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NOTES

CAN A DEBTOR VOID A REAL PROPERTY LIEN THAT EXCEEDS THE VALUE OF THE COLLATERAL?: AN INTERPRETATION OF SECTION 506(d) OF THE BANKRUPTCY CODE

Congress enacted the Bankruptcy Reform Act of 1978 (Bankruptcy Code)¹ to provide for equitable distribution among creditors of a bankrupt debtor's assets and to provide the debtor with a fresh start.² When a debtor files a petition in bankruptcy³ the

1. Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified as amended at 11 U.S.C. §§ 101-1330 (1982)). The Bankruptcy Reform Act of 1978 (Bankruptcy Code) repealed and replaced the National Bankruptcy Act of 1898. Bankruptcy Act of 1898, ch. 541, 30 Stat. 544, *amended by* Act of June 22, 1938, ch. 575, 52 Stat. 840, *repealed by* Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified as amended at 11 U.S.C. §§ 101-1330 (1982)). *See generally* B. WEINTRAUB & A. RESNICK, *BANKRUPTCY LAW MANUAL XXVIII* (1986) (describing history of Bankruptcy Reform Act of 1978). Congress enacted the Bankruptcy Reform Act of 1978 to modernize the bankruptcy laws. S. REP. NO. 989, 95th Cong., 1st Sess., *reprinted in* 1978 U.S. CODE CONG. & ADMIN. NEWS 5757, 5788.

2. *See* REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. Doc. No. 137, 93d Cong., 1st Sess., pt. I, at 71 (1973) (stating that Congress enacted federal bankruptcy laws to provide debtors with fresh start and to protect interest of creditors); *see also* Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934) (stating that one of primary purposes of bankruptcy is to relieve honest debtor from oppressive indebtedness and thus permit debtor fresh start); Burlingham v. Crouse, 228 U.S. 459, 473 (1913) (stating that dual purpose of bankruptcy is, first, to convert debtor's bankruptcy estate into cash and distribute cash among creditors and, second, to give debtor fresh start). *See generally* B. WEINTRAUB & A. RESNICK, *supra* note 1, at 1-3, 1-4 (describing purposes of bankruptcy laws).

The discharge provision of Chapter Seven best exemplifies the fresh start policy of the Bankruptcy Code. *See* 11 U.S.C. § 727 (1982 & Supp. IV 1986) (providing debtor with discharge of all prebankruptcy debts); *see also* S. REP. No. 989, *supra* note 1, at 5793 (stating that discharge provision exemplifies Bankruptcy Code's fresh start policy). Although Congress intended to provide debtors with a discharge of debts and thus a fresh start, Congress also intended to provide creditors with an equitable distribution of the debtor's assets. *See* 11 U.S.C. § 704(1) (1982 & Supp. IV 1986) (providing that bankruptcy trustee shall collect and reduce to money property of bankruptcy estate); *id.* § 726 (dictating order in which trustee must distribute to creditors property of estate, which trustee has reduced to money under § 704 of Bankruptcy Code); *infra* note 5 (describing concept of property of estate under § 541 of Bankruptcy Code); *infra* note 3 (describing Chapter Seven proceeding in bankruptcy).

3. *See* 11 U.S.C. § 301 (1982) (providing that debtor's filing of petition with bankruptcy court commences voluntary case and order of relief). A voluntary petition in bankruptcy is a petition that the debtor files. *Id.* An involuntary petition in bankruptcy is a petition that one or more creditors file. *See id.* § 303(b) (providing that creditors who file petition under Chapter Seven or Chapter Eleven commence involuntary case in bankruptcy court).

The Bankruptcy Code contains four types of bankruptcy cases: liquidation under Chapter Seven, reorganization under Chapter Eleven, adjustment of a family farmer's debts under Chapter Twelve, and adjustment of an individual's debts under Chapter Thirteen. *See id.* §§

nonexempt⁴ property of the debtor becomes the bankruptcy estate.⁵ The debtor's real estate, often encumbered with several liens, typically becomes a part of the debtor's bankruptcy estate.⁶ Upon the debtor's filing of the bankruptcy petition, the Bankruptcy Code provides the debtor with an automatic stay⁷ that prevents lienholders from using property of the bank-

701-766, 1101-1174, 1201-1231, 1301-1330 (describing four types of bankruptcy proceedings under Bankruptcy Code). Commentators have divided the four specific types of bankruptcy into two general forms of bankruptcy: liquidation proceedings under Chapter Seven and rehabilitation proceedings under Chapters Eleven, Twelve, and Thirteen. D. EPSTEIN, J. LANDERS & S. NICKELS, *DEBTORS AND CREDITORS* 706 (3d ed. 4th printing 1987). Generally, in a liquidation proceeding, a trustee collects the debtor's nonexempt property, which is property that is eligible to become property of the bankruptcy estate, converts that property to cash, and distributes the cash to the creditors. 11 U.S.C. §§ 704, 726 (1982 & Supp. IV 1986). Chapter Seven provides that a debtor may receive a discharge of his debts. *Id.* § 727. Alternatively, in a rehabilitation proceeding the debtor usually retains his assets and attempts, with future earnings, to pay his creditors. *Id.* §§ 1306(b), 1322(a). Chapter Eleven of the Bankruptcy Code allows a financially distressed business enterprise to restructure its finances and continue to operate and pay creditors. 11 U.S.C. §§ 1101-1171 (1982); see S. REP. No. 989, *supra* note 1, at 5795 (providing that Congress intended for financially distressed businesses to reorganize and subsequently to pay debts). Although individuals are eligible for relief under Chapter Eleven, Congress designed Chapter Eleven primarily for businesses. S. Rep. No. 989, *supra* note 1, at 5795. Chapter Twelve of the Bankruptcy Code, which is another type of rehabilitative chapter, allows a farmer to restructure his debts and to pay creditors. 11 U.S.C. §§ 1201-1231 (1982). Like Chapter Twelve, Chapter Thirteen of the Bankruptcy Code enables individual debtors, under court protection and supervision, to apply a portion of the debtor's future earnings to pay creditors. *Id.* §§ 1301-1330; see S. REP. No. 989, *supra* note 1, at 5799 (providing that purpose of Chapter Thirteen is to permit individual, by making periodic payments to trustee, to pay debts and avoid bankruptcy).

4. See 11 U.S.C. § 522 (1982 & Supp. IV 1986) (providing that nonexempt property is property that debtor may retain and thus may prevent from becoming property of bankruptcy estate). In allowing the debtor to exempt certain property from the bankruptcy estate, Congress intended to provide a debtor with the basic necessities of life so that even if creditors take the debtor's nonexempt property, creditors will not leave the debtor destitute. H.R. REP. No. 595, 95th Cong., 1st Sess., *reprinted in* 1978 U.S. CODE CONG. & ADMIN. NEWS 5963, 6087.

5. 11 U.S.C. § 541 (1982 & Supp. IV 1986). A petitioner's commencement of a bankruptcy case creates a bankruptcy estate. *Id.* § 541(a). The bankruptcy estate includes all of the debtor's legal or equitable interests in property, as of the commencement of the bankruptcy case. *Id.* § 541(a)(1).

6. See *id.* § 541(a)(1) (providing that when debtor files petition in bankruptcy, debtor's legal or equitable interests in property become property of estate).

7. *Id.* § 362. A bankruptcy stay prohibits the commencement or continuation of any proceeding against the bankrupt. R. KRATOVIL & R. WERNER, *REAL ESTATE LAW* 394 (9th ed. 1988). When a party files a petition in bankruptcy, the automatic stay arises by operation of law. 11 U.S.C. § 362(a) (1982 & Supp. IV 1986). The automatic stay is a fundamental protection that the Bankruptcy Code provides to a debtor in bankruptcy. S. REP. No. 989, *supra* note 1, at 5840. The automatic stay stops all collection efforts, all harassment, and all foreclosure actions by creditors. *Id.*

Although the automatic stay provides debtors with immediate relief from creditors, the automatic stay also prevents one creditor from pursuing remedies against the debtor's assets to the detriment of other creditors. B. WEINTRAUB & A. RESNICK, *supra* note 1, at 1-31. The automatic stay, therefore, ensures that a bankruptcy court will distribute fairly and equally the debtor's assets among creditors. *Id.* Accordingly, Congress did not intend for the automatic

ruptcy estate to foreclose on their liens.⁸ To prevent lienholders from recovering on claims to the extent that the claims exceed the fair market value of the property of the bankruptcy estate, debtors recently have attempted to use section 506(d) of the Bankruptcy Code to void liens to the extent that the liens exceed the fair market value of the debtor's real property.⁹ Section 506(d) of the Bankruptcy Code provides that a creditor's lien which is not an allowed secured claim¹⁰ is void.¹¹ Under the Bankruptcy

stay to alter the substantive rights of creditors. *Id.* Congress intended merely that the automatic stay stop creditors' collection efforts pending a bankruptcy court's determination of the creditors' and debtors' rights. *Id.*

The automatic stay terminates automatically when the debtor's property is no longer property of the bankruptcy estate. 11 U.S.C. § 362(c)(1) (1982); *see supra* note 5 (description of property of estate). Property ceases to be property of the bankruptcy estate upon a trustee's sale or abandonment of the property or upon a bankruptcy court's exempting the property from the bankruptcy estate. B. WEINTRAUB & A. RESNICK, *supra* note 1, at 1-44. The automatic stay also terminates when the bankruptcy court closes the case, dismisses the case, or denies or grants a discharge to the debtor. 11 U.S.C. § 362(c)(2)(A)-(C) (1982 & Supp. IV 1986); *see supra* note 2 (discussing discharge). Although the automatic stay may terminate automatically, a bankruptcy judge, upon a motion of any interested party who seeks relief from the stay, may terminate, annul, modify, or condition the stay with cause. 11 U.S.C. §§ 362(d), (d)(1), (d)(2)(A) (1982 & Supp. IV 1986).

8. 11 U.S.C. § 362 (1982 & Supp. IV 1986); *see supra* note 7 (discussing automatic stay).

