No. 18-747

In The
Supreme Court of the United States

SONJA RITTER,

Petitioner,

v.

LOIS BRADY, CHAPTER 7 TRUSTEE,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

MOTION FOR LEAVE TO FILE BRIEF AS AMICI CURIAE AND BRIEF AMICI CURIAE OF THE HONORABLE EUGENE WEDOFF (RET.), THE HONORABLE LEIF CLARK (RET.), AND A GROUP OF LAW PROFESSORS IN SUPPORT OF PETITIONER

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MOTION FOR LEAVE TO FILE BRIEF AMICI CURIAE

Pursuant to Supreme Court Rule 37.2(b), the Honorable Eugene Wedoff (ret.), the Honorable Leif Clark (ret.) and the below group of law professors, respectfully seek leave to submit the accompanying brief as amici curiae in support of petitioner. The petitioner consented to the filing of an amicus brief but the respondent did not consent.

The petition for a writ of certiorari asks this Court to overrule *Dewsnup v. Timm*, 502 U.S. 410 (1992), (Pet. i) and by so doing to reverse the decision of the Ninth Circuit. Your amici support the petitioner's request. Our brief addresses important reasons which justify overruling *Dewsnup*, and which are not the principal focus of petitioner's brief, or which warrant further amplification.

Specifically, the question presented by the petitioner is whether debtors under Chapter 7 of the U.S. Bankruptcy Code[1] may "avoid" (e.g., "strip down" or "strip off") a mortgage lien on their home when it is determined that the lien has no economic value, or is worth less than the value of the Chapter 7 debtor's home. This narrow, but recurring legal question is resolved by reference to Code subsections 506(a) and 506(d). Prior to *Dewsnup* many courts had held that this "avoidance" of a lien was precisely what the Code provided. Section 506(a) states that an allowed claim is a "secured claim" in an amount equal to the value of

[1] 11 U.S.C. § 101 *et seq*. (the "Code").

the collateral securing such claim and "is an unsecured claim to the extent" the collateral is worth less than the lender's claim. A lien on collateral is "void" to the extent the collateral is worth less than the debt. "To 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).

Dewsnup declined to permit the avoidance of liens in Chapter 7 despite the plain language of 506(d). *Dewsnup* has been highly criticized by scholars and subsequent courts, and has not been fully embraced by this Court in its subsequent decisions.

Your amici include three former United States Bankruptcy judges. Their views are informed by their extensive experience in presiding over numerous Chapter 7 bankruptcy cases. These judges have witnessed the harmful effects of *Dewsnup* on Chapter 7 debtors, as well as its disruptive effect on the administration of the bankruptcy system.

More recently, both former Judge Eugene Wedoff, who is the immediate past president of the American Bankruptcy Institute, and former Judge Bruce Markell have been appointed to the new Consumer Bankruptcy Commission created by the American Bankruptcy Institute. In this role, each of these judges is currently involved with in-depth and scholarly reviews of the important and critical issues confronting the consumer bankruptcy system; and each of these judges has concluded that *Dewsnup* has caused undue

harm to individual debtors and is based on a flawed textual interpretation of the Code.

Three of the proposed amici are active law professors (as is former Judge Markell). Professor Kenneth Klee served as associate counsel to the Committee on the Judiciary, U.S. House of Representatives, and was one of the principal drafters of the 1978 Code. Professor Klee's views are based on his first-hand knowledge. His prior writings,[2] which have been quoted by numerous courts of appeal, point out that § 506(a) and (d) of the Code were intended to provide for the bifurcation of the claim of a secured lender into an allowed secured claim and an allowed unsecured claim, and that such bifurcation would thus "avoid" that portion of the lien which had no economic value. Professor Klee supports the view that *Dewsnup* has failed to apply the correct textual interpretation intended by Congress.

Second, our proposed brief demonstrates that *Dewsnup* has created confusion and disruption by requiring that § 506 be interpreted differently in different Code chapters. Chapters 11 and 13 both utilize the *identical* Code language found in § 506; yet, in each of these chapters the courts have uniformly rejected the *Dewsnup* interpretation of § 506. This is because the *Dewsnup* interpretation would, in the words of some courts, "gut" and "convulse" the normal operation of bankruptcy law.

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[2] *See*, *e.g.*, Kenneth N. Klee, *All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code*, 53 Am. Bankr. L.J. 133, 152 (1979).

Third, we identify relevant legal scholarship and empirical studies that demonstrate the serious financial harm caused by *Dewsnup's* misconstruction of § 506. Chapter 7 debtors often have liens on their homes which exceed the value of the home. Section 506 was intended to alleviate this problem by permitting liens with little or no value to be either "stripped off" or "stripped down." This outcome mirrors what occurs under state law foreclosure where a lender obtains the value of the collateral, and then has an unsecured claim for the balance. *Dewsnup* is a rigid barrier to the goal of achieving an economic "fresh start" by Chapter 7 debtors.

