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I. Introduction

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA)'s[1] codified protections to common-interest associations create a death-trap for honest bankruptcy debtors trying to achieve a fresh start. Because it is impossible to compel foreclosure and because the current economic and legislative environment creates strong incentives not to foreclose, association fees may accrue indefinitely, a problem the debtor is powerless to correct.

Associations, including homeowner associations (HOAs) and condominium associations, are real estate developments or neighborhoods with individually owned lots or units "burdened by a servitude that imposes [a nonavoidable] obligation . . . to pay dues or assessments."[2] Mandatory member assessments provide a means for members to share the cost of otherwise cost-prohibitive amenities.[3] Associations are creatures of state law and each state has an enabling statute that sanctions the formation of the association upon meeting certain requirements.[4]

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1. *See* Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 (codified as amended in scattered sections of 11 U.S.C.) [hereinafter BAPCPA].

2. RESTATEMENT (THIRD) OF PROP.: SERVITUDES § 1.8 (2000) [hereinafter SERVITUDES]. There are approximately 314,000 such communities accounting for 62.3 million residents in the United States. *Industry Data National Statistics*, CMTY. ASS'NS INST., http://www.caionline.org/info/research/Pages/default.aspx (last visited Apr. 2, 2012) (on file with the Washington and Lee Law Review). Approximately 52–55% of this total is contributable to HOAs, while 38–42% is contributable to condominiums. *Id.*

3. *See* WAYNE S. HYATT, CONDOMINIUM AND HOMEOWNER ASSOCIATION PRACTICE: COMMUNITY ASSOCIATION LAW § 1.05 (3d ed. 2001) (noting that associations use mandatory assessments to maintain common areas, allowing members to spread costs among each other).

4. *See, e.g.*, VA. CODE ANN. § 54.1-2346 (West 2011) (providing the license requirements for an association under Virginia law); *see also* DAVID CLURMAN & EDNA L. HEBARD, CONDOMINIUMS AND COOPERATIVES 12–13 (1970) (describing

Contrary to the traditional use of bankruptcy, many debtors are choosing to surrender[5] their homes in bankruptcy because of decreases in home values[6] and equity.[7] The depressed real estate market combined with other disincentives to foreclose means lenders are not rushing to foreclose on delinquent borrowers.[8] While the Bankruptcy Code (Code) provides debtors with an option to surrender property, it does not compel foreclosure sale by a lender.[9] Absent foreclosure, debtors still own their homes,

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states' common-interest association enabling statutes as the "legislative sanction on the effectiveness of [the declaration] among participating owners, and between the latter and outsiders").

5. *See* 11 U.S.C. § 521(a)(2)(A) (2010) (providing Chapter 7 debtors with an option to surrender encumbered property); *id.* § 1325(a)(5)(C) (providing Chapter 13 debtors with a similar option). The difference between a Chapter 7 and a Chapter 13 bankruptcy is basic. Chapter 7 equates to a liquidation in which the trustee sells a debtor's nonexempt property and pays creditors in a proscribed priority with the proceeds. *See* DAVID EPSTEIN ET AL., BANKRUPTCY § 1-8 (1993). Chapter 13 equates to a reorganization of debt in which the trustee pays creditors through a three-to-five-year repayment plan. *See id.*

6. *See Historical Data Exhibit 9. Existing Home Prices: 1969–Present,* U.S. DEP'T OF HOUS. & URBAN DEV., http://www.huduser.org/portal/periodicals/ushmc/fall11/USHMC_3q11_historical.pdf (reporting a median inflation-adjusted home sales price of $221,900 in 2006, $198,100 in 2008, and $172,900 in 2010).

7. *See* Press Release, CoreLogic, Q2 2010 Negative Equity (Aug. 26, 2010), http://www.corelogic.com/about-us/news/asset_upload_file301_4022.pdf (noting "that 11 million, or 23 percent, of all residential properties with mortgages were in negative equity"); *see also* Pigg v. BAC Home Loans Servicing, LP (*In re* Pigg), 453 B.R. 728, 733 (Bankr. M.D. Tenn. 2011) (noting that Congress never contemplated a situation in which so many borrowers with negative equity would be filing bankruptcy and surrendering their properties). The number of debtors surrendering their homes is also contributable to the increases in the number of bankruptcy filings. *See Table 770. Bankruptcy Petitions Filed and Pending by Type and Chapter: 1990 to 2009*, U.S. CENSUS BUREAU, http://www.census.gov/compendia/statab/2011/tables/11s0771.pdf (showing an increase from 2007 Chapter 7 and 13 filings of 435,064 and 291,560, respectively, to 870,266 and 379,939 in 2009, respectively).

8. *See In re Pigg*, 453 B.R. at 733 ("With the real estate collapse, lenders, who otherwise have the right to do so, are choosing not to foreclose on their collateral leaving homeowners in limbo."); Les Christie, *Foreclosure Free Ride: 3 Years, No Payments*, CNNMONEY (Jan. 1, 2012), http://money.cnn.com/2011/12/28/real_estate/foreclosure/index.htm (last visited Apr. 2, 2013) ("Nationwide, the average time it takes to process a foreclosure—from the first missed payment to the final foreclosure auction—has climbed to 674 days from 253 days just four years ago. . . .") (on file with the Washington and Lee Law Review).

9. *See* Arsenault v. JP Morgan Chase Bank, N.A. (*In re* Arsenault), 456

even after bankruptcy discharge.[10] The result is that a borrower-debtor's fresh start becomes solely dependent on their lender's decision to foreclose.

As a primary goal of bankruptcy, a fresh start is premised on the philosophy that only when a person is relieved of his past financial burdens can that person reenter society as a productive citizen.[11] Bankruptcy does not, however, ensure a fresh start with respect to every debt owed by the debtor. Section 523[12] provides an exhaustive list of debts that survive discharge.[13] While cutting to the heart of a debtor's fresh start, these exceptions to discharge are "the product of countervailing policy considerations in which the scales of justice tip in favor of certain creditors."[14] Some of the exceptions are based on the defenseless nature of the creditor or the egregious nature of the debtor's debt.[15]

B.R. 627, 630 (Bankr. S.D. Ga. 2011) ("[T]he act of [surrendering] does not obligate [lender] to transfer title out of Debtors' names."); *see also In re Pigg*, 453 B.R. at 732 ("Nothing in the law can require [a] Bank to foreclose.").

10. *See* RESTATEMENT (THIRD) OF PROP.: MORTGAGES § 4.1 (1997) [hereinafter MORTGAGES] (noting that the borrower still owns the home up until the time of foreclosure sale); *see also* DAVID A. SCHMUDDE, A PRACTICAL GUIDE TO MORTGAGES AND LIENS § 5.02(b)(c) (2004) (explaining that only a foreclosure sale ends debtor's interest in the property).

11. *See* Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934) (noting that the purpose of bankruptcy is to give "the honest but unfortunate debtor . . . a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt").

12. *See* 11 U.S.C. § 523 (2010).

13. *See id*. (providing a list of claims that are excluded from discharge).

14. George H. Singer*, Section 523 of the Bankruptcy Code: The Fundamentals of Nondischargeability in Consumer Bankruptcy*, 71 AM. BANKR. L.J. 325, 326 (1997). These countervailing policy goals include the need to resolve "the competing claims of multiple creditors," and to free "debtor[s] from [their] financial past." CHARLES J. TABB, THE LAW OF BANKRUPTCY § 1.1 (2d ed. 2009). These goals are inherently in conflict.

15. *See* § 523(a)(5), (15) (protecting claims by former spouses and children of the debtor); § 523(2), (4), (6), (9), (11), (13) (protecting claims by victims of fraud, embezzlement, willful and malicious injury, or drunk driving, and recipients of restitution orders, fines, or penalties); *see also* KAREN GROSS, FAILURE AND FORGIVENESS 27–28 (1997) (describing § 523 as "bankruptcy's gatekeeper" keeping debtors' "bad debts from partaking in the system's benefits"); Margaret Howard, *A Theory of Discharge in Consumer Bankruptcy*, 48 OHIO ST. L.J. 1047, 1050–58 (1987) (noting the concern for dishonest debtors taking advantage of the system and the additional protection required by certain creditors).

In 1994, associations made the § 523 list with the enactment of § 523(a)(16),[16] which excluded future assessments, arising after bankruptcy petition, from discharge if the debtor continued to reside on the property or rented it out.[17] Associations were the victims of freeriding members—members that file bankruptcy to discharge future assessments, but continue to reside in their properties, pay their mortgages, and assume the benefits procured by the association without paying any assessments.[18] These freeriders exemplify the dishonest, bad faith debtors that § 523 seeks to protect against.

In 2005, BAPCPA expanded protection to associations by completely excluding future assessments from discharge, regardless of the debtors' use of the property after filing.[19] Thus, between surrendering their homes in bankruptcy and the lenders' eventual foreclosure sale, member-debtors continue to be liable for accumulating association dues postdischarge, continue to face collection efforts from their associations for nondischarged postpetition assessments, and must choose between spending disposable income on abandoned property or risking the inability to rebuild their credit. This Note will argue that associations were adequately protected from freeriders with the 1994 version of § 523(a)(16). BAPCPA's broadened protection is overinclusive, engulfing honest debtors that cannot transfer their property due to a lack of equity and lender delay. Moreover, a modified standard, closer to that of the 1994 version of § 523(a)(16), applied to both Chapter 7 and 13 debtors,[20] would better serve

16. *See* Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 309, 108 Stat. 4106, 4137 (codified as amended at 11 U.S.C. § 523(a)(16) (1994)) (current version at 11 U.S.C. § 523(a)(16) (2010)) [hereinafter Reform Act].

17. *See id.*

18. *See* Marvin J. Nodiff & Benjamin S. Gage, *Post-petition Assessments: "Fresh Start" or "Head Start,"* 50 J. MO. B. 237, 238–39 (1994) (describing the "head start," rather than "fresh start," that would be given to members who were able to assume the benefits of the associations at the expense of other members).

19. *See* BAPCPA § 412 (codified as amended at 11 U.S.C. § 523(a)(16) (2005)) (current version at 11 U.S.C. § 523(a)(16) (2010)).

20. Currently, § 523(a)(16) is only applicable in Chapter 7 cases. *See* 11 U.S.C. § 1328(a)(2) (2005) (omitting § 523(a)(16)'s application to Chapter 13 discharge).

the goals of the Code. Any additional protection required by associations is better accomplished through contract or state law.

This Note is structured as follows. Part II will consider whether accumulating assessments, coming due after filing, are dischargeable debts but for the application of § 523. This is included for two reasons. First, the determination remains relevant in Chapter 13 cases in which § 523(a)(16) does not apply. Second, the determination is relevant as to the congressional purpose of § 523(a)(16). If future assessments are nondischargeable, § 523(a)(16) is superfluous, excluding from discharge something that is already nondischargeable. If assessments are dischargeable, then the intended purpose of the section can be compared to its unintended results. In addition to providing a brief history of § 523(a)(16), Part III will critique the unintended results of the Section and determine if a death-trap has been created. Part IV proposes a legislative solution and provides two judicial solutions. Part V will conclude.

II. Assessments Are Prepetition Debts Under § 101

Assessments represent the sole source of income available to associations to cover their expenditures.[21] They are established at the beginning of each year and payable by the record member as of the due date, with membership being mandatory.[22] The obligation to pay assessments is set out in the declaration, which is a recorded document "binding . . . every person who becomes a

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21. *See* WAYNE S. HYATT & PHILIP S. DOWNER, CONDOMINIUM AND HOMEOWNER ASSOCIATION LITIGATION § 6.1 (1987) (listing other common names for assessments such as "maintenance fees" and "association dues"). Approximately $40 billion was collected in assessments in 2010. CMTY. ASS'NS INST., *supra* note 2.

22. *See* WARREN FREEDMAN & JONATHAN B. ALTER, THE LAW OF CONDOMINIA AND PROPERTY OWNERS' ASSOCIATIONS 81–84 (1992) ("Annual assessments will be established prior to the beginning of each fiscal year and will be payable on a monthly basis.").

property owner in the project."[23] The obligation to pay assessments ends only when the record owner changes.[24]

Chapter 7 and 13 discharges only relieve debtors of prepetition debts—those that arise "before the commencement of the case."[25] For purposes of this Part, it must be determined whether the obligation to pay future assessments, which arise from the declaration, is a prepetition debt.[26] This is important for two reasons: First, § 523(a)(16), exempting assessments from discharge, applies only to Chapter 7 discharge, so the determination of whether the claim for future assessments arises "before [or after] the commencement of the case" remains relevant in Chapter 13 cases.[27] Second, the determination may shed light on Congress's intentions when enacting § 523(a)(16). If assessments coming due after a debtor's filing are not dischargeable prepetition debts, § 523(a)(16) is superfluous, excluding from discharge something that is already excluded. Alternatively, Congress may have intended the Section to provide interpretive guidance on the dischargeability of accumulating assessments. If assessments coming due after a debtor's filing are dischargeable prepetition debts, then the policy considerations behind § 523(a)(16) can be compared to its results for overinclusiveness and unintended consequences.

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23. HYATT, *supra* note 3, § 1.06(e) ("The declaration is a document containing the plan of development and the essentials of ownership, the method of operation, and the rights and responsibilities of the association and the owners within the association.").

24. *See* FREEDMAN & ALTER, *supra* note 22, at 83 (describing "the assessment contract as an affirmative covenant inserted into the Declaration"); *see also id.* (noting that an "owner's dissatisfaction or displeasure" is not a justifiable grounds for nonpayment).

25. *See* 11 U.S.C. § 727 (2005); *see also* § 1328 (providing for the discharge of prepetition debts provided for in the plan). Similarly, the automatic stay only protects debtors against the attempted collection of prepetition debts during the time between debtor's petition and discharge. *See* § 362(a)(1) (2010).

26. *See* Maple Forest Condo. Ass'n v. Spencer (*In re* Spencer), 457 B.R. 601, 605 (Bankr. E.D. Mich. 2011) (noting that the dischargeability of accruing assessments depends on whether they arise prepetition or postpetition); *see also* Liberty Cmty. Mgmt., Inc. v. Hall (*In re* Hall), 454 B.R. 230, 233 (Bankr. N.D. Ga. 2011) (noting that the application of the automatic stay to the collection of assessments depends on when the debt arises because the automatic stay "applies only to pre-petition claims").