9. *See* *Worrell v. Federal Land Bank of St. Louis*, 67 Bankr. 16, 17 (Bankr. C.D. Ill. 1986) (Chapter Seven debtor attempted to void under § 506(d) portion of real estate mortgage lien to extent that lien exceeded fair market value of property); *Maitland v. Central Fidelity Bank (In re Maitland)*, 61 Bankr. 130, 131 (Bankr. E.D. Va. 1986) (Chapter Seven debtors sought to use § 506(d) to void liens against real property to extent that liens exceeded value of property); *Lindsey v. Federal Land Bank of St. Louis (In re Lindsey)*, 64 Bankr. 19, 21 (Bankr. C.D. Ill. 1986) (Chapter Seven debtor attempted to void under § 506(d) real property mortgage to extent that mortgage exceeded value of property); *In re Sloan*, 56 Bankr. 726, 726 (Bankr. D. Colo. 1986) (Chapter Seven debtor sought to use § 506(d) to void creditor's lien on residence of debtor); *Lyons v. First Pa. Bank (In re Lyons)*, 46 Bankr. 604, 605 (Bankr. N.D. Ill. E.D. 1985) (Chapter Seven debtors attempted to use § 506(d) to void mortgage on principal residence to extent that amount of mortgage exceeded value of residence); *Cordes v. Geico Fin. Serv., Inc. (In re Cordes)*, 37 Bankr. 582, 584 (Bankr. C.D. Cal. 1984) (Chapter Seven debtors attempted to void under § 506(d) lien on residence to extent that lien exceeded amount of creditor's secured claim); *In re Mahaner*, 34 Bankr. 308, 310 (Bankr. W.D.N.Y. 1983) (Chapter Seven debtors attempted to void under § 506(d) real property lien that exceeded value of collateral); *Brace v. State Farm Mutual Auto. Ins. Co.*, 33 Bankr. 91, 92 (Bankr. S.D. Ohio, W.D. 1983) (Chapter Seven debtors argued that because first mortgage exceeded fair market value of debtors' real estate, debtors could void under § 506(d) second mortgage that was totally unsecured claim); *Tanner v. FinanceAmerica Consumer Discount Co. (In re Tanner)*, 14 Bankr. 933, 935 (Bankr. W.D. Pa. 1981) (Chapter Seven debtor attempted to void real property lien under § 506(d) to extent that lien exceeded value of collateral); *Walker v. First Fed. Sav. & Loan (In re Walker)*, 11 Bankr. 43 (Bankr. N.D. Ill., E.D. 1981) (Chapter Thirteen debtors attempted to void under § 506(d) remainder of second real property mortgage that was unsecured claim).

10. *See infra* note 11 (definition of secured claim).

11. 11 U.S.C. § 506(d) (1982 & Supp. IV 1986). Section 506(a) of the Bankruptcy Code provides, in pertinent part:

a) An allowed claim of a creditor secured by a lien on property in which the estate

Code, a creditor has an allowed secured claim to the extent of the value of the property serving as collateral.¹² A creditor has an unsecured claim,

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.

Id. § 506(a). Additionally, section 506(a) provides that in determining the value of the creditor's interest in the estate's interest in the property, a bankruptcy court should consider the purpose of the valuation and the proposed use of the property. *Id.* Section 506(d) of the Bankruptcy Code provides that "to the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void. . ." *Id.* § 506(d).

12. *Id.* § 506(a); see S. REP. NO. 989, *supra* note 1, at 5854 (providing that creditor has secured claim to extent of value of his collateral); *supra* note 11 (providing statutory language of § 506(a)).

The Bankruptcy Code defines the term "claim" as a right to payment. 11 U.S.C. § 101(4) (1982 & Supp. IV 1986); see S. REP. NO. 989, *supra* note 1, at 5807-08 (explaining that Congress broadly defined term "claim" to enable bankruptcy courts to deal with all of debtor's legal obligations, regardless of remoteness of obligation). Accordingly, a creditor under the Bankruptcy Code is a holder of a claim against the debtor. 11 U.S.C. § 101(9) (1982 & Supp. IV 1986). The Bankruptcy Code allows a creditor to file with the bankruptcy court proof of his claim. *Id.* § 501(a). Although the Bankruptcy Code does not mandate that a creditor file proof of his claim, a creditor should file proof of his claim when filing would serve some purpose. See S. REP. NO. 989, *supra* note 1, at 5847 (providing that creditor should file proof of claim, for example, when creditor has lien that is undersecured and creditor asserts claim for balance of debt); see also 11 U.S.C. § 506(d)(2) (1982 & Supp. IV 1986) (providing that to maintain his lien, creditor with secured claim does not need to file proof of claim). If a creditor files proof of his claim, the Bankruptcy Code provides that unless a party in interest objects, the claim automatically is an allowed claim. 11 U.S.C. § 502(a) (1982 & Supp. IV 1986); see S. REP. NO. 989, *supra* note 1, at 5848 (providing that proof of claim is prima facie evidence of claim, which is allowed claim unless party in interest objects to claim). If a party in interest objects to a claim, the bankruptcy court must determine after notice and hearing the validity and amount of the claim. 11 U.S.C. § 502(b) (1982 & Supp. IV 1986); see *id.* § 502(b)(1)-(8) (listing grounds for disallowance of claim in whole or in part).

Although section 502 of the Bankruptcy Code governs the allowance of creditors' claims, section 506(a) governs the secured status of creditors' claims. Compare *id.* § 502 (listing circumstances under which bankruptcy court may allow or disallow creditor's claim); with *id.* § 506(a) (defining secured claim). Section 506(a) of the Bankruptcy Code provides that a creditor has a secured claim to the extent of the value of his collateral and the creditor has an unsecured claim for the balance of his claim. *Id.* § 506(a); see H.R. REP. NO. 595, *supra* note 4, at 6141 (stating that creditor's claim is secured claim to extent of value of property serving as collateral and creditor's claim is unsecured to extent of balance of creditor's claim).

The legislative history to section 506(a) of the Bankruptcy Code reveals that Congress divided claims into secured and unsecured claims to protect the interests of both debtors and creditors. 11 U.S.C. § 506(a) (1982); see H.R. REP. NO. 595, *supra* note 4, at 6141 (stating that Congress divided claims into secured and unsecured claims to protect both debtors' and creditors' interests). Section 506(a) protects the creditor's interest because once the court determines that the creditor has a secured claim, the court must protect the collateral. 11 U.S.C. § 506(a) (1982); see H.R. REP. NO. 595, *supra* note 4, at 6141 (stating that if bankruptcy court determines that creditor has secured claim, bankruptcy court must not allow bankruptcy estate to destroy collateral). Section 506(a) protects the debtor's interest because, by determining the amount of the secured claim, a court facilitates reorganization in the business context and repayment plans in the consumer context. 11 U.S.C. § 506(a) (1982); see H.R. REP. NO. 595, *supra* note 4, at 6141 (stating that § 506(a) allows bankruptcy court to facilitate business reorganization and thus protect debtor's interest).

however, to the extent that the allowed claim exceeds the value of the property serving as collateral.¹³ In responding to debtors' attempts in a bankruptcy proceeding to void liens under section 506(d) of the Bankruptcy Code, bankruptcy courts inconsistently have determined whether a debtor may void a creditor's real property lien to the extent that the lien exceeds the value of the collateral.¹⁴

Although debtors recently have attempted to retain property of the bankruptcy estate by voiding liens to the extent that the liens exceed the fair market value of the property,¹⁵ under state law debtors who wish to

13. See 11 U.S.C. § 506(a) (1982) (providing that creditor has unsecured claim to extent that value of creditor's interest in estate's interest in property is less than amount of allowed claim).

14. See *Worrell v. Federal Land Bank of St. Louis*, 67 Bankr. 16, 20 (Bankr. C.D. Ill. 1986) (holding that § 506(d) permits Chapter Seven debtor to void portion of real estate mortgage lien to extent that lien exceeded fair market value of real estate); *Lindsey v. Federal Land Bank of St. Louis (In re Lindsey)*, 64 Bankr. 19, 24 (Bankr. C.D. Ill. 1986) (holding that § 506(d) allows Chapter Seven debtor to void real property mortgage to extent that mortgage exceeds value of property); *Lyons v. First Pa. Bank (In re Lyons)* 46 Bankr. 604, 607 (Bankr. N.D. Ill. E.D. 1985) (holding that Chapter Seven debtors could use § 506(d) to void mortgage on principal residence to extent that amount of mortgage exceeds value of residence); *Brace v. State Farm Mutual Auto. Ins. Co.*, 33 Bankr. 91, 95 (Bankr. S.D. Ohio, W.D. 1983) (holding that because amount of debtors' first mortgage exceeded fair market value of debtors' real estate, debtors could void under § 506(d) second mortgage that was totally unsecured claim); *Tanner v. FinanceAmerica Consumer Discount Co. (In re Tanner)*, 14 Bankr. 933, 939 (Bankr. W.D. Pa. 1981) (holding that debtor may void real property lien pursuant to § 506(d) to extent that lien exceeded value of collateral); *Walker v. First Fed. Sav. & Loan (In re Walker)*, 11 Bankr. 43, 44 (Bankr. N.D. Ill. E.D. 1981) (holding that second mortgagee had secured lien on debtors' realty to extent that value of realty exceeded first mortgage, and accordingly, Chapter Thirteen debtors could void under § 506(d) remainder of second mortgage that was unsecured claim). *But see Maitland v. Central Fidelity Bank (In re Maitland)*, 61 Bankr. 130, 135 (Bankr. E.D. Va. 1986) (holding that Chapter Seven debtors may not use § 506(d) to void liens against real property to extent that liens exceed value of property); *In re Sloan*, 56 Bankr. 726, 726 (Bankr. D. Colo. 1986) (holding that Chapter Seven debtor may not use § 506(d) to void creditor's lien on residence of debtor); *Cordes v. Geico Fin. Serv., Inc. (In re Cordes)* 37 Bankr. 582, 584 (Bankr. C.D. Cal. 1984) (holding that Chapter Seven debtors could not void under § 506(d) lien on residence to extent that lien exceeded amount of creditor's secured claim); *In re Mahaner*, 34 Bankr. 308, 310 (Bankr. W.D.N.Y. 1983) (holding that § 506(d) of Bankruptcy Code does not authorize Chapter Seven debtors to void real property lien that exceeded value of collateral).