For the foregoing reasons, we respectfully request that the court grant leave to file the accompanying brief.

Respectfully submitted,

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INTEREST OF AMICI CURIAE[3]

The amici curiae are three retired United States Bankruptcy Judges and a group of bankruptcy law professors. Our interest in submitting this brief is to ask this Court to overrule *Dewsnup v. Timm*, 502 U.S. 410 (1992), and by so doing to reverse the decision of the Ninth Circuit. We identify relevant legal scholarship and empirical studies that demonstrate the serious financial harm caused by *Dewsnup's* misconstruction of § 506 of the U.S. Bankruptcy Code.[4] This harm is recurring, and affects both individual Chapter 7 debtors, commercial bankruptcy debtors and the larger macro economy.

The Honorable Eugene Wedoff (ret.) served as a United States Bankruptcy Judge in the Northern District of Illinois in Chicago from 1987 to 2015. Judge Wedoff was formerly a partner at Jenner & Block. He served as a member and chair of the Advisory Committee on Bankruptcy Rules from 2004 to 2014 and as a governor, secretary, and president of the National Conference of Bankruptcy Judges through 2015. He is the immediate past president of the American Bankruptcy Institute, a Fellow of the American College of

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[3] Pursuant to Supreme Court Rule 37, counsel of record for petitioner and respondent received notice of the intent to file this brief more than ten days before its due date. Petitioner has consented to its filing. Respondent did not consent. No counsel for a party authored this brief in whole or in part, and no person other than amici or their counsel contributed any money to fund its preparation or submission

[4] 11 U.S.C. § 101 *et seq*. (the "Code").

Bankruptcy and a member of the National Bankruptcy Conference.

The Honorable Leif M. Clark (ret.) served as a United States Bankruptcy Judge for the Western District of Texas from 1987 to 2012. He served on the endowment boards for both the American Bankruptcy Institute and the National Conference of Bankruptcy Judges. He is a member of the American College of Bankruptcy and the National Bankruptcy Conference, and continues to speak on bankruptcy topics nationwide.

Professor Kenneth N. Klee is a Professor of Law Emeritus at the UCLA School of Law and a founding partner of Klee, Tuchin, Bogdanoff & Stern LLP. Professor Klee served as associate counsel to the Committee on the Judiciary, U.S. House of Representatives, and was one of the principal drafters of the 1978 Bankruptcy Code. From 1992 to 2000, he served as a member of the Advisory Committee on Bankruptcy Rules to the Judicial Conference of the United States. He served as a commissioner on the American Bankruptcy Institute's Commission to Study the Reform of Chapter 11.

Professor Bruce A. Markell is the Professor of Bankruptcy Law and Practice at Northwestern Pritzker School of Law, part of Northwestern University. He is a former Bankruptcy Judge and a former member of the Ninth Circuit's Bankruptcy Appellate Panel. He is a co-author of four casebooks in bankruptcy, contracts, secured transactions, and securitization. He is

a founding member of the International Insolvency Institute, a member of the Board of Editors of Collier on Bankruptcy, a member of the American Law Institute, a conferee of the National Bankruptcy Conference, and a fellow of the American College of Bankruptcy, where he was the Scholar in Residence from 2013 to 2016. He serves as a commissioner on the American Bankruptcy Institute's Commission on Consumer Bankruptcy.

Professor Michael D. Sousa is an Associate Professor of Law at the University of Denver Sturm College of Law. He received his J.D. from Rutgers University School of Law, his LL.M. from St. John's University School of Law, his Master's of Arts degree in anthropology from the University of Denver. He sits on the Editorial Boards for both the American Bankruptcy Institute Law Review and the American Bankruptcy Law Journal.

Professor Jack F. Williams is a Professor of Law at Georgia State University and the Center for Middle East Studies Institute, where he teaches and/or conducts research on bankruptcy and business reorganizations; remedies; mergers and acquisitions; taxation; and statistics. He is the Scholar in Residence of the Association of Insolvency and Restructuring Advisors and a fellow in the American College of Bankruptcy. He holds a B.A. in economics from the University of Oklahoma, a J.D. with High Honors from George Washington University National Law Center, and a Ph.D. in archaeology from the University of Leicester in Leicester, United Kingdom.

David R. Kuney has served as an Adjunct Professor at the Georgetown University Law Center, American University's Washington College of Law and at New York Law School. He currently serves on the Board of Directors of the American Bankruptcy Institute. He is a fellow in the American College of Bankruptcy and the American College of Real Estate Lawyers.

