

March 1993

Florida's Treatment of Entirety Property: Do Unsecured Joint Creditors Lose the Benefit of Their Bargain or Achieve a Higher Status Than Specifically Provided by the Bankruptcy Code?

Julio E. Castro

Follow this and additional works at: <https://scholarship.law.ufl.edu/flr>



Part of the [Law Commons](#)

Recommended Citation

Julio E. Castro, *Florida's Treatment of Entirety Property: Do Unsecured Joint Creditors Lose the Benefit of Their Bargain or Achieve a Higher Status Than Specifically Provided by the Bankruptcy Code?*, 45 Fla. L. Rev. 275 (1993).

Available at: <https://scholarship.law.ufl.edu/flr/vol45/iss2/5>

This Note is brought to you for free and open access by UF Law Scholarship Repository. It has been accepted for inclusion in Florida Law Review by an authorized editor of UF Law Scholarship Repository. For more information, please contact kaleita@law.ufl.edu.

**FLORIDA'S TREATMENT OF ENTIRETY PROPERTY:
DO UNSECURED JOINT CREDITORS LOSE THE
BENEFIT OF THEIR BARGAIN OR ACHIEVE A HIGHER
STATUS THAN SPECIFICALLY PROVIDED BY THE
BANKRUPTCY CODE?**

*Julio E. Castro III **

I.	INTRODUCTION	275
II.	OVERVIEW OF ENTIRETY PROPERTY	277
III.	ENTIRETY PROPERTY UNDER THE OLD BANKRUPTCY ACT	279
IV.	ENTIRETY PROPERTY UNDER THE BANKRUPTCY CODE . . .	281
	A. <i>Inclusion Within the Bankruptcy Estate</i>	281
	B. <i>Overview of Section 522(b)(2)(B)</i>	284
	C. <i>The Sumy Decision</i>	286
	D. <i>Florida's Treatment of Entirety Property</i>	289
V.	PROPOSED TREATMENT OF ENTIRETY PROPERTY	292
	A. <i>Exempt Entirety Property from the Bankruptcy Estate</i>	293
	B. <i>Limit the Exemption Under Section 522(b)(2)(B)</i>	294
	C. <i>Disallow the Exemption to the Extent of Joint Claims and Distribute the Proceeds to All Unsecured Creditors</i>	296
	D. <i>Congress Should Amend the Relevant Code Sections</i> .	298
VI.	CONCLUSION	298

I. INTRODUCTION

A current issue in bankruptcy law is the treatment of entirety property. The different treatments courts afford this property determines both the amount of property subject to sale and which creditors receive the proceeds. The significance of these decisions carries beyond the bankruptcy context to the initial credit decision, affecting how creditors structure transactions to minimize the risks inherent in the lending process. The

* This note is dedicated to my wife, Tana, and mother, Nelsy, who have always encouraged me to pursue excellence.

Bankruptcy Code allows states to “opt out” of the federal exemptions and replace them with exemptions afforded by the particular state.¹ A majority of states have, in fact, opted out and thus state exemptions are the primary source of determining the pool of assets to satisfy creditor claims.²

In Florida, married couples enjoy the protection of liberal exemption laws.³ Specifically, Article X, Section 4 of the Florida Constitution protects a married couple’s residence from a forced sale by a general creditor.⁴ In addition, a husband and wife can hold both non-residential real property and personal property by the entirety creating similar protection.⁵ For example, a creditor of one spouse cannot levy and execute on property owned by a husband and wife as tenants by the entirety.⁶ The purpose of the liberal exemptions for Florida residents is to ensure the availability of minimal assets in the event the debtor suffers financial difficulty.⁷

Because Florida has opted to apply its exemptions in bankruptcy proceedings, a debtor in bankruptcy enjoys the same protections afforded by nonbankruptcy law. If one spouse files for bankruptcy, that spouse can exempt entirety property from the pool of assets available to creditors to the extent the property is “exempt . . . under applicable nonbankruptcy law.”⁸ However, the bankruptcy courts’ inconsistent treatment of entirety property, both in the amount of the exemption and the distribution of the proceeds, has created uncertainty between debtors and creditors.⁹ A pri-

1. See *infra* notes 58-61 and accompanying text.

2. See *infra* notes 58-61 and accompanying text.

3. See Michael G. Williamson & Benjamin P. Butterfield, *Florida Exemption Laws—Haven For Debtors or Protection From Destitution?*, 15 STETSON L. REV. 437, 437-41 (1986) (noting Florida exemption laws provide debtor residents the opportunity for abuse).

4. See FLA. CONST. art. X, § 4. Article X, Section 4 provides in part:

(a) There shall be exempt from forced sale under process of any court, and no judgment, decree or execution shall be a lien thereon, except for the payment of taxes and assessments thereon, obligations contracted for the purchase, improvement or repair thereof, or obligations contracted for house, field or other labor performed on the realty, the following property owned by a natural person:

(1) a homestead, if located outside a municipality, to the extent of one hundred sixty acres of contiguous land and improvements thereon, which shall not be reduced without the owner’s consent by reason of subsequent inclusion in a municipality; or if located within a municipality, to the extent of one-half acre of contiguous land, upon which the exemption shall be limited to the residence of the owner or his family;

(2) personal property to the value of one thousand dollars.

(b) These exemptions shall inure to the surviving spouse or heirs of the owner.

Id.

5. See *infra* text accompanying notes 11-21.

6. *Stanley v. Powers*, 153 Fla. 359, 166 So. 843, 846 (Fla. 1936).

7. *West Fla. Grocery Co. v. Teutonia Fire Ins. Co.*, 74 Fla. 220, 77 So. 209, 212 (Fla. 1917).

8. Bankruptcy Reform Act of 1978, 11 U.S.C. § 522(b)(2)(B) (1988).

9. See Benjamin C. Ackerly, *Tenants by the Entirety Property and the Bankruptcy Reform Act*,

mary debtor concern is how much entirety property the debtor will retain as exempt to ensure a "fresh start."¹⁰ On the other hand, creditors have two main concerns in the bankruptcy context. The first is whether tenancy by the entirety property is included in the bankruptcy estate to settle claims.¹¹ The second is which creditors will benefit from the distribution of the proceeds from the sale of entirety property.¹² Because the Eleventh Circuit Court of Appeals has not decided these issues, uncertainty continues to exist in the bankruptcy area in Florida.

This note focuses on the different treatment of entirety property by the bankruptcy courts. Part II provides an overview of the concept of entirety property. Part III reviews the treatment of entirety property under the old Bankruptcy Act of 1898. Part IV analyzes the treatment of entirety property under the new Bankruptcy Code. This section also discusses how federal and Florida courts treat entirety property. Part V offers a solution to resolve the issues involved in treating entirety property. Part VI suggests problems the bankruptcy courts will face until Congress amends the relevant statutes.

II. OVERVIEW OF ENTIRETY PROPERTY

Tenancy by the entirety is a form of concurrent ownership of property enjoyed by married couples in Florida.¹³ To create a tenancy by the en-

21 WM. & MARY L. REV. 701, 701 (1980); Patrick J. Concannon, *Bankruptcy and Tenancy by the Entirety Property: Its Treatment Under the Code and in the Courts*, 58 UMKC L. REV. 501 (1990) (analyzing the different treatments of entirety property under the new bankruptcy code); Lawrence Kalevitch, *Some Thoughts on Entireties in Bankruptcy*, 60 AM. BANKR. L.J. 141, 145-47 (1986) (discussing the Fourth Circuit's varied treatment before the *Sumy* decision); Williamson & Butterfield, *supra* note 3, at 453-58 (noting the different treatments of entirety property in bankruptcy); Paul C. Wilson, "Fresh" Start or "Head Start": Missouri Courts Rethink the Role of Tenancies by the Entirety in Bankruptcy, 56 MO. L. REV. 817, 817 (1991) (noting the varied treatment of entirety property in Missouri).

10. The Committee of the Judiciary of the House of Representatives recognized that "an individual debtor [can] take out of the estate that property that is necessary for a fresh start and for the support of himself and his dependents." H.R. REP. NO. 595, 95th Cong., 2d Sess. 176 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6136.

11. *See In re Anderson*, 132 B.R. 657, 659 (Bankr. M.D. Fla. 1991).

12. *See id.*

13. RALPH E. BOYER, *FLORIDA REAL ESTATE TRANSACTIONS* § 20.02 (1992); PAUL C. GIBSON, *FLORIDA REAL ESTATE TRANSACTIONS* § 5.03 (1993). There are two other types of concurrent ownership of property: joint tenancy and tenants in common. *See* BOYER, *supra* §§ 20.01, .03. A thorough discussion of these types of concurrent ownerships are beyond the scope of this note. However, a few comments about tenants and joint tenancy are necessary in order to appreciate the significance of the tenancy by the entirety.