27. *See* 11 U.S.C. § 1328(a)(2) (2005) (omitting § 523(a)(16)'s application from Chapter 13 discharge).

Section 101[28] of the Code defines "debt" as a "liability on a claim."[29] A "claim" is defined as a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured."[30] For the debt to be deemed a dischargeable prepetition claim, § 101(5) requires a "right to payment" to exist at the time the debtor files his petition for bankruptcy.[31] "Right to payment" connotes a timing aspect, but Congress declined to define the term.[32]

The Supreme Court has interpreted "right to payment" as an "enforceable obligation of the debtor."[33] State law is unanimously clear that an association-member's enforceable obligation to pay assessments arises from the declaration, which creates a "personal obligation [against] the owner, as well as constituting a lien against the [property]."[34] This definition presents two problems. First, the exact time an enforceable obligation against the debtor comes into existence remains unclear. Second, in addition to creating a personal obligation against the debtor, the declaration also creates a claim against the debtor's property, and claims against property generally survive discharge.[35]

In an attempt to solve these problems, courts have compared the declaration and its obligation-to-pay assessments to two common footings found in the Code: claims resulting from

28. *See* 11 U.S.C. § 101 (2010) (providing definitions of terms).

29. *Id.* § 101(5).

30. *Id.* § 101(12).

31. *Id.* § 101(5).

32. *See id.* § 101 (declining to define "right to payment" and giving no direction as to when a right to payment arises).

33. *See* Penn. Dep't of Pub. Welfare v. Davenport, 495 U.S. 552, 559 (1990); *see also* EPSTEIN, *supra* note 5, § 3-6 ("[A] claim arises under the bankruptcy law when the debtor acts to obligate herself (whether by law or agreement) to pay money (either now or later) even though the obligation was contingent.").

34. HYATT & DOWNER, *supra* note 21, § 6.16; *see also, e.g.*, FLA. STAT. ANN. § 718.116 (West 2011) (establishing personal liability against the owner and a lien against the property for unpaid assessments).

35. *Compare* 11 U.S.C. § 524(a)(2) (2010) (noting that discharge "operates as an injunction against the commencement or continuation of an action . . . to collect, recover or offset any such debt as personal liability of the debtor"), *with id.* § 524(j)(1) (providing that the discharge injunction of (a)(2) does not apply to secured creditors with "a security interest in real property that is the principal residence of the debtor").

prepetition contracts and claims against a debtor's property interest. If the declaration is a prepetition contract, the association's right to all future assessments (whether owed and payable before or after debtor's bankruptcy petition) are dischargeable as prepetition debts.[36] If the declaration is a property interest, the association's right to all future assessments stems from ownership of the property, which cannot be determined until an individual assessment is due, and will be deemed nondischargeable as postpetition claims.[37] Because of the peculiar nature of the declaration, however, neither category perfectly encompasses the declaration.

A. Declaration as a Prepetition Contract

In the traditional contract setting, the party's enforceable obligation against the other party occurs when the contract becomes binding on both parties, even if the obligation is not performed until sometime in the future.[38] The same holds true for assessments arising from the declaration if the declaration can be designated a contract that existed before the date of filing.[39] The Seventh Circuit, in *In re Rosteck*,[40] held that future assessments coming due after the debtor's filing were dischargeable as

36. *See In re* Rosteck, 899 F.2d 694, 696 (B.A.P. 7th Cir. 1990) (finding that accumulating HOA assessments coming due after debtor's filing are derived from a prepetition contract and are, therefore, dischargeable).

37. *See* River Place E. Hous. Corp. v. Rosenfeld (*In re* Rosenfeld), 23 F.3d 833, 836 (4th Cir. 1994) (finding that postpetition HOA assessments do not meet the definition of "debt" at the time of filing because they arise from the declaration—a real property interest).

38. *See* Avellino & Bienes v. M. Frenville Co. (*In re* M. Frenville Co.), 744 F.2d 332, 336 (3d Cir. 1984) (describing a surety contract as having "a right to payment, albeit contingent, upon the signing of the agreement" (citing *In re* THC Fin. Corp., 686 F.2d 799, 802–04 (9th Cir. 1982)), *overruled by* Grossman's Inc. v. Brunt (*In re* Grossman's Inc.), 607 F.3d 114 (3d Cir. 2010) (en banc); *see also* EPSTEIN, *supra* note 5, § 3-6 ("A contract claim can arise as soon as the contract is made.").

39. *See* FREEDMAN & ALTER, *supra* note 22, at 82–83 (describing the declaration as a contract, but emphasizing that it is also a property interest).

40. *See In re Rosteck*, 899 F.2d at 697 (noting that the assessments were "discharged by the bankruptcy court in its discharge order"). In *Rosteck*, the debtors were sued for nonpayment of HOA fees several months after moving out and receiving a discharge. *Id.* at 695.

contingent future payments arising from a prepetition contract that "existed when [debtors] filed their bankruptcy petition."[41] The fact that the future assessments could not be levied against the debtor until a future date after filing did not preclude them from discharge.[42]

Courts that have found the declaration to be a prepetition contract rely on the expansive definition of "claim."[43] Congress intended "claim" to be construed as broadly as possible.[44] It includes *any* "right to payment, whether or not such right is . . . contingent, matured, [or] unmatured."[45] Claims are contingent "if the debt is one which the debtor will be called upon to pay only upon the occurrence or happening of an extrinsic event."[46] The

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41. *See id*. at 697 (noting that "the condominium declaration is a contract" and fees governed by that contract arise prepetition and are extinguished by bankruptcy discharge). Several other cases have determined that assessments arose from a prepetition contract. *See In re* Garcia, 168 B.R. 320, 326 (Bankr. E.D. Mich. 1993) (discharging accumulating assessments because they arise from a prepetition contract), *overruled by* Maple Forest Condo. Ass'n v. Spencer (*In re* Spencer), 457 B.R. 601, 609 (Bankr. E.D. Mich. 2011); *In re* Elias, 98 B.R. 332, 337 (Bankr. N.D. Ill. 1989) (determining assessments dischargeable because they "occur postpetition but arise out of a prepetition contract"); *In re* Ryan, 100 B.R. 411, 416 (Bankr. N.D. Ill. 1989) (determining that assessments arise from a prepetition contract (citing Household Fin. Corp. v. Hansberry, 20 B.R. 870, 873 (Bankr. S.D. Ohio 1982)).

42. *See In re* Rosteck, 899 F.2d 694, 696–97 (B.A.P. 7th Cir. 1990) (describing the date of payment as the maturing of a contingent liability); Cohen v. N. Park Parkside Cmty. Ass'n (*In re* Cohen), 122 B.R. 755, 758 (Bankr. S.D. Cal. 1991) ("The date on which the homeowner's association levied its assessments is irrelevant for determining when the debt arose.").

43. *See In re Rosteck*, 899 F.2d at 696–97 (noting that assessments coming due after filing satisfy the "broad definitions of claim and debt"); *In re* Pratola, 152 B.R. 874, 877 (Bankr. D.N.J. 1993) (recognizing that under the broad definition of "claim," "the debtor clearly had a debt for future condominium common expense assessments when she filed her bankruptcy petition"); *In re Elias*, 98 B.R. at 335 (stressing the broad definition of "debt" with legislative history).

44. *See* S. REP. NO. 95-989, at 22 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5808 ("By this broadest possible definition . . . the bill contemplates that all legal obligations of the debtor, no matter how remote or contingent, will be able to be dealt with in the Bankruptcy case."); *see also* Johnson v. Home State Bank, 501 U.S. 78, 83 (1991) ("Congress intended by [§ 101's] language to adopt the broadest available definition of 'claim.'" (citations omitted)).

45. 11 U.S.C. § 101(5)(A) (2010).

46. All Media Props., Inc. v. Best (*In re* All Media Props., Inc.), 5 B.R. 126, 133 (Bankr. S.D. Tex. 1980), *aff'd,* 646 F.2d 193 (5th Cir. 1981) (per curiam); *see also In re* Dill, 30 B.R. 546, 549 (B.A.P. 9th Cir. 1983) (noting that contingent

Rosteck court characterized accruing association assessments as contingent claims because debtors "agreed to make payments, but whether and how much they actually had to pay depended on future uncertain events," such as continued ownership and the association continuing to levy assessments.[47] Similarly, accruing assessments have been defined as "the periodic maturing of [the association]'s prepetition claim."[48]

The theory that assessments coming due after a debtor's filing are dischargeable because the declaration is a prepetition contract that becomes binding against the debtor upon taking ownership of the property has one serious flaw.[49] It is not clear whether a declaration is even a contract—it is not signed by the parties;[50] the declaration is missing other necessary components of a contract, including consideration and meeting of the minds;[51] the declaration is commonly described as a servitude and, therefore, outside the scope of contract law.[52]

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claims are those coming due on the occurrence of a future event).

47. *In re Rosteck*, 899 F.2d at 696–97. *But see In re* Spencer, 457 B.R. 601, 614 (Bankr. E.D. Mich. 2011) (describing "[t]he contingency upon which the bankruptcy courts in the *Rosteck* line of cases relied [a]s merely illusory [because] it remains within the power of a debtor to prevent the contingency."); Beeter v. Tri-City Prop. Mgmt. Servs., Inc. (*In re* Beeter), 173 B.R. 108, 123 (Bankr. W.D. Tex. 1994) ("There comes a point when a potential future liability becomes so speculative that it cannot justifiably be deemed a 'claim' for bankruptcy purposes."). Some courts require the contingency of "the uncertain future event . . . occur with some probability beyond the control of the debtor," unlike the debtor's ability to sell the property. *In re Spencer*, 457 B.R. at 613. Part III will argue that, given the current condition of the housing market, it may be that the debtors' ability to unilaterally relinquish title to an underwater property is illusory.

48. *In re* Wasp, 137 B.R. 71, 72 (Bankr. M.D. Fla. 1992) ("Any Association fees coming due after Debtors' filing of their bankruptcy petition were no more than unmatured portions of their original liability to the Association."); *In re* Turner, 101 B.R. 751, 754 (Bankr. D. Utah 1989), *superseded by In re* Colon, 465 B.R. 657 (Bankr. D. Utah 2011); *In re* Montoya*,* 95 B.R. 511, 513 (Bankr. S.D. Ohio 1988) (discharging accruing assessments as unmatured claims).

49. *See* FREEDMAN & ALTER, *supra* note 22, at 82 (noting that the obligation to pay assessments is binding upon ownership).

50. *See id*. at 61 (describing the declaration as a document that is filed with the locality by the developer).

51. *See In re Beeter*, 173 B.R. at 115 (noting that neither consideration nor meeting of the minds is present as required by contract law).

52. *See infra* note 63 and accompanying text (describing declarations and their accompanying assessments as based in real property law).

B. Declaration as an Executory Contract

A specific type of prepetition contract is an executory contract. If the declaration is deemed an executory contract, "it can be rejected, and any liability for future assessments would be relegated to the status of a prepetition claim, easily discharged in the bankruptcy process."[53] An executory contract is "a contract under which the obligation of both the [debtor] and the other party to the contract are so far unperformed that failure of either to complete performance would constitute a material breach excusing performance by the other."[54] Under this definition, the declaration may qualify: Associations have an ongoing obligation to provide services, while debtors have an ongoing obligation to pay assessments, and the failure of either to perform would be a material breach of the declaration.[55] For the reasons below, this theory has been widely dismissed.[56]

The primary reason this theory has been rejected is the same reason the *Rosteck* line is criticized—the declaration cannot be rejected as an executory contract because it is not a contract in the first place.[57] Rather, it is a servitude representing a real property interest.[58] Allowing the debtor to reject the declaration unilaterally would allow him to give up the burden of having to

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53. Beeter v. Tri-City Prop. Mgmt. Servs., Inc. (*In re* Beeter), 173 B.R. 108, 113–14 (Bankr. W.D. Tex. 1994).

54. Vern Countryman, *Executory Contracts in Bankruptcy: Part I*, 57 MINN. L. REV. 439, 460 (1973).

55. *See In re* Miller, 125 B.R. 441, 443 (Bankr. W.D. Pa. 1991) (describing the declaration as an executory contract). *But see* FREEDMAN & ALTER, *supra* note 22, at 82 ("[T]he obligation of the unit owner to pay assessments is independent of the association's obligation to maintain the premises.").

56. *See In re* Rivera, 256 B.R. 828, 834 (Bankr. M.D. Fla. 2000) (consolidating cases and providing three reasons a declaration is not an executory contract); *In re* Garcia, 168 B.R. 320, 324 (Bankr. E.D. Mich. 1993) ("[R]eject[ing] the concept that condominium fees in this case represent an executory contract."), *overruled by* Maple Forest Condo. Ass'n v. Spencer (*In re* Spencer), 457 B.R. 601, 609 (Bankr. E.D. Mich. 2011); *In re* Case, 91 B.R. 102, 103–04 (Bankr. D. Colo. 1988) (rejecting the notion that the declaration constituted an executory contract).

57. *See In re Case*, 91 B.R. at 104 (rejecting the executory contract theory because the "declaration creates and defines the Debtors' interests in the real property" rather than in contract).

58. *See infra* note 63 and accompanying text.

pay, but continue to accept the benefits of ownership.[59] Even if the court establishes that an executory contract exists, 11 U.S.C. § 365[60] gives only the trustee and not the debtor the power to reject it.[61] The executory contract definition requires a material breach by a party to the contract, so trustee rejection "would not constitute a breach relieving the debtor of the debtor's obligation to perform" because the trustee is not a party to the contract.[62] Accordingly, the declaration cannot be considered an executory contract for the purpose of determining if assessments are prepetition debts.

C. Declaration as a Property Interest

The problem with the contract theories noted in subparts A and B is that the declaration is a covenant that runs with the land, giving the association a real property interest in the debtor's property.[63] The association's interest in its members'

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59. *See* Beeter v. Tri-City Prop. Mgmt. Servs., Inc. (*In re* Beeter), 173 B.R. 108, 115 (Bankr. W.D. Tex. 1994) ("In order for a debtor to 'reject' a declaration . . . the debtor would also have to somehow 'part' with the benefits of the putative 'executory contract,' [which is] not possible."); *see also In re Rivera*, 256 B.R. at 834 ("[D]ebtor cannot simultaneously accept the benefits and reject the burdens of an executory contract. . . ." (citing *In re Beeter*, 173 B.R. at 113–16)). *But see In re Miller*, 125 B.R. at 443 (allowing debtor to reject his executory contract).