STATEMENT

The question presented in this appeal is "whether *Dewsnup v. Timm*, 502 U.S. 410 (1992) should be overruled." (Pet. i). When stated in common bankruptcy vernacular, the issue is whether individual debtors in Chapter 7 bankruptcy cases may "avoid" (e.g., "strip off" or "strip down") a mortgage lien on their home when the value of the home is less than the mortgage debt.[5] This issue is likely to arise when the mortgage is a "second mortgage" and the value of the home is less than the outstanding balance on the first mortgage.

The resolution of this issue is governed by §§ 506(a) and 506(d) of the Code. Section 506(a) states that an allowed claim is a "secured claim" in an amount equal to the value of the collateral securing

[5] The Code defines a "lien" as any "charge against or interest in property to secure payment of a debt or performance of an obligation." 11 U.S.C. § 101(37). The Code does not use the term "collateral" but instead refers to the creditor's interest in the estate's interest in such property. *See* § 506(a). We use "collateral" for clarity's sake.

such claim and "is an unsecured claim to the extent" the collateral is worth less than the lender's claim. A lien on collateral is "void" to the extent the collateral is worth less than the debt. "To 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).

Section 506 functions through "bifurcation" of a secured claim.[6] The bifurcation is based on the value of the collateral. The first component is the allowed secured claim, which is equal to the value of the collateral. The second component is the allowed unsecured claim which arises whenever the collateral has a value lower than the mortgage debt. The lien on the unsecured component is thus "void." This outcome essentially replicates what would occur under a state law foreclosure, where a secured lender receives the value of the collateral by conducting a foreclosure sale, and then has only an unsecured claim for the balance.

This lien avoidance is a critical aspect of the fresh start in bankruptcy. In a Chapter 7 bankruptcy, if the value of a home is less than the mortgage debt that the home secures, the mortgage lender would have an allowed secured claim equal to the value of the home, and an allowed unsecured claim for the balance of the mortgage. With respect to the unsecured portion of its claim, the lender would then receive a pro rata share

[6] "Section 506 requires a bifurcation of a 'partially secured' or 'undersecured' claim into separate and independent secured claim and unsecured claim components." *U.S. v. Ron Pair Enter. Inc.*, 489 U.S. 235, 239 n.3 (citing 3 Collier on Bankruptcy ¶ 506.04, p. 506-15 (15th ed. 1988)).

of the proceeds once the debtor's assets are liquidated by the trustee, the same as other unsecured creditors. The lender's unsecured claim, to the extent unpaid, is then "discharged," the same as all other unsecured claims. The debtor receives an economic "fresh start" and the lender receives the same recovery as if there had been a state law foreclosure.

This guiding principle that § 506 bifurcates a secured lender's claim into a secured and unsecured component is a bedrock principle that governs all of the Code's chapters. Amicus Professor Kenneth Klee, one of the principal drafters of the 1978 Code,[7] explained this bifurcation process, noting that the value of a lender's collateral is determinative. "The claim is an allowed secured claim to the extent of the value of the collateral, and is an unsecured claim to any extent that the value of the collateral is less than the allowed claim."[8] Professor Klee gives an example of an allowed claim of $1,000 secured by collateral worth $400 which would give rise to an allowed secured claim of $400 and an allowed unsecured claim of $600. *Id*.

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[7] "Professor Klee served as associate counsel to the Committee on the Judiciary, U.S. House of Representatives, and was one of the principal drafters of the Bankruptcy Code." *In re Philadelphia Newspapers, LLC*, 599 F.3d 298, 331 (3d Cir. 2010).

[8] Kenneth N. Klee, *All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code*, 53 Am. Bankr. L.J. 133, 152 (1979). While Professor Klee was discussing cramdown under Chapter 11 he noted that § 506 "will apply as in a liquidation case." *Id*. at 152.

This Court initially interpreted § 506 precisely as articulated by Professor Klee. *U.S. v. Ron Pair Enter. Inc.*, 489 U.S. 235 (1988). Yet this focus on the "value" of the collateral was lost in *Dewsnup* in which the Court held that a lien could be avoided only if the underlying claim was not an "allowed claim." By "allowed claim" the Court presumably meant the claim was not subject to a legal challenge under applicable law. *See* 11 U.S.C. § 502(b)(1) which states that a claim shall be allowed except to the extent that "such claim is unenforceable against the debtor . . . under any agreement or applicable law . . . "

Dewsnup's holding overlooked the question of the value of the lender's collateral, and permits avoidance only in the rare instance when there is some legal defect with the claim. *Dewsnup* thus permitted that component of a lien which was not supported by any economic value to survive post-bankruptcy, and thus to pose a life-long threat of foreclosure. This Court noted its reservations about its own ruling, saying it might have ruled otherwise if it were writing on a "clean slate," and expressed doubt that the same rule applied in other Code chapters. *Dewsnup*, 502 U.S. 417, n.3.

