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Balancing the Rights of Debtors and Creditors: $522(f)(1) of the Bankruptcy Code

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BALANCING THE RIGHTS OF DEBTORS AND CREDITORS: § 522(F)(1) OF THE BANKRUPTCY CODE

INTRODUCTION

Through the bankruptcy laws, society attempts to achieve a proper balance between the interests of failed debtors and unfortunate creditors.[1] The continually changing economic and social environment, however, makes the endeavor to achieve the "right" balance extremely difficult.[2] Nevertheless, whether a "right" balance can ever be found, the bankruptcy laws must, *at a minimum*, set forth clear rules and provide for predictable results so that creditors, debtors and their attorneys can plan their future relationships.[3]

Currently, § 522(f)(1) of the Bankruptcy Code ("Code")—the provision allowing a debtor to avoid a judicial lien where the lien "impairs" the debtor's exempt property—is dramatically failing to provide this clarity and predictability.[4] The judicial decisions involving the interpretation and application of § 522(f)(1) have consistently contradicted one another.[5] Moreover, despite the 1994 Amendments to the

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[1] *See generally* Jane Forbes, *In Re Lucas: A Blueprint For Unlimited Exemptions in Bankruptcy*, 23 U. TOL. L. REV. 565, 565–66 (1992); Rhett Frimet, *The Birth of Bankruptcy in the United States*, 96 COM. L.J. 160, 160 (1991);Lawrence Ponoroff and F. Stephen Knippenberg, *The Immovable Object Versus the Irresistible Force: Rethinking the Relationship Between Secured Credit and Bankruptcy Policy*, 95 MICH. L. REV. 2234, 2235 (1997).

[2] *See* KAREN GROSS, FAILURE AND FORGIVENESS: REBALANCING THE BANKRUPTCY SYSTEM 92–93 (1997); RICHARD B. HERZOG, JR., BANKRUPTCY: A CONCISE GUIDE FOR CREDITORS AND DEBTORS 3–4 (1983).

[3] *See* GROSS, *supra* note 2, at 92–93; HERZOG, *supra* note 2, at 3–4.

[4] 11 U.S.C. §§ 101–1330 (1994); *see, e.g.*, *In re* Finn, 211 B.R. 780, 784 (B.A.P. 1st Cir. 1997) (DeJesus, J., dissenting) (arguing for adoption of entire lien avoidance approach); *In re* Ryan, 210 B.R. 7, 12 (Bankr. D. Mass. 1997) (adhering to full avoidance approach); *see also* East Cambridge Sav. Bank v. Silveira, Memorandum & Order, 1, 7 (No. 96–11388–WGY) (D. Mass. 1997), *vacated and remanded*, 1998 WL 175119 (1st Cir. Apr. 21, 1998); Gonzalez v. First Nat'l Bank of Boston, 191 B.R. 2, 3–4 (Bankr. D. Mass. 1996) ("*Gonzalez II*"). *But see* East Cambridge Sav. Bank v. Silveira, 1998 WL 175119, at *4, 6 (1st Cir. Apr. 21, 1998). Section 522(f)(1) allows debtors to avoid judicial and non-purchase money liens that impair exempt property. *See* 11 U.S.C. § 522(f)(1) (1994). Although § 522(f)(1) also provides for the avoidance of non-purchase money liens, for purposes of the article, I will only address judicial liens. Moreover, while there are numerous types of exemptions, for purposes of this article, I will focus primarily on the homestead exemption.

[5] 11 U.S.C. § 522(f)(1); *see, e.g.*, *Finn*, 211 B.R. at 784; *Silveira*, Memorandum & Order at 7; *Gonzalez II*, 191 B.R. at 3–4; Bellenoit v. Avco Leasing Serv., 157 B.R. 185, 186–87 (Bankr. D. Mass. 1992); *In re* Bovay, 112 B.R. 503, 503 (Bankr. N.D.N.Y. 1989); *In re* Cravey, 100 B.R. 119, 120 (Bankr. S.D. Ga. 1989).

Code—which were intended to clarify this provision's ambiguities—courts continue to produce different results.[6] The varying opinions handed down by Massachusetts courts exemplify the confusion caused by § 522(f)(1).[7] Although the United States Court of Appeals for the First Circuit, in *East Cambridge Savings Bank v. Silveira*, recently adopted the "full avoidance" approach, thereby resolving the issue for that circuit, the conflicting decisions of the lower courts illustrate the confusion that is bound to arise in other circuits.[8]

Part I of this Note explains briefly the bankruptcy process and the policy objectives behind the bankruptcy and exemption laws.[9] Part II details the various approaches different courts took prior to the 1994 Amendments to the Code when interpreting and applying § 522(f)(1).[10] Part III sets forth Congress's response to the confusion resulting from these inconsistent judicial approaches and explains the 1994 Code Amendments.[11] Part IV describes the different approaches courts, particularly Massachusetts courts, have taken subsequent to the passage of the 1994 Code Amendments in interpreting and applying § 522(f)(1).[12] Last, Part V explains the flaws plaguing most of the approaches and sets forth the reasons why the "full lien avoidance" approach, as ultimately adopted by the First Circuit, is the correct approach.[13]

I. BACKGROUND

The United States is a capitalist society where individuals are encouraged to be innovative and to take risks.[14] Our economy and way of life improve when individuals take risks that turn out to be successful.[15] What happens, however, to those individuals who take risks, but fail? One option that the federal government, pursuant to the United States Constitution, has given these individuals is bankruptcy.[16]

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[6] 11 U.S.C. § 522(f)(2) (1994); *see, e.g., Finn*, 211 B.R. at 784; *Silveira*, Memorandum & Order, at 7; *Ryan*, 210 B.R. at 12; *Gonzalez II*, 191 B.R. at 3–4. *But see Silveira*, 1998 WL 175119, at *4, 6.

[7] 11 U.S.C. § 522(f)(2); *see, e.g., Finn*, 211 B.R. at 784; *Silveira*, Memorandum & Order, at 7; *Ryan*, 210 B.R. at 12; *Gonzalez II*, 191 B.R. at 3–4. *But see Silveira*, 1998 WL 175119, at *4, 6.