60. *See* 11 U.S.C. § 365 (2005) (providing the Code's treatment of executory contracts but giving no definition for one).

61. *See id.* (giving the trustee the power to "assume or reject any executory contract"); *see also* Eastover Bank for Sav. v. Sowashee Venture (*In re* Austin Dev. Co.), 19 F.3d 1077, 1081 (5th Cir. 1994) (distinguishing "rejection" from "termination" of the contract); *In re* Raymond, 129 B.R. 354, 358 (Bankr. S.D.N.Y. 1991) (analogizing trustee's rejection of a declaration to a trustee's rejection of a lease).

62. *See In re* Rivera, 256 B.R. 828, 834 (Bankr. M.D. Fla. 2000); *see also* Behrens v. Woodhaven Ass'n, 87 B.R. 971, 974 (Bankr. N.D. Ill. 1988) ("[The association] does not seek to enforce this contract against the trustee or the estate. It seeks to enforce the contract against the Debtors personally. The Debtors could not assume or reject that contract under 11 U.S.C. § 365.").

63. *See* River Place E. Hous. Corp. v. Rosenfeld (*In re* Rosenfeld), 23 F.3d 833, 833 (4th Cir. 1994) ("The key to distinguishing a right to payment that is or is not subject to . . . discharge is simply whether the right to payment is based on a property interest or something else."); *see also* FREEDMAN & ALTER, *supra* note 22, at 62, 82 (describing declarations as "servitudes running with the land," creating a real property interest). The affirmative covenant "for the payment of

properties is protected by the Fifth Amendment of the Constitution.[64] As a property interest, there are two reasons to call into question whether the association's right to payment constitutes a prepetition debt. First, as a property interest, the enforceable obligation against the debtor for assessments arises through the continued ownership of the property after filing—a postpetition act.[65] Second, secured property interests are protected under the Code and generally survive discharge.[66]

The distinction between secured claims against debtors' real property and claims against debtors individually, and the ability to separate them, is crucial to this theory. The Supreme Court in *Johnson v. Home State Bank*[67] used the "enforceable obligation" interpretation of "right to payment" to distinguish the lender's dischargeable claim against the debtor (the in personam liability) from the nondischargeable claim against the property (the in rem liability).[68] Upon the debtor's discharge, the lender could not seek

money" is a real property interest if it is deemed to run with the land. *See* SERVITUDES, *supra* note 2, § 1.3; *see also id.* cmt. e ("[It is] a servitude if either the benefit or the burden runs with the land."). While states differ in their requirements for a covenant to run with the land, laws uniformly provide that an association's declaration for assessments runs with the land. *See* HYATT & DOWNER, *supra* note 21, § 6.3 ("[I]f carefully drafted, the affirmative covenant to pay assessments to the association runs with the land and is binding on all successors-in-title."). The law is moving towards reliance on the intention of the parties rather than formalities in determining whether a covenant runs with the land. *See* SERVITUDES, *supra* note 2, § 2.4 cmt. 1 (noting that the majority of states have done away with horizontal privity as a requirement for a covenant to run with the land).

64. *See, e.g.*, *In re Rivera*, 256 B.R. at 833–34 ("A homeowners' association's right to impose postpetition assessments pursuant to a recorded Declaration of Covenants and Restrictions is within the scope of the traditional property interests protected by the Fifth Amendment.").

65. *See* Maple Forest Condo. Ass'n v. Spencer (*In re* Spencer), 457 B.R. 601, 607 (Bankr. E.D. Mich. 2011) (noting that the obligation to pay assessments comes from "the act of retaining ownership of the property").

66. *See* 11 U.S.C. § 524(a)(2) (2010) (declining to apply the discharge to claims against debtor's property).

67. *See* Johnson v. Home State Bank, 501 U.S. 78, 83 (1991) (holding that "[a] surviving mortgage interest [of a Chapter 7 discharge] corresponds to an 'enforceable obligation' of the debtor").

68. *See id.* at 85–86 (noting that such interpretation of "claim" was consistent with the Code's structure); *see also* Cen-Pen Corp. v. Hanson, 58 F.3d 89, 92 (4th Cir. 1995) (noting that discharge has "no effect on an *in rem* claim against the debtor's property").

payment from the debtor.[69] Rather, it would be limited to foreclosing and satisfying its claim with the collateral sale proceeds.[70]

Like a mortgage, the declaration creates a nondischargeable lien against the debtor's property that enables the "creditor to seek satisfaction from a particular piece of property."[71] Unlike a mortgage, in which "the in personam liability on a mortgage is a matter of contract," the covenant to pay assessments "is an integral part of the property which the debtor acquired when the debtor [took] title to the property."[72] Thus, the association's claim against the debtor for future assessments cannot be separated from its interest in the debtor's property.[73] The result is a debtor's personal obligation to pay assessments, like any other servitude running with the land, which cannot be discharged as a claim against the debtor individually.[74]

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69. *See* 11 U.S.C. § 524(a)(1) (2010) (precluding creditors from attempting to collect debts against the debtor after discharge).

70. *See Johnson*, 501 U.S. at 86.

71. FREEDMAN & ALTER, *supra* note 22, at 83.

72. *In re* Rivera, 256 B.R. 828, 833–34 (Bankr. M.D. Fla. 2000); *see also* Liberty Cmty. Mgmt., Inc. v. Hall (*In re* Hall), 454 B.R. 230, 241 (Bankr. N.D. Ga. 2011) (distinguishing a covenant to pay assessments from a mortgage). The *Hall* court distinguished a covenant to pay HOA assessments from a mortgage by noting that mortgages are based on a debt while assessments are based on a covenant. *See id.* Further, the assessments could not be liquidated upon default like a mortgage, and the duty to pay assessments ended upon terminating ownership, whereas a borrower is obligated to pay his mortgage postownership unless released. *See id.*

73. *See* Maple Forest Condo. Ass'n v. Spencer (*In re* Spencer), 457 B.R. 601, 607 (Bankr. E.D. Mich. 2011) ("The obligations [to pay future assessments] affix and inhere in the property itself."). *But see In re* Wasp, 137 B.R. 71, 73 (Bankr. M.D. Fla. 1992) (distinguishing the discharged personal obligation to pay assessments from the claim the association has against the property for unpaid assessments).

74. *See* Beeter v. Tri-City Prop. Mgmt. Servs., Inc. (*In re* Beeter), 173 B.R. 108, 118 (Bankr. W.D. Tex. 1994) (comparing the obligation to pay assessments to "prohibitions on making changes to the exterior of the unit," which are not considered dischargeable claims); SERVITUDES, *supra* note 2, § 7.9 ("No servitude . . . is extinguishable in a bankruptcy proceeding, unless otherwise required by statute."). *But see* Cohen v. N. Park Parkside Cmty. Ass'n (*In re* Cohen), 122 B.R. 755, 758 (Bankr. S.D. Cal. 1991) (discharging accruing assessments arising from a covenant running with the land because the signing of the covenants, conditions, and restrictions (CC&Rs) took place before filing).

This concept—that the claim for assessments arises from a nondischargeable property interest with the personal obligation to pay assessments inextricably intertwined—is the position held by a strong majority of courts.[75] As a property interest, it must survive discharge.[76] The reason is simple; a debtor should not, upon discharge, be entitled to more property rights than he had before the bankruptcy.[77]

If a debtor entered a prepetition contract to pay his neighbor $100 to cut his grass for each of the next twelve months, the debtor, upon meeting certain criteria, could avoid future payments by filing bankruptcy because the obligation arose before filing, even if payment was secured by debtor's property. If, however, the debtor and his neighbor each gave the other a property interest—such as an equitable servitude—in the other's land in exchange for lawn care, it could not be discharged because the "prepetition ownership or covenanting ownership" does not create the obligation to pay assessments;[78] rather, the postpetition "act of retaining ownership" would alone create the neighbor's right to payment.[79]

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75. *See In re Beeter*, 173 B.R. at 122 ("[E]ach new month's ownership carries with it a new personal liability, arising out of the equitable servitude that burdens that ownership.").

76. *See, e.g.*, 11 U.S.C. § 524(a)(1) (2010) (declining to include secured claims against property within the scope of discharge); *see also* TABB, *supra* note 14, § 10.1 (noting that claims against "the debtor's property are not discharged").

77. *See* Cen-Pen Corp. v. Hanson, 58 F.3d 89, 93 (4th Cir. 1995) ("The simple expedient of passing their residence through the bankruptcy estate could not vest in the [debtors] a greater interest in the residence than they enjoyed prior to filing. . . ." (citing Second Nat'l Bank of Saginaw v. Honaker (*In re* Honaker), 4 B.R. 415, 417 (Bankr. E.D. Mich. 1980)). If association members could rid themselves of the obligation to pay assessments in the future by simply filing bankruptcy, the property rights of all other members would be substantially burdened.

78. *In re Spencer*, 457 B.R. at 607; *In re Beeter*, 173 B.R. at 118 ("Simply locating the source of the obligation as the Declaration, and noting that the property was purchased prior to filing the petition does not end the inquiry, for the nature and *duration* of the obligation and its attachment to an interest in property necessarily complicates the issue.").

79. Maple Forest Condo. Ass'n v. Spencer (*In re* Spencer), 457 B.R. 601, 607 (Bankr. E.D. Mich. 2011); *see also In re Beeter*, 173 B.R. at 122 ("[T]he liability does not arise 'as of' the day the debtor acquires the property, but 'as a result of' the fact that, on the first of any given month, the debtor is the current owner of the property.").

D. Right to Payment Determined by State Cause of Action

In addition to defining the declaration as a prepetition contract or property interest to determine when the claim for assessments arises, some courts have relied on when the association could sue the debtor for unpaid assessments. In *Maple Forest Condominium Ass'n v. Spencer*,[80] the court determined the association's right to future assessments was a postpetition debt because no state-law cause of action for the assessments existed on the date of filing.[81] Similarly, the court in *Liberty Community Management, Inc. v. Hall*[82] found no right to payment existed because the association had no "right to enforce payment" at the time of filing.[83] In effect, because an action for missed payments cannot be brought until they are in fact missed, there is no right to payment at the time of filing, rendering the claim postpetition and nondischargeable.[84]

The problem with the analysis used by the *Hall* and *Spencer* courts is that it replicates the test used in *Avellino & Bienes v. M.*

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80. *See In re Spencer*, 457 B.R. at 616 (determining that an association's claim for unpaid assessments coming due after debtor's filing is not discharged). In *Spencer*, the debtor surrendered his condominium around the date of filing his petition, but the lender took no action, even after the automatic stay was lifted. *See id*. at 604 (noting that the lender could foreclose on the property but had not done so). The association filed a complaint "seeking declaratory judgment that postpetition assessments were not discharged by the bankruptcy proceedings." *Id*. at 605.

81. *See id*. at 606 (noting that because the association had no lawful right to future assessments on the date of filing, no right to payment existed).

82. *See* Liberty Cmty. Mgmt., Inc. v. Hall (*In re* Hall), 454 B.R. 230, 241 (Bankr. N.D. Ga. 2011) (determining assessments arise postpetition because a "creditor's right to payment simply does not exist at the time of a debtor's bankruptcy filing"). In *Hall*, the condominium association filed a proof of claim for unpaid arrears three years after the petition was filed, and debtor sought a court order finding the association in violation of the automatic stay. *See id*. at 232. The court described the obligation to pay HOA assessments as "an ongoing service contract" that required payment from the owner at the time payment was due. *Id*. at 234.

83. *Id*. at 234 ("For instance, [the association] would not be able to assess a lien or sue for the unpaid post-petition assessments because the assessments do not even exist.").

84. *See In re Spencer*, 457 B.R. at 606 (determining that the association could not have brought any action for postpetition assessments as of the day of petition).

Frenville Co.,[85] a Third Circuit case that has received much criticism for its reliance on state law to determine when a claim arises.[86] If dischargeable claims exist only if the creditor could have sued on the date of filing, too many otherwise-dischargeable claims would be precluded from discharge, which is contrary to Congress's broad definition of "claim."[87] Accordingly, this approach to determine when assessments arise, like the executory contract approach, is inappropriate.

E. Conclusion on Claim

Because the use of an executory contract and *Frenville* analysis are inappropriate to determine if accruing assessments are prepetition debts, the determination turns on the prepetition contract–property interest distinction. If accumulating assessments cannot be cabined within § 101(5)'s broad definition, "the policies underlying the fresh start, implemented by the grant of the discharge in bankruptcy, would be unacceptably compromised" because debtors will continue to be responsible for accruing assessments after filing and subsequent discharge.[88] The legislative history of § 523(a)(16), discussed in Part III, cites

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85. *See* Avellino & Bienes v. M. Frenville Co. (*In re* M. Frenville Co.), 744 F.2d 332, 337 (3d Cir. 1984) (determining a claim arises when a state cause of action can be brought (citing Vanston Bondholders Prot. Comm. v. Green, 329 U.S. 156, 161 (1946))), *overruled by* Grossman's Inc. v. Brunt (*In re* Grossman's Inc.), 607 F.3d 114 (3d Cir. 2010) (en banc). In *Frenville*, the creditor sought relief from the automatic stay to include the Chapter 7 debtors "as third-party defendants in the New York state [indemnification] proceeding." *Id.* at 334–35. The issue was whether a right to payment existed at filing if the cause of action "did not arise until after . . . filing." *Id.* at 335.

86. *See, e.g.*, Firearms Imp. & Exp. Corp. v. United Capital Ins. Co. (*In re* Firearms Imp. & Exp. Corp.), 131 B.R. 1009, 1015 (Bankr. S.D. Fla. 1991) (describing *Frenville* "as one of the most criticized and least followed precedents decided under the current Bankruptcy Code"); *see also* EPSTEIN, *supra* note 5, § 11-3 ("Even if state law determines the existence of a claim (i.e., if a claim exists), it is entirely appropriate for federal bankruptcy law to determine, for bankruptcy purposes, *when* the claim arises.").

87. *See In re Grossman's Inc.*, 607 F.3d at 121 (overturning *Frenville* because of its conflict with the Code's broad treatment of "claim").