Ms. Ritter's case illustrates the recurring harm caused by *Dewsnup.* After she filed for bankruptcy, she was granted a discharge of all unsecured claims. She timely filed a motion to avoid the PNC Bank lien. Dkt. 14. No one objected to her motion, but the court failed to act. Years later Ms. Ritter learned she could not refinance her home because PNC's lien was still of record. She filed a motion asking the bankruptcy court to

reopen her bankruptcy and to rule on her motion to avoid the PNC lien. Dkt. 17. Neither the Chapter 7 Trustee nor PNC objected. The bankruptcy court nevertheless denied her motion, citing *Dewsnup* as controlling. Pet. App. 17a.

Ms. Ritter appealed to the Bankruptcy Appellate Panel (which affirmed on *Dewsnup* grounds. Pet. App. 4a), and then to the Ninth Circuit. The Ninth Circuit affirmed the decisions below based *solely* on a legal determination, stating that "lien avoidance mechanism in 11 U.S.C. § 506(d) is not available when a claim secured by a lien has been allowed under § 502," citing *Dewsnup* and *Bank of Am. N.A. v. Caulkett*, 135 S.Ct. 1995, 1999-2001 (2015). Pet. App 3a. The bankruptcy court's refusal to reopen Ms. Ritter's bankruptcy case and to grant the motion to avoid the PNC lien raises the narrow legal question of whether *Dewsnup* should be overruled. We urge this Court to do so.

SUMMARY OF ARGUMENT

Your amici urge this Court to grant the petition for the following reasons:

First, by granting certiorari this Court will have an opportunity to consider overruling *Dewsnup*. *Dewsnup* disregarded the fundamental statutory mandate to look to the *value* of the lien as determining the lienholder's rights and instead looked to whether the underlying claim was valid under nonbankruptcy law and thus was an "allowed claim." This shift was

incorrect and has been widely criticized by this Court and others.

Second, overruling *Dewsnup* will resolve an irreconcilable conflict between lien avoidance in Chapters 11 and 13 of the Code and lien avoidance under Chapter 7. The Code's statutory language should be interpreted consistently across all chapters. *Till v. SCS Credit Corp.*, 541 U.S. 465, 466 (2004). Under *Dewsnup* the Code is asymmetrical, providing different treatment to different debtors under the same statutory language.

Third, *Dewsnup* continues to cause financial harm to a large number of debtors seeking relief under Chapter 7. Approximately 700,000 Chapter 7 cases are filed each year.[9] Empirical research shows that second mortgages pose substantial economic burdens to Chapter 7 debtors.[10] *Dewsnup* prevents these debtors from obtaining a genuine fresh start, and thus is at odds with this Court's landmark decision in *Local Loan Co. v. Hunt*, 292 U.S. 234, 245 (1934), which recognized that an individual's opportunity to obtain an economic fresh start is in the nature of a personal liberty, "quite as much as, if not more than, it is a property right."

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[9] The number of non-business bankruptcy filings in 2017, 2016, and 2015 was as follows: 770,901, 808,781 and 911,086, respectively. *March 2017 Bankruptcy Filings Down 4.7 Percent*, United States Courts (Apr. 19, 2017), http://www.uscourts.gov/news/2017/04/19/march-2018-bankrutpcy-filings-down-47-percent [https://perma.cc/LB7B-CAEA].

[10] *See* Teresa A. Sullivan, et al., *As We Forgive Our Debtors, Bankruptcy and Consumer Credit in America*, 133-134 (1999).

This case presents an ideal vehicle for the Court to overrule *Dewsnup*. The facts are undisputed and the ruling below was squarely based on *Dewsnup*.

ARGUMENT

I. The Court should overrule *Dewsnup*.

A. Sections 506(a) and 506(d) of the Bankruptcy Code base the right to avoid a lien on the value of a lender's collateral.

Sections 506(a) and (d) of the Code are not ambiguous. They plainly require that a secured claim be "bifurcated" into a secured claim and an unsecured claim, with the value of the collateral determining the amount of the secured claim. The rights of a lender with a secured claim then rise or fall on the basis of the collateral's value.

The language is straightforward. Section 506(a) states that "an allowed claim of a creditor secured by a lien on property [of the debtor] . . . is a secured claim to the extent of the value of [the collateral] . . . and is an unsecured claim to the extent that the value of [the collateral] is less than the amount of such allowed claim."

Section 506(d) applies this fundamental bifurcation of the claim to lien avoidance: "To the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void. . . ." Justice Scalia made this point emphatically. "Section 506(d)

unambiguously provides that to the extent a lien does not secure such a claim it is rendered void." *Dewsnup*, 502 U.S. 420 (Scalia, J., dissenting).

Plain meaning should control here. "When the words of a statute are unambiguous, then . . . judicial inquiry is complete." *Conn. Nat'l Bank v. Germain*, 503 U.S. 249 (1992). "[W]here as here, the statute's language is plain, 'the sole function of the courts is to enforce it according to its terms.'" *U.S. v. Ron Pair*, 489 U.S. at 241.