Tenants In Common:

This form of concurrent ownership requires the unity of possession. GIBSON, *supra*, § 5.01. Thus each tenant must be able to have use of the property. *Id.* Creditors of an individual tenant may enforce a claim against the individual interest. RICHARD R. POWELL & PATRICK J. ROHAN, 4A

tirety, the four unities of possession, title, time, and interest must be present.¹⁴ A fifth unity of marriage distinguishes this estate from the common law joint tenancy.¹⁵ A married couple can create entirety property in both realty and personalty.¹⁶ Thus, in Florida a husband and wife can enjoy the protections afforded entirety property in all their assets.

There are two fundamental benefits of ownership as tenants by the entirety. First, neither spouse may sell or encumber entirety property without the consent of the other spouse.¹⁷ Because each spouse is considered an owner of an entire indivisible interest in the property, both parties must act in concert in order to convey the property.¹⁸ The purpose of this rule is to ensure that neither spouse acts unilaterally to the detriment of the other spouse.¹⁹ The second principal benefit is that entirety property is not subject to levy and execution by a creditor with a claim solely against one spouse.²⁰ Thus, the non-debtor spouse is protected from the creditors of the debtor spouse.²¹ The creditor with a single claim can only proceed against that spouse's individual assets.²²

POWELL ON REAL PROPERTY ¶ 605(2) (1993).

Joint Tenancy:

This form of concurrent ownership is held by two or more people and requires the four unities of time, title, possession, and interest. GIBSON, *supra*, § 5.02. Each interest in a joint tenancy is subject to claims of creditors. POWELL & ROHAN, *supra*, ¶ 618[1][c]. The lien creditor would become a tenant in common and could seek partition of the property. GIBSON, *supra*, § 5.02.

See generally John M. Starling, *The Tenancy by the Entireties in Florida*, 14 FLA. L. REV. 111 (1961) (discussing the origins and application of the concept of entirety property in Florida). *But cf.* Paul Ritter, *A Criticism of the Estate by the Entirety*, 5 FLA. L. REV. 153 (1952) (arguing for the abrogation of the doctrine of tenancy by the entirety).

14. *First Nat'l Bank v. Hector Supply Co.*, 254 So. 2d 777, 781 (1971). Possession requires both husband and wife to have joint ownership and control of the property. *Id.* Time requires the interest to commence simultaneously. *Id.* Title requires the interest to be from the same instrument. *Id.* Interest requires that the spouses' interests be the same. *Id.*

15. *Id.*; see also GIBSON, *supra* note 13, § 5.03 (stating that marriage is required as well as unity of interest, time, title, and possession for tenancy by the entireties).

16. *Great S.W. Fire Ins. Co. v. Dewitt*, 458 So. 2d 398, 400 (Fla. 1st DCA 1984). The Florida Supreme Court has stated:

In realty matters, where property is acquired specifically in the name of the husband and wife, we consider it to be a rule of construction that a tenancy by the entireties is created, although fraud may be proven. But in personalty matters, a different standard obtains: not only must the form of the estate be consistent with entirety requirements, but the intention of the parties must be proven.

Hector, 254 So. 2d at 780 (citation omitted). Self serving statements are insufficient in establishing a tenancy by the entirety in personalty. *In re Shaland*, 133 B.R. 166, 168 (Bankr. S.D. Fla. 1991).

17. See *supra* note 13; BOYER, *supra* note 13, § 20.02.

18. See *Bailey v. Smith*, 89 Fla. 303, 103 So. 833, 834 (Fla. 1925); GIBSON, *supra* note 13, § 5.03.

19. GIBSON, *supra* note 13, § 5.03.

20. *Id.*

21. *Id.*

22. *Stanley v. Powers*, 123 Fla. 359, 166 So. 843, 845-46 (Fla. 1936).

Creditors are aware of the unique status afforded married couples who hold property by the entirety. To ensure recourse against all of a married couple's assets, creditors will negotiate to have both spouses liable on a debt.²³ Thus, a joint creditor can levy and satisfy the debt against a greater pool of assets. The ability to levy on the entirety property diminishes the protection available to married couples but the joint creditor usually gives the debtor more favorable terms in exchange for for this added protection. Consequently, the joint creditor enjoys this greater protection vis-à-vis a single creditor under Florida law.

III. ENTIRETY PROPERTY UNDER THE OLD BANKRUPTCY ACT

The controversy with entirety property arises when a husband and wife owe a joint obligation to a creditor and one spouse files for bankruptcy.²⁴ Under section 70(a)(5) of the old Bankruptcy Act, the bankruptcy estate included all property "which prior to the filing of the petition [the debtor] could by any means have transferred or which might have been levied upon and sold under judicial process."²⁵ State law prohibited a spouse from transferring entirety property or allowing creditors to levy solely upon the debtor's interest in entirety property.²⁶ Thus, the estate excluded the debtor spouse's interest in entirety property.²⁷ In addition, the debtor received a discharge from all obligations, including the joint debts owed with the nonfiling spouse.²⁸ The discharge insulated the debtor from future personal liability on all the debts subject to the discharge.²⁹

After the bankrupt spouse received the discharge, the creditors with joint claims were unable to obtain and execute a judgment against the entirety property because only the nonfiling spouse was personally liable on the debt.³⁰ Therefore, the creditor could only obtain and execute a judgment on the assets of the nonfiling spouse because the bankrupt spouse's discharge eliminated his or her liability.³¹ This result deprived joint creditors of the benefit of their bargain.³²

23. Williamson & Butterfield, *supra* note 3, at 462 (noting that creditors may also protect their interests by securing an interest in property of the debtor).

24. See *supra* note 9 and accompanying text.

25. The Bankruptcy Act of 1898, ch. 541, § 70(a)(5), 30 Stat. 544, 566 (repealed 1978).

26. See *supra* text accompanying notes 13-22.

27. Phillips v. Krakower, 46 F.2d 764, 765 (4th Cir. 1931).

28. *Id.*

29. *Id.*

30. *Id.*

31. *Id.*

32. *Id.* The Phillips court noted that the purpose of the Bankruptcy Act was to distribute equitably the debtor's assets among the debtor's creditors and not to allow the debtor to use bankruptcy to perpetrate a fraud. *Id.*

A majority of courts recognized this inequitable gap in the old Bankruptcy Act and allowed joint creditors to get relief from the automatic stay to pursue their claims in state court.³³ The Fourth Circuit, in *Reid v. Richardson*,³⁴ recognized that a discharge would absolve the bankrupt debtor of all legal responsibility on debts both joint and several in the federal courts.³⁵ Consequently, the discharge would reduce the creditor's joint claim to a single obligation of the nonfiling spouse.³⁶ The court agreed with the lower court that to allow the joint debtors to keep the entirety property without subjecting the property to claims in bankruptcy was tantamount to "legal fraud."³⁷ The Fourth Circuit held that the old Bankruptcy Act did not contemplate this result and lifted the automatic stay to allow the joint creditor to proceed in state court to satisfy its claim.³⁸

A minority of courts adhered to the literal language of the old Bankruptcy Act and allowed the bankrupt debtor's discharge.³⁹ Therefore, if joint creditors did not act promptly before the debtor filed for bankruptcy, the debtor's discharge would eliminate his or her personal liability, and the creditor would no longer be able to proceed against the entirety property for satisfaction of its claim.⁴⁰ The courts' inconsistent treatment of entirety property created uncertainty for all parties under the old Bankruptcy Act.

33. *Id.* at 766.

34. 304 F.2d 351 (4th Cir. 1962).

35. *Id.* at 354.

36. *See id.*

37. *Id.* Judge Parker, to whom the *Reid* court cited, defined "legal fraud" as the "effectual withdrawing of the property from the reach of those entitled to subject it to their claims, for the beneficial ownership and possession of those who created the claims against it." *Phillips*, 46 F.2d at 765.

38. *Reid*, 304 F.2d at 355.

39. *See Fetter v. United States*, 269 F.2d 467 (6th Cir. 1959). In *Fetter*, a husband and wife were jointly liable on unsecured notes. *Id.* at 468. The husband filed for bankruptcy and received a discharge on all the debts. *Id.* After the discharge, a joint creditor of the married couple filed suit to levy and execute on the entirety property. *Id.* The Sixth Circuit held that the husband's discharge relieved him from liability on the claim and the joint creditor could not proceed on the entirety property. *Id.* at 471. This case illustrated the problems under the old act when the creditor did not obtain a relief from the stay to satisfy the joint obligation. *See also Harris v. Manufacturers Nat'l Bank*, 457 F.2d 631, 636 (6th Cir.) (refusing to adopt a state remedy which directly conflicts with the specific requirements of the Bankruptcy Act and noting that Congress was aware of the problem of allowing the bankrupt to obtain a discharge without having to surrender entirety property to the trustee), *cert. denied*, 409 U.S. 885 (1972).