[8] 1998 WL 175119, at *5; *see generally Finn*, 211 B.R. at 784; *Ryan*, 210 B.R. at 12; *Silveira*, Memorandum & Order, at 7; *Gonzalez II*, 191 B.R. at 3–4.

[9] *See infra* notes 14–63 and accompanying text.

[10] *See infra* notes 64–210 and accompanying text.

[11] *See infra* notes 211–33 and accompanying text.

[12] *See infra* notes 234–313 and accompanying text.

[13] *See infra* notes 314–75 and accompanying text.

[14] *See* HERZOG, *supra* note 2, at 2–3.

[15] *See id.*

[16] 11 U.S.C. §§ 101–1330 (1994). Article I, Section 8, Clause 4 of the United States Constitu-

Whether the bankruptcy laws stem from society's sense of compassion for other people or from its own self-interest in avoiding having these individuals become dependent upon the state for support, the Code is designed to relieve some of the hardships endured by those individuals who have tried but failed.[17]

A. *The Bankruptcy Process*

When a debtor files a petition for bankruptcy, all of the debtor's property is placed into the bankruptcy "estate."[18] From this estate, the secured creditors, in order of priority, are paid their debts owed.[19] The remainder of the estate's assets, if any exist, are then pooled together and distributed to the unsecured creditors on a pro rata basis.[20]

Section 522(b) of the Code allows a debtor to exempt certain property from the estate.[21] Section 522(b) provides in relevant part: "[A]n individual debtor may exempt from property of the estate the property listed in either paragraph (1) or . . . paragraph (2) of this section."[22] Paragraph (1) provides for federal exemptions listed under § 522(d), unless a state, pursuant to paragraph (2)(A), "opts-out" of the federal exemption laws.[23] Paragraph (2)(A) allows a state to establish its own exemption laws, thereby "opting-out" of the federal exemption scheme.[24]

To protect exempt property, § 522(f)(1) permits a debtor to avoid judicial liens that "impair an exemption."[25] Section 522(f)(1) provides in relevant part:

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tion provides "[t]he Congress shall have power . . . to establish . . . uniform laws on the subject of bankruptcies throughout the United States." U.S. CONST. art. I, § 8, cl. 4.

[17] 11 U.S.C. §§ 101–1330. The Honorable William Houston Brown explained that by providing a debtor with a fresh-start, bankruptcy "shift[s] the burden of support for the debtor and the debtor's dependents from the public to private credit sources." Honorable William Houston Brown, *Political and Ethical Considerations of Exemption Limitations: The "Opt-Out" as Child of the First and Parent of the Second*, 71 AM. BANKR. L.J. 149, 163 (1997).

[18] 11 U.S.C. §§ 541, 542 (1994). An individual may file a voluntary petition for bankruptcy or a debtor's creditors may file an involuntary petition. *See id.*

[19] *Id.* § 507 (1994).

[20] *Id.*

[21] *Id.* § 522(b) (1994). In 1991, in *Owen v. Owen*, the United States Supreme Court explained that although a state may establish its own exemption scheme, it may not write its exemption laws in a manner that attempts to circumvent a debtor's avoidance powers under § 522(f)—such as defining exempt property in a way that excludes property that is encumbered by a judicial lien. 500 U.S. 305, 313–14 (1991); *see also* 11 U.S.C. § 522(f).

[22] 11 U.S.C. § 522(b).

[23] *Id.* § 522(b)(1).

[24] *Id.* § 522(b)(2)(A).

[25] *Id.* § 522(f)(1). A lien that is avoided becomes unsecured and the claim is pooled together with all other unsecured claims. *See supra* note 19 and accompanying text.

> Notwithstanding any waiver of exemptions but subject to paragraph (3), 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—
> (A) a judicial lien . . .[26]

Through the interplay of § 522(b)'s right to exempt property and § 522(f)(1)'s avoidance powers, the Code enables a debtor to keep a certain amount of property after bankruptcy.[27]

B. *Policies*

1. The Bankruptcy Code

The Code has three primary objectives: 1) to relieve an honest debtor of some of the hardships resulting from overwhelming debt obligations; 2) to prevent fraudulent debtor conduct that is harmful to creditors; and 3) to provide some protection for creditors against other creditors.[28] The first of these objectives is achieved through the Code's fresh-start policy.[29] The fresh-start policy is intended to serve two functions: 1) to enable a particular debtor to once again return to society as a productive member, and 2) to provide an incentive for potential future entrepreneurs to take reasonable risks.[30]

First, to enable a particular debtor to once again return to society as a productive member, the Code attempts to provide a debtor with the financial means necessary to start life anew.[31] As Randell Schmit explained, "allowing the debtor to keep this property after bankruptcy ensures that the debtor does not become a ward of the state."[32] Further, the Code attempts to preserve a debtor's self-esteem, thereby helping to ensure that the debtor has the mental capacity to once again be a productive member of society.[33]

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[26] 11 U.S.C. § 522(f)(1).

[27] *Id.* §§ 522(b), 522(f)(1).

[28] *See* Frimet, *supra* note 1, at 160.

[29] *See* GROSS, *supra* note 2, at 91; HERZOG, *supra* note 2, at 3–5; Brown, *supra* note 17, at 163.

[30] *See* GROSS, *supra* note 2, at 91; HERZOG, *supra* note 2, at 7.

[31] *See* GROSS, *supra* note 2, at 91; Brown, *supra* note 17, at 163.

[32] Randall B. Schmidt, *R.I.P. Chabot? Ninth Circuit Bankruptcy Debtor's Right to Avoid a Judicial Lien on a Homestead is Still "Impaired" and the Clarification Doctrine in Doubt After* In re Wilson, 31 U.S.F. L. REV. 1051, 1055 (1997) (citing *In re* Pladson, 35 F.3d 462, 464 (9th Cir. 1994)).

[33] *See* HERZOG, *supra* note 2, at 7.