Section 506's emphasis on the value of the lien is consistent with the constitutional foundation that protects a secured claim "to the extent of the value of the property," and that "there is no constitutional claim of the creditor to more than that." *Wright v. Union Cent. Life Ins. Co.*, 311 U.S. 273, 278 (1940). As Amicus Professor Bruce Markell correctly points out, "[t]he Supreme Court has never held that a secured creditor's property rights extend beyond the collateral itself, [but rather] has found that a secured creditor's rights end when there is no value for their claims." Bruce A. Markell, *Loser's Lament: Caulkett and ASARCO*, Bankr. Law Ltr. 35:8 (August 2015).

Prior to *Dewsnup* this Court stated that § 506 "governs the definition and treatment of secured claims." *Ron Pair*, 489 U.S. at 238-39. The Court explicitly endorsed the notion that § 506 bifurcates a claim into two separate and independent components and that the portion that lacks any value is an unsecured claim. "Subsection (a) of § 506 provides that a claim is

secured only to the extent of the value of the property on which the lien is fixed; the remainder of the claim is unsecured." *Id*. at 239. This Court gave an example showing that if property has a value of $60,000 and a creditor's claim of $100,000 is secured by a lien on that property, then the creditor has a secured claim only to the extent of $60,000. *Id*. at n.3. "The remainder of that claim is considered unsecured," *id*. at 1029, and thereby the lien is void.

The bankruptcy system functioned well prior to *Dewsnup*. The courts of appeals agreed on how § 506 was to be interpreted: "[t]he majority view and the view of every Circuit Court of Appeals that has ruled upon the issue is that unsecured real estate mortgage liens can be voided by the Bankruptcy Court pursuant to § 506(d)." *In re Moses*, 110 B.R. 962, 963 (Bankr. N.D. Okla. 1990) (citations omitted).

Likewise, prior to *Dewsnup*, while the bankruptcy courts consistently protected a secured lender up to the value of its lien, they also avoided that component of the lien which was not supported by any value, in order to also provide a debtor with a fresh start. "[A] Chapter 7 debtor may use § 506(d) to void an unsecured portion of a lien simply based on the plain language of that section . . . [T]he avoidance of an unsecured real estate mortgage is consistent with the Code's policy of providing the debtor with a fresh start." *In re Garnett*, 88 B.R. 123, 125 (Bankr. W.D. Ky. 1988).

B. *Dewsnup* incorrectly looked to the "allowability" of a claim rather than to the value of the collateral.

When it issued the *Dewsnup* decision in 1992, this Court departed from *Ron Pair*, and disrupted the bankruptcy system by creating a troublesome, internal Code inconsistency. Instead of adopting a plain language view of § 506, *Dewsnup* held that "the words 'allowed secured claim' in § 506(d) need not be read as an indivisible term of art defined by reference to § 506(a)," but instead "should be read term-by-term to refer to any claim that is, first, allowed, and, second, secured." 502 U.S. at 415. If a claim "has been 'allowed' . . . and is secured by a lien with recourse to the underlying collateral, it does not come within the scope of § 506(d)." *Id*. Read that way, section 506(d) has "the simple and sensible function of voiding a lien whenever a claim secured by the lien itself has not been allowed." *Id*. at 415-416.

This interpretation deprived the statutory words of any real purpose. Allowability requires a claim to be "enforceable" under applicable law. 11 U.S.C. § 502(b)(1). Under normal state law principles a lien can be enforced only if the underlying claim is valid. If a creditor's claim is unenforceable outside of bankruptcy, there would be no claim, secured or unsecured or otherwise—that could be enforced in bankruptcy. The Code's drafters had no need to repeat the rudimentary concept that a secured lender can only enforce a

valid claim.[11] Thus, "allowability" was never intended to be the controlling test; value is the actual, intended test for voidability.

The Court noted serious concerns about its own conclusions in *Dewsnup*. First *Dewsnup* read the language in § 506(a) differently from the same language used in § 506(d). This gave the Court pause: "Were we writing on a clean slate, we might be inclined to agree with petitioner that the words 'allowed secured claim' must take the same meaning in § 506(d) as in § 506(a)." 502 U.S. at 417. Second, the Court recognized that its view of § 506 might be inconsistent with how the same words are interpreted in other Code provisions. "We express no opinion as to whether the words 'allowed secured claim' have different meaning in other provisions of the Bankruptcy Code." *Dewsnup*, 502 U.S. at 417, n.3.