88. *In re* Montoya, 95 B.R. 511, 514 (Bankr. S.D. Ohio 1988); *see also* Behrens v. Woodhaven Ass'n, 87 B.R. 971, 975 (Bankr. N.D. Ill. 1988) (noting that to hold otherwise would "effectively gut the careful protections Congress afforded" debtors).

Rosteck, indicating Congress, in protecting associations, believed it was excluding from discharge an otherwise dischargeable prepetition contract.[89] Therefore, the Section is not superfluous.

If Congress thought it was excluding a prepetition claim from discharge when enacting § 523(a)(16), then accumulating assessments should be discharged as prepetition contracts in Chapter 13 cases in which § 523(a)(16) does not apply.[90] Surprisingly, courts in Chapter 13 cases continue to disagree over whether the declaration is a prepetition contract or a nondischargeable property interest.[91] It seems unlikely that Congress meant § 523(a)(16) to serve a clarification role for two reasons: First, the Section includes no language about the timing of the debt.[92] Second, it seems impractical to clarify assessments in Chapter 7 cases, but decline to do so in the Chapter 13 cases.[93] Accordingly, we can surmise that by purposely excluding a prepetition claim from discharge, Congress intended to pursue some kind of policy objective.

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89. *See* 140 CONG. REC. 27,687 (1994) (recognizing that assessments accruing after discharge would otherwise be dischargeable).

90. *See* 11 U.S.C. § 1328(a) (2005) (defining the scope of Chapter 13 discharge, but declining to incorporate § 523(a)(16)); *see also In re* Hawk, 314 B.R. 312, 316–17 (Bankr. D.N.J. 2004) ("By defining the parameters of when post-petition fees and assessments can and cannot [be] discharged, Congress was implicitly stating that these future assessments are claims."). *But see* Foster v. Double R Ranch Ass'n (*In re* Foster), 435 B.R. 650, 659 (B.A.P. 9th Cir. 2010) (doubting that "the omission of § 1328(a) in § 523(a)(16) or vice versa evinces a legislative intent" that assessments be dischargeable under § 1328(a)).

91. *Compare In re Hawk*, 314 B.R. at 316 (determining that postpetition assessments "are a pre-petition claim because they arose upon the Debtor taking title to the property, which occurred pre-petition"), *with In re Foster*, 435 B.R. at 662 (noting that the nondischargeability of accruing assessments is warranted because "debtor's continued interest in real property").

92. *See* CHARLES JORDAN TABB, THE LAW OF BANKRUPTCY § 10.25 (1997) ("Nothing in the 1994 amendment of [§ 523(a)(16)] alters the time when the claim is deemed to arise.").

93. *But see* Liberty Cmty. Mgmt., Inc. v. Hall (*In re* Hall), 454 B.R. 230, 238 (Bankr. N.D. Ga. 2011) ("It is just as likely that Congress was implying that post-petition assessments are not really claims at all, and that the amendment was necessary to correct the mischaracterization of post-petition assessments as claims.").

III. Statutory Exemption from Discharge

An otherwise dischargeable claim may be excluded from discharge by 11 U.S.C. § 523.[94] Section 523 serves as the Code's "gatekeeper," excluding claims from discharge that Congress deems unworthy to "partake[e] in the system's benefits."[95] The exceptions to discharge represent the "policy considerations" of Congress as to which debts should survive discharge.[96] This Part will first lay out the history and policy considerations behind § 523(a)(16). Because we know from Part II that Congress likely intended future assessments to be deemed dischargeable debts, this Part will conclude by critiquing the policy considerations behind § 523(a)(16) and comparing the intended results to the actual.

A. Bankruptcy Reform Act of 1994

The Bankruptcy Reform Act of 1994 (1994 Reform Act)[97] included the initial version of § 523(a)(16),[98] representing Congress's first accorded protection to associations. The Section provided:

> (a) A discharge . . . does not discharge an individual debtor from any debt—
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> . . . .

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94. *See* 11 U.S.C. § 523 (2010) (providing an exclusionary list of excluded claims from Chapter 7 discharge); *see also* 11 U.S.C. § 727(a) (2005) (incorporating all of § 523 into a Chapter 7 discharge); *id.* § 1328(a) (providing Chapter 13 debtor with a "superdischarge" by only incorporating portions of § 523 and, thus, allowing for more dischargeable claims).

95. GROSS, *supra* note 15, at 27–28; *see also* Howard, *supra* note 15, at 1050–58 (noting the concern for dishonest debtors taking advantage of the bankruptcy system and the additional protection required by certain creditors).

96. Singer, *supra* note 14, at 336. *But see* EPSTEIN, *supra* note 5, § 7-24 (noting that not "everyone would agree to those policies").

97. *See* Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, 108 Stat. 4106 (codified as amended in scattered sections of 11 U.S.C.), *amended by* BAPCPA.

98. *See id.* § 309 (codified as amended at 11 U.S.C. § 523(a)(16) (1994)) (current version at 11 U.S.C. § 523(a)(16) (2010)) (excluding postpetition condominium and cooperative housing dues from dischargeability if certain requirements are met).

> (16) for a fee or assessment that becomes due and payable after the order for relief to a membership association with respect to the debtor's interest in a dwelling unit that has condominium ownership or in a share of a cooperative housing corporation, but only if such fee or assessment is payable for a period during which—
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> (A) the debtor physically occupied a dwelling unit in the condominium or cooperative project; or
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> (B) the debtor rented the dwelling unit to a tenant and received payments from the tenant for such period, but nothing in this paragraph shall except from discharge the debt of a debtor for a membership association fee or assessment for a period arising before entry of the order for relief in a pending or subsequent bankruptcy case.[99]

The legislative history of the Section indicates that Congress sought to protect associations from the abuse of freeriding member-debtors—those discharged debtors who continued to inhabit their property, pay their mortgages, and receive all the benefits of ownership, but refused to pay their ongoing association fees.[100] By allowing assessments to be discharged if the debtor no longer resided in or rented out the property, Congress seems to have avoided the question of whether accumulating assessments constitute a dischargeable prepetition debt, and attempted to achieve a policy goal.[101] This "you stay, you pay" theory paralleled a pre-existing line of cases that discharged accumulating assessments only if debtor vacated the property.[102] This line of cases had balanced the Code's desire to

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99. *Id.*

100. *See* 140 CONG. REC. S4526 (daily ed. Apr. 20, 1994) (statement of Sen. Strom Thurmond) (noting that association members "may be unfairly burdened by increases in their association fees if their neighbors declare bankruptcy and receive a discharge of the association fees which are due in the future").

101. *See* Old Bridge Estates Cmty. Ass'n v. Lozada (*In re* Lozada), 214 B.R. 558, 561 (Bankr. E.D. Va. 1997) (interpreting the Reform Act's § 523(a)(16) as striking "an equitable balance" between courts finding that accruing assessments arise prepetition and those finding that the assessments arise postpetition), *aff'd* 176 F.3d 475 (E.D. Va. 1999) (per curiam).

102. *See In re* Pratola, 152 B.R. 874, 876 (Bankr. D.N.J. 1993) (holding an association in contempt for attempting to collect assessments after the debtor vacated the property), *superseded by In re* Mattera, 203 B.R. 565 (Bankr. D.N.J. 1997); *In re* Ryan, 100 B.R. 411, 416 (Bankr. N.D. Ill. 1989) ("If . . . the debtor surrenders possession and tenders the ownership interest to the association before or upon filing a petition . . . [the] obligation to pay postpetition

provide debtors with a fresh start and the protection associations required from freeriding members who remained on the premises.[103]

The 1994 version of § 523(a)(16) did, however, create some problems. It referred to condominium and cooperatives assessments but failed to mention homeowner associations.[104] This omission created confusion as to whether the Section applied to HOA assessments.[105] The Section also did not apply to Chapter 13 debtors because § 1328(a),[106] defining the scope of Chapter 13 discharge, did not include reference to § 523(a)(16).[107] In Chapter 13 cases, courts continued to disagree on whether accruing assessments constituted a dischargeable debt.[108] The Section was also criticized for not affording associations enough protection

assessments may be discharged."); *In re Montoya,* 95 B.R. 511, 513 (Bankr. S.D. Ohio 1988) (finding accumulating assessments dischargeable because the debtor vacated the property upon filing). *But see* Beeter v. Tri-City Prop. Mgmt. Servs., Inc. (*In re* Beeter), 173 B.R. 108, 112 (Bankr. W.D. Tex. 1997) (describing this line of cases as "results-oriented" with no basis in the Code).

103. *See In re Ryan*, 100 B.R. at 416 (describing its decision as "a fair accommodation of the rights and needs of the association while accomplishing the broad goals of the Bankruptcy Code"); *see also In re Pratola*, 152 B.R. at 877 (describing the *Ryan* rule as a "fair compromise" between debtor's entitlement to a fresh start and the potential abuses by freeriding debtors).

104. *See* Reform Act § 309 (codified as amended at 11 U.S.C. § 523(a)(16) (1994)) (current version at 11 U.S.C. § 523(a)(16) (2010)) (omitting homeowner association dues from the discharge exclusion).

105. *Compare In re Lozada*, 214 B.R. at 563 (determining that "homeowner's assessments and fees do not fall within the provisions of § 523(a)(16)" because they were left out of the statute's unambiguous language), *with In re* Rivera, 256 B.R. 828, 832 (Bankr. M.D. Fla. 2000) (referring to the legislative history's clear intention to include homeowner association assessments).

106. *See* Reform Act § 302 (codified as amended at 11 U.S.C. § 1328(a) (1994)) (current version at 11 U.S.C. § 1328(a) (2005)).

107. *See id*. (excluding § 523(a)(16) as an exception from Chapter 13 discharge).

108. *Compare In re* Mattera, 203 B.R. 565, 567–68 (Bankr. D.N.J. 1997) (finding that a Chapter 13 debtor's ongoing HOA assessments were "contingent, unmatured, unliquidated and unfixed debt[s]" that were dischargeable if provided for in the plan), *with* Montclair Prop. Owners Ass'n, Inc. v. Reynard (*In re* Reynard), 250 B.R. 241, 244 (Bankr. E.D. Va. 2000) (finding HOA assessments assessed after filings are properly classified as postpetition rather than prepetition debts and are, therefore, nondischargeable even if included in the plan (citing River Place E. Hous. Corp. v. Rosenfeld (*In re* Rosenfeld), 23 F.3d 833, 837 (4th Cir. 1994))).

because associations would be harmed if they could not collect from vacating debtors.[109]

B. Bankruptcy Abuse Prevention and Consumer Protection Act of 2005

In 2005, Congress enacted BAPCPA in an attempt to curb the perceived abuse of the Code.[110] The overhaul expanded § 523(a)(16)'s[111] exclusion of accruing assessments from discharge to a complete bar, regardless of whether the debtor continued to inhabit or rent out the property:

> (a) A discharge . . . does not discharge an individual debtor from any debt—
>
> . . . .
>
> (16) for a fee or assessment that becomes due and payable after the order for relief to a membership association with respect to the debtor's interest in a unit that has condominium ownership, in a share of a cooperative corporation, or a lot in a homeowners association, for as long as the debtor or the trustee has a legal, equitable, or possessory ownership interest in such unit, such corporation, or such lot, but nothing in this paragraph shall except from discharge the debt of a debtor for a membership association fee or assessment for a period arising before entry of the order for relief in a pending or subsequent bankruptcy case.[112]

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109. *See* Alfred Q. Ricotta, Note & Comment, *Community Association and Bankruptcy: Why Postpetition Assessments Should Not Be Dischargeable*, 15 BANKR. DEV. J. 187, 217–20 (1998) (proposing that Congress again amend § 523(a)(16) to a flat exclusion of association fees from dischargeability).

110. *See* H.R. REP. NO. 109-31, at 1 (2005), *reprinted in* 2005 U.S.C.C.A.N. 88, 88 (responding to "many of the factors contributing to the increase in consumer bankruptcy filings"). The general consensus is that the BAPCPA amendments were a continuation of a trend to shift the Code from a previously debtor-friendly Code to one giving more preference to creditors. *See* Donald Hackney, Matthew McPherson, & Daniel Friesner, *Investigating the Unintended Consequences of the 2005 BAPCPA "Means Test" on the Bankruptcy Chapter Choice Decision*, 4 J. ECON. BANKING & FIN. 1, 2 (2011) ("BAPCPA provides a thorough overhaul of the Bankruptcy Code, generally rendering the Code more creditor-friendly.").

111. *See* BAPCPA § 412 (codified as amended at 11 U.S.C. § 523(a)(16) (2005)) (current version at 11 U.S.C. § 523(a)(16) (2010)).

112. *Id.*

The amendment's legislative history evinces an intention "to broaden protections accorded to community associations with respect to fees or assessments . . . irrespective of whether or not the debtor physically occupies such property."[113] Courts, in Chapter 7 cases, concede the Section is intended to "preempt any argument that postpetition fees and assessments should be considered prepetition obligations."[114] The Section, as amended, remains inapplicable to Chapter 13 cases.[115] In Chapter 13 cases, courts continue to struggle in determining whether accumulating assessments constitute a dischargeable claim under § 101(5).[116]

C. BAPCPA § 523(a)(16)'s Death-Trap

Armed with the history and policy goals of § 523(a)(16), its effectiveness can now be critiqued. First, it must be determined if the Section was amended under the faulty assumption that vacating debtors could easily divest themselves of ownership and

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113. *See* H.R. REP. NO. 109-31, at 68, *reprinted in* 2005 U.S.C.C.A.N. 88, 154. Compared to the legislative history of the 1994 creation of § 523(a)(16), the reasons for the 2005 expansion of § 523 seemed to not have been debated. *See* Pigg v. BAC Home Loans Servicing, LP (*In re* Pigg), 453 B.R. 728, 733 (Bankr. M.D. Tenn. 2011) (describing § 523(a)(16)'s expanded coverage as "the result of some special interest lobbying"); *see also* Thomas F. Waldron & Neil M. Berman, *Principled Principles of Statutory Interpretation: A Judicial Perspective After Two Years of BAPCPA*, 81 AM. BANKR. L.J. 195, 216 (2007) ("[I]t is not clear what helpful legislative history exists for BAPCPA.").