Second, the fresh-start policy is designed to provide an incentive for people to take the risks essential to the proper functioning of our capitalist society.[34] By providing debtors with a fresh-start, the Code assures potential future entrepreneurs that some protection exists for them in the event of failure.[35] Thus, the fresh-start policy acts as an incentive for people to take reasonable risks.[36]

In addition to providing honest debtors with some relief from overwhelming debt obligations, the Code also endeavors to protect creditors from fraudulent and harmful debtor activity.[37] The Code does not permit individuals to take unreasonable risks with the comfort of knowing that bankruptcy will absolve them entirely of all the consequences of the failed endeavors.[38] Rather, the Code is designed to protect only the "honest" debtor—one who has taken reasonable risks, has tried and has failed.[39] Thus, the Code endeavors to strike a balance between relieving some of the hardships faced by "honest" debtors and partially protecting the rights of creditors.[40] Moreover, by protecting creditors, the Code helps to protect future debtors.[41] As Judge Posner stated, "the welfare of debtors and of creditors is intertwined; the fewer the protections for creditors, the higher interest rates are, and interest is paid by debtors; conversely, the greater the protection for creditors, the lower interest rates are, and debtors as a group benefit."[42]

To further the Code's objective of protecting creditors from harmful debtor activity, Congress has built various safeguards into the Code.[43] For example, once a debtor has received a bankruptcy discharge, that debtor cannot receive another discharge for the next six years.[44] Also, with regard to exemptions, § 522(f) allows a debtor to avoid only *judicial* or *non-purchase money liens* and only *to the extent* that they impair an exemption.[45] Thus, these safeguards, along with numer-

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[34] *See id.* at 2–3.

[35] *See* 11 U.S.C. § 522; HERZOG, *supra* note 2, at 2–3.

[36] *See* GROSS, *supra* note 2, at 91–93; HERZOG, *supra* note 2, at 2–3.

[37] *See* Forbes, *supra* note 1, at 565–66; Frimet, *supra* note 1, at 160.

[38] *See* GROSS, *supra* note 2, at 93; Forbes, *supra* note 1, at 565–66.

[39] *See* Brown, *supra* note 17, at 163.

[40] *See* GROSS, *supra* note 2, at 93; Brown, *supra* note 17, at 163; Frimet, *supra* note 1, at 160.

[41] *See In re* Thompson, 867 F.2d 416, 419 (7th Cir. 1989) (citing *In re* Xonics Imaging, Inc., 837 F.2d 763, 765 (7th Cir. 1988)).

[42] *Id.*

[43] *See, e.g.*, 11 U.S.C. §§ 522(f), 541 (1994).

[44] *See id.* § 727(a)(8). Even within the six-year period, however, an individual debtor previously granted a discharge under Chapter 7 might still be able to get relief from creditors by filing under Chapter 13, the payback section of the Code. *Id.* § 1328; *see also* KENNETH J. DORAN, PERSONAL BANKRUPTCY AND DEBT ADJUSTMENT 5 (1996).

[45] *See* 11 U.S.C. § 522(f).

ous other protections, help protect creditors from unreasonable debtor activity, which in turn also protects future debtors.[46] Nevertheless, a constant tension exists between relieving an honest debtor of the hardships resulting from overwhelming debt obligations and protecting the rights of creditors.[47]

Finally, the Code seeks to protect creditors from each other.[48] The federal bankruptcy system is premised upon the notion that creditors in like positions should be treated equally.[49] Because a debtor filing bankruptcy is usually insolvent, there generally will not be enough assets to satisfy all outstanding debt obligations.[50] Thus, creditors frequently lose money as a result of a debtor filing bankruptcy.[51] Recognizing this probable result, the bankruptcy system is designed to prevent a "race of diligence."[52] A race of diligence is the scramble that occurs when all of a debtor's creditors resort to garnishment, foreclosure, levy and execution to satisfy the debtor's obligations.[53] The race of diligence results in an unequal distribution of the debtor's assets, which is contrary to the goals behind the Code.[54] Thus, to preserve the remaining assets, ensure an orderly distribution of these assets and prevent creditor harassment of debtors, the Code contains various provisions to discourage creditors from racing to collect their debts owed.[55]

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[46] *See, e.g.*, 11 U.S.C. § 547 (trustee has power to avoid transfers of debtor's interest in property deemed preferential); *Id.* § 362(a) (automatic stay, beginning when a debtor files bankruptcy, halts most debt collection activity against debtor by creditors); *see also Thompson*, 867 F.2d at 419 (citing *Xonics Imaging*, 837 F.2d at 765).

[47] *See* GROSS, *supra* note 2, at 91; HERZOG, *supra* note 2, at 2–3.

[48] *See* Frimet, *supra* note 1, at 160.

[49] *See* GROSS, *supra* note 2, at 158. The Code sets up a complex priority system among creditors depending on the source of a creditor's claim and whether it is secured or unsecured. *See* 11 U.S.C. § 507 (1994). A secured claim is one backed by a lien on property owned by the debtor. *See* DORAN, *supra* note 44, at 50. Moreover, a lien is a "charge against or interest in property to secure payment of a debt for performance of an obligation." 11 U.S.C. § 101(37) (1994). An unsecured claim, on the other hand, is not backed by any collateral. *See* DORAN, *supra*, at 51. After all secured creditors are paid, in order of priority, the unsecured creditors receive any remaining money on a pro rata basis. *See* 11 U.S.C. § 507.

[50] *See* HERZOG, *supra* note 2, at 4.

[51] *See id.*

[52] *See id.*

[53] *See id.*

[54] *See id.*

[55] *See supra* notes 43–54 and accompanying text.