40. *Harris*, 457 F.2d at 636; *see also supra* notes 24-32 and accompanying text (explaining why the creditor could not proceed against entirety property after bankruptcy).

IV. ENTIRETY PROPERTY UNDER THE BANKRUPTCY CODE

The Bankruptcy Reform Act of 1978,⁴¹ hereinafter referred to as the Code, replaced the old Bankruptcy Act of 1898.⁴² However, the Code's treatment of entirety property when one spouse files for bankruptcy remains uncertain.⁴³ Under the Code, the initial inquiry is to determine the status of entirety property within the estate.⁴⁴ The second question is to determine the extent of the distribution of the debtor's interest in entirety property to the creditors of the estate.⁴⁵ Although these inquiries seem straightforward, the bankruptcy courts have inconsistently addressed these issues.⁴⁶ This section will analyze the relevant Code sections and examine the different treatments by the courts.

A. Inclusion Within the Bankruptcy Estate

Section 541(a)(1) of the Code replaced former section 70(a) of the predecessor act.⁴⁷ Subject to a few exceptions, section 541(a)(1) creates an estate comprised of "all legal or equitable interests of the debtor in property as of the commencement of the case."⁴⁸ This all-inclusive provision of the Code represents a significant departure from the practice under the old act. For example, section 70(a)(5) of the old act required the debtor to meet a "transferability or leviability" test before inclusion within the

41. Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified as amended at 11 U.S.C. §§ 101-1330 (1988 & Supp. IV 1992)).

42. Section 401, 92 Stat. at 2682 (repealing the Bankruptcy Act of 1898). *See generally* U.S. CONST. art. I, § 8 (stating that Congress has the power to establish uniform laws on the subject of bankruptcy).

43. *See supra* note 9 and accompanying text.

44. *In re Anderson*, 132 B.R. 657, 659 (Bankr. M.D. Fla. 1991).

45. *Id.*

46. *See supra* note 9 and accompanying text.

47. *See supra* note 42.

48. 11 U.S.C. § 541(a)(1) (1988). Section 541(b) provides in part that:

Property of the estate does not include—

- (1) any power that the debtor may exercise solely for the benefit of an entity other than the debtor;
- (2) any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease before the commencement of the case under this title, and ceases to include any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease during the case;
- (3) any eligibility of the debtor to participate in programs authorized under the Higher Education Act of 1965 (20 U.S.C. 1001 et seq.; 42 U.S.C. 2751 et seq.), or any accreditation status or State licensure of the debtor as an educational institution.

11 U.S.C. § 541(b) (Supp. IV 1992). Section 541(c)(2) provides an exception for: "A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title." 11 U.S.C. § 541(c)(2) (1988).

estate.⁴⁹ Because the debtor can not individually transfer the entirety property, nor can creditors levy solely on the debtor's interest, the property under the old act was not subject to administration by the trustee.⁵⁰ The Code, on the other hand, requires inclusion of all the debtor's legal and equitable interests.⁵¹ This results in a larger estate than under the old act.

The estate under the old act also was more limited because exempt property under state law was specifically excluded from administration by the trustee.⁵² The Supreme Court, in *Lockwood v. Exchange Bank*,⁵³ confirmed the unambiguous language of the statute holding that Congress intended exempt property to remain with the debtor and not pass to the trustee.⁵⁴ Under the Code, the legislative history of section 541(a) reveals congressional intent to depart from the *Lockwood* holding by including exempt property as part of the bankruptcy estate. The legislative history states:

Paragraph (1) has the effect of overruling *Lockwood v. Exchange Bank*, 190 U.S. 294 (1903), because it includes as property of the estate all property of the debtor, even that needed for a fresh start. After the property comes into the estate, then the debtor is permitted to exempt it under proposed 11 U.S.C. 522, and the court will have jurisdiction to determine what property may be exempted and what remains as property of the estate.⁵⁵

Therefore, all of the debtor's property interests become property of the estate subject to exemption by another Code section.⁵⁶

49. Bankruptcy Act of 1898, ch. 541, § 70(a)(5), 30 Stat. 544, 566 (repealed 1978). Section 70(a)(5) includes all "property which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against." *Id.*; see also *In re Koehler*, 6 B.R. 203, 205 (Bankr. M.D. Fla. 1980) (providing an overview of the treatment of entirety property under the pre-Code law).

50. Bankruptcy Act of 1898, ch. 541, § 70(a)(5), 30 Stat. 544, 566 (repealed 1978).

51. See 11 U.S.C. § 541 (1988 & Supp. IV 1992).

52. Bankruptcy Act of 1898, ch. 541, § 70(a), 30 Stat. 544, 565 (repealed 1978). Section 70(a) provided that title shall vest in the trustee of a bankrupt estate "as of the date he was adjudged a bankrupt, except in so far as it is to property which is exempt." *Id.*

53. 190 U.S. 294 (1903).

54. *Id.* at 299-300.

55. H.R. REP. NO. 595, 95th Cong., 2d Sess. 368 (1978), reprinted in 1978 U.S.C.C.A.N. 5963, 6324 (footnotes omitted).

56. *Id.* In addition, the Committee on the Judiciary of the House of Representatives stated:

[A]ll interests, such as interests in real or personal property, tangible and intangible . . . whether or not transferable by the debtor [are included in the estate].

. . . Certain restrictions on the transferability of property will prevent the trustee from realizing on some items of property of the estate. But on the whole, the trustee will be able

To further support the all-inclusiveness of section 541(a), judges and commentators point out that if the Code excluded entirety property from the bankruptcy estate, then other sections of the Code would be nullities.⁵⁷ Specifically, sections 522(b)(2)(B) and 363(h) rely on the inclusion of entirety property within the bankruptcy estate. Section 522(b)(2)(B) exempts the debtor's interest in entirety property "to the extent that such interest . . . is exempt . . . under applicable nonbankruptcy law."⁵⁸ Section 363(h) permits the trustee to sell the debtor's interest in entirety property provided certain qualifications are met.⁵⁹ These two sections indicate that Congress intended to include the debtor's interest in property by the entirety as property of the estate and to exempt or sell the interest through other Code sections.⁶⁰

to bring all property together for a coherent evaluation of its value and transferability, and then to dispose of it for the benefit of the debtor's creditors.

H.R. REP. NO. 595, 95th Cong., 2d Sess. 175-77 (1978), reprinted in 1978 U.S.C.C.A.N. 5963, 6136-37 (footnotes omitted).

57. See *In re Amici*, 99 B.R. 100, 102 (Bankr. M.D. Fla. 1989) (stating that § 363(h) authorizes the trustee to sell the entirety property and that exempting the debtor's interest would render this section meaningless); Kalevitch, *supra* note 9, at 142-43; Wilson, *supra* note 9, at 824.

58. 11 U.S.C. § 522(b)(2)(B) (1988). Section 522(b)(2)(B) provides that

any interest in property in which the debtor had, immediately before the commencement of the case, an interest as a tenant by the entirety or joint tenant to the extent that such interest as a tenant by the entirety or joint tenant is exempt from process under applicable nonbankruptcy law.

Id.

59. 11 U.S.C. § 363(h) (1988). Section 363(h) allows the trustee:

Notwithstanding subsection (f) of this section, the trustee may sell both the estate's interest, under subsection (b) or (c) of this section, and the interest of any co-owner in property in which the debtor had, at the time of the commencement of the case, an undivided interest as a tenant in common, joint tenant, or tenant by the entirety, only if—

- (1) partition in kind of such property among the estate and such co-owners is impracticable;
- (2) sale of the estate's undivided interest in such property would realize significantly less for the estate than sale of such property free of the interests of such co-owners;
- (3) the benefit to the estate of a sale of such property free of the interests of co-owners outweighs the detriment, if any, to such co-owners; and
- (4) such property is not used in the production, transmission, or distribution, for sale, of electric energy or of natural or synthetic gas for heat, light, or power.

Id.; see also *In re Geoghegan*, 101 B.R. 329, 331 (Bankr. M.D. Fla. 1989) (noting that if the trustee cannot meet the requirements of § 363(h), the property must be abandoned). Congress also provided protection for the nonfiling spouse by allowing the nonfiling spouse a right of first refusal at a sale of entirety property. See 11 U.S.C. § 363(i) (1988). Additionally, the trustee is required to distribute the value of the spouse's interest in the proceeds to the spouse, if the property is sold to a third party. See 11 U.S.C. § 363(j).