15. See *Worrell v. Federal Land Bank of St. Louis*, 67 Bankr. 16, 17 (Bankr. C.D. Ill. 1986) (debtors requested that bankruptcy court determine maturity and amount of payment on secured portion of creditors' claim after bankruptcy court had voided unsecured portion of creditors' claim); *Lindsey v. Federal Land Bank of St. Louis*, 64 Bankr. 19, 20 (Bankr. C.D. Ill. 1986) (debtors petitioned court to value real estate and to determine how, when, and what amount debtors must pay creditors to retain title to property free of creditors' liens); *Cordes v. Geico Financial Services, Inc.*, 37 Bankr. 582, 583 (Bankr. C.D. Cal. 1984) (debtors sought to have bankruptcy court declare creditor's claim unsecured in amount that claim exceeded value of property, have creditor reduce debt to value of property, and pay off secured claim); *In re Mahaner*, 34 Bankr. 308, 309 (Bankr. W.D.N.Y. 1983) (noting that debtors wanted bankruptcy court to determine value of debtors' encumbered property and void liens to extent that liens exceeded value of property so that debtors could pay senior lienholder value of lien and thus redeem property).

retain property encumbered with senior and junior mortgages generally must pay the lienholders the amount outstanding on both the senior and junior mortgages.¹⁶ Under state law if a debtor with senior and junior mortgages on his real estate defaults on the mortgage payments, the senior lienholder¹⁷ typically has two options to protect his interest in the debtor's property.¹⁸ First, the senior lienholder can foreclose on the debtor's real estate.¹⁹ If the senior lienholder forecloses and sells the debtor's property to satisfy the debt, the senior lienholder may recover from the sale proceeds the amount of the outstanding debt on the senior lien.²⁰ If the property at the foreclosure sale sells for a price exceeding the value of the senior lien, the junior lienholder recovers the excess amount to the extent of the value of his lien.²¹

In addition to foreclosing on his lien, a senior lienholder may protect his interest in the debtor's property, second, by bidding in at the foreclosure sale.²² Senior lienholders bid in at foreclosure sales primarily when the senior lienholder believes that the property is worth more than the highest bid at the foreclosure sale.²³ By bidding in at the sale, the senior lienholder offers to relinquish his lien in exchange for the property.²⁴ After buying the property at the foreclosure sale, the senior lienholder subsequently may sell the property at a profit to satisfy his interest.²⁵ If a junior lienholder, similarly, anticipates that the proceeds of the foreclosure sale will not satisfy both the senior and junior liens encumbering the property, the junior

16. See *In re Carter*, 56 F. Supp. 385, 388 (W.D. Va. 1944) (providing that lienholder has right under state law to have property serve as collateral and to take property if debtor defaults on mortgage payments); R. KRAVOTIL & R. WERNER, *supra* note 7, at 389 (stating that before foreclosure sale, mortgagor may pay off mortgage and redeem property).

17. See R. KRAVOTIL & R. WERNER, *supra* note 7, at 372 (explaining that senior mortgage is first mortgage on property).

18. See *infra* notes 19-25 and accompanying text (describing senior lienholder's options under state law upon debtor's default on mortgage payments).

19. See G. NELSON & D. WHITMAN, *REAL ESTATE FINANCE LAW* § 7.6 (2d ed. 1985) (discussing lienholder's right to foreclose upon mortgagor's default on mortgage payments).

20. *Id.* at §§ 7.6, 7.14.

21. *Id.* at § 7.31.

22. R. KRAVOTIL & R. WERNER, *supra* note 7, at 395; see *In re Carter*, 56 F. Supp. 385, 388 (W.D. Va. 1944) (providing that to protect interests during foreclosure sale of mortgaged property, creditor may bid at foreclosure sale and may apply amount of debt to bid).

23. G. NELSON & D. WHITMAN, *supra* note 19, at §§ 7.16, 7.17.

24. See R. KRAVOTIL & R. WERNER, *supra* note 7, at 390 (noting that courts regard mortgage foreclosure sale as payment of mortgage debt in amount equal to sale price). The mortgagee typically is the only bidder at the foreclosure sale. *Id.* at 395. The court allows the mortgagee, by bidding up to the amount of the mortgage debt and by not producing any payment, to buy the property. *Id.* The court does not expect the mortgagee to pay for property when the mortgagee's bid equals the mortgage debt, because the court would have to pay, from the foreclosure sale proceeds, the mortgagee for the mortgage debt. *Id.* If any remaining debt exists on the mortgage after the court sells the property at the foreclosure sale, the mortgagee with the unsatisfied debt may seek a deficiency judgment for the remainder of the debt. *Id.* at 390.

25. See generally G. NELSON & D. WHITMAN, *supra* note 19, at § 7.17 (explaining that after foreclosure sale, purchaser has title to property).

lienholder may bid in at the foreclosure sale.²⁶ By bidding in at the foreclosure sale and buying the property, the junior lienholder attempts to reduce his losses because the junior lienholder can pay off the senior lienholder and subsequently sell the property at a price exceeding the purchase price.²⁷ Thus, under state law both senior and junior lienholders have the right to retain their liens to satisfy the debts.²⁸ Consequently, a debtor at state law may not void liens to the extent that the liens exceed the value of the property, subsequently pay off the senior lien, and thus retain the property.²⁹ Instead, under state law a debtor who wishes to retain his property must pay all of the lienholders the value of their liens.³⁰

Although a debtor under state law may not void liens to the extent that the liens exceed the value of the collateral, some bankruptcy courts have allowed debtors to void liens to the extent that the liens exceed the value of the debtor's property.³¹ In *Tanner v. FinanceAmerica Consumer Discount Co.*³² the United States Bankruptcy Court for the Western District of Pennsylvania held that a debtor may void pursuant to section 506(d) of the Bankruptcy Code a real property mortgage to the extent that the mortgage exceeds the value of the collateral.³³ In *Tanner* a debtor, Tanner, filed a

26. *Id.*

27. *Id.*; See R. KRAVOTIL & R. WERNER, *supra* note 7, at 372 (providing that because foreclosure of senior lien extinguishes junior lien, junior lienholder can prevent extinguishment of junior lien by paying off senior lien).

28. See *supra* notes 16-27 and accompanying text (describing senior and junior lienholders' rights under state law to maintain lien to satisfy debt).

29. See generally R. KRAVOTIL & R. WERNER, *supra* note 7, at 389-96 (discussing mortgagee's right to foreclose on debtor's property after debtor defaults on mortgage payments).

30. *Id.*

31. See *Worrell v. Federal Land Bank of St. Louis*, 67 Bankr. 16, 20 (Bankr. C.D. Ill. 1986) (holding that § 506(d) permits Chapter Seven debtor to void portion of real estate mortgage lien to extent that lien exceeded fair market value of real estate); *Lindsey v. Federal Land Bank of St. Louis (In re Lindsey)*, 64 Bankr. 19, 24 (Bankr. C.D. Ill. 1986) (holding that § 506(d) allows Chapter Seven debtor to void real property mortgage to extent that mortgage exceeds value of property); *Lyons v. First Pa. Bank (In re Lyons)* 46 Bankr. 604, 607 (Bankr. N.D. Ill. E.D. 1985) (holding that Chapter Seven debtors could use § 506(d) to void mortgage on principal residence to extent that amount of mortgage exceeds value of residence); *Brace v. State Farm Mutual Auto. Ins. Co.*, 33 Bankr. 91, 95 (Bankr. S.D. Ohio, W.D. 1983) (holding that because amount of debtors' first mortgage exceeded fair market value of debtors' real estate, debtors could void under § 506(d) second mortgage that was totally unsecured claim); *Tanner v. FinanceAmerica Consumer Discount Co. (In re Tanner)*, 14 Bankr. 933, 939 (Bankr. W.D. Pa. 1981) (holding that debtor may void real property lien pursuant to § 506(d) to extent that lien exceeded value of collateral); *Walker v. First Fed. Sav. & Loan (In re Walker)*, 11 Bankr. 43, 44 (Bankr. N.D. Ill., E.D. 1981) (holding that second mortgagee had secured lien on debtors' realty to extent that value of realty exceeded first mortgage, and accordingly, Chapter Thirteen debtors could void under § 506(d) remainder of second mortgage that was unsecured claim).

32. 14 Bankr. 933 (Bankr. W.D. Pa. 1981).

33. *Tanner v. FinanceAmerica Consumer Discount Co.*, 14 Bankr. 933, 937 (Bankr. W.D. Pa. 1981).

voluntary petition in bankruptcy under Chapter Seven³⁴ of the Bankruptcy Code.³⁵ Tanner's home had a fair market value of twenty thousand dollars, but three mortgages encumbered the home.³⁶ The defendant, Finance-America, owned the junior mortgage on Tanner's home.³⁷ The balances on the senior mortgages totaled \$23,980 and thus exceeded the fair market value of the debtor's home.³⁸ The debtor petitioned the court to declare the third mortgage unsecured under section 506(a) of the Bankruptcy Code and, consequently, void pursuant to section 506(d).³⁹ The junior lienholder, however, contended that the Bankruptcy Code explicitly does not authorize the debtor to void the defendant's mortgage lien.⁴⁰

Disagreeing with the junior lienholder, the *Tanner* court held that section 506(d) authorized the debtor to void the real property mortgage to the extent that the mortgage exceeded the value of the collateral.⁴¹ The *Tanner* court advanced four justifications for allowing a debtor to void a lien to the extent that the lien exceeded the value of the collateral.⁴² The bankruptcy court considered, first, the language of section 506(d) of the Bankruptcy Code.⁴³ In examining the language of section 506(d), the *Tanner* court noted that Congress broadly defined the term "lien" in section 101(33) of the Bankruptcy Code as an interest in property to secure payment of a debt.⁴⁴ The *Tanner* court reasoned that Congress would not define the term "lien" broadly in section 101(33) but narrowly construe the term "lien" in section 506(d) of the Bankruptcy Code to exclude real property mortgages.⁴⁵ The *Tanner* court concluded, therefore, that the term "lien" in section 506(d)

34. 11 U.S.C. §§ 701-766 (1982); *see supra* note 3 (explaining liquidation proceeding under Chapter Seven of Bankruptcy Code).