2. Exemption Laws

The exemption laws are designed primarily to further the Code's fresh-start policy.[56] Section 522(b) allows a debtor to exempt certain property from the bankruptcy estate, thereby permitting the debtor to retain specified property after bankruptcy.[57] As the Supreme Court explained, "the section [§ 522] . . . was enacted to protect the debtor's essential needs and to enable him to have a fresh-start economically."[58]

Section 522(f)(1) is designed to protect this exempt property by allowing a debtor to avoid a judicial lien that impairs an exemption.[59] In effect, § 522(f)(1) helps prevent a race to the courthouse between a creditor and debtor.[60] Thus, a creditor merely beating a debtor to the courthouse—getting a judgment lien before the debtor files for bankruptcy—should not, and does not, mean that the slower debtor forfeits otherwise exempt property.[61] As Judge Posner explained, "[i]t [§ 522(f)(1)] allows the debtor to avoid a judicial lien on exempt property—that is, a lien obtained by a creditor who has beaten the debtor to court."[62] Thus, by allowing a debtor to avoid judicial liens that impair an exemption, § 522(f)(1) protects a debtor's exempt property.[63]

II. Judicial Interpretation and Application of § 522(f)(1) Prior to the 1994 Amendments

A. *Three Fact Patterns*

When addressing the issue of the avoidance of judicial liens that impair exempt property under § 522(f)(1), one of three fact patterns will usually be present.[64] The first fact pattern entails an unavoidable encumbrance, such as a mortgage, that is equal to or greater than the value of the property.[65] For example, a debtor owns a home valued at $100,000, which is encumbered by a $100,000 first mortgage.

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[56] *See* Herzog, *supra* note 2, at 3–5.

[57] *See* 11 U.S.C. § 522(b). Section 522(b) provides in pertinent part, "[n]otwithstanding section 541 of this title, an individual debtor may exempt from property of the estate the property listed in either paragraph (1) or, in the alternative, paragraph (2) of this section." *Id.*

[58] *See* United States v. Security Indus. Bank, 459 U.S. 70, 83 (1982); *see also* Arthur Winston, Complete Guide To Credit and Collection Law 145 (1996) (assets deemed necessary for sustenance and living).

[59] *See* 11 U.S.C. § 522(f)(1).

[60] *Id.*; *see also* Herzog, *supra* note 2, at 4.

[61] *See* Herzog, *supra* note 2, at 4; *see also Thompson*, 867 F.2d at 418–19.

[62] *Thompson*, 867 F.2d at 418–19 (citing H.R. Rep. No. 95-595, 5787, 6087–88 (1978)).

[63] *See* 11 U.S.C. § 522(f)(1).

[64] *See infra* notes 65–67.

[65] *See, e.g.*, *In re* Simonson, 758 F.2d 103, 105 (3d Cir. 1985); *In re* Bovay, 112 B.R. 503, 503 (Bankr. N.D.N.Y. 1989).

Under the second fact pattern, the unavoidable encumbrance and exemption consume the full value of the property.[66] For example, the debtor owns a home worth $100,000, which is subject to a $90,000 first mortgage. Moreover, the debtor is allowed a $10,000 exemption.

Under the third fact pattern, there exists equity in the property beyond the unavoidable encumbrance and exemption, but the equity is less than the amount of the judicial lien.[67] For example, the debtor owns a home valued at $100,000, which is encumbered by a $60,000 first mortgage. Moreover, the debtor is entitled to a $20,000 homestead exemption. Thus, there exists $20,000 in equity beyond the unavoidable encumbrance and exemption. In addition, the creditor has a $30,000 judicial lien.

B. *Judicial Approaches*

1. Situations Involving the First Fact Pattern

Prior to the 1994 Amendments to the Code, courts interpreted and applied § 522(f)(1) in vastly different ways, even when considering the same fact pattern.[68] When there is no equity in the property beyond the unavoidable encumbrances, a recurring question is whether there exists any exemption that can be impaired.[69] The central issue to which courts provide different interpretations is the correct definition of the word "interest," as used in § 522(f)(1)'s phrase "avoid the fixing of a lien on an interest of the debtor . . . ."[70] While some courts narrowly define "interest" to entail the quantity of equity in the property, other courts broadly interpret "interest" to encompass equitable interests, such as the right of possession.[71]

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[66] *See, e.g.*, Bellenoit v. Avco Leasing Serv., 157 B.R. 185, 186–87 (Bankr. D. Mass. 1992).

[67] *See, e.g.*, East Cambridge Sav. Bank v. Silveira, 1998 WL 175119, at *4, 6 (1st Cir. Apr. 21, 1998); *In re* Finn, 211 B.R. 780, 781 (B.A.P. 1st Cir. 1997); East Cambridge Sav. Bank v. Silveira, Memorandum & Order, 1, 3–4 (No. 96–11388–WGY) (D. Mass. 1997) *vacated and remanded*, 1998 WL 175119 (1st Cir. Apr. 21, 1998); *In re* Ryan, 210 B.R. 7, 8 (Bankr. D. Mass. 1997).

[68] *See generally In re* Witkowski, 176 B.R. 114, 116–17; *see also infra* notes 69–210.

[69] *See Simonson*, 758 F.2d at 108; *Bovay*, 112 B.R. at 504–05; *In re* Cravey, 100 B.R. 119, 121–22 (Bankr. S.D. Ga. 1989); *see also* Holloway v. John Hancock Mut. Life Ins., 81 F.3d 1062, 1068–69 (11th Cir. 1996).

[70] 11 U.S.C. § 522(f)(1) (1994); *see Simonson*, 758 F.2d at 108; *Bovay*, 112 B.R. at 504–05; *Cravey*, 100 B.R. at 121–22.

[71] *See infra* notes 72–118.

a. *The Complete Avoidance Approach*

Under the complete avoidance approach, courts emphasize the Code's fresh-start policy and interpret broadly the word "interest" to include equitable interests.[72] The complete avoidance approach is illustrated by *In re Cravey*.[73] In 1989, in *Cravey*, the United States Bankruptcy Court for the Southern District of Georgia held that, pursuant to § 522(f)(1), the judicial liens were avoided completely.[74] The debtor's property was valued at $85,000.[75] To secure an $83,891.65 debt, debtors conveyed title to this property to Vidalia Federal Savings & Loan Association.[76] The debtors later filed a motion to avoid judicial liens held by a second creditor—the respondents—alleging that these liens impaired exemptions to which the debtors were entitled to under the Georgia exemption statute.[77] The respondents, however, argued that because the debtors no longer had legal title to the property, the debtors had no interest in the property to which they could claim an exemption.[78]

In finding for the debtors, the court engaged in a two-part analysis.[79] The court first addressed the issue of whether the debtors were entitled to the claimed exemption under state law, explaining that under § 522 an exemption must first exist to trigger the lien avoidance provision—§ 522(f)(1).[80] Focusing on the word "interest," as used in the state exemption law, the court expressly differentiated between the meaning of the word "interest" and "equity."[81] The court broadly interpreted the word interest and explained that equity is only one form of interest.[82] The court noted, "a debtor's 'interest' is not synonymous with a debtor's 'equity' . . . ."[83] The court explained that interest includes residual rights, such as the right of possession, the right to enjoy future equity created by repayment of the debt and the right to reclaim

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[72] *See, e.g., Holloway*, 81 F.3d at 1069; *Cravey*, 100 B.R. at 122.

