. As set forth previously, § 506(a) splits allowed claims of undersecured creditors into a secured portion and an unsecured portion – secured claims are to be paid in full, while unsecured claims receive a pro rata share of the remaining assets, if any, following the payment of secured claims.

Section 506(d) addresses secured claims that are disallowed. Should a secured claim be disallowed, the lien is voided as the underlying debt has been deemed invalid. The effect of § 506(d) is to eliminate the potential of a creditor to usurp a bankruptcy court's finding that an underlying debt is invalid by enforcing its lien rights in state court.

Moreover, the House Report explained the operation of § 506(d) and expressly provided that liens pass through the bankruptcy case unaffected. The House Report provides, in pertinent part:

> Subsection (d) permits liens to pass through the bankruptcy case unaffected. However, if a party in interest requests the court to determine and allow or disallow the claim

> secured by the lien under section 502 and the claim is not allowed, then the lien is void to the extent that the claim is not allowed.

H.R. Rep. No. 95-595, at 357 (1977); *see also Dewsnup*, 502 U.S. at 219 (stating "Congress must have enacted the Code with a full understanding of this practice" and citing the aforementioned House Report).

Rather than eliminate decades of bankruptcy practice, *Dewsnup* stands for the long-held proposition that where a secured claim is allowed, it cannot be voided absent certain exceptions inapplicable to this case. As the Respondent has a secured claim that has been fully allowed under § 502, Petitioners should not permitted to void any portion of the underlying lien, irrespective of the value of the collateral. Accordingly, this Court should deny the Petition.

IV. THE SUPREME COURT EXPANDED *DEWSNUP* IN THE *CAULKETT* OPINION

In the face of the aforementioned scholarly criticism, this Court reviewed *Dewsnup*'s holding in *Bank of America, N.A. v. Caulkett*, 575 U.S. 790, 135 S. Ct. 1995 (2015). In *Caulkett*, Chapter 7 debtors moved to strip off or void junior mortgage liens under § 506(d). *Id*. at 1998. As opposed to *Dewsnup*, the liens in *Caulkett* were entirely underwater rather than partially underwater. *Id*. at 1998, 1999. Confronting the debtors' arguments, this Court pointed to the definition of "secured claim" as used in § 506(d): "any claim 'secured by a lien and . . . fully allowed pursuant to § 502.'" *Id*. at 1999, quoting *Dewsnup*, 502 U.S. at 416. Accordingly, this Court refused to distinguish *Dewsnup* because the value of the collateral made no

difference in the analysis of whether the creditor's claim was first, allowed, and second, secured. *Id*. at 2000. This Court, despite urging from the debtors, rejected the opportunity to limit the scope of *Dewsnup* to partially underwater liens. *Id*. at 2000-2001. "The reasoning of *Dewsnup* dictates that a debtor in a Chapter 7 bankruptcy proceeding may not void a junior mortgage lien under § 506(d) when the debt owed on a senior mortgage lien exceeds the current value of the collateral." *Id*. at 2001.

Here, notwithstanding Petitioners' position that the debtors in *Caulkett* did not ask the Court to overturn *Dewsnup*, this Court had every opportunity to limit the scope of *Dewsnup* and elected not to. Perhaps most tellingly, Justice Scalia, who issued a dissenting opinion in *Dewsnup*, joined in the unanimous *Caulkett* opinion. To the extent that *Dewsnup*'s reasoning was flawed, this Court took no steps to moderate *Dewsnup*'s reach despite a seemingly clear path to doing so.

V. CONGRESS HAS SIMILARLY LEFT *DEWSNUP* UNTOUCHED

In addition to this Court's review of the *Dewsnup* holding in *Caulkett*, Congress has not expressed an interest in clarifying § 506(d) or altering the judicial interpretation of § 506(d) despite several opportunities to do so. In 2005, approximately 13 years subsequent to *Dewsnup*, Congress made sweeping and extensive changes to the Code in the 2005 Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA"), Pub. L. 109-8, 119 Stat. 23. Notwithstanding the substantial changes implemented in the BAPCPA, *Dewsnup*'s interpretation of § 506(d) remained unchanged.

Congress is presumed to be aware of the federal courts' interpretations of statutes when re-enacting those statutes or enacting amendments to those statutes. *Lorillard v. Pons*, 434 U.S. 575, 580, 98 S. Ct. 866 (1978) ("Congress is presumed to be aware of an administrative or judicial interpretation of a statute and to adopt that interpretation when it re-enacts a statute without change."); *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833, 846, 106 S. Ct. 3245 (1986). Such acquiescence "'enhance[s] even the usual precedential force'" that courts accord the interpretations of statutes. *Watson v. United States*, 552 U.S. 74, 82-83 (2007); *Ankenbrandt v. Richards*, 504 U.S. 689, 700-701 (1992) (observing congressional inaction following statutory interpretation by the courts, noting that "Congress made substantive changes to the statute in other respects").

Here, despite an overhaul to the Code in 2005, Congress did not modify § 506(d) in response to *Dewsnup*'s interpretation of that section. Nor did Congress ever express an intent to change the interpretation of or clarify its intentions under § 506(d). Just as this Court had an opportunity to overrule, or at least recede from, *Dewsnup* in its review *Caulkett*, Congress has had an opportunity to address the well-settled interpretation of § 506(d) and has not done so. Accordingly, Congress has implicitly acquiesced in *Dewsnup*'s interpretation of § 506(d) and this Court should deny the Petition.

CONCLUSION

There is no circuit conflict with this case or other compelling reason to grant certiorari review. For the foregoing reasons, this Court should deny the petition for certiorari.

Respectfully submitted,

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