35. *Tanner*, 14 Bankr. at 934.

36. *Id.* at 935. In *Tanner* the debtor alleged that her home had a fair market value of \$20,000. *Id.* at 934. After hearing evidence relating to the value of the debtor's home, the *Tanner* court found that the debtor's home had a fair market value of \$20,000. *Id.* at 935.

37. *Id.*

38. *Id.*

39. *Id.*

40. *Id.*

41. *Id.* at 939.

42. *Id.* at 935-39; *see infra* notes 43-65 and accompanying text (listing *Tanner* court's justifications for allowing debtor to void real property mortgage that exceeded value of property serving as collateral).

43. *Tanner*, 14 Bankr. at 935; *see supra* note 11 (language of § 506(d)).

44. *Tanner*, 14 Bankr. at 935; 11 U.S.C. § 101(33) (1982 & Supp. IV 1986); *see* S. REP. NO. 989, *supra* note 1, at 5811 (providing that Congress broadly defined term "lien" as charge against or interest in property to secure payment of debt or performance of obligation). The Bankruptcy Code identifies three types of liens. 11 U.S.C. §§ 101(32), (45), (47) (1982 & Supp. IV 1986). First, a debtor and creditor may create a lien by agreement. *Id.* § 101(45). Liens created by agreement, which the Bankruptcy Code labels security agreements, include real property mortgages. *Id.* § 101(45); S. REP. NO. 989, *supra* note 1, at 5812. Second, a judicial lien is a lien that a creditor obtains by judgment, levy, sequestration, or other legal or equitable proceeding. 11 U.S.C. § 101(32) (1982 & Supp. IV 1986). Third, a statutory lien is a lien that arises solely by force of statute on the occurrence of specified circumstances. *Id.* § 101(47).

45. *Tanner*, 14 Bankr. at 935.

of the Bankruptcy Code included real property mortgages.⁴⁶ The *Tanner* court noted, additionally, that when Congress desired to provide special treatment for a real property mortgage, Congress clearly indicated its intent.⁴⁷

After considering the plain meaning of the language in section 506(d), the *Tanner* court examined, second, whether by interpreting the term “lien” in section 506(d) to include real property mortgages, courts consistently would promote the overall purpose of the Bankruptcy Code.⁴⁸ The *Tanner* court reasoned, specifically, that by allowing a debtor to void a real property mortgage to the extent that the mortgage exceeds the value of the collateral, the court would promote the fresh start policy of the Bankruptcy Code.⁴⁹ The *Tanner* court recognized that a fresh start grants a debtor a discharge from debts and provides the debtor with a new financial start.⁵⁰ The *Tanner* court stated that a new financial start should permit the property that a debtor acquires after filing for bankruptcy not to be subject to claims of prebankruptcy creditors.⁵¹ The *Tanner* court reasoned, accordingly, that by partaking in the profits of the debtor’s postbankruptcy property acquisitions, a prebankruptcy creditor maintaining a mortgage that is an undersecured claim will impair the debtor’s fresh start.⁵²

In addition to reasoning that a broad interpretation of the term “lien” would promote the fresh start policy of the Bankruptcy Code, the *Tanner* court reasoned, third, that section 506(d) of the Bankruptcy Code allows a creditor to receive in bankruptcy the same property value that the creditor would receive under state law.⁵³ The *Tanner* court reasoned, specifically, that under section 506 of the Bankruptcy Code, creditors should receive through the valuation procedure in bankruptcy the same property value that the creditors would receive under state law in a forced sale of the debtor’s nonexempt property.⁵⁴ The bankruptcy court recognized that under state law the senior lienholder typically would foreclose on the debtor’s property, receive less than fair market value of the property at the forced sale, and leave the junior lienholder with an unsatisfied claim.⁵⁵ The *Tanner* court

46. *Id.* at 936.

47. *Id.* To illustrate congressional intent to provide special treatment for real property security interests, the *Tanner* court cited section 1322(b)(2), which permits a debtor in a Chapter Thirteen plan to modify the rights of the holders of secured and unsecured claims, except claims secured by real property mortgages. *Id.* at 935; 11 U.S.C. § 1322(b)(2) (1982 & Supp. IV 1986).

48. *Tanner*, 14 Bankr. at 936.

49. *Id.*; see *supra* note 2 and accompanying text (discussing fresh start policy of Bankruptcy Code).

50. *Tanner*, 14 Bankr. at 936.

51. *Id.* The *Tanner* court characterized both appreciation of property and an increase of equity ownership by the reduction of an outstanding mortgage as examples of property that a debtor acquires after bankruptcy. *Id.*

52. *Id.*

53. *Id.* at 936-37.

54. *Id.* at 937.

55. *Id.*

recognized, further, that the purchaser of the debtor's property at the foreclosure sale would receive the property unencumbered.⁵⁶ The *Tanner* court reasoned, therefore, that in failing to void a lien that exceeds the value of the collateral, the court would benefit the lienholder more in a bankruptcy proceeding than in a state law foreclosure sale.⁵⁷ The *Tanner* court concluded, accordingly, that by allowing a lienholder a greater benefit in a bankruptcy proceeding than under state law, the court would frustrate Congress' intent to provide debtors with relief under the Bankruptcy Code.⁵⁸

The *Tanner* court addressed, finally, the constitutionality of section 506(d) of the Bankruptcy Code.⁵⁹ The *Tanner* court initially found that section 506(d) of the Bankruptcy Code does not authorize a court to unconstitutionally abridge a lienholder's due process rights under the fifth amendment of the United States Constitution.⁶⁰ In finding that a court by voiding liens, does not unconstitutionally abridge a lienholder's due process rights, the *Tanner* court noted that the lienholder's completely unsecured⁶¹ claim is an "empty legal right," rather than a valuable property right.⁶² The *Tanner* court reasoned, therefore, that in voiding a mortgage that exceeds the value of the collateral, the court would not unconstitutionally deprive a lienholder of property.⁶³ The bankruptcy court reasoned, further, that at a state law foreclosure sale a completely unsecured mortgagee would lose his lien.⁶⁴ The *Tanner* court concluded, accordingly, that because the court was permitting the result that would occur under state law, section 506(d) of the Bankruptcy Code constitutionally allows a bankruptcy court to void liens that exceed the value of the collateral.⁶⁵

56. *Id.*

57. *Id.*

58. *Id.* In addition to interpreting the statutory language and examining the legislative history of section 506(d) of the Bankruptcy Code, the *Tanner* court used case precedent to support its ruling that section 506(d) applies to real property mortgages. *See id.* at 937-38 (examining case law interpretation of § 506(d)); *see also* *Geiger v. Geiger*, 12 Bankr. 410, 411 (Bankr. E.D. Wis. 1981) (holding that § 506(d) authorizes debtor to void real property mortgages); *Pitre v. First Federal Savings & Loan Ass'n*, 11 Bankr. 777, 781 (Bankr. E.D.N.D. Ill. 1981) (stating that Congress intended § 506(d) to prevent creditor with lien exceeding value of collateral from realizing future benefits as result of property appreciating in value or as result of debtor making payments on senior claims secured by same property); *Walker v. First Fed. Sav. & Loan*, 11 Bankr. 43, 44 (Bankr. N.D. Ill. E.D. 1981) (voiding, under § 506(d) second mortgage to extent that second mortgage exceeded value of collateral); *In re Hotel Associates*, 3 Bankr. 340, 342 (Bankr. E.D. Pa. 1980) (noting that if court disallows claim, then lien is void under § 506(d) to extent that court disallows claim).

59. *Tanner*, 14 Bankr. at 938-39.

60. *Id.*; U.S. CONST. amend. V.

61. *See* 11 U.S.C. § 506(a) (1982) (providing that creditor has secured claim to extent of value of collateral and unsecured claim for balance of claim). A completely unsecured claim is a claim that totally exceeds the value of the collateral. *Id.*

62. *Tanner*, 14 Bankr. at 938.

63. *Id.*

64. *Id.*

65. *Id.*

Although the *Tanner* court permitted a debtor to use section 506(d) of the Bankruptcy Code to void a real property lien to the extent that the lien exceeds the value of the collateral, some bankruptcy courts have not permitted a debtor to use section 506(d) to void liens to the extent that the liens exceed the value of the collateral.⁶⁶ For example, in *In re Mahaner*⁶⁷ debtors owned real estate having a fair market value of \$87,500.⁶⁸ Lincoln Trust Bank, however, held a first mortgage on the property for \$41,646.82.⁶⁹ Additionally, Marine Bank (Marine) owned second and third mortgages totalling eighty thousand dollars.⁷⁰ After the debtors filed a Chapter Seven petition, the United States Bankruptcy Court for the Western District of New York granted the debtors a stay under section 362 of the Bankruptcy Code, which prevented the creditors from collecting their claims or from enforcing their liens.⁷¹ To redeem the debtors' property to the extent of Marine's lien, the debtors sought a continuation of the stay so that the court could determine, first, whether the real estate was secured property under section 506(a) and, second, whether Marine had a secured claim on the real estate to the extent of their lien.⁷²

The *Mahaner* court held that the debtors could not use section 506(d) of the Bankruptcy Code to void a real property lien to the extent that the lien exceeds the value of the collateral.⁷³ In holding that the debtor may not use section 506(d) to void a real property lien, the *Mahaner* court reasoned, first, that by allowing a debtor to void a real property lien under section 506(d), the court would render meaningless section 722 of the Bankruptcy Code.⁷⁴ The *Mahaner* court explained that section 722 of the Bankruptcy Code authorizes a debtor to pay a lienholder the value of the encumbered property and thus redeem personal property from a lien.⁷⁵ The bankruptcy court noted, however, that under section 722 a debtor may redeem only personal property, not real property.⁷⁶ The *Mahaner* court

66. See *supra* note 14 (listing courts that allow and disallow debtors' use of § 506(d) to void real property lien that exceeds value of collateral).