60. See H.R. REP. NO. 595, 95th Cong., 2d Sess. 176-77 (1978), reprinted in 1978 U.S.C.C.A.N. 5963, 6136-38. In addition, the House Judiciary Committee in its Report addressed the issue of whether the debtor's interest in entireties property is property of the estate when it stated:

The bill also changes the rules with respect to marital interests in property With respect to other co-ownership interest, such as tenancies by the entirety, joint tenancies, and

It is clear that section 541(a) of the Code includes property held by the entirety. The legislative history and the interrelationships among the code sections evidences congressional intent to include the debtor's interest in entireties property within the bankruptcy estate. Once included under section 541(a)(1), the debtor can exempt the property under section 522(b)(2)(B). If the debtor cannot exempt the interest in the entirety property, then the trustee may dispose of the nonexempt interest under section 363(h) provided certain conditions are met.

B. Overview of Section 522(b)(2)(B)

Once the entirety property is included in the estate under section 541 of the Code, the debtor is entitled to exempt certain property under section 522.⁶¹ The policy behind the bankruptcy exemptions is to permit the debtor to come out of bankruptcy with adequate possessions to begin a fresh start.⁶² Section 522(b)(1) provides a schedule of federal exemptions available to the debtor in those states which authorize the use of the federal exemptions.⁶³ Florida, like many states, has "opted out" of the federal exemptions and allows the debtor those exemptions available under state and federal nonbankruptcy law.⁶⁴ The Code specifically provides for the exemption

tenancies in common, the bill does not invalidate the rights, but provides a method by which the estate may realize on the value of the debtor's interest in the property while protecting the other rights. The trustee is permitted to realize on the value of the property by being permitted to sell it without obtaining the consent or a waiver of rights by the spouse of the debtor or the co-owner, as may be required for a complete sale under applicable State law.

Id. at 6137-38 (footnotes omitted).

61. See *supra* text accompanying notes 54-59.

62. H.R. REP. NO. 595, 95th Cong., 2d Sess. 176 (1978), reprinted in 1978 U.S.C.C.A.N. 5963, 6136.

63. 11 U.S.C. § 522(b)(1) (1988). Under the Bankruptcy Act of 1898, the debtor was entitled to the exemptions in effect in the state of the debtor's domicile at the time of the filing. Bankruptcy Act of 1898, ch. 541, § 6, 30 Stat. 544, 548 (repealed 1978).

64. FLA. STAT. § 222.20 (1991). Section 222.20 of the Florida Statutes provides:

In accordance with the provisions of s. 522(b) of the Bankruptcy Code of 1978 (11 U.S.C. s. 522(b)), residents of this state shall not be entitled to the federal exemptions provided in s. 522(d) of the Bankruptcy Code of 1978 (11 U.S.C. s. 522(d)). Nothing herein shall affect the exemptions given to residents of this state by the State Constitution and the Florida Statutes.

Id. The states that have opted out include: "Alabama, Arizona, Arkansas, California, Colorado, Delaware, Florida, Georgia, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Mississippi, Missouri, Montana, Nebraska, Nevada, New Hampshire, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, South Dakota, Tennessee, Utah, Virginia, West Virginia, and Wyoming." 7 COLLIER ON BANKRUPTCY 1 n.6 (Lawrence P. King ed., 15th ed., 1993). The legislative history provides a list of federal nonbankruptcy law that the debtor may use to exempt property if the states "opt-out" of the federal exemptions provided under § 522(d). H.R. REP. NO. 595, 95th Cong., 2d Sess. 360 (1978), reprinted in 1978 U.S.C.C.A.N. 5963, 6316. These federal laws include:

of entirety property in section 522(b)(2)(b), stating:

Notwithstanding section 541 of this title, an individual debtor may exempt from property of the estate the property listed in . . . paragraph (2) of this subsection [A]ny interest in property in which the debtor had, immediately before the commencement of the case, an interest as a tenant by the entirety . . . to the extent that such interest . . . is exempt from process under applicable nonbankruptcy law.⁶⁵

The controversy in Florida, as well as other states that recognize tenancy by the entireties, involves determining the extent the entirety interest is exempt under applicable nonbankruptcy law.⁶⁶

Under state law, a creditor cannot levy and execute a judgment on the debtor's interest in entirety property, but a joint creditor can satisfy its claim

-
- Foreign Service Retirement and Disability payments, 22 U.S.C. 1104;
 - Social security payments, 42 U.S.C. 407;
 - Injury or death compensation payments from war risk hazards, 42 U.S.C. 1717;
 - Wages of fishermen, seamen, and apprentices, 46 U.S.C. 601;
 - Civil service retirement benefits, 5 U.S.C. 729, 2265;
 - Longshoremen's and Harbor Workers' Compensation Act death and disability benefits, 33 U.S.C. 916;
 - Railroad Retirement Act annuities and pensions, 45 U.S.C. 228(L);
 - Veterans benefits, 45 U.S.C. 352 (E);
 - Special pensions paid to winners of the Congressional Medal of Honors, 38 U.S.C. 3101; and
 - Federal homestead lands on debts contracted before issuance of the patent, 43 U.S.C. 175.

Id.

65. 11 U.S.C. § 522(b)(2)(B) (1988). Congress was not clear with the treatment of entirety property under current § 522(b)(2)(B). However, the House and Senate considered changes to § 522(b)(2)(B). *Napotnik v. Equibank & Parkvale Sav. Ass'n*, 679 F.2d 316, 321 (3d Cir. 1982). One consideration included:

(b) Notwithstanding section 541 of this title, an individual debtor may exempt from property of the estate

(2) any property or interest of the debtor in property, as of the date of the filing of the petition, to the extent that such property or interest in property is exempt or not subject to process or levy under Federal law, other than subsection (d) of this section, or is exempt or not subject to levy by a creditor, of only the debtor, on a simple contract whether or not such a creditor exists, under State or local law that is applicable on the date of the filing of the petition at the place in which the debtor's domicile has been located for the 180 days immediately preceding the date of the filing of the petition, or for a longer portion of such 180-day period than in any other place.

Id. (quoting 126 CONG. REC. S15163 (daily ed. Dec. 1, 1980) and 126 CONG. REC. H9293 (daily ed. Sept. 22, 1980)). This proposed amendment would have allowed a debtor who files for bankruptcy to exempt that part of his entirety interest that would have been subject to claims by joint creditors. *Id.*

66. See 11 U.S.C. § 522(b)(2)(B) (1988).

against entirety property.⁶⁷ Does it follow that entirety property is not exempt to the extent of the amount of all joint creditors' claims in bankruptcy? The courts are split on this issue.⁶⁸ Some courts have held that so long as one joint creditor exists on the date of the petition, the debtor's entire interest in entirety property is available for distribution to all creditors.⁶⁹ Congress did not clearly answer this question in the language of section 522(b)(2)(B).⁷⁰ Thus, a critical two-prong inquiry remains: (1) how much of the debtor's interest in the entirety property is available for distribution, and (2) which creditors should benefit from the debtor's denied exemption?⁷¹

C. *The Sumy Decision*

Analyzing section 522(b)(2)(B), the Fourth Circuit held that entirety property is not exempt to the extent of joint creditors' claims against the estate.⁷² In *Sumy v. Schlossberg*,⁷³ the bankruptcy trustee objected to the debtor's exemption of entirety property under section 522.⁷⁴ The court held that the entirety property was not exempt to the extent that the debtor and the nonfiling spouse were indebted to joint creditors.⁷⁵ The Fourth Circuit reasoned that because a joint creditor can satisfy claims with a judgment on entirety property under state law, a debtor loses the benefit of section 522(b)(2)(B) to the extent of joint claims.⁷⁶ Therefore, the debtor's interest in entirety property can be administered in bankruptcy under section 363(h)

67. See *supra* text accompanying notes 13-22.

68. Compare *Napotnik*, 679 F.2d at 321 (holding that the debtor's interest in the entirety property is available to the extent of the joint obligations) with *In re Amici*, 99 B.R. 100, 103 (Bankr. M.D. Fla. 1989) (holding that provided a joint creditor exists at the date of filing the petition, the debtor's entire interest is available to satisfy the interests of all creditors pursuant to § 726).

69. *Amici*, 99 B.R. at 103.