[73] 100 B.R. at 122.

[74] *See id.*

[75] *See id.* at 120.

[76] *See id.* at 120–21.

[77] *See id.* at 119. The court turned to the state exemption statute because, pursuant to § 522(b)(2)(A), Georgia has opted out of the federal exemption scheme. *See id.* at 119, 121.

[78] *See Cravey*, 110 B.R. at 121.

[79] *See id.*

[80] *See id.*

[81] *See id.* at 121–22.

[82] *See id.*

[83] *See Cravey*, 110 B.R. at 122.

legal title through such repayment.[84] Consequently, the court concluded that the debtors had exemptible interests in the property.[85]

Second, the court addressed the issue of whether the lien, in fact, impaired the exemption.[86] Emphasizing the debtor's interest in the creation of future equity, the court reasoned that this residual interest must be considered when addressing any lien avoidance issue in order to further the Code's fresh-start policy.[87] The court explained that to allow the judicial liens to survive bankruptcy would hinder the purpose behind the federal lien avoidance provisions, which the court explained was "to provide property necessary for the debtor's fresh-start exempt from further claims of pre-petition creditors."[88] The court reasoned that the Code's fresh-start policy required that any post-bankruptcy appreciation in the property must accrue for the benefit of the debtor.[89] Thus, the court held that, pursuant to § 522(f)(1), the judicial liens were completely avoided.[90]

b. *The Not Impair Approach*

In contrast to the complete avoidance approach, some courts have adopted the "not impair" approach.[91] Under this approach, courts adhere to a strict reading of the statutory language and narrowly interpret the word "interest" as meaning the quantity of equity remaining in the property.[92] The court in *In re Simonson* adopted the not impair approach.[93] In 1985, in *Simonson*, the United States Court of Appeals for the Third Circuit held that the debtors had no interest in the property to which an exemption could attach and therefore, the judicial liens could not be avoided under § 522(f)(1).[94]

The debtors' property had a fair market value of less than $80,872.12 and they agreed to sell it for $58,250.[95] The property was en-

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[84] *See id.* at 121–22.

[85] *See id.* at 122.

[86] *See id.* at 121–22.

[87] *See id.* at 122.

[88] *Cravey*, 110 B.R. at 122.

[89] *See id.*

[90] *See id.*

[91] *See, e.g.*, *Simonson*, 758 F.2d at 106; *In re* Seltzer, 185 B.R. 116, 119 (Bankr. E.D.N.Y. 1995); Sheaffer v. Marshall Nat'l Bank & Trust Co., 159 B.R. 758, 762 (Bankr. E.D. Va. 1993); *Bovay*, 112 B.R. at 506. I have designated my own name for this approach for easy reference when I subsequently refer to it.

[92] *See, e.g.*, *Simonson*, 758 F.2d at 106; *Sheaffer*, 159 B.R. at 762; *see also Holloway*, 81 F.3d at 1068.

[93] *See* 758 F.2d at 106.

[94] *See id.*

[95] *See id.* at 105.

cumbered by two mortgages totaling $66,460.79.[96] Moreover, the debtors claimed a $15,000 homestead exemption.[97] The property also was subject to two judicial liens equaling $14,411.33.[98] Using the agreed-upon liquidation value of the property as the reference point, the court noted that there remained no equity in the property beyond the unavoidable encumbrances.[99] The court narrowly interpreted the word "interest" as meaning the quantity of equity in the property.[100] Moreover, the court stated that Congress intended the word "interest" to mean an interest of the debtor "measured by taking into account those interests of other parties which may not be avoided under § 522(f)."[101] Thus, the court implicitly reasoned that senior *unavoidable encumbrances* were responsible for the impairment and not the *judicial liens.*[102]

Rejecting the reasoning behind the complete avoidance approach, the court stated that it could not find any support that Congress intended § 522 to be a means of protecting for the debtor the creation of future equity in property.[103] Rather, the court reasoned that § 522 only was intended to protect the fixed amount of an allowable exemption.[104] Thus, the court concluded that in the absence of any remaining equity in the property, the "problem of lien avoidance under § 522(f) simply does not arise," and therefore, the judicial lien could not be avoided as impairing an exemption.[105]

Similarly, the court in *In re Bovay* followed the not impair approach, although applying different reasoning.[106] In 1989, in *Bovay*, the United States Bankruptcy Court for the Northern District of New York held that the judicial lien could not be avoided because it did not impair any exempt property.[107] The debtor's property was valued at $45,000 and was encumbered by two mortgages totaling $23,491.17 and an unavoidable tax lien of $47,551.49.[108] Thus, there was no equity in the property beyond the unavoidable encumbrances.[109]

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[96] *See id.*
[97] *See id.*
[98] *See Simonson*, 758 F.2d at 105.
[99] *See id.* at 106.
[100] *See id.* at 105–06.
[101] *Id.* at 105.
[102] *See id.* at 105–06.
[103] *See Simonson*, 758 F.2d at 106.
[104] *See id.*
[105] *Id.*
[106] 112 B.R. at 504–06.
[107] *See id.* at 506.
[108] *See id.* at 503.
[109] *See id.*