67. 34 Bankr. 308 (Bankr. W.D.N.Y. 1983).

68. *In re Mahaner*, 34 Bankr. 308, 308 (Bankr. W.D.N.Y. 1983).

69. *Id.* at 309.

70. *Id.*

71. See *id.* (stating that debtors sought continuation of automatic stay); 11 U.S.C. § 362 (1982 & Supp. IV 1986) (automatic stay provision); *supra* note 7 (describing automatic stay).

72. *Mahaner*, 34 Bankr. at 309; see 11 U.S.C. § 722 (1982) (redemption provision). Section 722 of the Bankruptcy Code allows a debtor to pay lienholders the amount of the allowed claim and thus redeem tangible personal property intended primarily for personal, family, or household use. 11 U.S.C. § 722 (1982); see S. REP. No. 989, *supra* note 1, at 6088 (stating that § 722 allows debtor to retain necessary property and to avoid high replacement costs).

73. *Mahaner*, 34 Bankr. at 309.

74. *Id.*

75. *Id.*; 11 U.S.C. § 722 (1982); see *supra* note 72 (explaining § 722 redemption provision of Bankruptcy Code).

76. *Mahaner*, 34 Bankr. at 309; see 11 U.S.C. § 722 (1982) (providing that debtor may redeem tangible personal property intended primarily for personal, family, or household use).

reasoned, accordingly, that by allowing a Chapter Seven debtor to redeem under section 506(d) real property that the debtor could not redeem under section 722, a court would render section 722 of the Bankruptcy Code meaningless.⁷⁷

After reasoning that a bankruptcy court should not allow a debtor to use section 506(d) to redeem real property in a liquidation proceeding, the *Mahaner* court reasoned, second, that by allowing a debtor to obtain in the liquidation⁷⁸ proceeding more property than a debtor could obtain in the rehabilitative⁷⁹ proceedings, the court would promote an unsound policy of discouraging debtors from using the rehabilitative chapters of the Bankruptcy Code.⁸⁰ The *Mahaner* court recognized that although Congress intended for debtors to use the rehabilitative chapters of the Bankruptcy Code to repay unsecured creditors, the liquidation chapter of the Bankruptcy Code provides unsecured creditors with little or no satisfaction of their claims.⁸¹ The *Mahaner* court found, also, that the legislative history of the Bankruptcy Code strongly encourages repayment plans, rather than liquidation procedures.⁸² The *Mahaner* court reasoned, accordingly, that Congress likely would not intend a debtor in a liquidation proceeding to use section 506(d) to void liens that a debtor in a rehabilitative proceeding could not void.⁸³ The *Mahaner* court noted that instead of allowing a debtor to use section 506(d) to void liens, Congress intended a trustee administering the debtor's bankruptcy estate to use section 506(d) to sell the collateral and to extinguish the entire lien even though the sale fully would not satisfy the debt.⁸⁴

After reasoning that Congress likely would not intend debtors in a liquidation proceeding to use section 506(d) to void liens that a debtor could not void in a rehabilitative proceeding, the *Mahaner* court reasoned, finally, that an interpretation of section 506(d) that allows courts to void liens in excess of the value of the collateral constitutes an unconstitutional taking of property without adequate compensation to the creditors.⁸⁵ Initially, the *Mahaner* court defined the term "mortgage" as a property interest.⁸⁶ The

77. *Mahaner*, 34 Bankr. at 309. The *Mahaner* court stated that in recognizing section 722 as the exclusive Chapter Seven redemption provision, the court would not render section 506 meaningless because section 506 applies to the rehabilitative chapters regarding the treatment of secured claims. *Id.* The bankruptcy court noted, further, that section 506 applies to both the liquidation and rehabilitative chapters when a trustee sells the property. *Id.*; see *supra* note 3 (describing liquidation and rehabilitative chapters of Bankruptcy Code).

78. See *supra* note 3 (describing liquidation chapter of Bankruptcy Code).

79. *Mahaner*, 34 Bankr. at 309.

80. *Id.*

81. *Id.* See generally S. REP. NO. 989, *supra* note 1, at 5878-925 (legislative history of liquidation chapter and rehabilitative chapters of Bankruptcy Code).

82. *Mahaner*, 34 Bankr. at 309. See generally S. REP. NO. 989, *supra* note 1, at 5878-929 (legislative history of liquidation chapter and rehabilitative chapters of Bankruptcy Code).

83. *Mahaner*, 34 Bankr. at 309.

84. *Id.*

85. *Id.* at 310.

86. *Id.*

Mahaner court noted that a mortgagee has a right under state law to realize upon the collateral, which is the property that the debtor uses to secure the mortgage.⁸⁷ The bankruptcy court noted that a mortgagee often recognizes that his mortgage may be more valuable than the market value of the collateral at a given time.⁸⁸ The *Mahaner* court reasoned, therefore, that a mortgagee anticipating that the defaulting mortgagor's property may appreciate in value may choose not to foreclose immediately.⁸⁹ The *Mahaner* court concluded that by voiding a real property lien that exceeds the value of the collateral, a court deprives the mortgagee of the right to foreclose on property that may appreciate in value.⁹⁰ The *Mahaner* court reasoned, thus, that a mortgagee who forecloses on collateral before the debtor-mortgagor files a petition in bankruptcy may purchase the property at the foreclosure sale and, consequently, benefit from the appreciated property.⁹¹ The *Mahaner* court concluded, accordingly, that by voiding a lien that exceeds the value of the collateral, a court unconstitutionally deprives the mortgagee of the right to maintain the mortgage to enjoy the benefits of appreciated property.⁹² The *Mahaner* court, consequently, granted Marine's motion to lift the stay to allow Marine to begin foreclosure proceedings under state law.⁹³

In determining whether section 506(d) allows a debtor to void a real property lien that exceeds the value of the collateral, the *Tanner* reasoning is unsatisfactory for four reasons.⁹⁴ First, in its statutory interpretation of section 506(d), the *Tanner* rationale places too much emphasis on the term "lien," rather than on the term "void."⁹⁵ Second, the *Tanner* reasoning fails to examine thoroughly the legislative history of section 506(d) of the Bankruptcy Code.⁹⁶ Third, the *Tanner* rationale fails to acknowledge that by allowing a debtor to void a real property lien that exceeds the value of the collateral, a court would deprive junior lienholders in bankruptcy

87. *Id.* The *Mahaner* court explained that a mortgagee has a number of years after the mortgagor defaults on the mortgage payments to begin a foreclosure proceeding. *Id.*; see *Boyarsky v. Froccaro*, 125 Misc. 2d 352, 479 N.Y.S.2d. 606, 612 (Sup. Ct. 1984) (providing that mortgage stands for debt or obligation to be secured, due from mortgagor to mortgagee, right to foreclose, and reciprocal right to redeem).

88. *Mahaner*, 34 Bankr. at 310.

89. *Id.*

90. *Id.*

91. *Id.*

92. *Id.*

93. *Mahaner*, 34 Bankr. at 310.

94. See *infra* notes 95-125 and accompanying text (discussing reasons that *Tanner* justifications for holding that debtor may void lien under § 506(d) are unsatisfactory); *supra* notes 32-65 and accompanying text (discussing *Tanner*).

95. See *infra* notes 99-107 (explaining reasons that *Tanner's* statutory interpretation argument is misguided); *supra* notes 43-47 (explaining *Tanner's* statutory interpretation analysis).

96. See *infra* notes 108-15 and accompanying text (explaining that *Tanner* court failed to explore thoroughly legislative history of § 506(d) of Bankruptcy Code); *supra* notes 48-52 (discussing *Tanner* court's examination of legislative history to § 506(d)).

proceedings of the potential benefits of appreciated property from which the junior lienholder could benefit under state law.⁹⁷ Finally, the *Tanner* rationale fails to recognize that by allowing a debtor to void a real property lien that exceeds the value of the collateral, a court may be unconstitutionally depriving the junior lienholder of property.⁹⁸

The *Tanner* rationale is unsatisfactory, first, because in its interpretation of section 506(d), the *Tanner* rationale places too much emphasis on the term "lien," rather than on the term "void."⁹⁹ The term "lien" is not the critical word in section 506(d) of the Bankruptcy Code.¹⁰⁰ An interpretation solely of the meaning of the term "lien" does not clarify the meaning of section 506(d) of the Bankruptcy Code.¹⁰¹ Although the *Tanner* rationale may interpret correctly the term "lien" as including real property mortgages, the *Tanner* rationale fails to inquire into the meaning that Congress intended for the critical term "void."¹⁰² By focusing its interpretation of section 506(d) on the term "lien," the *Tanner* rationale mistakenly assumes that the term "void" in section 506(d) is unambiguous.¹⁰³ Courts, however, have interpreted the term "void" in different ways.¹⁰⁴ Some courts have stated that Congress intended the term "void" in section 506(d) to permit a trustee to sell the collateral and extinguish the entire lien even though the sale proceeds fully do not satisfy the debt.¹⁰⁵ Another court has stated that Congress intended the term "void" in section 506(d) to permit valid liens to survive the bankruptcy proceeding.¹⁰⁶ Because of the ambiguity of the

97. See *infra* notes 116-20 and accompanying text (describing how *Tanner* reasoning deprives junior lienholders in bankruptcy proceeding of potential benefits of appreciated property); *supra* notes 53-58 and accompanying text (explaining *Tanner* court's argument that in bankruptcy proceeding, junior lienholder receives same value for property that junior lienholder would receive under state law).

98. See *infra* notes 121-26 and accompanying text (describing how *Tanner* reasoning may unconstitutionally deprive junior lienholder of property); *supra* notes 59-65 (discussing *Tanner* court's constitutional analysis of whether court may void lien under § 506(d) to extent that lien exceeds value of collateral).