70. See *supra* notes 65-66 and accompanying text.

71. See *In re Anderson*, 132 B.R. 657, 659 (Bankr. M.D. Fla. 1991). Much of the controversy has centered around the application of § 522(b)(2)(B). See *Amici*, 99 B.R. at 102. However, after determining the amount of property available, the courts differ on whether only the joint creditors should share in the proceeds or whether all unsecured creditors under the distribution scheme of § 726 should share. Compare *Sumy v. Schlossberg*, 777 F.2d 921, 932 (4th Cir. 1985) (giving the proceeds of the sale to only the joint creditors) with *Amici*, 99 B.R. at 102-03 (allowing all creditors to benefit from the distribution of the sale proceeds). Congress has provided under § 726(a)(1) that distributions be made first to priority claims under § 507. See 11 U.S.C. § 726(a)(1) (1988). Second, all allowed unsecured claims of both single and joint creditors shall be paid. 11 U.S.C. § 726(a)(2) (1988). This section is Congress' only articulated scheme for distribution of proceeds of the estate. Thus, the remainder of this note will focus not only on the extent of the exemption available to the debtor, but the propriety of distributing the proceeds solely to joint creditors or to all creditors that would have equal priority under § 726(a)(2).

72. *Sumy*, 777 F.2d at 932.

73. 777 F.2d 921 (4th Cir. 1985).

74. *Id.* at 922.

75. *Id.* at 932.

76. *Id.* at 927.

to the extent of joint claims for the benefit of joint creditors.⁷⁷ Any creditor with a claim only against the debtor would not benefit from the sale of the entirety property.⁷⁸ Excess proceeds, if any, would be exempt for the debtor.⁷⁹

The *Sumy* court refused to follow *Greenblatt v. Ford*,⁸⁰ an earlier Fourth Circuit decision.⁸¹ The *Ford* court exempted a debtor's entirety property from the bankruptcy estate because the debtor's interest was exempt from levy and execution by both individual and joint creditors under Maryland law.⁸² The *Ford* court's interpretation of section 522(b)(2)(B) focused on the notion that an individual interest in entirety property cannot be subject to the claims of any creditors.⁸³ Thus, the debtor's individual interest was exempt in bankruptcy.⁸⁴ The *Sumy* court distinguished *Ford* because the facts in *Ford* did not indicate the presence of joint creditors.⁸⁵ Consequently, the *Sumy* court refused to adopt the *Ford* court's suggestion in dicta that since an individual interest is exempt under state law, the exemption should apply in bankruptcy.⁸⁶

The *Sumy* court voiced concern over the foreseeable consequences of lifting the automatic stay and allowing joint creditors to pursue their claims in state court.⁸⁷ Guided by the fundamental bankruptcy principle of equal treatment of similarly situated creditors, the court recognized that lifting the stay would only create a race among joint creditors to obtain a judgment and execution against the debtor's property.⁸⁸ State law would determine priority, and diligent creditors would be rewarded for their efforts at the expense of other creditors.⁸⁹ Thus, the result would violate bankruptcy's equal treat-

77. *Id.* at 931-32.

78. *See id.* at 927-28.

79. *Id.*

80. 638 F.2d 14 (4th Cir. 1981).

81. *Sumy*, 777 F.2d at 926.

82. *Ford*, 638 F.2d at 15.

83. *See id.*

84. *See id.*

85. *Sumy*, 777 F.2d at 926.

86. *Id.*

87. *Id.* Section 362 operates as an injunction, applicable to all creditors, against the commencement or continuation of any action adverse to the debtor or the debtor's property. *See* 11 U.S.C. § 362 (1988).

88. *Sumy*, 777 F.2d at 932. The court seems to define similarly situated creditors as creditors with claims against both spouses. *See id.* However, the Code under the distribution scheme of § 726(a)(2) provides equal treatment for all unsecured claims, individual and joint, despite the unique status of joint creditors under state law. 11 U.S.C. § 726 (1988); *see also supra* note 68 (giving a brief explanation of the controversy concerning the payment of joint creditors under § 726).

89. *Id.* at 932. Moreover, the court noted that by allowing the joint creditors to pursue their claims in state court, each creditor could incur additional and duplicative expenses which could be eliminated by administering the property in the bankruptcy court. *See id.* In addition, some joint creditors may not have the incentive to pursue their claims because of the low dollar amount, thus losing

ment principle.⁹⁰

The *Sumy* court also recognized the potential problems associated with exempting the property.⁹¹ A discharge in bankruptcy relieves the debtor of personal liability on all prebankruptcy debts.⁹² After bankruptcy, the debtor is no longer obligated on a joint claim with the nonfiling spouse.⁹³ Thus, the joint creditor can no longer proceed on the entirety property because the claim has been reduced to one solely against the nonfiling spouse.⁹⁴ To protect the joint creditor's bargain, the *Sumy* court noted that bankruptcy courts could allow joint creditors to proceed in state court as a condition of the debtor's discharge, but acknowledged that some bankruptcy courts may not allow this result.⁹⁵ Additionally, the court stated that section 522(c) protects the debtor's exempt property from the claims of creditors that arose before the commencement of the case.⁹⁶

According to the *Sumy* court, the debtor may use the Code's broad powers to avoid liens on the exempt property.⁹⁷ The debtor, under section 522(f), may avoid any pre-petition lien to the extent the lien impairs the exemption on entirety property.⁹⁸ Thus, the joint creditor would be stripped

out on the opportunity to satisfy their claims against the joint debtors' property. *Id.*

90. *Id.*

91. *Id.* at 929-31.

92. *Id.* at 929. Section 524(a) of the Bankruptcy Reform Act provides:

A discharge in a case under this title—

(1) voids any judgment at any time obtained, to the extent that such judgment is a determination of the personal liability of the debtor with respect to any debt discharged under section 727, 944, 1141, or 1328 of this title, whether or not discharge of such debt is waived;

(2) operates as an injunction against the commencement or continuation of an action, the employment of process, or any act, to collect, recover or offset any such debt as a personal liability of the debtor, whether or not discharge of such debt is waived.

11 U.S.C. § 524(a) (1988).

93. *See Sumy*, 777 F.2d at 929.

94. *See id.*

95. *Id.* at 930 & n.20.

96. *Id.* at 930-31. Section 522(c) provides: "Unless the case is dismissed, property exempted under this section is not liable during or after the case for any debt of the debtor that arose . . . before the commencement of the case . . ." 11 U.S.C. § 522(c) (1988). Thus, if the court exempted the entirety property, after the debtor received the discharge, the property would be protected by this section from action by the creditor subsequent to the case. *See id.*

97. *Sumy*, 777 F.2d at 930.

98. *Id.* Section 522(f) provides in relevant part:

Notwithstanding any waiver of exemptions, the debtor may avoid the fixing of a lien on an interest of the debtor in property to the extent that such lien impairs an exemption to which the debtor would have been entitled under subsection (b) of this section, if such lien is—

(1) a judicial lien . . .

11 U.S.C. § 522(f) (1988). Thus, any pre-petition liens by the joint creditor can be avoided by this section. *See id.*

of any interest the creditor had before bankruptcy.⁹⁹ In effect, exempting the entirety property would permit the debtor to use the Code to commit "legal fraud."¹⁰⁰ Therefore, the court justified removing the entirety property from the exemption of section 522(b)(2)(B) to avoid this inequitable result.¹⁰¹

The Third and Sixth Circuit Courts of Appeals agree with the *Sumy* decision.¹⁰² The courts focus on the fact that under state law a joint creditor can levy and execute on the entirety property.¹⁰³ As the Fourth Circuit noted, exempting the entirety property completely would allow the debtor to achieve an improper result unavailable outside of bankruptcy.¹⁰⁴ Thus, the property is not exempt under section 522(b)(2)(B).¹⁰⁵ Additionally, the courts distribute the proceeds only to the joint creditors,¹⁰⁶ but it is questionable whether this result is consistent with the distribution scheme of section 726.¹⁰⁷

D. Florida's Treatment of Entirety Property

The Florida bankruptcy courts differ in their treatment of entirety property. One Florida court agrees with the approach taken by the federal court.¹⁰⁸ In *In re Colston*,¹⁰⁹ Bankruptcy Judge George Proctor of the Middle District of Florida, held that a debtor owing a joint obligation with the nonfiling spouse could not exempt the entirety property.¹¹⁰ The debtor sought to exempt personal property held with the nonfiling spouse as tenants by the entirety.¹¹¹ Judge Proctor reasoned that because joint creditors can satisfy claims against entirety property under Florida law, the property was not exempt to the extent of joint claims in bankruptcy.¹¹² Furthermore, the bankruptcy trustee succeeds to the rights of the joint creditors and can administer entirety property according to section 363(h).¹¹³ Thus, the trustee

99. *Sumy*, 777 F.2d at 930.

100. *Id.*; see also *supra* note 37 (giving a definition for legal fraud).