The court engaged in a three-step analysis to determine whether the judicial lien impaired the debtor's exemption.[110] The court first determined that the negative number that resulted after subtracting the unavoidable encumbrances from the fair market value of the property was equivalent to the debtor having zero equity in the property.[111] Second, the court explained that the debtor, nevertheless, had an "interest" in the property.[112] Relying on precedent, the court conceded that the debtor had residual interests in the form of "his right to possess the property and to build up his equity in the future."[113] The court next explained, however, that these residual interests were not exemptions to which the debtor would have been entitled.[114] Adhering to the plain language of the state's exemption statute, the court reasoned that an exemption that could be impaired is limited to the quantity of equity remaining after the unavoidable encumbrances are subtracted from the fair market value of the property.[115] Consequently, the court noted that because the unavoidable encumbrances exceeded the value of the property, there was no exemptible interest that a judicial lien could impair.[116] The court implicitly reasoned that the *judicial lien* did not impair any exemption because the *unavoidable encumbrances* already had impaired the exemption.[117] Thus, the court held that the judicial lien could not be avoided under § 522(f)(1).[118]

2. Situations Involving the Second and Third Fact Patterns

When there is either no equity or only some equity—but less than the value of the judicial lien—existing beyond the unavoidable encumbrances and the exemption, courts generally have taken one of three different approaches: 1) the "full avoidance" approach; 2) the "carve-out" approach; or 3) the "subordination" approach.[119]

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[110] *See id.* at 504–05.

[111] *See Bovay*, 112 B.R. at 504.

[112] *See id.* at 504–05.

[113] *Id.* at 504 (citing Alu v. State of N.Y. Dep't of Taxation & Fin., 41 B.R. 955, 957 (Bankr. E.D.N.Y. 1984)).

[114] *See id.* at 505.

[115] *See id.* The court turned to the state exemption statute because, pursuant to § 522(b)(2)(A), New York has opted out of the federal exemption scheme. *See* 11 U.S.C. § 522(b)(2)(A). The state's exemption statute provides for exemption of "[p]roperty . . . not exceeding ten thousand dollars in value above liens and encumbrances." 112 B.R. at 504 (citing N.Y. C.P.L.R. § 5206(a) (McKinney's Supp. 1990)).

[116] *See Bovay*, 112 B.R. at 505.

[117] *See id.* at 503, 505–06.

[118] *See id.* at 506.

[119] *See, e.g.*, *In re* Chabot, 992 F.2d 891, 895–96 (9th Cir. 1993) (following carve-out approach);

a. *The Full Avoidance Approach*

One approach some courts have taken when addressing the second and third fact patterns is the full avoidance approach.[120] Under this approach, courts adhere to a strict reading of the statutory language and narrowly interpret a debtor's "interest" in the property as meaning the quantity of equity in the property.[121] Moreover, courts adhering to the full avoidance approach interpret § 522(f)(1)'s phrase "to the extent" as meaning any portion of the judicial lien that is unsecured.[122]

The court in *In re Carney* followed the full avoidance approach.[123] In 1985, in *Carney*, the United States Bankruptcy Court for the District of Massachusetts held that the portion of the judicial lien that exceeded the debtor's equity in the property could be completely avoided under § 522(f)(1).[124] The debtor owned a home valued at $59,000, which was subject to a $35,000 mortgage.[125] Moreover, the debtor claimed a $12,500 homestead exemption.[126] Thus, there remained $11,500 in equity beyond the unavoidable encumbrances and exemption.[127] In addition, Cain obtained a judicial lien in the amount of $3993.85 and Colony Ford Truck Sales procured a judicial lien in the sum of $10,103.34.[128]

In addressing the issue of lien avoidance under § 522(f)(1), the court adhered to a strict reading of the statutory language and interpreted narrowly the debtor's "interest" in the property as meaning the quantity of equity in the property.[129] Moreover, the court interpreted the phrase "to the extent" as meaning any portion of the lien that exceeded the remaining equity in the property.[130] The court explained that Cain's lien, which had priority over Colony's lien, did not impair

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Bellenoit, 157 B.R. at 189–90 (adhering to subordination approach); *In re* Carney, 47 B.R. 296, 299 (Bankr. D. Mass. 1985) (following full avoidance approach).

[120] *See, e.g.*, *Carney*, 47 B.R. at 299; *In re* Duncan, 43 B.R. 833, 840 (Bankr. D. Alaska 1984); *see also infra* notes 121–36 and accompanying text.

[121] *See, e.g.*, *Carney*, 47 B.R. at 299; *Duncan*, 43 B.R. at 838; *see also infra* notes 123–36 and accompanying text.

[122] *See, e.g.*, *Carney*, 47 B.R. at 299; *Duncan*, 43 B.R. at 838; *see also infra* notes 123–36 and accompanying text.

[123] 47 B.R. at 299.

[124] *See id.*

[125] *See id.* at 297.

[126] *See id.*

[127] *See id.*

[128] *See Carney*, 47 B.R. at 297–98.

[129] *See id.* at 299.

[130] *See id.*

the exemption and therefore, the entire lien was valid.[131] The court reasoned that there was sufficient equity in the property to which the lien could attach.[132]

The court then noted that after Cain's lien, there remained only $7506.15 in equity to which Colony's $10,103.34 judicial lien could attach.[133] To determine whether Colony's judicial lien impaired the debtor's exemption, the court set forth a three-step test: 1) subtract all consensual liens from the value of the property; 2) subtract the exemption claimed from the remaining value; and 3) from the remainder, subtract the judicial liens.[134] The court explained that *to the extent* that all or any portion of a judicial lien exceeds the remainder left over from step two, it may be avoided.[135] Applying the three-part test, the court determined that the judicial lien impaired the debtor's exemption to the extent of $2597—the $10,103.34 judicial lien less the $7506.15 of remaining equity—and thus, the court concluded that the lien could be avoided to that extent.[136]

b. *Carve-out Approach*

A second approach taken by some courts is the "carve-out" approach.[137] Under this approach, courts interpret the phrase "to the extent" as a limiting phrase, meaning to the extent of an allowable exemption.[138] Thus, where there is insufficient equity to which an exemption can attach, courts following the carve-out approach hold that the exemption is carved out of the judicial lien.[139] As a result, the

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[131] *See id.*

[132] *See id.*

[133] *See Carney*, 47 B.R. at 299.