99. See *Tanner*, 14 Bankr. at 935 (interpreting § 506(d) of Bankruptcy Code).

100. See *id.* (focusing on term "lien"); *infra* notes 101-107 and accompanying text (explaining *Tanner* court's error in focusing on term "lien").

101. See 11 U.S.C. § 506(d) (1982 & Supp. IV 1986) (providing that to extent that lien secures claim against debtor that is not allowed secured claim, lien is void).

102. See *Tanner*, 14 Bankr. at 935 (interpreting § 506(d) of Bankruptcy Code); 11 U.S.C. § 506(d) (1982 & Supp. IV 1986) (providing that to extent that lien secures claim against debtor that is not allowed secured claim, lien is void).

103. See *Tanner*, 14 Bankr. at 935 (interpreting § 506(d) of Bankruptcy Code); *infra* notes 104-06 and accompanying text (discussing various interpretations of term "void" in § 506(d)).

104. See *infra* notes 105-06 and accompanying text (listing courts' differing interpretations of term "void" in § 506(d) of Bankruptcy Code).

105. *In re Mahaner*, 34 Bankr. at 308, 309 (Bankr. W.D.N.Y. 1983); see *Maitland v. Central Fidelity Bank*, 61 Bankr. 130, 134 (Bankr. E.D. Va. 1986) (following *Mahaner* court's interpretation of § 506(d) of Bankruptcy Code).

106. See *In re Tarnow*, 749 F.2d 464, 466 (7th Cir. 1984) (stating that § 506(d) of Bankruptcy Code allows valid liens to survive bankruptcy proceeding). The *Tarnow* court stated that section 506(d) allows a bankruptcy court to void liens that are not valid secured

term "void" in section 506(d) of the Bankruptcy Code, the *Tanner* reasoning's failure to interpret the vital term "void" weakens the *Tanner* analysis.¹⁰⁷

In addition to assuming that the term "void" in section 506(d) of the Bankruptcy Code is unambiguous, the *Tanner* reasoning, second, fails to explore thoroughly the legislative history of section 506(d) of the Bankruptcy Code.¹⁰⁸ Although the *Tanner* reasoning understandably interprets section 506(d) as being consistent with the fresh start policy of the Bankruptcy Code, the legislative history of section 506(d) specifically does not indicate that Congress intended for debtors to use section 506(d) to void real property liens to gain a fresh start.¹⁰⁹ The legislative history of section 506(d) suggests, instead, that Congress included the term "void" in section 506(d) to ensure that valid security interests survive the bankruptcy proceeding.¹¹⁰ One court has noted that section 506(d) appears literally to provide that if a party requests that a bankruptcy court disallow a claim, and the bankruptcy court does disallow the claim, then the lien that secures the claim is void.¹¹¹ This court noted, further, that Congress enacted section 506(d) to permit valid liens to survive the bankruptcy proceeding.¹¹² By allowing the debtor in a bankruptcy proceeding to void a valid lien, however, the *Tanner* reasoning unfairly gives the debtor in a bankruptcy proceeding a windfall that the debtor would not receive under state law.¹¹³ Although the *Tanner* rationale does provide the debtor with a fresh start, the *Tanner* rationale provides little indication that Congress intended section 506(d) specifically to effectuate a debtor's fresh start.¹¹⁴

claims. *Id.* at 466. The *Tarnow* court explained that if a creditor does not have a valid secured claim, then the creditor does not have a valid lien, which is security for the claim. *Id.*

107. See *supra* notes 99-106 and accompanying text (explaining that by failing to interpret ambiguous term "void" in § 506(d), *Tanner* court unsatisfactorily analyzed § 506(d) of Bankruptcy Code).

108. See *Tanner*, 14 Bankr. at 933, 936 (discussing legislative history of § 506(d) of Bankruptcy Code); *supra* notes 48-52 and accompanying text (discussing *Tanner* court's interpretation of § 506(d) of Bankruptcy Code); *infra* notes 109-14 (discussing *Tanner* court's failure to explore thoroughly legislative history of § 506(d) of Bankruptcy Code).

109. See *Tanner*, 14 Bankr. at 936 (discussing interpretation of legislative history of § 506(d) of Bankruptcy Code); H.R. REP. NO. 595, *supra* note 4, at 6313. (outlining legislative history of § 506(d) and failing to provide specifically that purpose of § 506(d) is to grant debtor fresh start); *supra* note 2 and accompanying text (discussing fresh start policy of Bankruptcy Code).

110. H.R. REP. NO. 595, *supra* note 4, at 6313. The legislative history of section 506(d) of the Bankruptcy Code reveals that section 506(d) permits liens to survive the bankruptcy case. *Id.* The legislative history also reveals that if a party in interest requests the court to determine and allow or disallow the claim secured by the lien and if the court disallows the claim, then the lien is void to the extent that the claim is not allowed. *Id.*

111. See *In re Tarnow*, 749 F.2d 464, 466 (7th Cir. 1984) (stating that § 506(d) of Bankruptcy Code allows valid liens to survive bankruptcy proceeding).

112. *Id.*

113. See *supra* notes 15-30 and accompanying text (explaining that under state law debtor may not void lien to extent that lien exceeds value of collateral).

114. See *Tanner*, 14 Bankr. at 936. (discussing interpretation of legislative history of § 506(d) of Bankruptcy Code and emphasis on fresh start policy).

In addition to questionably assuming that Congress intended for section 506(d) to provide the debtor with a fresh start, the *Tanner* reasoning, third, deprives junior lienholders in bankruptcy proceedings of the potential benefits of appreciated property that the junior lienholder could receive under state law.¹¹⁵ In concluding that section 506 of the Bankruptcy Code allows lienholders to receive in a bankruptcy proceeding the same property value that the lienholders would receive at a state law foreclosure sale, the *Tanner* reasoning assumes that the property at a forced sale would sell for the same price that the bankruptcy court finds the property to be worth.¹¹⁶ At a state law foreclosure sale, however, the property may have appreciated in value, a bidder may purchase the property at a price exceeding the bankruptcy court's value of the property, and the proceeds from the sale may satisfy partially or fully the junior lienholder's lien.¹¹⁷ Although property at a foreclosure sale generally sells for a price lower than fair market value, a bidder still may purchase the property at the foreclosure sale at a price exceeding the value that the bankruptcy court attached to the property.¹¹⁸ Accordingly, the *Tanner* reasoning that section 506 of the Bankruptcy Code allows lienholders to receive in a bankruptcy proceeding the same property value that the lienholders would receive under state law is questionable.¹¹⁹

In addition to assuming that a junior lienholder at a foreclosure sale would not receive partial payment of his lien, the *Tanner* reasoning, finally, questionably concludes that by voiding a lien that exceeds the value of the collateral, a court is not unconstitutionally depriving a junior lienholder of property.¹²⁰ Some courts, however, have acknowledged that a lienholder has

115. See *id.* 14 Bankr. at 936-37 (stating that § 506 of Bankruptcy Code allows creditors to receive in bankruptcy same property value that creditors receive at state law foreclosure sale). But see *In re Mahaner*, 34 Bankr. 308, 310 (Bankr. W.D.N.Y. 1983) (stating that by voiding under § 506(d) lien to extent that lien exceeds value of collateral, bankruptcy court deprives lienholder of opportunity to buy at forced sale property that may have appreciated in value); *infra* notes 116-19 and accompanying text (explaining weakness of *Tanner* court's claim that § 506 allows creditors to receive in bankruptcy same property value that creditors would receive in forced sale of property under state law).

116. See *Tanner*, 14 Bankr. at 936-37 (stating that § 506 of Bankruptcy Code allows creditors to receive in bankruptcy proceeding same property value that creditors would receive at state law foreclosure sale).

117. See *In re Mahaner*, 34 Bankr. 308, 310 (Bankr. W.D.N.Y. 1983) (stating that lienholder who forecloses may bid for property, buy property, and benefit if property has appreciated in value). See generally G. NELSON & D. WHITMAN, *supra* note 19, at §§ 7.6-32 (discussing state law foreclosure sales).

118. See generally G. NELSON & D. WHITMAN, *supra* note 19, at § 7.17 (discussing procedure of bidding at foreclosure sales); cf. *In re Endlich*, 47 Bankr. 802, 804 (Bankr. E.D.N.Y. 1985) (stating that real property increased in value since appraisal two years ago).

119. See *Tanner*, 14 Bankr. at 936-37 (reasoning that § 506 allows bankruptcy court to give creditor in bankruptcy proceeding same property value that creditor would receive at state law foreclosure sale); *supra* notes 115-18 and accompanying text (suggesting that *Tanner* rationale questionably assumes that § 506(d) of Bankruptcy Code permits lienholders to receive in bankruptcy same property value that lienholder would receive at state law foreclosure sale).

120. See *Tanner*, 14 Bankr. at 938 (discussing constitutionality of § 506(d) of Bankruptcy

a right to maintain his lien to satisfy the debt.¹²¹ By voiding in a bankruptcy proceeding a lien to the extent that the lien exceeds the value of the property, a bankruptcy court deprives the junior lienholder of the chance to maintain the lien to satisfy the debt.¹²² The property may have appreciated in value to such an extent that at a foreclosure sale a junior lienholder could receive partial or full payment of his lien.¹²³ Similarly, a junior lienholder may wish to bid in at the foreclosure sale, offer the value of his lien for the purchase price of the property, buy the property, and sell the property at a profit.¹²⁴ Consequently, the *Tanner* reasoning questionably concludes that by voiding a lien, a bankruptcy court is not unconstitutionally depriving a lienholder of property.¹²⁵

While the *Tanner* reasoning has several weaknesses, the *Mahaner* reasoning has a number of strengths.¹²⁶ First, rather than focusing solely on the fresh start policy of the Bankruptcy Code, the *Mahaner* reasoning examines whether Congress intended for a debtor to redeem under section 506(d) real property that a debtor could not redeem under the liquidation provisions of the Bankruptcy Code.¹²⁷ Second, by not allowing a debtor to void liens and receive in a liquidation proceeding more property than a debtor would receive in a rehabilitative proceeding, the *Mahaner* reasoning

Code); *see also In re Mahaner*, 34 Bankr. 308, 310 (Bankr. W.D.N.Y. 1983) (stating that by voiding liens to extent that liens exceed value of collateral, bankruptcy court may unconstitutionally deprive junior lienholder of benefits of appreciated property); *infra* notes 121-25 and accompanying text (discussing reasons that *Tanner* court questionably concludes that by voiding liens under § 506(d), bankruptcy court does not unconstitutionally deprive lienholder of property).