114. *In re* Ames, 447 B.R. 680, 682 n.3 (Bankr. D. Mass. 2011); *see also In re* Barr, 457 B.R. 733, 738 (Bankr. N.D. Ill. 2011) (finding that § 523(a)(16) forbids the discharge of debtor's accruing assessments); *In re Pigg*, 453 B.R. at 732 (recognizing the "harsh" application of § 523(a)(16) to the facts).

115. *See* 11 U.S.C. § 523(a) (excluding Chapter 13 discharge under § 1328(a) from its application). *But see id*. (incorporating § 1328(b) for Chapter 13 debtors seeking a hardship discharge). Courts are in consensus on the fact that § 523(a)(16) does not affect Chapter 13 discharge. *See, e.g.*, Foster v. Double R Ranch Ass'n (*In re* Foster), 435 B.R. 650, 658–59 (B.A.P. 9th Cir. 2010) (noting "that § 523(a)(16) is inapplicable to the discharge under § 1328(a)"); *In re* Danastorg, 382 B.R. 585, 588 (Bankr. D. Mass. 2008) ("[T]he Court finds that section 523(a)(16) is inapplicable to Chapter 13 cases . . . .").

116. *Compare In re* Colon, 465 B.R. 657, 660 (Bankr. D. Utah 2011) (determining accumulating "HOA assessments meet the definition of 'claim' under § 101(5) and 'claims' can be provided for in chapter 13 plans"), *with In re Foster*, 435 B.R. at 660–61 (finding the association's claims for assessments do not arise until after discharge because they arise from a covenant running with the land rather than a prepetition contract).

escape nondischargeable accruing assessments. Second, if § 523 is where Congress excludes debts from discharge to achieve policy goals, it must be determined if the policies behind § 523(a)(16) were achieved. Third, if § 523 is a gatekeeper, excluding bad faith debts from discharge, it must be determined whether the breadth of the statute is overinclusive, engulfing honest debtors.

1. BAPCPA's Faulty Assumptions and Disincentive to Foreclose

Before critiquing the policies and goals of § 523(a)(16), it is important to recognize that the primary problem faced by debtors is foreclosure delay by lenders. Debtors, who have surrendered and vacated their property, continue to be burdened with accumulating assessments. They wait helplessly for their lenders to exercise their foreclosure rights, the delay of which may benefit the lenders.[117] Section 523(a)(16) was likely amended under the assumption that lenders would continue to promptly foreclose on surrendered properties as they had done in the past, or that debtors would continue to have alternative ways to divest themselves of property. The combination of the mortgage crisis and the inability for debtors to divest themselves of their property has proven this assumption defective.

a. The Mortgage Crisis

Prior to BAPCPA's enactment in 2005, home prices had been steadily increasing for the previous fifteen years.[118] With the choice to foreclose and resell the collateral at a small loss or to just let the property sit vacant bringing in no money, lenders generally found it beneficial to accept the inevitable foreclosure cost and resell the property.[119] Unfortunately, home prices fell

117. *See In re Pigg*, 453 B.R. at 735 (noting that no law requires foreclosure and that lenders may find it advantageous to not foreclose on underwater properties in the current depressed real estate market).

118. *See Historical Data Exhibit 9. Existing Home Prices: 1969–Present*, *supra* note 6 (indicating that median sales prices for existing homes of $96,400 in 1990, $114,600 in 1995, $143,600 in 2000, and $219,600 in 2005).

119. *See* Maple Forest Condo. Ass'n v. Spencer (*In re* Spencer), 457 B.R. 601, 612 (Bankr. E.D. Mich. 2011) ("In ordinary circumstances, a creditor with a

substantially[120] and "11 million, or 23 percent, of all residential propert[y owners] with mortgages [now have] negative equity."[121] Today, on average, a lender takes 647 days to complete the foreclosure process and auction off the property.[122] Several factors, resulting primarily from the mortgage crisis, may be causing lenders to delay the sale of foreclosed property.

First, as delinquencies have increased,[123] the number of foreclosures has risen substantially,[124] creating a backlog of paperwork and slowing lenders as they attempt to complete foreclosures.[125] Second, the oversupply of foreclosed properties has saturated the market, driving home prices down.[126] Lenders

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senior security interest in real property will act to foreclose upon the property or accept a deed in lieu of foreclosure soon after the lifting of the bankruptcy stay.").

120. *See Historical Data Exhibit 9. Existing Home Prices: 1969–Present*, *supra* note 6 (reporting a median inflation-adjusted existing home sales price of $221,900 in 2006, $198,100 in 2008, and $172,900 in 2009). "The foreclosure crisis, generally considered the worst since the Great Depression of the 1930s, began in late 2006." James R. Hagerty, *Foreclosures, Overdue Mortgages Increase Again: Troubles Extend Into Prime Loans Via Option ARMs*, WALL ST. J., Sept. 6, 2008, at A3.

121. CoreLogic, *supra* note 7. These homeowners are commonly referred to as being "underwater" or "upside-down" in their mortgage. *See* David Streitfeld, *No Help in Sight, More Homeowners Walk Away*, N.Y. TIMES, Feb. 3, 2010, at A1 (describing an underwater home as a property with a mortgage valued as greater than the fair market value of the property).

122. Christie, *supra* note 8. In Florida and New York, the average time between default and actual foreclosure relieving the borrower of all ownership is 1,027 and 906 days, respectively. *Id*.

123. *See Table 1194. Delinquency Rates and Charge-Off Rates on Loans at Insured Commercial Banks: 1990 to 2009*, U.S. CENSUS BUREAU, http://www.census.gov/compendia/statab/2011/tables/11s1194.pdf (indicating an increase in the percentage of residential mortgages in delinquency from 1.55% in 2005 to 9.10% in 2009).

124. *See Table 1193. Mortgage Originations and Delinquency Foreclosure Rates: 1990 to 2009*, U.S. CENSUS BUREAU, http://www.census.gov/compendia/statab/2011/tables/11s1193.pdf (indicating an increase from $1 billion worth of mortgages in the foreclosure process in 2005 to $4.6 billion in foreclosure in 2009).

125. *See* Maple Forest Condo. Ass'n v. Spencer (*In re* Spencer), 457 B.R. 601, 612 (Bankr. E.D. Mich. 2011) ("The confluence of economic forces has flooded the market [with foreclosures] and jammed the usual flow of the foreclosure process, with upstream effects on bankruptcy proceedings.").

126. *See* Nick Timiraos, *Home Sales Climb But Prices Decline*, WALL. ST. J., Nov. 22, 2011, at A4 (estimating "that there are 1.6 million single-family homes in some stage of default or foreclosure that will ultimately be taken back and

are choosing to temporarily refrain from foreclosing with the hope that reduced supply may allow home prices to level out or possibly increase.[127] Third, in response to the increased rate of foreclosures and public outcry, legislatures and courts have increased the hurdles for lenders to foreclose through consumer protection laws and judicially mandated procedural requirements.[128]

BAPCPA's version of § 523(a)(16) was presumably passed with the assumption that home prices would continue to rise and lenders would find it in their best interest to foreclose.[129] In the event a lender chooses not to promptly sell collateral, increased home prices would provide debtor-members with the needed equity to sell the property themselves and escape accruing assessments. If the amendment was passed on these failed premises, then reason exists to amend it.

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resold by banks over the next 18 months").

127. *See In re Spencer*, 457 B.R. at 612 ("With mortgage debt frequently exceeding the value of the property and limited demand in the market, lenders have less incentive to move swiftly because they can no longer expect to obtain full satisfaction on their loans."); *see also* Antoinette Martin, *Many Foreclosures, Few Listings*, N.Y. TIMES, Oct. 16, 2011, at RE8 (noting that the number of homes being foreclosed upon is not keeping up with the number of foreclosed homes sold, creating a shadow inventory).

128. *See generally* Dodd–Frank Act, Pub. L. No. 111-203, § 408, 124 Stat. 1376, 1955–2113 (2010) (codified as amended in scattered sections of 12 U.S.C.) (providing procedural mechanisms to ensure foreclosures are performed in an equitable manner). Even states have joined the regulatory scheme. *See, e.g.*, CAL. CIV. CODE § 2923.5 (West 2010) (preventing lenders from filing a notice of default with borrowers until 30 days after initial contact with the borrower or after satisfying the statutorily mandated "due diligence" requirements); MD. CODE ANN., COM. LAW § 13-301 (West 2011) (proscribing certain lender practices during the foreclosure process); *see also, e.g.*, HSBC Bank USA v. Taher, 932 N.Y.S.2d 760, 760 (N.Y. Sup. Ct. 2011) ("The New York State court system has instituted a new filing requirement in residential foreclosure cases to protect the integrity of the foreclosure process and prevent wrongful foreclosures."); David Streitfeld, *Foreclosures Slow as Document Flaws Emerge*, N.Y. TIMES, Oct. 1, 2010, at A1 (predicting foreclosure evictions to slow sharply as a result of courts cracking down on lawyers "accused of cutting corners in their pursuit of rapid home repossessions").

129. *See* Pigg v. BAC Home Loans Servicing, LP (*In re* Pigg), 453 B.R. 728, 733 (Bankr. M.D. Tenn. 2011) ("Congress . . . could not have foreseen the world and United States financial crisis that crashed Wall Street, sunk the real estate market, and affected, to some degree, almost every American.").

b. Inability to Force Foreclosure

In guaranteeing a fresh start, one would surmise that the Code would provide a mechanism to allow the debtor to eliminate all interest in encumbered property so as to avoid future liability associated with the property. No federal or state law, however, allows a court to compel a lender to foreclose.[130] This is disturbing because relief from accumulating assessments now depends on a lender's willingness to foreclose.

Sections 521[131] and 1325[132] of the Code provide a mechanism for debtors to surrender encumbered property to the lender.[133] By surrendering their properties, debtors are notifying the trustees and creditors that they are making the collateral available for foreclosure or repossession.[134] Because the Code does not define "surrender," its interpretation has fallen to the courts.[135] Courts have determined that the option to surrender does not require the creditor "to accept possession or to foreclose or repossess" the surrendered property.[136] Additionally, bankruptcy courts lack the jurisdiction to force lenders to foreclose.[137] Recently, in *Arsenault*

130. *See id.* at 735 ("Nothing in the law can require [a lender] to foreclose.").

131. *See* 11 U.S.C. § 521 (2010).

132. *See id.* § 1325.

133. *See id.* § 521(a)(2)(A) (providing Chapter 7 debtors with an option to surrender encumbered property); *see also id.* § 1325(a)(5)(C) (providing Chapter 13 debtors with the same option).

134. *See* Pratt v. Gen. Motors Acceptance Corp. (*In re* Pratt), 462 F.3d 14, 18–19 (1st Cir. 2011) (noting the "most sensible connotation of 'surrender' . . . is that the debtor agreed to make the collateral *available* to the secured creditor"); *see also* Maple Forest Condo. Ass'n v. Spencer (*In re* Spencer), 457 B.R. 601, 612 (Bankr. E.D. Mich. 2011) ("Debtor's 'surrender' merely establishes that Debtor will not oppose the transfer of collateral.").

135. *See In re* Service, 155 B.R. 512, 514 (Bankr. E.D. Mo. 1993) (noting that courts have taken up the role to define "surrender").

136. Canning v. Beneficial Me., Inc., 462 B.R. 258, 264 (B.A.P. 1st Cir. 2011) (citing *In re Pratt*, 462 F.3d at 19); *see also* Canning v. Beneficial Me., Inc. (*In re* Canning), 442 B.R. 165, 172 (Bankr. D. Me. 2011) (noting that the surrender option "does not force creditors to assume ownership or take possession of collateral"), *aff'd* 462 B.R. 258 (B.A.P. 1st Cir. 2011). *But see In re Spencer*, 457 B.R. at 612 ("As more mortgages go 'under water,' the courts are increasingly called upon to chart the extent of the legal effect of surrender and transfer of property." (citing *In re* Burgueno*,* 451 B.R. 1, 3 (Bankr. D. Ariz. 2011))).

137. *See In re Service*, 155 B.R. at 515 ("[T]he court cannot compel acceptance of the surrendered property . . . ."); *In re* Heck*,* No. 09-31512 TEC, 2011 WL 133015, at *1 (Bankr. N.D. Cal. Jan. 13, 2011) (recognizing the lack of

v. JP Morgan Chase Bank,[138] the court addressed whether "the creditor can be compelled to take affirmative steps to accept surrendered collateral" in light of the recent decline in real estate values.[139] Though recognizing the inability of debtors to achieve a fresh start without such a remedy, the court fell back on precedent.[140]

Many courts have sympathized with debtors' inability to compel foreclosure and receive a fresh start, but cannot reconcile this compassion with the Code's inability to accommodate them.[141] Their response is that the burden of accumulating assessments terminates upon property conveyance, and debtors can proactively divest themselves of ownership.[142] This

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subject matter jurisdiction to reopen a closed case to require a lender to foreclose); *In re* White, 282 B.R. 418, 443 (Bankr. N.D. Ohio 2002) (finding no jurisdiction to compel foreclosure because "the Code does not provide for the court or the debtor to direct the means by which the secured creditor deals with the surrendered property").

138. *See* Arsenault v. JP Morgan Chase Bank (*In re* Arsenault), 456 B.R. 627, 631 (Bankr. S.D. Ga. 2011) (holding that despite the debtor's inability to receive a fresh start, the Chapter 13 debtor could not require a secured creditor to take title or foreclose on surrendered property). In *Arsenault*, Chapter 13 debtors surrendered and vacated their property and brought an action against their lender for a "violation of automatic stay" after the lender took no action on the property. *Id.* at 628. Debtors argued that the confirmation order created a binding contract that forced their lender to take title to the surrendered property. *Id.* at 629. The court did not agree. *See id.* at 629–32.

139. *See id.* at 631.

140. *See id.* at 632 (noting that without lender foreclosure, the borrower continues to be charged for assessments, insurance, and maintenance related to ownership of the property (citing *In re Canning*, 442 B.R. at 172)).

141. *See* Beeter v. Tri-City Prop. Mgmt. Servs., Inc. (*In re* Beeter), 173 B.R. 108, 118 (Bankr. W.D. Tex. 1994) ("[Accumulating assessments are] an incident of ownership, and only termination of that ownership can bring an end to the ongoing liability. Bankruptcy, not surprisingly, cannot solve all of life's problems. This is one liability that resists bankruptcy relief."); *see also In re* Cormier, 434 B.R. 222, 224 (Bankr. D. Mass. 2010) (noting the current "inadequacy of existing state and federal laws to provide meaningful, responsible solutions" to debtors facing accumulating assessments, but reconciling its decision to not compel foreclosure because "judges are interpreters and not architects of the law").