Justice Scalia, dissenting, recognized that *Dewsnup* would likely be disruptive and create interpretive problems for the courts. "Almost point for point, today's opinion is the methodological antithesis of *Ron Pair*—and I have the greatest sympathy for Courts of Appeals who must predict what manner of statutory construction we shall use for the next Bankruptcy Case." 502 U.S. at 435. He predicted that *Dewsnup*

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[11] The term "claim" means a "right to payment." 11 U.S.C. § 101(5). While this definition includes a "disputed" claim, the holder must ultimately have a "right" to payment to hold a "claim."

would lead to the "destruction of predictability." *Id*. And so it has.

Dewsnup's disruptive effect became apparent with the passage of time. Justice Thomas observed that "[t]he methodological confusion created by *Dewsnup* has enshrouded both the Courts of Appeals and . . . Bankruptcy Courts." *Bank of America Nat. Trust & Sav. Ass'n v. 203 N. LaSalle St. P'ship*, 526 U.S. 434, 463 (1999) (concurring).

Justice Gorsuch, then sitting on the Tenth Circuit, expressed the same concern about the lack of consistency resulting from *Dewsnup*, stating that "every federal court of appeals to consider the question has already refused to extend *Dewsnup's* definition of the term 'secured claim' to other statutory provisions using that term in Chapter 13." *In re Woolsey*, 696 F.3d 1266, 1276 (10th Cir. 2012).

Dewsnup was the subject of this Court's scrutiny in *Caulkett*, 135 S.Ct. 1995. There, the petitioner asked the Court to avoid a lien that was wholly unsecured, as opposed to the partially unsecured lien in *Dewsnup*. This Court acknowledged that "under [the] straightforward reading of the statute, the debtors would be able to void the Bank's claims." *Id*. at 1999. What prevented application of the "normal rule of statutory construction" was only the prior ruling in *Dewsnup*. *Id*.

Significantly, however, the Court noted *three times* that the petitioner in *Caulkett* had not asked the Court to overrule *Dewsnup*, but only to distinguish it on the grounds that *Caulkett* involved a wholly underwater

lien.[12] This Court rejected the distinction argument on the grounds that it involved unworkable line drawing. Thus, the opportunity to overrule *Dewsnup* was not squarely presented.

The petitioner in this case now squarely seeks that overruling. *Dewsnup* and *Caulkett* reflect the same textual infirmity. Rather than distinguishing a case involving a wholly unsecured loan versus a partially unsecured loan, this Court should apply the same textual interpretation to both fact patterns based on this Court's sound precedent in *Ron Pair* and overrule *Dewsnup.*

II. The Court should grant the petition for certiorari in order to resolve the conflict created by *Dewsnup* and thereby to provide a consistent interpretation of §§ 506(a) and (d) among the Code's chapters.

A. *Dewsnup's* interpretation of § 506 is not followed in Chapter 11 cases.

Granting the petition for certiorari will permit this Court to resolve the conflict with how courts interpret § 506 in the other Code chapters, and in particular, with Chapter 11. While the present appeal does not involve a Chapter 11 case, the correct interpretation of

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[12] "The debtors do not ask us to overrule *Dewsnup.*" *Id*. at 1999-2000. "Despite this criticism, the debtors have repeatedly insisted that they are not asking us to overrule *Dewsnup*." *Id*. at 2000 n.†. And, "The debtors here have not asked us to overrule *Dewsnup* . . . " *Id*. at 2001.

§§ 506(a) and (d) is settled law under Chapter 11. The very same understanding should control in Chapter 7 as well. There is no sound basis to continue to fence-off Chapter 7 from the well-understood avoidance scheme by applying the holding in *Dewsnup*.

Courts have refused to apply *Dewsnup* to Chapter 11 because its interpretation of § 506 is both textually unsound and its logic is antithetical to the entire purpose of Chapter 11. In Chapter 11, § 506(a) and § 506(d) function to permit the "bifurcation" of secured claims into a secured portion and an unsecured portion; bifurcation is the process that results in lien "avoidance" and without such bifurcation the entire process of reorganization would be "gutted" as explained below.

Most courts agree that *Dewsnup* does not apply in the reorganization chapters. "A great majority of the courts that have considered the issue in reorganization cases have concluded that the holding in *Dewsnup* should be limited to Chapter 7 cases and should not prevent lien stripping in reorganization cases." *See In re Heritage Highgate Inc.*, 679 F.3d 132 (3d Cir. 2012) holding that applying *Dewsnup* would convulse Chapter 11:

> The Code makes that clear: "the process of lien stripping is ingrained in the reorganization provisions of the Bankruptcy Code to such an extent that any attempt to extend the holding in *Dewsnup* to Chapter 11 cases would require that numerous provisions of

> the statute be ignored or construed in a very convoluted manner."(citations omitted).

Id. at 144.

As noted by another court, applying *Dewsnup* in other Code chapters would "gut the sum and substance of the reorganization and rehabilitation of debt concept under the Bankruptcy Code." *In re Johnson*, 386 B.R. 171, 177 (Bankr. W.D. Pa. 2008).