[134] *See id.*

[135] *See id.*

[136] *See id.*

[137] *See, e.g.*, *In re* Sanders, 39 F.3d 258, 262 (10th Cir. 1994); *Chabot*, 992 F.2d at 896; *In re* Cerniglia, 137 B.R. 722, 725–26 (Bankr. S.D. Ill. 1992); *In re* Sanglier, 124 B.R. 511, 514 (Bankr. E.D. Mich. 1991).

[138] *See, e.g.*, *Sanders*, 39 F.3d at 261–62; *Chabot*, 992 F.2d at 895–96; *Cerniglia*, 137 B.R. at 725–26; *Sanglier*, 124 B.R. at 515.

[139] *See, e.g.*, *Sanders*, 39 F.3d at 261–62; *Chabot*, 992 F.2d at 895–96; *Cerniglia*, 137 B.R. at 725–26; *Sanglier*, 124 B.R. at 515. These courts explain that the exemption is carved out of the judicial lien even when the lien is at the time valued at zero, as in the first fact pattern. *See Sanders*, 39 F.3d at 261–62; *Chabot*, 992 F.2d at 895–96; *Cerniglia*, 137 B.R. at 725–26; *Sanglier*, 124 B.R. at 515. Thus, theoretically, the carve-out approach also can be applied to fact pattern one—no equity exists beyond the unavoidable encumbrance. *See Sanders*, 39 F.3d at 261–62; *Chabot*, 992 F.2d at 895–96; *Cerniglia*, 137 B.R. at 725–26; *Sanglier*, 124 B.R. at 515. The result, however, is the same as the full avoidance approach, because the dollar amount of the exemption is zero. *See Sanders*, 39 F.3d at 261–62; *Chabot*, 992 F.2d at 895–96; *Cerniglia*, 137 B.R. at 725–26; *Sanglier*, 124 B.R. at 515; *see also Cravey*, 100 B.R. at 120.

maximum amount of a judicial lien that a debtor can avoid is the amount of a claimed exemption.[140]

The Supreme Court's decision in *Dewsnup v. Timm* is essential to the reasoning behind the carve-out approach.[141] In 1992, in *Dewsnup*, the United States Supreme Court held that, pursuant to § 506(d), the debtor could not "strip down" a creditor's lien—granted by a deed of trust—on real property to a judicially determined value.[142] The debtor argued that because the $119,000 lien exceeded the fair market value of the property—judicially determined to be $39,000—the Court should, pursuant to § 506(d), reduce the lien to the value of the property ("strip down").[143] The Court, however, noted that § 506(d) only applies when a claim is "not an allowed secured claim."[144] As a result, because the claim here was an allowed secured claim under § 502, the Court explained that the lien could not be stripped down under § 506(d).[145] The Court reasoned that to allow such a reduction would leave any future appreciation in the property to the benefit of the debtor, which the Court explained, should accrue for the benefit of the creditor.[146]

The Court garnered support for its position against lien-stripping from the pre-Code rule that liens on real property generally pass through bankruptcy unaffected.[147] The Court explained that pre-Code rules remain applicable unless a Code provision expressly states otherwise.[148] Here, the Court explained, the Code has not so spoken.[149] Consequently, the Court held that the entire lien passed through bankruptcy unaffected.[150]

Relying in part on *Dewsnup*, the United States Bankruptcy Court for the Southern District of Illinois in *In re Cerniglia* adopted the

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[140] *See, e.g.*, *Sanders*, 39 F.3d at 261–62; *Chabot*, 992 F.2d at 895–96; *Cerniglia*, 137 B.R. at 726–27; *Sanglier*, 124 B.R. at 514, 515.

[141] 502 U.S. 410, 416–20 (1992).

[142] *See id.*; *see also* 11 U.S.C. § 506(d) (1994). Section 506(d) states in pertinent part: "[t]o the extent that a lien secures a claim against the debtor that is not an allowed secured claim, such lien is void . . . ." 11 U.S.C. § 506(d). *Dewsnup* concerns the issue of lienstripping. *See* 502 U.S. at 416–20. Lienstripping occurs when a court reduces the amount of a lien so that it equals the judicially determined fair market value of the property. *See id.* Thus, the remaining portion of the lien is nullified. *See id.*

[143] *See Dewsnup*, 502 U.S. at 413.

[144] *Id.*; *see also* 11 U.S.C. §§ 502(a), 506(d). Section 502(a) states in relevant part: "[a] claim or interest . . . is deemed allowed, unless a party in interest . . . object[s]." 11 U.S.C. § 502(a) (1994).

[145] *See Dewsnup*, 502 U.S. at 417; *see also* 11 U.S.C. §§ 502(a), 506(d).

[146] *See Dewsnup*, 502 U.S. at 417.

[147] *See id.* at 419 (citing Long v. Bullard, 117 U.S. 617, 620–21 (1886)).

[148] *See id.*

[149] *See id.*

[150] *See id.* at 420.

carve-out approach with respect to § 522(f)(1).[151] In 1992, in *Cerniglia*, the court held that the judicial lien did not attach to the debtor's exempt property and therefore, the lien could not be avoided under § 522(f)(1).[152] The debtor's residence was valued at $115,000 and was encumbered by a $101,105.99 mortgage.[153] Moreover, the debtor claimed a $15,000 homestead exemption.[154] The property also was subject to a $358,986.70 judicial lien.[155]

The court began its analysis by noting that there were two lines of cases interpreting and applying § 522(f)(1) differently: those courts adopting the full avoidance approach and those following the carve-out approach.[156] The court explained that the difference between each of these approaches was their contrary allocation of any post-bankruptcy appreciation: the full avoidance approach entitles the debtor to any post-bankruptcy appreciation, while the carve-out approach gives such appreciation to the creditor.[157] The court then discredited the full avoidance approach by explaining that it has been implicitly rejected by the Supreme Court.[158] Noting that the full avoidance approach incorporates § 506(d)'s "strip down" analysis into § 522(f)(1)'s lien avoidance process, the court explained that this "lien-stripping" rationale is no longer valid following the Supreme Court's rejection of the "strip-down" of liens under § 506(d).[159]

The court then alluded to the Supreme Court's reaffirmation of the pre-Code rule that liens on real property survive bankruptcy in the absence of a statutory provision providing otherwise.[160] The court implicitly determined that this pre-Code rule is partially preempted by § 522(f)(1), which allows a debtor to avoid a judicial lien "to the extent" it impairs an exemption.[161] Thus, the court recognized that through the interplay of § 522(f)(1) and the pre-Code rule, a lien that impairs an exemption is only avoided to the extent of an allowable exemption.[162]

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[151] 137 B.R. at 725.
[152] *See id.* at 728.
[153] *See id.* at 723.
[154] *See id.*
[155] *See id.*
[156] *See Cerniglia*, 137 B.R. at 723–24.
[157] *See id.* at 724.
[158] *See id.* (citing *Dewsnup*, 502 U.S. at 417–20).
[159] *See id.*
[160] *See id.* at 725 (citing *Dewsnup*, 502 U.S. at 419).
[161] *See Cerniglia*, 137 B.R. at 724–25.
[162] *See id.* at 725.