142. *See* River Place E. Hous. Corp. v. Rosenfeld (*In re* Rosenfeld), 23 F.3d 833, 837–38 (4th Cir. 1994) (proposing that debtors use a deed in lieu of foreclosure to end their interest in the property); Maple Forest Condo. Ass'n v. Spencer (*In re* Spencer), 457 B.R. 601, 616 (Bankr. E.D. Mich. 2011) (basing its analysis on the "underlying assumption that [a] Debtor is capable of divesting ownership of the property"); *In re* Burgueno, 451 B.R. 1, 4 n.9 (Bankr. D. Ariz.

presumption, that debtors can use self-help to end accumulating assessments, is flawed for several reasons.

Upon discharge, the lender's claim against the debtor will be limited to in rem rights and any deficiency will be classified as a dischargeable, unsecured claim.[143] The debtor could sell the property, but if the outstanding mortgage exceeds the value of the property, the new buyer must take title subject to the debtor's mortgage.[144] Rational buyers will not take title to overencumbered property, and a new lender will not finance the transaction unless title is clear. Thus, absent the use of a mechanism discussed below, debtors cannot just sell their property unless equity is present.

Some courts have reconciled a debtor-member's inability to compel foreclosure with the availability of a deed in lieu of foreclosure, a quitclaim deed, or a short-sale. A deed in lieu of foreclosure allows the borrower to turn over his equitable interest in the property to the lender for "full or partial satisfaction of the mortgage obligation."[145] A quitclaim deed allows a borrower to deed the property back to the lender.[146] In a short-sale, the lender grants the borrower permission to sell the property for less than the balance on the mortgage with the promise of not seeking a deficiency.[147] In normal market conditions, these foreclosure

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2011) (proposing debtor use a quitclaim deed to divest himself of the property). *But see* Canning v. Beneficial Me., Inc., 462 B.R. 258, 268 (B.A.P. 1st Cir. 2011) (recognizing the debtors' inability to divest themselves of ownership of the surrendered property but still finding no violation by the lender of the discharge injunction in its "refusal to foreclose or discharge its mortgage").

143. *See* 11 U.S.C. § 506(a)(1) (2005) (providing that a claim remains secured to the extent it is set off by the value of debtor's encumbered property); *see also* Johnson v. Home State Bank, 501 U.S. 78, 81 (1991) (providing that in personam liability rather than in rem liability on a mortgage is extinguished by bankruptcy discharge).

144. *See In re Spencer*, 457 B.R. at 614 ("It is not necessary that Debtor be able to sell the property at a price sufficient to extinguish his personal liability on the mortgages encumbering it."); *see also* SCHMUDDE, *supra* note 10, § 7.01 (noting that the mortgage continues to exist until it is paid in full, released, or foreclosed upon by a superior lien).

145. MORTGAGES, *supra* note 10, § 8.5 cmt. b.

146. *See In re Burgueno*, 451 B.R. at 4 n.9 (defining a quitclaim deed).

147. *See* Wells Fargo Bank, N.A. v. Perkins, No. 10AP-1022, 2011 WL 4790766, at *5 (Ohio Ct. App. Aug. 2, 2011) ("The mortgage holder agrees to release its mortgage lien on the property in return for the proceeds from the sale of the property, even though the proceeds are less than the mortgage loan

substitutes are promising because they allow the lender to avoid substantial foreclosure costs, while also allowing the debtor to avoid accumulating assessments and other carrying costs associated with continued property ownership.[148]

These solutions present issues for debtors with underwater mortgages. First, the debtor cannot force the lender to accept a foreclosure substitute.[149] Second, because these are only foreclosure substitutes, they do not terminate junior liens like a traditional foreclosure does.[150] Junior lienholders have nothing to gain from accepting the short-sale, and priority lenders accepting a deed in lieu of foreclosure or a quitclaim deed will have to assume any junior liens, effectively making them unavailable to any underwater borrowers with multiple mortgages.[151] Short-sales require the borrower to find a new buyer, which may prove difficult with the surplus supply of homes on the market.[152] Quitclaim deeds and deeds in lieu of foreclosure require lenders

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balance."). Absent a prior agreement, the lender will sue the borrower for any deficiency resulting from the foreclosure sales price being less than the balance of the mortgage obligation. *See* MORTGAGES, *supra* note 10, § 8.4 cmt. a.

148. *See* SCHMUDDE, *supra* note 10, § 5.10 (describing the potential cost-saving advantages of workout plans with lenders); *see also* Michael Powell, *Short Sales Resisted as Foreclosures Are Revived*, N.Y. TIMES, Oct. 24, 2010, at A1 (describing short-sales as "a less disruptive solution" compared to foreclosure); Ruth Simon & James R. Hagerty, *Why Lenders Are Leery of Short Sales*, WALL ST. J., Apr. 17, 2008, at D1 ("[A] short sale might seem like a win-win for everyone involved.").

149. *See* Pigg v. BAC Home Loans Servicing, LP (*In re* Pigg), 453 B.R. 728, 733 (Bankr. M.D. Tenn. 2011) ("[Debtors] cannot force lenders to accept [a] deed in lieu of foreclosure . . . ."); *In re* Burgueno, 451 B.R. 1, 4 n.9 (Bankr. D. Ariz. 2011) (querying whether a quitclaim deed would require acceptance by the lender under Arizona common law); *In re* Cormier, 434 B.R. 222, 228 n.8 (Bankr. D. Mass. 2010) (noting that a bank has no duty to accept a deed in lieu of foreclosure); Harvest Homebuilders LLC v. Commonwealth Bank and Trust Co., 310 S.W.3d 218, 221 (Ky. Ct. App. 2010) (finding no breach of the implied covenant of good faith and fair dealing when the lender did not consent to short-sale by the borrower).

150. MORTGAGES, *supra* note 10, § 8.5 cmt. b (explaining that only foreclosure by a senior lien wipes out junior liens).

151. *See* Simon & Hagerty, *supra* note 148 (noting that a short sale also requires approval of the mortgage servicers who "must consider the interests of the investors who own the loans" in the secondary market).

152. *See* Powell, *supra* note 148 ("Short sales are also hindered when homeowners fail to forward the proper papers, have tax liens or cannot find a buyer.").

to become responsible for taxes, selling costs, maintenance, and insurance on a property that may take months to resell in the current market.[153]

Lenders are deterred from accepting the use of these foreclosure substitutes when nonacceptance entails immediate cost savings (avoiding having to find a new purchaser in a deed in lieu of foreclosure or quitclaim deed or having to perform due diligence on a short-sale transferee) along with the realization that the association is incentivized to keep up the property at its own expense.[154] Thus, the current economic environment makes these alternatives to foreclosure useless to debtors with underwater mortgages. If courts dismiss the effects of § 523(a)(16) under the assumption that debtors can use self-help to end accumulating assessments, then it is possible that Congress, in amending the Section, used the same faulty assumption.

2. Section 523(a)(16)'s Ineffectiveness in Protecting Associations

As evident from the legislative histories of the Section as originally enacted and amended, Congress clearly meant to protect associations.[155] The combination of lender delay and lack of member equity has, however, rendered § 523(a)(16) of little value to associations. Debtors on tight budgets or ignorant of § 523(a)(16) do not pay assessments, and associations must continue to maintain the property to avoid depressed home prices resulting from unmaintained, surrendered properties.[156] Lenders,

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153. *See* Frank A. St. Claire, *Special Problems in Real Property Foreclosures*, *in* REAL ESTATE FORECLOSURES 73, 92–93 (1992) (describing the flaws of deeds in lieu of foreclosure as a mechanism to divest ownership).

154. *See In re Pigg*, 453 B.R. at 732 n.5 (explaining the cost incurred by associations in maintaining property owned by nonpaying members to avoid depreciated values to surrounding properties).

155. *See* 140 CONG. REC. S4526 (daily ed. Apr. 20, 1994) (statement of Sen. Strom Thurmond) ("[A]ssociations may be unfairly burdened if members can file bankruptcy to discharge future assessments, but continue to reside on the property and receive benefits from the association."); H.R. REP. NO. 109-31, at 68 (2005), *reprinted in* 2005 U.S.C.C.A.N. 88, 154 (attempting to expand the protections accorded to associations with BAPCPA's amendment to § 523(a)(16)).

156. *See In re* Colon, 465 B.R. 657, 664 (Bankr. D. Utah 2011) (recognizing

as the true beneficiaries of § 523(a)(16), are allowed to collect an inventory of surrendered homes, presumably to time the market for higher resale values, and avoid any associated inventory cost.[157]

Further, lender delay is causing associations financial distress because they cannot get new dues-paying members into the units.[158] Because liens for unpaid dues are subordinate in priority to lenders' mortgages, and there is likely no equity to foreclose on a subordinate lien, the associations must choose between charging higher dues or allowing properties to go unmaintained.[159] It is not practical for an association to foreclose on its lien for unpaid assessments because the association will have to (1) incur all foreclosure cost, and (2) find a buyer willing to take the overencumbered property, still subject to a lender's

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the HOA's "duties to maintain the neighborhood for the benefit of homeowners continue, yet it is saddled with an empty property that is not paying dues for such purposes").

157. *See* Pigg v. BAC Home Loans Servicing, LP (*In re* Pigg), 453 B.R. 728, 732 n.5 (Bankr. M.D. Tenn. 2011) ("The economics of the situation allow the Bank to sit idle and not foreclose as long as the debtor, not the Bank is liable for the HOA fees. . . . [T]he Bank receives the benefit of the HOA services such as landscaping improvements, common area maintenance, signage, and security.").

158. *See* Trevor G. Pinkerton, Comment, *Escaping the Death Spiral of Dues and Debt: Bankruptcy and Condominium Association Debtors*, 26 EMORY BANKR. DEV. J. 125, 125 (2009) (suggesting Chapter 11 bankruptcy for associations in distress during this mortgage crisis).

159. *See* Liberty Cmty. Mgmt., Inc. v. Hall (*In re* Hall), 454 B.R. 230, 240 (Bankr. N.D. Ga. 2011) ("If the assessments are [not collected], lawns may go unmown and pools may go uncleaned—all of which can lead to reduced property values for the individual units."); Rachel Furman, Note & Comment, *Collecting Unpaid Assessments: The Homeowner Association's Dilemma When Foreclosure Is No Longer a Viable Option*, 19 J.L. & POL'Y 751, 754–57 (2011) (noting that lender delay on an underwater mortgage means the association must continue to maintain a property with no fees being collected from the unit owner). Before the drop in home values, many HOAs were successfully able to use the threat of foreclosure to compel payment of delinquent HOA fees. *See* Furman, *supra*, at 757. If the threat did not work, lenders would step in and foreclose rather than have a new, and possibly unqualified, owner assume the mortgage. *See id.* at 758–59 (noting that if the HOA foreclosed and took the property to auction, the lender may be stuck with an unqualified high bidder). As prices have fallen and the market of potential buyers has shrunk, lenders may find it quite advantageous to sit idle and allow the association to auction the property to a new buyer who will assume the mortgage. *Id.* (noting that with the high cost of foreclosure, a lender is better off with the association initiating the foreclosure).

priority lien.[160] Associations could potentially protect themselves from lenders' inaction by including a clause for priority lien status in their declarations.[161] However, this would inevitably diminish the marketability of the units because lenders would charge higher rates, or refuse to lend at all, in an attempt to hedge the risk of holding a subordinate lien on a property that has fallen in value.[162]

Section 523(a)(16) attempted to cure a perceived inequity faced by associations when members use bankruptcy to discharge future assessments. However, the circumstances of decreased home values and lender delay have shifted these benefits to lenders. As a result, debtors' fresh start is placed in the lenders' unbridled discretion to foreclose.[163]

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160. *See* Lawrence Roberts, *Will HOA Lawsuits Compel Lenders to Foreclose on Shadow Inventory?*, IRVINE HOUSING BLOG (June 16, 2010), http://www.irvinehousingblog.com/blog/comments/will-hoa-lawsuits-compel-lenders-to-foreclose-on-shadow-inventory/ (last visited Apr. 2, 2013) (noting that it is in the association's best interest to get new dues-paying owners into surrendered units, but the risk of having to take title to the property at foreclosure auction because no buyer can be found far outweighs the burden of freeriding members) (on file with the Washington and Lee Law Review).

161. *See* Cypress on Sunland Homeowners Ass'n v. Orlandini, 257 P.3d 1168, 1177 (Ariz. Ct. App. 2011) (interpreting Arizona's code § 33-1807 as subordinating any HOA assessment lien to that of the first mortgage holder but noting that the association could have protected itself with the appropriate language in the declaration); *see also* ARIZ. REV. STAT. § 33-1807 (2012). *But see* Thaler v. Household Fin. Corp., 95 Cal. Rptr. 2d 779, 781 (Cal. Ct. App. 2000) (holding that an HOA's assessment lien filed after the deed of trust is subordinated even though the condominium covenants, conditions, and restrictions give priority to the HOA).

162. *See Orlandini*, 257 P.3d at 1177 (noting that the association likely chose not to protect itself with priority lien status so as to encourage cheaper financing for its owners).

163. *See In re* Pratola, 152 B.R. 874, 878 (Bankr. D.N.J. 1993) ("The fact that both the mortgagee-bank and the condominium association both refused to accept tender of a deed from the debtor should not operate against the debtor's entitlement to a 'fresh start' which the Bankruptcy Code was meant to provide."); *see also* Pigg v. BAC Home Loans Servicing, LP (*In re* Pigg), 453 B.R. 728, 733 (Bankr. M.D. Tenn. 2011) ("If the lender never forecloses, that homeowner's liability for the HOA fees continues in perpetuity.").