101. *Id.*

102. *Liberty State Bank & Trust v. Grosslight*, 757 F.2d 773, 777 (6th Cir. 1985) (noting that judicial economy would be better served if the property were administered by the bankruptcy court); *Napotnik*, 679 F.2d at 321 (holding that entirety property is not exempt to the extent of joint claims).

103. *Sumy*, 777 F.2d at 928 & n.13.

104. *Id.* at 929.

105. *Id.* at 932.

106. See *id.* None of the circuit courts have addressed why they did not follow the distribution scheme of § 726. This issue has been addressed by Florida's state courts. See *infra* text accompanying notes 111-40.

107. See *supra* note 71.

108. See *In re Colston*, 87 B.R. 193, 195 (Bankr. M.D. Fla. 1988).

109. 87 B.R. 193 (Bankr. M.D. Fla. 1988).

110. *Id.* at 194.

111. *Id.*

112. *Id.*

113. *Id.* at 195.

can distribute the proceeds to joint creditors in an amount equal to their joint claims.¹¹⁴ Any excess proceeds, above the amount of the joint claims, qualifies for the exemption under section 522(b)(2)(B).¹¹⁵ This approach is problematic because it ignores the distribution scheme of section 726 by creating a sub-class of creditors with joint claims that enjoy greater priority than other unsecured creditors.¹¹⁶

Chief Judge Alexander Paskay recognized that distributing the proceeds from the sale of entirety property only to joint creditors was contrary to the distribution scheme provided for in the Code.¹¹⁷ In *In re Amici*,¹¹⁸ the debtor claimed as exempt certain personal property that the trustee sought to liquidate under section 363(h).¹¹⁹ Chief Judge Paskay stated that section 522(b)(2)(B) did not create an additional exemption, but rather was a recognition by Congress of the immunity available under state law for entirety property.¹²⁰ The entirety property is exempt if no joint creditors of the debtor existed at the commencement of the case.¹²¹ Because there was a joint creditor of the debtor and the nonfiling spouse, the court held that the entirety property was not exempt.¹²² The court further held that the proceeds from the liquidation under section 363(h) should be distributed to all creditors pursuant to section 726.¹²³ Thus, joint creditors would have to share equally with other unsecured creditors.¹²⁴

114. *Id.*

115. *See id.*

116. *See In re Amici*, 99 B.R. 100, 102 (Bankr. M.D. Fla. 1989). The Southern District of Florida is in accord with Judge Proctor. *In re Kimmel*, 131 B.R. 223 (Bankr. S.D. Fla. 1991). The debtor tried to exempt both real and personal property held as tenants by the entirety. *Id.* at 225. Judge Weaver limited the exemption on the entirety property to the excess amount of the debtor's interest above the joint claims. *Id.* at 231. Judge Weaver did not specifically state which creditors benefit from the inclusion of the debtor's interest in the entirety property within the estate. *See id.* However, the case relied upon by Judge Weaver for a limited exemption, distributed the proceeds to the joint creditors. *Id.* at 228.

117. *Amici*, 99 B.R. at 102. Judge Paskay was one of the first Florida judges to recognize that entirety property was not exempt when joint creditors of the husband and wife existed. *In re Koehler*, 6 B.R. 203, 205-06 (Bankr. M.D. Fla. 1980). Chief Judge Paskay reasoned that the entirety property was not specifically exempt by statute in Florida. *Id.* at 205. Rather, because of the nature of the ownership interest involved which gives each tenant full undivided ownership control over the property, such entirety property was immune from process by a single creditor. *Id.* at 206. However, Florida law recognized the right of joint creditors to reach entirety property. *Id.* Thus, to the extent joint creditors existed who otherwise could have reached the entirety interest under Florida law, the entirety property was not exempt under § 522(b)(2)(B). *Id.* However, Chief Judge Paskay did not discuss which creditors benefitted from the inclusion of entirety property within the estate. *See id.*

118. 99 B.R. 100 (Bankr. M.D. Fla. 1989).

119. *Id.* at 101.

120. *Id.* at 102.

121. *Id.* at 102-03.

122. *Id.* at 102.

123. *See id.* at 102-03.

124. *See id.*

Chief Judge Paskay recognized the difficulty involved in dealing with entirety property.¹²⁵ Under his approach, joint creditors would be unable to enforce a claim in bankruptcy that they could have enforced outside of bankruptcy.¹²⁶ On the other hand, distributing the proceeds to joint creditors would set up a sub-class of creditors entitled to greater priority than the distribution scheme set up in section 726.¹²⁷ Chief Judge Paskay stated that this distribution violates section 726 because unsecured joint creditors would receive greater priority than other unsecured creditors.¹²⁸ Relying on *Moore v. Bay*,¹²⁹ which is now codified in section 544(b), Chief Judge Paskay noted that the Supreme Court voided a chattel mortgage, not only for the benefit of creditors that existed on the date of execution, but for all creditors who could not have attacked the chattel mortgage under local law.¹³⁰ It follows that, to the extent a joint creditor could have reached the property, the trustee should liquidate the property for the benefit of all creditors under section 363(h).¹³¹ Therefore, Chief Judge Paskay concluded that Congress intended section 522(b)(2)(B) to determine the extent of the exemption under state law while section 726 provides for the distribution of property included within the estate.¹³²

Judge Thomas Baynes of the Middle District of Florida added an interesting twist to Paskay's approach announced in *Amici*.¹³³ On similar facts, in *In re Anderson*,¹³⁴ Judge Baynes held that if a joint creditor existed that could "have process issue[d] under state law," the trustee can administer the debtor's interest under section 363(h).¹³⁵ Once the trustee administered the property, Judge Baynes held that the entirety property lost its legal effect and became property held as tenants in common by both husband and wife.¹³⁶ This result is based upon the fact that the trustee's sale destroyed the unities associated with entirety property.¹³⁷ Thus, the property no longer enjoyed any unique status, and the proceeds from the debtor's interest were subject to distribution under section 726 for the benefit of all creditors.¹³⁸ Moreover, this approach allows the joint creditor to share in the debtor's interest in

125. *Id.* at 102.

126. *Id.*

127. *Id.*

128. *Id.*

129. 284 U.S. 4 (1931).

130. *Amici*, 99 B.R. at 102.

131. *See id.* at 102-03.

132. *See id.*

133. *In re Anderson*, 132 B.R. 657 (Bankr. M.D. Fla. 1991).

134. 132 B.R. 657 (Bankr. M.D. Fla. 1991).

135. *Id.* at 659-60.

136. *Id.* at 660.

137. *See generally* Starling, *supra* note 13 (discussing the concept of entirety property in Florida).

138. *Anderson*, 132 B.R. at 660.

bankruptcy and satisfy any deficiency by pursuing the nonfiling spouse's interest as a tenant in common.¹³⁹

In *In re Boyd*,¹⁴⁰ Judge Lewis Killian, from the Northern District of Florida, determined that section 522(b)(2)(B) provides a debtor with an exemption only for an amount in excess of all joint creditors' claims in bankruptcy.¹⁴¹ Judge Killian, relying on the same reasoning Judge Paskay used in *Amici*, held that the proceeds from the sale of the debtor's interest should benefit all creditors under section 726.¹⁴² Judge Killian's approach differs from Chief Judge Paskay's approach only in the amount available for distribution.¹⁴³ Judge Killian limits this amount to the extent of all joint creditor claims.¹⁴⁴

It is clear that the bankruptcy judges in Florida differ on the treatment of entirety property in bankruptcy. One approach accepted by Florida courts allows the trustee to sell the debtor's interest in entirety property and distribute the proceeds only to the joint creditors of the debtor. This creates a sub-class of creditors not specifically provided for in the Code. In contrast, a second approach includes entirety property within the estate and distributes the proceeds to all creditors pursuant to section 726. A further wrinkle to this approach allows an exemption for the debtor's interest in excess of the joint claims in bankruptcy. This inconsistent treatment in Florida creates uncertainty in commercial transactions, and a change is needed to ensure predictability.

V. PROPOSED TREATMENT OF ENTIRETY PROPERTY

The Eleventh Circuit Court of Appeals has yet to determine the extent to which entirety property is available to satisfy the claims of creditors. There are four possible solutions for the treatment of entirety property in bankruptcy. First, the property can be included in the bankruptcy estate but exempted under section 522(b)(2)(B).¹⁴⁵ Second, the court can limit the exemption available under section 522(b)(2)(B) to the debtor's interest in excess of joint obligations and distribute the proceeds from the sale of the

139. *See id.* This holding reversed an earlier decision by Judge Baynes of the Middle District in *In re Geoghegan*, 101 B.R. 329 (Bankr. M.D. Fla. 1989). Judge Baynes held that entirety property is not exempt to the extent of claims by joint creditors. *Id.* at 331-32. Additionally, Judge Baynes held that the proceeds should go to benefit the joint creditors. *Id.* Judge Baynes recognized, however, that this was inconsistent with the distribution scheme of § 726. *Id.* Judge Baynes reasoned that no other method appears reasonable in light of the earlier rulings by the Florida courts. *Id.* at 331 (citations omitted).