121. *See Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555, 580 (1935) (stating that essence of mortgage is right of mortgagee to insist upon full payment before mortgagee relinquishes security); *In re Mahaner*, 34 Bankr. 308, 310 (Bankr. W.D.N.Y. 1983) (stating that by voiding lien to extent that lien exceeds value of property, bankruptcy court may unconstitutionally deprive junior lienholder of property).

122. *In re Mahaner*, 34 Bankr. 308, 310 (Bankr. W.D.N.Y. 1983); *see supra* notes 16-30 and accompanying text (discussing lienholder's rights under state law to maintain lien to satisfy debt).

123. *See Mahaner*, 34 Bankr. at 310 (discussing lienholder's rights under state law foreclosure sale); *supra* notes 16-30 and accompanying text (discussing lienholder's right under state law to maintain lien to satisfy debt).

124. *See Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555, 580 (1935) (providing that to protect right to full payment of mortgaged property, mortgagee allowed to bid at foreclosure sale).

125. *See supra* notes 121-24 and accompanying text (discussing reasons that *Tanner* court questionably reasons that by voiding lien under § 506(d), bankruptcy court does not unconstitutionally deprive lienholder of property).

126. *Compare supra* notes 94-125 and accompanying text (discussing weaknesses of *Tanner* reasoning) with *infra* notes 127-47 and accompanying text (discussing strengths of *Mahaner* reasoning).

127. *See supra* notes 73-77 and accompanying text (explaining *Mahaner* court reasoning that Congress did not intend for debtor to use § 506(d) to redeem real property that debtor could not redeem under liquidation provisions of Bankruptcy Code); *infra* notes 130-36 and accompanying text (explaining that *Mahaner* court correctly avoids focusing on whether debtor's ability to void liens is consistent with fresh start policy).

discourages debtors from perceiving that liquidation is better than rehabilitation.¹²⁸ Finally, the *Mahaner* reasoning promotes results that most closely approximate state law results and, consequently, preserves in a bankruptcy proceeding a creditor's rights under state law.¹²⁹

The *Mahaner* reasoning, first, correctly avoids focusing on whether a debtor's ability to void liens under section 506(d) promotes the fresh start policy of the Bankruptcy Code.¹³⁰ By not focusing on the fresh start policy, the *Mahaner* reasoning recognizes that the legislative history does not indicate that Congress intended for section 506(d) to further the fresh start policy of the Bankruptcy Code.¹³¹ The *Mahaner* reasoning, instead, recognizes that the debtors voiding junior liens intend to pay senior lienholders the value of the lien and thus redeem their property.¹³² By recognizing that debtors intend to use section 506(d) to redeem their property, the *Mahaner* reasoning correctly examines specific liquidation provisions to discern whether Congress intended for a debtor to redeem real property in a liquidation proceeding.¹³³ The *Mahaner* reasoning convincingly explains that because section 722 of the Bankruptcy Code does not allow a debtor in a liquidation proceeding to redeem real property, a court should not allow a debtor in a liquidation proceeding to use section 506(d) to redeem property.¹³⁴ The *Mahaner* reasoning recognizes, accordingly, that although the fresh start policy is one general policy of the Bankruptcy Code, Congress did not intend for every section of the Bankruptcy Code to further the fresh start policy.¹³⁵ The *Mahaner* reasoning, thus, follows a specific statutory section

128. See *supra* notes 78-84 and accompanying text (explaining *Mahaner* rationale that courts should not allow debtor to receive in liquidation proceeding more property than debtor would receive in rehabilitative proceeding); *infra* notes 137-41 and accompanying text (explaining that *Mahaner* court convincingly reasons that by allowing debtors to receive more property in liquidation proceeding than in rehabilitative proceeding, court would encourage debtors to liquidate, rather than rehabilitate).

129. See *supra* notes 74-92 and accompanying text (outlining *Mahaner* court's reasoning that debtor may not void under § 506(d) lien to extent that lien exceeds value of property); *infra* notes 142-47 and accompanying text (describing ways that *Mahaner* reasoning preserves in bankruptcy proceeding creditors' rights under state law).

130. See *Mahaner*, 34 Bankr. at 309 (avoiding analysis of § 506(d) in terms of fresh start policy of Bankruptcy Code); *supra* notes 74-77 and accompanying text (discussing *Mahaner* reasoning that because debtor may not redeem real property under § 722 of Bankruptcy Code, debtor should not be able to redeem real property under § 506(d) of Bankruptcy Code).

131. See *Mahaner*, 34 Bankr. at 309 (avoiding analysis of § 506(d) in terms of fresh start policy of Bankruptcy Code); H.R. REP. No. 595, *supra* note 4, at 6316 (providing legislative history of § 506(d) and failing to state that purpose of § 506(d) is to give debtors fresh start).

132. *Mahaner*, 34 Bankr. at 309.

133. See *id.* (noting that debtor may not redeem real property under § 722 of Bankruptcy Code).

134. 11 U.S.C. § 722 (1982); see *Mahaner*, 34 Bankr. at 309 (stating that debtor should not receive in liquidation proceeding more property than debtor would receive in rehabilitative proceeding); *supra* notes 74-77 and accompanying text (discussing *Mahaner* reasoning that by allowing debtor to void real property lien under § 506(d), court would render meaningless § 722 of Bankruptcy Code).

135. See *Mahaner*, 34 Bankr. at 309 (examining redemption policy of § 722 of Bankruptcy

of the Bankruptcy Code that does not allow a debtor to redeem real property in a liquidation proceeding, over the more general fresh start policy.¹³⁶

After reasoning that a bankruptcy court should not allow debtors to use section 506(d) to redeem real property in a liquidation proceeding, the *Mahaner* rationale, second, convincingly explains that Congress did not intend a debtor to receive in a liquidation proceeding more property than the debtor could receive in a rehabilitative proceeding.¹³⁷ Examining the legislative history of the Bankruptcy Code, the *Mahaner* reasoning correctly recognizes that Congress intended to encourage debtors who are eligible for a rehabilitation plan to use a rehabilitation plan.¹³⁸ A debtor who could redeem real estate in a liquidation proceeding likely would not use the rehabilitative proceedings.¹³⁹ The *Mahaner* reasoning concludes that by allowing a debtor to void liens and to redeem real estate in a liquidation proceeding, courts would frustrate Congress' intent to encourage debtors to use the rehabilitative chapters.¹⁴⁰ Accordingly, the *Mahaner* reasoning convincingly examines the use of section 506(d) in conjunction with policies of the Bankruptcy Code other than solely the fresh start policy.¹⁴¹

In addition to examining the relation between section 506(d) and the rehabilitative chapters, the *Mahaner* reasoning, finally, promotes results that most closely approximate state law results.¹⁴² One court has noted that, in deciding whether a debtor can void a lien in a bankruptcy proceeding, courts should examine whether the debtor could void the lienholder's interest under state law.¹⁴³ One commentator has noted, also, that bankruptcy should

Code, which does not allow debtor to redeem real property in bankruptcy proceeding); *supra* notes 74-77 and accompanying text (discussing redemption policy of § 722, which does not allow debtor to redeem real property in liquidation chapter of Bankruptcy Code).

136. *Mahaner*, 34 Bankr. at 309; *supra* notes 130-135 and accompanying text (discussing *Mahaner* reasoning that because § 722 of Bankruptcy Code does not allow debtor in liquidation proceeding to redeem real property, bankruptcy courts should not allow debtor in liquidation proceeding to use § 506(d) to redeem real property).

137. *Mahaner*, 34 Bankr. at 309.

138. *Id.* See generally S. REP. No. 989, *supra* note 1, at 5795-99 (summarizing congressional intent in enacting rehabilitative sections of Bankruptcy Code).

139. *Mahaner*, 34 Bankr. at 309.

140. *Id.*

141. See *id.* (examining rehabilitative policies of Chapter Eleven and Chapter Thirteen of Bankruptcy Code instead of fresh start policy to determine whether bankruptcy courts should allow debtor to use § 506(d) to void real property lien to extent that lien exceeds value of collateral).

142. See *id.* at 309-10 (discussing reason that courts should not allow debtor to void under § 506(d) liens to extent that liens exceed value of collateral); *infra* notes 143-47 (explaining that *Mahaner* reasoning preserves in bankruptcy proceeding creditors' rights under state law); *supra* notes 16-30 (describing lienholder's rights under state law foreclosure sale).

143. *Lyons v. First Pa. Bank*, 46 Bankr. 604, 606 (Bankr. N.D. Ill., E.D. 1985) (acknowledging that in deciding whether debtor may void lien in bankruptcy proceeding, courts should examine whether debtor has power under state law to void lien).

not alter creditors' rights under state law.¹⁴⁴ For example, if under state law, a lienholder may retain his lien until the debtor satisfies the debt, a lienholder in a bankruptcy proceeding similarly should retain his lien.¹⁴⁵ The commentator has noted, thus, that because bankruptcy is a proceeding that supplies a collective forum for creditors to divide a debtor's assets, bankruptcy should take state law rights, such as preservation of a lienholder's lien, and translate those rights into the collective forum.¹⁴⁶ The *Mahaner* reasoning promotes fair results for both debtors and creditors because the *Mahaner* reasoning, accordingly, takes both debtors' and creditors' rights at state law and translates those rights into a bankruptcy proceeding.¹⁴⁷

Both the *Tanner* court and the *Mahaner* court recognize that the legislative history to section 506(d) of the Bankruptcy Code is sparse.¹⁴⁸ The *Tanner* and *Mahaner* rationales, however, differently examine whether a bankruptcy court may void under section 506(d) of the Bankruptcy Code a lien to the extent that the lien exceeds the value of the collateral.¹⁴⁹ The *Tanner* rationale relies mainly on the plain language and a literal interpretation of section 506(d) to support a bankruptcy court's voiding of a lien to the extent that the lien exceeds the value of the collateral.¹⁵⁰ In contrast, the *Mahaner* rationale relies mainly on policy arguments to support a bankruptcy court's refusal to void a lien to the extent that the lien exceeds the value of the collateral.¹⁵¹ Until Congress clarifies whether a debtor may use section 506(d) of the Bankruptcy Code to void liens to the extent that the liens exceed the fair market value of the collateral, bankruptcy courts should follow the *Mahaner* analysis.¹⁵² The *Mahaner* reasoning benefits creditors by preserving the creditors' rights available under state law in the

144. See Jackson, *Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain*, 91 YALE L.J. 857-907 (1982) (discussing reasons that bankruptcy law should recognize in bankruptcy proceedings creditors' rights under state law, such as security interests).