3. Section 523(a)(16)'s Overinclusiveness

Prior to 1994, courts following the prepetition contract theory would discharge all assessments coming due after filing.[164] This gave incentive to abusive, bad faith freeriders, who would discharge future assessments, continue to inhabit their property by continuing to pay their mortgage, and receive all the benefits of community ownership without paying assessments. The 1994 version of the statute adequately protected associations from these freeriders. Freeriders, who continued to inhabit the property and procure benefits from the association, remained liable for assessments coming due after filing.[165]

BAPCPA's amendments sought to expand the protections afforded to associations.[166] The expansion, however, is overinclusive. In addition to preventing freeriders from partaking in the Code's benefits, the Section engulfs honest, good faith debtors who are unable to discontinue their interests in overencumbered property.[167] While the amendment could potentially lead to higher collection rates for associations, it pursues a new type of debtor, different from the egregious debtors, like drunk drivers, that § 523 has traditionally protected against.[168] This nontraditional use of § 523 has left debtors at the mercy of lenders' willingness to foreclose. If lenders do not timely foreclose, debtors will face collection efforts by their association,

164. *See In re* Rosteck, 899 F.2d 694, 698 (B.A.P. 7th Cir. 1990) (discharging all future assessments because debtors "had a debt for future condominium assessments when they filed their bankruptcy petition").

165. *See* Reform Act § 309 (codified as amended at 11 U.S.C. § 523(a)(16) (1994)) (current version at 11 U.S.C. § 523(a)(16) (2010)) (discharging future assessments if the debtor vacated the premises and did not rent it out).

166. *See* H.R. REP. NO. 109-31, at 68 (2005), *reprinted in* 2005 U.S.C.C.A.N. 88, 154 (noting that the intention of BAPCPA's amendment to § 523(a)(16) was an expansion to the protections accorded to associations).

167. *See In re Pigg*, 453 B.R. at 733 (noting that BAPCPA's § 523(a)(16) effectively "deprives the debtor of a fresh start, and thwarts the goals of the entire Bankruptcy Code"). *But see In re* Raymond, 129 B.R. 354, 359 (Bankr. S.D.N.Y. 1991) (concluding that discharging assessments coming due after filing would give debtor a head start instead of a fresh start).

168. *See* 11 U.S.C. § 523(a)(9) (2010) (preventing debtors from discharging debts associated with damages resulting from driving under the influence of drugs or alcohol).

preventing the reestablishment of credit.[169] After the subsequent foreclosure, unpaid assessments may still be collected.[170] Alternatively, debtors could remain on the property at the cost of continuing to make mortgage payments on overencumbered property and being constrained as to where they can live and find work.

In addition to the policy consideration of preventing bad faith debtors from partaking in the bankruptcy process, § 523 also seeks to protect certain worthy creditors from their debtors utilizing bankruptcy to the creditors' detriment.[171] Both unsecured taxing authorities and recipients of domestic support fall under this category.[172] Associations, however, differ from these two protected creditors because associations maintain an in rem claim against the debtors' property.[173] Even localities with real property tax claims, secured by the property and coming due after filing, do not receive protection under § 523. Accordingly, absent the need for protection from bad faith debtors, associations do not seem to require additional protection from the Code. Rather, it seems like a strong lobbying group has created a preferred creditor.[174]

IV. Possible Solutions

This Part will provide three solutions to § 523(a)(16)'s death-trap. The first is a proposal to amend § 523(a)(16) to a slight

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169. *See* Pigg v. BAC Home Loans Servicing, LP (*In re* Pigg), 453 B.R. 728, 733 (Bankr. M.D. Tenn. 2011) ("[Debtors] cannot truly be given a fresh start because HOA fees are still accumulating until a lender chooses to foreclose.").

170. *In re* Ames, 447 B.R. 680, 684 (Bankr. D. Mass. 2011) (allowing the association to pursue any unpaid assessments coming due between the member's bankruptcy filing and the eventual foreclosure).

171. *But see* Howard, *supra* note 15, at 1057 (describing this policy as "fairly weak").

172. *See* 11 U.S.C. § 523(a)(1) (2010) (excluding unsecured taxes from discharge); *id.* § 523(a)(5) (excluding domestic obligations from discharge).

173. *See* FREEDMAN & ALTER, *supra* note 22, at 151 (noting that upon a member's bankruptcy discharge, "the association's remedy for post-petition assessment amounts is to exercise the lien and foreclosure rights against the property").

174. *See In re Pigg*, 453 B.R. at 733 (suggesting § 523(a)(16)'s expanded protections to associations is "the result of some special interest lobbying").

modification of the 1994 version of the statute. The amendment would require associations to seek additional protection by lien priority through their declarations and state legislatures. Because of the death-trap § 523(a)(16) creates for debtors, courts have begun experimenting with ways to circumvent the Section's harsh results. This Part will end with a critique of two methods courts have considered in getting around the section's harsh results.

A. Proposal to Amend § 523(a)(16)

Any proposal to amend § 523(a)(16) needs to account for the factors that have created the inequities faced by debtors and associations. The proposal should apply to both Chapter 7 and 13 debtors, and serve the goals of the Code in both rising and falling economic periods. It should be easy to administer, and add predictability to the marketplace, rather than give courts reason to sporadically circumvent the Section to avoid its inequitable results.[175] It needs to limit incentives to lenders to delay foreclosure on surrendered property because foreclosure provides the best solution: assessment-paying buyers to associations and a fresh start to debtors.

The 1994 version of § 523(a)(16), which based the dischargeability of accumulating assessments on the continued possession or use of the association's services, codified an identical line of cases predating § 523(a)(16)'s enactment.[176] In Chapter 13 cases, courts have continued to use this judge-created approach since § 523(a)(16)'s enactment.[177] The approach is founded on "equitable grounds" because it provides protection

175. *See id*. at 736 (compelling foreclosure to avoid § 523(a)(16)'s harsh results).

176. *See, e.g.*, *In re* Ryan, 100 B.R. 411, 417 (Bankr. N.D. Ill. 1989) (determining the dischargeability of assessments depends on whether the debtor vacated or remained on the property); *In re* Montoya, 95 B.R. 511, 513 (Bankr. S.D. Ohio 1988) (finding that postpetition assessments were discharged when debtor abandoned property before filing bankruptcy).

177. *See* Foster v. Double R Ranch Ass'n (*In re* Foster), 435 B.R. 650, 655 (B.A.P. 9th Cir. 2010) (stating the issue of dischargeability as dependent on whether "debtor continued to reside on the property"); *In re* Colon, 465 B.R. 657, 662–63 (Bankr. D. Utah 2011) (using the issue as stated in *Foster* (quoting *In re Foster*, 435 B.R. at 655)).

against freeriding debtors, while still providing vacating debtors with a fresh start as promised by the Code.[178]

The problem with the 1994 statute, which was not fixed with the 2005 amendment, was that while it solved the problem of freeriding member-borrowers, it left open the potential for abuse by freeriding lenders. Lenders, with their priority lien status, are given a legislative grace period to delay foreclosure until a suitable time and avoid all maintenance and carrying costs in the interim.[179] An amended, § 523(a)(16) should provide:

> (a) A discharge . . . does not discharge an individual debtor from any debt—
>
> . . . .
>
> (16) for a fee or assessment that becomes due and payable after the order for relief to a membership association with respect to the debtor's interest in a unit that has condominium ownership, in a share of a cooperative corporation, *or a lot in a homeowners association*, but only if such fee or assessment is payable for a period during which--
>
> (A) the debtor physically occupied a dwelling unit in the condominium or cooperative project; or
>
> (B) the debtor rented the dwelling unit to a tenant and received payments from the tenant for such period, but nothing in this paragraph shall except from discharge the debt of a debtor for a membership association fee or assessment for a period arising before entry of the order for relief in a pending or subsequent bankruptcy case; *or*
>
> *(C) the debtor surrenders the unoccupied property to its secured lien holder, limited to a period of 90 days measured as of the date of filing.*

For this proposal to apply to Chapter 13 debtors, § 1328(a)(2) must be amended to include § 523(a)(16). The proposal modifies the 1994 amendment by including "homeowners association" and subpart C. Pursuant to proposed § 523(a)(16), debtors who

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178. Eno v. Indian Country Campsites Recreation & Maint. Fund (*In re* Eno), 269 B.R. 319, 321–22 (Bankr. M.D. Pa. 2001); *In re Ryan,* 100 B.R. at 414 (describing its approach as furthering "the Code's 'fresh start' policy").

179. *In re* Miller, 125 B.R. 441, 443 (Bankr. W.D. Pa. 1991) (noting that the benefits provided by the association accrue solely "to the mortgage holder" after the debtor has vacated the property).

continue to use their property for personal use or for generating rental income would continue to be responsible for assessments coming due after filing. Absent debtors would be responsible for assessments for a period of three months following their surrendering and vacating of their property, recognizing the required time needed for foreclosure.

There may be no perfect balance between this three-party relationship of association, debtor, and lender. The proposal has its own flaws: First, lenders will likely use the three-month grace period to their full advantage, and not begin the foreclosure process until after the period expires. Second, the proposal will benefit debtors to the detriment of associations that are unable to collect from vacating members.[180]

Note that BAPCPA's § 523(a)(16) was intended to protect associations, but contributed to the opposite result. To combat these flaws and provide associations with ample protection, priority lien status needs to be given to associations. Drafting the declaration to give the lien for unpaid assessments priority over the mortgage would prompt foreclosure and payment of unpaid assessments.[181] And although it would increase the cost of financing purchases, preventing some sales, it would also insure against the noncollection of assessments and the resulting property value declines.

Each state provides a statutory hierarchy of lien priority.[182] Currently every state gives local real estate tax liens first priority over all other claims against the property.[183] With collection rates of over 99%, the real estate tax system is "one of the most efficient tax collection systems in the United States."[184] If associations occupied a similar position, they could promptly foreclose upon a member's default, ensuring payment of arrears

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180. *See* Ricotta, *supra* note 109, at 187 (noting the increased burden on associations if they are unable to collect from debtors that vacated under the 1994 amendment to § 523(a)(16)).

181. *But see* Thaler v. Household Fin. Corp., 95 Cal. Rptr. 2d 779, 781 (Cal. Ct. App. 2000) (declining to recognize the subordination clause in the association's declaration and giving the lender lien priority).

182. *See, e.g.*, MD. CODE. ANN., REAL PROP. § 7-104 (West 1997) (providing the statutory hierarchy for liens against real property in Maryland).

183. *See, e.g.*, VA. CODE. ANN. § 58.1-3340 (West 1950) (granting real estate tax liens seniority over all others filed against the property).

184. SCHMUDDE, *supra* note 10, § 11.03.

and avoiding freeriders. If associations were able to persuade Congress for protection in the federal Bankruptcy Code, I have no doubt they will be able to achieve similar results at the state level.[185]

B. Judicial Solutions

As an alternative or interim remedy to a legislative amendment, courts could provide relief to debtors that are the victims of lender delay. There are two conceivable ways a bankruptcy court can cause the lender to transfer title out of the borrower's name.

1. Section 105 Equitable Powers

Section 105[186] gives bankruptcy courts the power to fashion appropriate remedies "to carry out the provisions of [the Code]."[187] Equitable powers are used when applying the Code strictly to the facts would create an inequitable result.[188] Recently, in *Pigg v. BAC Home Loans Servicing, LP*,[189] the court used its § 105 equitable powers to prevent a debtor from "not truly be[ing] given a fresh start because HOA fees are still

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185. *See, e.g.*, N.J. STAT. ANN. § 46:8B-21(b) (1997) (granting lien priority status to associations over lenders).

186. *See* 11 U.S.C. § 105 (2010).

187. *Id.* "Federal Courts are courts in law and in equity, and a court of equity has traditionally had the power to fashion any remedy deemed necessary and appropriate to do justice in a particular case." Pigg v. BAC Home Loans Servicing, LP (*In re* Pigg), 453 B.R. 728, 734 (Bankr. M.D. Tenn. 2011) (quoting Carter Jones Lumber Co. v. Dixie Distrib. Co., 166 F.3d 840, 846 (6th Cir. 1999)).

188. *See* EPSTEIN, *supra* note 5, § 3-22 ("[A court's] authority [under] section 105(a) is to use the powers of equity, consistent with the law's purpose and policy, to fill gaps and to trim or mold statutes that apply imperfectly in the particular case because of peculiar circumstances.").

189. *See In re Pigg*, 453 B.R. at 733 (providing equitable relief to a debtor who surrendered property but whose lender refused to foreclose on the property). In *Pigg*, the debtor owned a condominium that was destroyed in the Nashville floods of 2010. *See id.* at 730. The debtor surrendered and vacated the property, and the lender changed the locks on the property. *See id.* Debtor sought to compel its lender to either accept a deed in lieu of foreclosure or to sell the house in foreclosure sale to stop the accumulating HOA fees. *Id.*

accumulating [pursuant to § 523(a)(16)] until a lender chooses to foreclose."[190] The court forced the transfer of title out of the debtor's name after the lender refused to take action.[191]

Section 105 equitable powers, however, "may only be exercised in a manner consistent with the provisions of the Bankruptcy Code."[192] Because the Code is meant to protect debtors and creditors alike, consideration must be given to both parties when a court uses its § 105 powers.[193] Both the *Pigg* and the *Arsenault* courts considered the interest of all concerned parties in determining the appropriate use of their § 105 powers with regard to accumulating assessments.[194] Thus, *Arsenault* and *Pigg* turn on the priority given to the Code's conflicting goals, with the court in *Pigg* compelling foreclosure and the court in *Arsenault* declining to do so.[195]

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190. *Id*. at 733. *But see In re* Barr, 457 B.R. 733, 738 (Bankr. N.D. Ill. 2011) (making no mention of debtor's inability to regain a fresh start with the accumulating assessments and rejecting any use of § 105 equitable powers). In *Barr*, the debtor filed a Chapter 7 petition two days after the building he lived in sustained flood damage. *See id*. at 734. The condominium association levied a special assessment against the debtor's property after the debtor's discharge. *See id*. at 735. The court "determine[d] that the debt is excepted from discharge under § 523(a)(16)." *Id*. at 738.

191. *See In re Pigg*, 453 B.R. at 736 (using 11 U.S.C. § 363(f) to permit the trustee to sell the property and distribute the proceeds to the borrower). Under § 363(f)(3), a trustee may sell the encumbered property if the lienholder consents, which the court found implicit through the lender's inaction to foreclose on the property. *See* 11 U.S.C. § 363 (2010); *see also In re Pigg*, 453 B.R. at 736 (citing several cases that have found consent under § 363(f) through creditor's inaction).