140. 121 B.R. 622 (Bankr. N.D. Fla. 1989).

141. *Id.* at 625.

142. *Id.*

143. *See supra* text accompanying notes 125-32.

144. *Boyd*, 121 B.R. at 624.

145. *Greenblatt v. Ford*, 638 F.2d 14, 15 (4th Cir. 1981).

nonexempt interest to joint creditors.¹⁴⁶ Third, instead of distributing the proceeds from the sale of entirety property to joint creditors, the court can distribute the proceeds to all creditors.¹⁴⁷ Finally, Congress can intervene and amend the relevant bankruptcy statutes to provide a uniform result.

It is clear Congress intended to include entirety property within the bankruptcy estate.¹⁴⁸ The legislative history and the interrelationships among the Code sections evidences a congressional intent to include the debtor's interest within the estate.¹⁴⁹ Once included in the estate, the court must decide the extent of the exemption available to the debtor under section 522(b)(2)(B) or the amount subject to sale under section 363(h).¹⁵⁰ If the court decides to permit the trustee to dispose of the debtor's interest, then the second inquiry is to determine which creditors benefit from the sale.¹⁵¹

A. *Exempt Entirety Property from the Bankruptcy Estate*

One alternative is for the court to completely exempt the debtor's interest in entirety property from the bankruptcy estate.¹⁵² Section 522(b)(2)(B) excludes from the bankruptcy estate the debtor's interest in entirety property "to the extent . . . exempt from process under applicable nonbankruptcy law."¹⁵³ Under Florida law, neither a single nor a joint creditor can levy solely on the interest of one spouse.¹⁵⁴ When one spouse files for bankruptcy, only that spouse's interest is included in the bankruptcy estate.¹⁵⁵ Thus, entirety property should be exempt from the estate because a joint creditor cannot levy solely on the interest of the debtor. However, as the Fourth Circuit suggested, this approach offers some potential problems inconsistent with the fundamental policies of the Code.¹⁵⁶

One problem results from the debtor obtaining a discharge in bankruptcy.¹⁵⁷ Because a discharge insulates the debtor from personal liability and serves as an injunction against postbankruptcy collection of prebankruptcy debts, the debtor is no longer personally obligated to the joint creditor. Consequently, the joint creditor is unable to proceed against the entirety property after bankruptcy because the discharge reduces the joint

146. See *Sumy*, 777 F.2d at 932.

147. *Amici*, 99 B.R. at 102-03.

148. See *supra* notes 47-60 and accompanying text.

149. See *supra* notes 47-60.

150. See *supra* notes 58-60 and accompanying text.

151. See *supra* notes 44-45 and accompanying text.

152. See *Ford*, 638 F.2d at 15.

153. 11 U.S.C. § 522(b)(2)(B) (1988).

154. See *supra* notes 6, 13-19 and accompanying text.

155. See *Phillips v. Krakower*, 46 F.2d 764, 765 (4th Cir. 1931).

156. *Sumy*, 777 F.2d at 932.

157. See *supra* notes 91-96 and accompanying text.

creditor's claim to one against the nonfiling spouse. Although the court may condition the discharge by permitting the joint creditor to obtain a judgment and allow execution in state court, the joint creditor would be subjected to the added expense of collecting the debt. Additionally, the debtor may resort to section 522(c) to protect property that is exempt in bankruptcy. Section 522(c) provides that a creditor cannot pursue exempt property, during or after discharge, to satisfy a debt that arose before bankruptcy.¹⁵⁸ In effect, the debtor is able to manipulate the Code to commit "legal fraud" which the bankruptcy courts condemn.¹⁵⁹

Another inequity resulting from exempting the entirety property completely from the estate is that the debtor, under section 522(f), can avoid any prepetition judicial liens on the entirety property.¹⁶⁰ For example, assume a joint creditor before bankruptcy obtains a judicial lien on the entirety property. One spouse, liable on the joint debt, then files for bankruptcy before the creditor executes on the property. The automatic stay of section 362 prohibits the joint creditor from proceeding with its claim in state court.¹⁶¹ During the bankruptcy proceeding, the court exempts the entirety property. After the property is exempted, the debtor may use section 522(f) to avoid the joint creditor's lien on the property.¹⁶² The effect of section 522(f) is to permanently strip the creditor of the lien on the property. Thus, the debtor can use the Code's broad power to reach an improper result that Congress did not intend. This result would not justify the inequitable harm caused to joint creditors who bargained for the right to seek recourse against the property of both spouses.

B. *Limit the Exemption Under Section 522(b)(2)(B)*

A fairer solution, that maintains the joint creditor's bargained for position, would be to limit the extent of the debtor's exemption under section 522(b)(2)(B).¹⁶³ This alternative entails exempting the entirety property to the "extent that such interest . . . is exempt . . . under applicable nonbankruptcy law."¹⁶⁴ Under Florida law, entirety property is exempt from the claims of a creditor of one spouse.¹⁶⁵ However, a joint creditor can satisfy claims against the entire undivided interest of the husband and wife.¹⁶⁶

158. See 11 U.S.C. § 522(c) (1988).

159. See *supra* note 37.

160. See *supra* notes 98-99 and accompanying text.

161. See 11 U.S.C. § 362 (1988).

162. See 11 U.S.C. § 522(f) (1988).

163. See *supra* notes 108-15.

164. 11 U.S.C. § 522(b)(2)(B) (1988); see also *supra* text accompanying notes 72-79 (providing an example of limiting the extent of the debtor's exemption).

165. See *supra* text accompanying notes 17-22.

166. See *supra* text accompanying notes 17-23.

Therefore, the debtor's interest in entirety property is not exempt to the extent of these joint claims.¹⁶⁷ In effect, this approach rejects the premise underlying the first solution, that a joint creditor cannot levy on the interest of one spouse. Instead, this approach recognizes that because a joint creditor can levy on entirety property under state law, the debtor's interest should not be exempt under federal bankruptcy law.¹⁶⁸ Under this approach, the trustee can dispose of the debtor's interest in entirety property and satisfy the claims of joint creditors while single creditors get nothing.¹⁶⁹ The excess proceeds, if any, would be exempt for the debtor.¹⁷⁰

The circuit courts agree with this approach.¹⁷¹ By disposing of the property under section 363(h), the courts eliminate the additional expense incurred by lifting the automatic stay and requiring joint creditors to satisfy their claims in state court.¹⁷² Arguably, these joint creditors bargained for a superior position over single creditors by providing the husband and wife more favorable terms on their obligation.¹⁷³ Thus, the joint creditor ensures recourse against a greater pool of assets. Presumably the joint creditor relied both on the ability to attach joint property and on the fact that a single creditor could not attach joint property. By giving the proceeds only to joint creditors, the court preserves this bargain. Therefore, the substantive rights of the joint creditors do not change and, as a result, the court fulfills the fundamental principle that similarly situated creditors will be treated equally.¹⁷⁴

However, this approach assumes a narrow definition of similarly situated creditors by only including unsecured joint creditors and excluding single creditors with claims of equal rank in bankruptcy.¹⁷⁵ Arguably, joint creditors bargained for certain rights to ensure recourse against property held both individually and by the entirety by husband and wife. Interpreting section 522(b)(2)(B) narrowly to exempt the debtor's entire interest, or to dispose of it for the benefit of all creditors, would strip the joint creditor of this negotiated advantage vis-à-vis single creditors. However, nothing in section 522(b)(2)(B) sets forth such a distribution for joint creditors.¹⁷⁶ Congress determined the treatment for similarly situated creditors under the distribution scheme of section 726.¹⁷⁷ Congress provided a broad meaning to similarly

167. See *supra* text accompanying notes 74-79.

168. See *supra* text accompanying notes 74-79.

169. See *supra* text accompanying notes 72-77.

170. See *supra* text accompanying notes 75-79, 112-15.

171. See *supra* text accompanying notes 102-05.

172. See *supra* note 89.

173. See *supra* note 23 and accompanying text.

174. See *supra* note 88.

175. See *supra* notes 112-16, 126-30 and accompanying text.

176. See *supra* note 71.

177. See *supra* note 71.

situated creditors under section 726 by requiring unsecured joint creditors to share equally with other unsecured creditors. Thus, this approach ignores the dictates of section 726 by creating a sub-class of priority not intended by Congress.