145. *Id.*

146. *Id.*

147. See *supra* notes 73-92 and accompanying text (discussing *Mahaner* rationale for not allowing debtor to void under § 506(d) lien to extent that lien exceeds value of collateral).

148. See *Mahaner*, 34 Bankr. at 309 (discussing meaning of § 506(d)); *Tanner*, 14 Bankr. at 936 (discussing legislative history of § 506(d)); H.R. REP. No. 595, *supra* note 4, at 6313 (outlining legislative history of § 506(d)).

149. See *Mahaner*, 34 Bankr. at 309-10 (examining reasons for not allowing debtor to void under § 506(d) of Bankruptcy Code lien to extent that lien exceeds value of collateral); *Tanner*, 14 Bankr. at 935-40 (examining reasons for allowing debtor to void under § 506(d) lien to extent that lien exceeds value of property).

150. *Tanner*, 14 Bankr. at 935; see *supra* notes 41-65 (discussing reasons that *Tanner* court held that debtor may use § 506(d) to void real property lien to extent that lien exceeds value of collateral).

151. *Mahaner*, 34 Bankr. at 309-10; see *supra* notes 74-93 and accompanying text (discussing reasons that bankruptcy courts should not allow debtors to use § 506(d) to void real property lien to extent that lien exceeds value of collateral).

152. See *infra* notes 153-54 and accompanying text (discussing reasons why bankruptcy courts should adopt *Mahaner* reasoning); *supra* notes 127-47 and accompanying text (discussing strengths of *Mahaner* reasoning).

bankruptcy proceeding.¹⁵³ Moreover, the *Mahaner* reasoning furthers the Bankruptcy Code's goal of equitably distributing among creditors a debtor's assets.¹⁵⁴ Courts should not follow the *Tanner* reasoning because the *Tanner* reasoning provides debtors with a windfall that the debtor ordinarily would not receive under state law.¹⁵⁵

In light of the difficulty of discerning congressional intent in enacting section 506(d), one practical solution is for bankruptcy courts to decline to value under section 506(a), and decline to subsequently void under section 506(d), the encumbered property of the bankruptcy estate.¹⁵⁶ Instead, because the encumbered property is of inconsequential value to the bankruptcy estate, bankruptcy courts should order the trustee to abandon¹⁵⁷ the encumbered property.¹⁵⁸ When the trustee abandons the encumbered property, the trustee releases the property to the debtor and the property ceases to be property of the bankruptcy estate.¹⁵⁹ If the debtor then petitions the bankruptcy court to void under section 506(d) the junior lien, the bankruptcy court should permit the junior lienholder to submit to the bankruptcy court a bid to buy the property.¹⁶⁰ By allowing the junior lienholder to buy the property, the bankruptcy court provides the junior lienholder with an opportunity to protect his interest in the property.¹⁶¹ If the junior lienholder believes that the property's value exceeds the amount of the senior lien, the junior lienholder typically would buy the property.¹⁶² If the junior lienholder buys the property, the senior lienholder would receive payment of the senior lien from the proceeds of the sale.¹⁶³ If the junior lienholder declines to buy the property, however, the bankruptcy court should void under section 506(d) the junior lien.¹⁶⁴ The senior lienholder, who still retains his lien on

153. See *supra* notes 142-47 and accompanying text (outlining ways that *Mahaner* reasoning preserves in bankruptcy proceeding creditors' rights under state law).

154. See *supra* notes 67-92 and accompanying text (presenting *Mahaner* rationale for not allowing debtor to void lien to extent that lien exceeds value of collateral).

155. See *supra* notes 108-14 and accompanying text (describing reasons that *Tanner* rationale provides debtor with windfall that debtor would not receive at state law).

156. Interviews with Joseph Ulrich, Professor of Law, Washington & Lee School of Law, in Lexington, Va. (Jan.-Apr. 1988). Professor Ulrich suggested the solution presented in notes 157-67 and the accompanying text. *Id.* See Jackson, *supra* note 144, at 857-907 (discussing reasons that bankruptcy law should recognize in bankruptcy proceedings creditors' rights under state law, such as security interests).

157. 11 U.S.C. § 554(b) (1982 & Supp. IV 1986).

158. Interviews with Joseph Ulrich, Professor of Law, Washington & Lee School of Law, in Lexington, Va. (Jan.-Apr. 1988).

159. See 11 U.S.C. § 554(b) (1982 & Supp. IV 1986) (providing that upon request of party in interest, court may order trustee to abandon any property of estate that is burdensome to estate or that is of inconsequential value and benefit to estate).

160. Interviews with Joseph Ulrich, Professor of Law, Washington & Lee School of Law, in Lexington, Va. (Jan.-Apr. 1988).

161. *Id.*

162. *Id.*

163. *Id.*

164. *Id.*

the property, thus would be free to foreclose on the debtor's property.¹⁶⁵ Realizing that the senior lienholder could foreclose on the property, the debtor might choose to pay off the senior lien.¹⁶⁶ If the debtor pays off the senior lien, the senior lienholder would receive satisfaction of his debt and the debtor could retain his home.¹⁶⁷ By allowing the junior lienholder to bid for and buy the property, bankruptcy courts would promote fair results for junior lienholders, senior lienholders, and for debtors.¹⁶⁸ Junior lienholders would benefit because the junior lienholder would lose his lien only if the junior lienholder declines to bid for and buy the property from the bankruptcy court.¹⁶⁹ Senior lienholders would benefit because the senior lienholder retains his lien until the debtor pays off the lien or until the senior lienholder forecloses and sells the property.¹⁷⁰ Debtors would benefit because if the trustee voids the junior lien, the debtor may retain his home by paying off the senior lien.¹⁷¹

In light of the diverging lines of authority on the proper use of section 506(d) of the Bankruptcy Code, Congress should clarify the meaning of section 506(d).¹⁷² In the absence of congressional action, however, bankruptcy courts should follow the *Mahaner* analysis and not allow debtors to void liens to the extent that the liens exceed the fair market value of the property.¹⁷³ Bankruptcy courts, further, could order that trustees abandon to the debtor the heavily encumbered property.¹⁷⁴ By abandoning heavily encumbered property and allowing the junior lienholder to buy the property, bankruptcy courts would give junior lienholders the opportunity to protect their interests in the debtor's property.¹⁷⁵ Senior lienholders would retain

165. See generally R. KRATOVIK & R. WERNER, *supra* note 7, at 389-96 (discussing state law foreclosure sales).

166. Interviews with Joseph Ulrich, Professor of Law, Washington & Lee School of Law, in Lexington, Va. (Jan.-Apr. 1988).

167. See R. KRATOVIK & R. WERNER, *supra* note 7, at 389 (providing that before foreclosure sale, mortgagor may pay off mortgage and stop foreclosure).

168. See *supra* notes 156-67 and accompanying text (explaining that bankruptcy court's decision to let junior lienholder bid for and buy property promotes fair results for senior and junior lienholders and for debtor).

169. See *supra* notes 156-64 (noting that junior lienholder would lose lien only if junior lienholder declines to bid for and buy property).

170. See *supra* notes 156-167 and accompanying text (explaining that by permitting junior lienholder to bid for and buy property, bankruptcy court promotes fair result for senior lienholder).

171. See *id.* (explaining that by voiding junior lien if junior lienholder declines to buy property, bankruptcy court promotes fair result for debtor). A debtor always has the option to pay off all of the liens to retain the property. See generally G. NELSON & D. WHITMAN, *supra* note 19, at § 7.3 (providing that mortgagee is entitled to payment in full and to retain lien on land until mortgagor pays debt in full).

172. See *supra* note 14 (listing two divergent lines of authority on whether debtor may use § 506(d) to void real property lien to extent that lien exceeds value of collateral).

173. See *supra* notes 126-47 (discussing strengths of *Mahaner* reasoning).

174. Interviews with Joseph Ulrich, Professor of Law, Washington & Lee School of Law, in Lexington, Va. (Jan.-Apr. 1988).

175. *Id.*

their liens and would be able to foreclose on the debtor's property.¹⁷⁶ Debtors also may be able to retain their property by paying off the liens.¹⁷⁷ By not allowing debtors initially to void liens to the extent that the liens exceed the value of the collateral, bankruptcy courts would preserve in bankruptcy creditors' rights under state law.¹⁷⁸ Further, bankruptcy courts would promote the Bankruptcy Code's objective of equitably distributing a debtor's assets among creditors.¹⁷⁹

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176. *Id.*

177. *Id.*

178. *See supra* notes 142-47 and accompanying text (explaining that *Mahaner* reasoning preserves in bankruptcy proceeding creditors' rights under state law).

179. *See supra* note 2 (describing Bankruptcy Code's policies of providing debtor with fresh start and of providing creditors with equitable distribution of debtor's assets); *supra* notes 130-36 (outlining *Mahaner* reasoning that recognizes that legislative history of § 506(d) does not indicate that Congress intended for § 506(d) to further fresh start policy of Bankruptcy Code).