Dewsnup, if applied, would convulse and gut Chapter 11's reorganization structure, for both individuals and business debtors, because § 506's bifurcation is at the core of debt restructuring. Business debtors frequently have large secured claims which exceed the value of the lender's collateral. *See*, *e.g.*, *203 N. LaSalle*, 526 U.S. 434 at 439 (noting that the secured creditor's claim was bifurcated into a secured claim and unsecured claim because "the value of the mortgaged property was less than the balance due the Bank.").

Bifurcation is the first step in restructuring debt. Once bifurcated, the secured claim may then be restructured based on the value of the collateral. For example, a secured claim could be restructured so as to be payable over a term of years, with a reduced interest rate. The lien on the unsecured portion is voided and the balance of the claim may be treated as an unsecured claim under the "cramdown" provisions of the Code. *See* 11 U.S.C. § 1129(b)(2)(B). It is precisely this bifurcation and "avoidance" that permits a debtor to match its debt obligations with its ability to generate

cash flow.[13] For the same reason, the argument that "liens pass through bankruptcy" is incorrect; if such were true, modern bankruptcy would cease to exist in its present form.

In short, there could be no Chapter 11 reorganization if somehow *Dewsnup's* holding were somehow applied. Nor is there any need to continue *Dewsnup's* legacy of perpetuating inconsistent interpretations of §§ 506(a) and (d) in different Code chapters. Thus, *Dewsnup* has required the courts to abandon the cardinal principle that "equivalent words have equivalent meaning when repeated in the same statute." *Cohen v. de la Cruz*, 523 U.S. 213, 220 (1998).

B. *Dewsnup's* interpretation of § 506 is not followed in Chapter 13.

This Court likewise abandoned the statutory construction of § 506 announced in *Dewsnup* when it considered lien avoidance in the context of a Chapter 13 case. *See Nobelman v. American Savings Bank*, 508 U.S. 324 (1993). "Most notably, the Supreme Court itself has declined to extend *Dewsnup's* understanding

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[13] Thus, in *203 N. LaSalle*, the debtor proposed a plan in which the bank's mortgage claim of $93 million was bifurcated into an allowed secured claim of $54.5 million (the value of the collateral) and an unsecured claim of $38.5 million. The secured claim was paid over 7 to 10 years. The Bank was then paid 16% of its unsecured claim, with the balance discharged. *Id.* at 439-440. This proposed plan was found defective by this Court but only because it did not satisfy the "new value" exception—an issue which is not pertinent here.

of the term 'secured claim' when it appears in Chapter 13." *In re Woolsey*, 696 F.3d at 1276 (discussing *Nobelman*).

The refusal to apply *Dewsnup* in Chapter 13, as with Chapter 11, is significant here as well. Mostly, it reflects a rejection of the statutory construct applied to §§ 506(a) and 506(d) in *Dewsnup*. Second, it reflects the notion that lien avoidance, in all chapters, is a primary tool in restructuring and providing a fresh start. Overruling *Dewsnup* would thus end the awkward need to continually fence-off *Dewsnup's* holding from every other chapter of the Code.

Chapter 13 is mostly designed for individuals who have a regular income, and debts that do not exceed a defined limit. 11 U.S.C. § 109(e). Such debtors may file a plan for repayment of debt over a plan term, (typically five years) and may restructure most secured claims through a lien avoidance power similar to that of Chapter 11. The one exception is that Chapter 13 includes an "anti-modification" provision that prohibits lien avoidance on a debtor's principal residence. 11 U.S.C. § 1322(b)(2).

In *Nobelman*, the question presented was whether a Chapter 13 debtor could strip down a partially unsecured mortgage lien on a primary residence. *Nobelman* acknowledged that valuation of collateral is central to determining which portions of a lender's claim are secured, and which are unsecured: "The portion of the

bank's claim that exceeds $23,500 [the judicial valuation of the home] is an 'unsecured claim componen[t]' under § 506(a)," 502 U.S. at 328 (citing *Ron Pair*, 489 U.S. 235, 239, n.3).

This Court declined to permit the lien avoidance in *Nobelman* solely because § 1322(b)(2), which applies only in Chapter 13, states that a plan cannot "modify the rights" of a secured lender holding a lien on a debtor's principal residence. Where the mortgage loan is only partially unsecured, the stripping of the lien would have required a revised mortgage contract to adjust the terms to fit the reduction and thus implicated the lender's "rights." *Dewsnup* did not control the outcome.