C. Disallow the Exemption to the Extent of Joint Claims and Distribute the Proceeds to All Unsecured Creditors

Under the third solution, some Florida courts recognize the problem under the second possible solution, and instead distribute the proceeds according to section 726.¹⁷⁸ In general, if entirety property is not exempt under Florida law, then in bankruptcy the debtor's interest in entirety property is available to all unsecured creditors.¹⁷⁹ The Florida courts rely on the reasoning that once property is included in the estate, the property should be distributed to all creditors under section 726.¹⁸⁰ Several Florida courts have held that to the extent a joint creditor has a claim against a debtor, entirety property is not exempt under section 522(b)(2)(B) and is included within the estate.¹⁸¹

Joint creditors argue that because their unique status under state law brings entirety property within the bankruptcy estate, they should benefit exclusively from the proceeds.¹⁸² Several Florida judges dismiss this argument, relying on a Supreme Court decision holding that the amount brought into the estate because of the status of one creditor inures to the benefit of all creditors.¹⁸³ The joint creditor in bankruptcy is not given any special treatment because of its unique status under several Florida cases including *Amici*, *Anderson*, and *Boyd*.¹⁸⁴ Thus, all unsecured creditors share equally in the proceeds from the sale of the entirety property.¹⁸⁵ This argument is further supported by the fact that Congress did not provide any special distribution rules for the benefit of joint creditors to dispose of entirety property.¹⁸⁶

A stronger argument by the joint creditors is that allowing all unsecured creditors to share equally in the entirety property proceeds changes the joint creditors' substantive rights and elevates the benefits inuring to the single creditor.¹⁸⁷ Judge Thomas Baynes noted that once the trustee realizes on the

178. See *supra* text accompanying notes 117-44.

179. See *supra* notes 117-39 and accompanying text.

180. See *supra* notes 117-24 and accompanying text.

181. See *supra* notes 108-14, 133-44 and accompanying text.

182. See *supra* notes 72-77 and accompanying text.

183. See *supra* notes 129-31 and accompanying text.

184. See *supra* notes 123-24, 136-38, 142 and accompanying text.

185. See *supra* notes 124, 138, 142 and accompanying text.

186. See *supra* note 71.

187. See *supra* notes 19-23 and accompanying text (discussing the substantive rights of joint credi-

debtor's interest under section 363(h), the entirety property loses its unique status and becomes property held as tenants in common by husband and wife.¹⁸⁸ Thus, the nonfiling spouse's proceeds would lose its entirety status.¹⁸⁹ Although the joint creditor lost the priority that the creditor would have against the filing spouse under Florida law, the discharge would not affect the joint creditor's entire claim because the nonfiling spouse would remain liable on the debt.¹⁹⁰ Consequently, the joint creditor could proceed against all of the nonfiling spouse's assets, including proceeds from entirety property.¹⁹¹ Arguably, in some situations, the joint creditor will not realize the full value of its claim. Even so, the loss realized by the joint creditor can be rationalized as a cost Congress imposed on joint creditors in bankruptcy because of the distribution scheme of section 726.¹⁹² Joint creditors can alleviate this problem either by lobbying Congress to provide better protection for their status or by securing a consensual lien that enjoys greater priority over unsecured creditors in bankruptcy.

Another argument suggesting that the substantive rights of joint creditors do not significantly change, focuses on the notion that the creditor does not have a fixed bargain. As noted earlier, joint creditors negotiate terms in order to obtain the greatest amount of leverage from debtors. By obligating both spouses, the joint creditor ensures recourse against all available assets, including entirety property. However, this assumes the entirety property is still available when the debtor defaults. As one commentator noted, outside of bankruptcy the debtor can voluntarily decide to liquidate the entirety property and satisfy the most problematic creditors with the proceeds.¹⁹³ Such debts may be of creditors with a claim against only one spouse. Thus, the unsecured joint creditor loses its unique position because the debtor chose to liquidate the entirety property in favor of another creditor. As such, the status of the entirety is merely fortuitous, and the joint creditor is dependent on the availability of the property in order to enjoy its bargain.

tors). The Fourth Circuit in *Sumy* questioned the exemption because under state law the joint creditors of a married couple could levy and execute on the entirety property. *Sumy*, 777 F.2d at 928. Thus, distributing the proceeds to all creditors would change the substantive rights allowed under state law. *See id.*

188. *Anderson*, 132 B.R. at 660.

189. *Id.*

190. *See supra* note 13 (discussing creditors' rights when property is held as tenants in common).

191. *See supra* notes 23, 136-39 and accompanying text.

192. *See supra* text accompanying notes 127-28 (discussing the § 726 distribution scheme which contemplates equal distribution to similarly situated creditors).

193. *Kalevitch, supra* note 9, at 148-49.

D. Congress Should Amend the Relevant Code Sections

The fourth alternative would be for Congress to amend the relevant Code Sections and expressly articulate the treatment of entirety property when one spouse files for bankruptcy.¹⁹⁴ Congress has a mandate to provide national bankruptcy laws.¹⁹⁵ When uncertainty exists to the extent found under section 522, the original purpose of having uniform laws is undercut. Debtors are unsure of their rights, or worse, they use the differences in the laws to file bankruptcy in a favorable forum. For example, the debtor can exempt the amount in excess of joint obligations by filing in the Northern District of Florida.¹⁹⁶ However, in Chief Judge Paskay's or Judge Baynes' court, if a joint creditor exists, the debtor's whole interest in entirety property becomes available to satisfy all creditors' claims.¹⁹⁷ This uncertainty forces traditionally conservative creditors to charge higher interest rates to compensate for the unexpected losses. Most significantly, the uncertain treatment creditors receive in bankruptcy encourages them to rush to state court at the first sign of the debtor's trouble to receive known state court remedies. Uniformity would ensure consistent treatment of entirety property and prevent forum shopping.

VI. CONCLUSION

It is obvious Congress was unaware of the confusion it created with section 522. The Eleventh Circuit has not decided this issue, so the treatment of entirety property remains a debatable issue. This uncertainty will undoubtedly put joint creditors on alert when joint debtors begin to fall behind in payments on their obligations. Thus, joint creditors' reactions may accelerate the debtor's decline into bankruptcy.

The new Code represents a significant departure from the old Bankruptcy Act of 1898 by requiring inclusion of all the debtor's legal and equitable interests in the estate. From this point, the analysis of the entirety property becomes a two prong inquiry: (1) to what extent is the debtor's interest exempt under section 522(b)(2)(B), and (2) which creditors will benefit from the proceeds of the sale of the debtor's interest. The Florida courts differ on both of these issues.

One approach adopted by the Florida courts exempts the entirety property proceeds in excess of any joint claims in the estate. Under state law, a

194. See *supra* note 65. An amendment may not provide the best result, but at least it would ensure consistency.

195. See U.S. CONST. art. I, § 8 (providing Congress with the power to establish uniform bankruptcy laws).

196. *In re Boyd*, 121 B.R. 622, 625 (Bankr. N.D. Fla. 1989).

197. *Anderson*, 132 B.R. at 660; *In re Amici*, 99 B.R. 100, 102-03 (Bankr. M.D. Fla. 1989).

joint creditor can only levy on the entirety property interest. Thus, in bankruptcy, the property should be administered for the benefit of joint creditors. This approach eliminates the inefficiencies caused by the court lifting the stay and allowing the joint creditor to pursue its claim in state court. Also, this approach preserves the unique status joint creditors bargained for by allowing only the joint creditors to share in the proceeds. Consequently, the substantive rights of the joint creditor are unchanged. However, this approach ignores the dictates of section 726 by creating a sub-class of creditors not intended by Congress.

The second approach adopted by the Florida courts recognizes the problems associated with distributing the proceeds in violation of section 726. In general, the courts hold that if a joint creditor exists on the date of bankruptcy, then the debtor's interest in entirety property is available for distribution to all creditors. One court modified this result by limiting the amount of the debtor's interest available for all creditors to the extent of the joint claims in the case. The courts rely on the rule established by the Supreme Court that the amount brought into the estate because of the special status of an individual creditor inures to the benefit of all the creditors. Additionally, the Code does not provide special treatment for joint creditors in bankruptcy. Thus, this approach is consistent with the Code and produces a more sound result.

A simpler solution would be for Congress to amend the relevant statutes and clearly articulate the treatment for entirety property. Congress is responsible for establishing uniform bankruptcy laws. An amendment will ensure consistent treatment and prevent forum shopping. Until Congress responds to this problem in bankruptcy, the courts will continue to offer different results for debtors and creditors depending on where the debtor files for bankruptcy.