192. United States v. Sutton, 789 F.2d 1305, 1308 (5th Cir. 1986).

193. *See* Arsenault v. JP Morgan Chase Bank, N.A. (*In re* Arsenault), 456 B.R. 627, 631 (Bankr. S.D. Ga. 2011) (noting the need to protect creditor rights when using the court's equitable powers); Pigg v. BAC Home Loans Servicing, LP (*In re* Pigg), 453 B.R. 728, 735 (Bankr. M.D. Tenn. 2011) (noting that any use of equitable power under § 105(a) is constrained by the provisions of the Bankruptcy Code and respect to the rights of lienholders must be given).

194. *See In re Arsenault*, 456 B.R. at 631 ("Congress sought to strike a balance among competing interest of debtors, creditors, and the government." (quoting *Sutton*, 786 F.2d at 1306)). The court determined that it was not the lender's responsibility to relieve the borrower of all incidents of ownership simply because the debtor did not want the property anymore. *See id*. (citing Canning v. Beneficial Me., Inc. (*In re* Canning), 442 B.R. 165, 172 (Bankr. D. Me. 2011), *aff'd* 462 B.R. 258 (B.A.P. 1st Cir. 2011)).

195. *Compare id*. (noting that debtor's "fresh start is not the only goal of bankruptcy"), *with In re Pigg*, 453 B.R. at 734 ("Equity requires that the court

In addition to consideration being given to all concerned parties, § 105 cannot be used "to create substantive rights that would otherwise be unavailable under the Code."[196] *Arsenault* expressed concern with giving a debtor the substantive right to force foreclosure—a right that was not bargained for in the mortgage origination process.[197] This argument has merit; these mortgages were made under the assumption that a lender may choose when to foreclose.[198] If courts, at the discretion of unsatisfied borrowers, began forcing foreclosure sales, a new risk, in the form of unpredictability, would enter the market.

Accordingly, § 105 is only a discretionary tool to be used in the most egregious circumstances. Mounting assessments on a debtor with an underwater mortgage seem inadequate to trigger its use. Absent the lender constructively taking possession of a debtor's property or the property being damaged by a natural disaster, § 105 will likely not be available.[199]

2. Violation of Automatic Stay or Discharge Injunction by Refusing to Foreclose or Release

A discharge creates a permanent statutory injunction preventing any collection efforts by a creditor, regardless of the design.[200] Similarly, the automatic stay prevents a creditor from

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prevent the debtor's fresh start from being completely eradicated by this legislated wrong without a remedy.").

196. *In re* Morristown & Erie R.R. Co., 885 F.2d 98, 100 (3d Cir. 1989).

197. *See In re Arsenault*, 456 B.R. at 630–31 ("[Section 105] does not authorize the bankruptcy courts to create substantive rights that are otherwise unavailable under applicable law, or constitute a roving commission to do equity." (quoting *Sutton,* 786 F.2d at 1308)).

198. *See* SCHMUDDE, *supra* note 10, § 5.01 (explaining that lenders are not required to foreclose and many times they are anxious to avoid it).

199. *Compare* Arsenault v. JP Morgan Chase Bank, N.A. (*In re* Arsenault), 456 B.R. 627, 630 (Bankr. S.D. Ga. 2011) (noting that "[t]here are no allegations that [lender] has taken possession of the property"), *with* Pigg v. BAC Home Loans Servicing, LP (*In re* Pigg), 453 B.R. 728, 732 (Bankr. M.D. Tenn. 2011) (noting the fact that lender changed the locks and placed a notice on the door excluding everyone, including the borrower).

200. *See* 11 U.S.C. § 524(a)(2) (2010) (providing that the discharge "operates as an injunction against" any process or act to recover "a personal liability of the debtor").

pursuing any collection technique of stayed claims.[201] Violations of the stay or discharge injunction can result in damages, including attorney fees and punitive damages.[202] While associations may continue to collect after a debtor's discharge, lenders are limited to their in rem rights (foreclosure) against the property.[203] If a lender unreasonably delays foreclosure, allowing assessments to accumulate until a borrower-debtor is forced to reaffirm the discharged mortgage payments owed to the lender, the lender will have effectively made a collection effort.[204] If debtors can prove violation, lenders may speed foreclosures to avoid penalties and costs.[205]

In *Pratt v. General Motors Acceptance Corp.,*[206] the court determined that a secured automobile lender's refusal to repossess or release its lien on surrendered property "was objectively and improperly 'coercive' [under] the circumstances"

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201. *See id.* § 362(a)(6) (forbidding "any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title").

202. *See id.* § 362(k); *see also id.* § 524(i).

203. *Compare id.* § 523(a)(16) (excluding assessments coming due after filing from discharge), *with id.* § 524 (declining to apply discharge to secured claims against debtors' real property); *see also* Johnson v. Home State Bank, 501 U.S. 78, 85 (1991) (limiting lender's claim to its in rem right against the debtor's secured property).

204. *But see In re* Ames, 447 B.R. 680, 683–84 (Bankr. D. Mass. 2011) (rejecting debtor's argument that lender's inaction constituted a violation of § 362's automatic stay).

205. *See* Pratt v. Gen. Motors Acceptance Corp. (*In re* Pratt), 462 F.3d 14, 19 (1st Cir. 2006) ("In assessing violations of the automatic stay and the discharge injunction, the core issue is whether the creditor acted in such a way as to 'coerce' or 'harass' the debtor improperly.").

206. *See id.* at 20 (finding no obligation by the secured lender to accept surrendered property but concluding that secured creditor's "refusal to release its valueless lien" on debtor's automobile was a violation of the discharge). In *Pratt*, prior to filing bankruptcy, the debtor financed a vehicle through the creditor. *See id.* at 15. Debtor indicated that he wanted to surrender the property, but the creditor never repossessed the vehicle. *See id.* Upon the vehicle becoming inoperable ten years later and the lender still not taking action, debtors filed suit asking the court to find the lender in violation of the discharge injunction. *Id.* at 16. The court recognized that § 521(a)'s surrender option does not require a secured creditor to accept surrendered property. *See id.* at 18–19 n.4 ("[A]s such a reading would be at odds with well-established law that a creditor's decision whether to foreclose on and/or repossess collateral is purely voluntary and discretionary.").

and, therefore, violated the discharge injunction.[207] The court listed five factors it considered material in finding the lender's inaction equated to objective coercion.[208] Of specific importance was the fact that lender had not "repossess[ed] the 'surrendered' vehicle because it was of insufficient value" and it was cost-prohibitive, "conditioned its release of the lien upon the [debtors'] agreement to repay the loan balance in full," and that without the lender's repossession or release of lien, the debtors would "retain[] indefinite possession of a worthless vehicle . . . together with all the attendant costs of possessing, maintaining, insuring, and/or garaging the vehicle."[209]

Debtors seeking to avoid accumulating association assessments and other carrying costs associated with surrendered property have relied on *Pratt*'s analysis in claiming that lenders' refusal to foreclose equates to a violation of the automatic stay or discharge injunction. Their attempts, however, have been unsuccessful. The *Arsenault* court found that the debtor had not met the high standard of "improper coercion or harassment in violation of the automatic stay."[210] Debtor's continued obligation to pay accumulating association assessments because of lender's delay was not a coercive act in violation of the automatic stay.[211] Dismissing accumulating real estate taxes, insurance premiums, and association assessments as "incidents of ownership,"[212] the court in *Canning v. Beneficial Maine, Inc.*[213] stressed the personal nature and lack of potential

207. *Id.* at 19. *But see id.* at 20 (noting "that a secured creditor invariably would [not] be in violation of the discharge injunction were it to insist upon its *in rem* rights under state law").

208. *Id.* at 20.

209. *Id.*

210. Arsenault v. JP Morgan Chase Bank, N.A. (*In re* Arsenault), 456 B.R. 627, 632 (Bankr. S.D. Ga. 2011).

211. *Id.*

212. *See* Canning v. Beneficial Me., Inc. (*In re* Canning), 442 B.R. 165, 172 (Bankr. D. Me. 2011) ("Forces remained at work that could make their continued ownership of the real estate uncomfortable—forces like [accumulating association fees,] accruing real estate taxes and the desirability of maintaining liability insurance for the premises. But those forces are incidents of ownership." (citing Foster v. Double R Ranch Assn. (*In re* Foster), 435 B.R. 650, 653 (B.A.P. 9th Cir. 2010))), *aff'd* 462 B.R. 258 (B.A.P. 1st Cir. 2011).

213. *See id.* at 170 (determining that lender's "refusal to foreclose . . . immediately upon [debtor's] post-discharge demand did not closely approach a

appreciation of the car surrendered in *Pratt* versus the potential for appreciation in real property.[214]

The court in *Pratt* emphasized that the coercive use of state law could "impinge upon the important federal interest served by the discharge injunction, which is to ensure that debtors receive a fresh start."[215] The accumulating assessment cases declining to follow *Pratt* have not given similar weight to the Code's guarantee of a fresh start.[216] Although the *Canning* court did not find the lender in violation of the discharge injunction after refusing to foreclose, it is conceivable that a court, in an accruing assessment case, could find the factors satisfied. For example, if the facts of *Pigg* are applied to the *Pratt* test, it is reasonable to conclude that the lender was in violation of the discharge injunction—the value of the collateral was minute relative to the loans, lender had taken no action, and costs were accumulating as a result of debtor holding the surrendered property.[217] In *Pigg*, however, the property had been significantly damaged by a natural disaster—a cause beyond that of the mortgage crisis, which has affected, to some extent, every homeowner with a mortgage.[218]

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violation" of the discharge injunction found in *Pratt*). In *Canning*, the debtors claimed that lender's refusal to foreclose on property "frustrated their right to surrender their home and attempted to coerce them to answer personally for their discharged debt." *Id*. at 171. Debtors argued that like the secured creditor in *Pratt*, Beneficial was not foreclosing because it was not cost-effective to do so. *See id*. The *Canning* court determined that there was no violation of the discharge injunction in lender's refusal to foreclose on surrendered property. *Id*.

214. *See id.* at 172 (noting "the collateral's worthlessness [in *Prat*t] and the fact that, unlike real estate, vehicles rarely appreciate in value over time" (quotation marks omitted)).

215. *See* Pratt v. Gen. Motors Acceptance Corp. (*In re* Pratt), 462 F.3d 14, 19 (1st Cir. 2006).

216. *See* Arsenault v. JP Morgan Chase Bank, N.A. (*In re* Arsenault), 456 B.R. 627, 631 (Bankr. S.D. Ga. 2011) (noting "[d]ebtors' fresh start is not the only interest addressed in the Bankruptcy Code"); *see also In re* Cormier, 434 B.R. 222, 232 (Bankr. D. Mass. 2010) (determining lender's decision to "not immediately accept a deed-in-lieu of foreclosure" was not in itself denying debtor a fresh start).

217. *See* Pigg v. BAC Home Loans Servicing, LP (*In re* Pigg), 453 B.R. 728, 732 (Bankr. M.D. Tenn. 2011) (noting the substantial loss of value due to flooding, accumulation of assessments, and lender's decision not to foreclose because of the depressed real estate market and associated cost of foreclosure).

218. *See id*. at 730 (discussing the extent of the damage to debtor's property). *But see In re* Warren, 457 B.R. 733, 735 (Bankr. N.D. Ill. 2011)

V. Conclusion

Any proposed protections granted to associations or debtors from lender delay may have unintended consequences. The proposed amendment to § 523(a)(16) will decrease assessment collection in the short-run and require increased dues among other members.[219] This problem can be hedged over time with contractual protections and changes in lien priority at the state level.

Any attempt to speed up foreclosures, either through judicial equitable powers or discharge injunction violations, must take into account the downsides of foreclosures. Increased foreclosure rates depress surrounding home values, increase crime rates, and harm local businesses.[220] Use of equitable powers and penalties for discharge injunction and stay violations create uncertainty, and lenders will likely hedge this uncertainty with higher rates. Higher rates will make financing difficult for borrowers, causing them to rush to the rental market and drive up rental costs.[221] There is also a moral hazard concern if borrowers, upon filing bankruptcy, can ask bankruptcy courts to compel foreclosure on risky home investments.[222]

On the other hand, the cost of a bankruptcy system on society includes a higher cost of credit and the potential for moral

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(providing no redress through equitable powers even when debtor's property was located in a flooded building).

219. *See* Ricotta, *supra* note 109, at 187 (criticizing the 1994 version of § 523(a)(16) because associations would have to charge higher assessments to dues-paying members to compensate for discharged assessments).

220. *See* Adam J. Levitin, *Resolving the Foreclosure Crisis: Modification of Mortgages in Bankruptcy*, 2009 WIS. L. REV. 565, 569 (2009) (noting the negative effects of foreclosures on third parties such as families and local businesses, as well as the negative impacts on local housing and commercial real estate prices); *see also id*. at 570 (noting the potential for increased crime rates and erosion of the tax base).

221. Motoko Rich, *Home Prices Are Down, but Rentals Are Rising*, ECONOMIX (Sept. 15, 2011, 5:26 PM), http://economix.blogs.nytimes.com/2011/09/15/home-prices-are-down-but-rentals-are-rising/ (last visited Apr. 2, 2013) (on file with the Washington and Lee Law Review).

222. *See* Thomas H. Jackson, *The Fresh-Start Policy in Bankruptcy Law*, 98 HARV. L. REV. 1393, 1402 (1985) (defining moral hazard as "a situation in which individuals systematically—and rationally—underestimate the real costs of engaging in a risky activity because those costs are borne by someone else").

hazard.[223] The economy cannot recover without a healthy consumer base free of prior poor economic decisions. The Code's fresh start can provide that base.

223. *See id*. at 1427–28 (increasing the availability of a fresh start would increase interest rates and lead to "an inevitable and substantial moral hazard problem"); Theodore Eisenberg, *Bankruptcy Law in Perspective*, 28 UCLA L. REV. 953, 983 (1981) ("Those debtors who pay their debts bear the assumed increased credit cost. Nonpaying debtors, to whose defaults the increased cost of credit is attributable, do not fully share in that increased cost."). *But see* Jackson, *supra* note 222, at 1402 (noting that bankruptcy "shifts the costs of overextending credit from debtors to creditors, who are in a better position to minimize those costs"); Howard, *supra* note 15, at 1066 (proposing that bankruptcy discharge does not increase the cost of credit because consumer credit is not perfectly elastic).