Significantly, however, *Dewsnup* has not been followed in Chapter 13 cases where the mortgage lien is *wholly unsecured*. This is because the courts view such a lien as not being a "secured claim" and hence as not being protected by the anti-modification language of § 1322. Such a lien is avoidable under § 506 and the logic of *Ron Pair*. *In re Tanner*, 217 F.3d 1357 (11th Cir. 2000). *See also Brendan Mortg. Inc. v. Lanum*, No. 13 C 5589, 2013 WL 6634012, at *3 (N.D. Ill. Dec. 16, 2013). ("The clear weight of appellate authority supports holding that a wholly unsecured lien on the debtor's principal residence, as determined by reference to § 506(a), may be stripped pursuant to § 1322(b)(2).")

III. This case presents an issue of recurring, national importance. *Dewsnup* continues to cause financial harm to numerous debtors. This case provides an ideal vehicle to overrule *Dewsnup*.

A. *Dewsnup* continues to cause financial harm by imposing barriers to a debtor's fresh start.

This appeal presents an issue of recurring importance. *Dewsnup's* harmful consequences continue to be experienced by numerous Chapter 7 debtors. Empirical data establishes that mortgage debt is one of the primary drivers of the need for Chapter 7 relief, as is the ability to avoid underwater liens. Chapter 7 debtors typically have mortgage obligations more onerous than the general population. "Homeowners in bankruptcy carry larger mortgages than the homeowning population in general. . . . The relative impact of these home mortgages is even greater than the direct comparison suggests. Not only do bankrupt debtors have higher mortgages, but they must pay them from lower incomes." Sullivan, *As We Forgive Our Debtors*, 133. Indeed, "for the typical homeowner mortgage debt alone is more than two and a half year's income." *Id*. Further, "[t]he burden of the mortgage debt on this average homeowner-debtor is almost three times larger [than the general population.] Thus, the home mortgage for a bankruptcy debtor is an 'extraordinary burden.'" *Id*.

Bankruptcy debtors often have second lien mortgages. In the general population, about 9.8% of all

homeowners put second mortgages of any size on their homes, compared with 32.6% of the bankrupt homeowners living in states permitting second mortgages." Sullivan, *As We Forgive Our Debtors*, 134. And these "[s]econd mortgages are short-term, higher payment obligations which force debtors to pay an even larger share of their income to keep their homes." *Id*. Debtors who are "entrepreneurs" often utilize second mortgages to obtain needed business cash. *Id*. at 141.

Mortgage debt has made it difficult for debtors to erase a negative net worth. "The homeowners in bankruptcy earn less and owe more than homeowners in the general population. They struggle with nonmortgage debts that would (and did) sink debtors without homes." *Id*. at 141. "Even with the equity they build up in their homes, debtors in bankruptcy have an average net worth so deep in the hole ($-13,337) that it would take the best part of a year's earnings without any expense just to make it to 'flat broke,' zero net worth." *Id*. at 141.

Reversal of *Dewsnup* would address and alleviate a financial crisis for Chapter 7 debtors, as well as provide a consistent and coherent interpretation of § 506 across all Code chapters.

B. *Dewsnup* is inconsistent with this Court's longstanding policy of protecting the fresh start of bankruptcy.

Over 200 years ago Sir William Blackstone wrote that through discharge "the bankrupt becomes a clear

man again; and, by the assistance of his allowance and his own industry, may become a useful member of the commonwealth." 2 *William Blackstone, Commentaries* *484. "A debtor whose obligations are not discharged faces considerable consequences; in many instances, failure to achieve discharge can amount to a financial death sentence." *In re Hyman*, 502 F.3d 61, 66 (2d Cir. 2007).

In perhaps its most important articulation of the core value of bankruptcy's fresh start, this Court held that the fresh start of bankruptcy is an essential aspect of one's financial and "personal liberty." *Local Loan Co. v. Hunt*, 292 U.S. 234, 245 (1934).

> The power of the individual to earn a living for himself and those dependent upon him is in the nature of a personal liberty quite as much as, if not more than, it is a property right. To preserve the free exercise is of the utmost importance, not only because it is a fundamental private necessity, but because it is a matter of great public concern. . . . The new opportunity in life and the clear field for future effort, which it is the purpose of the bankruptcy act to afford the emancipated debtor, would be of little value to the wage earner if he were obliged to face the necessity of devoting the whole or a considerable portion of his earnings for an indefinite period of time in the future to the payment of indebtedness incurred prior to his bankruptcy.

Id. at 245 (citations omitted).

C. This case presents an ideal vehicle to overrule *Dewsnup*.

This case provides an ideal vehicle for this Court to overrule *Dewsnup*. The issue of lien avoidance is squarely presented as a pure legal issue, and there are no factual disputes. *Dewsnup* has proven to be disruptive, at odds with this Court's prior rulings in *Ron Pair* and its progeny and a detriment to the principles set forth in *Local Loan.* Its reversal is fully justified.

CONCLUSION

We respectfully urge this Court to grant the petition for writ of certiorari.

Respectfully submitted,

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