Recognizing that the application of the carve-out approach often results in the survival of liens, which in turn clouds the debtor's title, the court explained that this result would not inhibit the debtor's fresh-start.[163] Interpreting narrowly the Code's fresh-start policy, the court emphasized that the exemption was limited only to the specific amount of the allowable exemption.[164] The court stated, "section 522(f)(1) was not intended to free the debtor's property completely of judicial liens. Rather it is the purpose and effect of this provision to preserve the debtor's exemption and thus his fresh-start by allowing avoidance of liens in the specific amount of the debtor's exemption."[165] In addition, the court explained that the exemption gives the debtor a "superior right" in the property up to the specific amount of the allowable exemption, thereby protecting the debtor's exemption after bankruptcy.[166] Thus, adhering to the plain language of § 522(f)(1), the court reasoned that a debtor's exemption is "impaired" to the extent a judicial lien attaches to any portion of the exemption.[167] Nevertheless, the court concluded that, pursuant to the state exemption law, the lien could not be avoided because the state law specifically prevents a judicial lien from attaching to a debtor's homestead interest.[168]

Similarly, the court in *City National Bank v. Chabot* followed the carve-out approach.[169] In 1993, in *Chabot*, the United States Court of Appeals for the Ninth Circuit held that the creditor's judicial lien could not be avoided because there was sufficient equity in the property to which the debtor's $45,000 exemption could attach.[170] The debtors owned a residence valued at $400,000, which was encumbered by two unavoidable deeds of trust equaling $124,953.30.[171] Moreover, the Chabots were entitled to a $45,000 homestead exemption.[172] Thus, there remained $230,046.68 in equity beyond the unavoidable encumbrances and homestead exemption.[173]

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[163] *See id.*

[164] *See id.*

[165] *Id.*

[166] *See Cerniglia*, 137 B.R. at 725.

[167] *See id.*

[168] *See id.* at 726–28. The court turned to the state exemption statute because, pursuant to § 522(b)(2)(A), Illinois opted out of the federal exemption scheme. *See id.*; *see also* 11 U.S.C. § 522(b)(2)(A).

[169] 992 F.2d at 895–96.

[170] *See id.* at 892, 896.

[171] *See id.* at 892.

[172] *See id.*

[173] *See id.*

Adhering to a strict reading of the statutory language, the court reasoned that § 522(f)(1)'s phrase "to the extent" limited the extent a judicial lien could impair an exemption to the amount of the claimed exemption.[174] The court explained that the exemption laws only entitle a debtor to the set amount of the exemption, "no more and no less."[175] Moreover, the court narrowly interpreted the Code's fresh-start policy as requiring the protection of only the specific amount of the allowable exemption.[176] The court explained that any post-bankruptcy appreciation should accrue for the benefit of the judicial lienholder.[177] Consequently, because there was sufficient equity to satisfy the $45,000 exemption, the court concluded that City National Bank's judicial lien of $241,579.08 survived bankruptcy in its entirety.[178]

c. *Subordination Approach*

A third approach taken by some courts is the "subordination" approach.[179] Under this approach, courts begin with an application of the carve-out approach, but then interpret differently the word "avoid" as meaning to subordinate, rather than to nullify.[180] The subordination approach was applied in *In re D'Amelio*.[181] In 1992, in *D'Amelio*, the United States Bankruptcy Court for the District of Massachusetts held that the judicial liens fully survived bankruptcy, although assuming a subordinate position to the claimed exemption.[182] The debtor and his spouse owned property valued at $154,000 as tenants-by-the-entirety.[183] The property was subject to a first mortgage of $86,829.36 and a second mortgage of $28,453.07.[184] Thus, there existed $38,717.57 in equity beyond the unavoidable encumbrances, of which the debtor's interest was $19,358.78—one-half interest in the property owned as tenants-by-the-entirety.[185] Moreover, the debtor claimed a $7900 homestead ex-

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[174] *See Chabot*, 992 F.2d at 895.

[175] *Id.* at 896.

[176] *See id.*

[177] *See id.*

[178] *See id.* at 892, 896.

[179] *See, e.g., Bellenoit*, 157 B.R. at 188; *In re* D'Amelio, 142 B.R. 8, 10 (Bankr. D. Mass. 1992).

[180] *See, e.g., Bellenoit*, 157 B.R. at 188; *D'Amelio*, 142 B.R. at 10.

[181] 142 B.R. at 10.

[182] *See id.* Judge Hillman later changed his interpretation of § 522(f) and in *In re Garro*, he adopted the carve-out approach. 161 B.R. 869, 870 (Bankr. D. Mass. 1993).

[183] *See D'Amelio*, 142 B.R. at 9.

[184] *See id.*

[185] *See id.*

emption.[186] Also, the debtor's interest was encumbered by judicial liens totaling $51,653.81.[187]

Partially adopting the reasoning of the carve-out approach, the court stated that § 522 limits the extent that a lien can be avoided to the amount of the claimed exemption.[188] The court relied on *Cerniglia* and that court's reference to the Supreme Court's holding that liens on real property generally survive bankruptcy unaffected.[189] Quoting *Cerniglia*, the court noted:

> [s]ection 522(f)(1) gives the debtor only a limited power to avoid liens in order to preserve his exemption. This power may not be expanded to allow avoidance of the unsecured portion of the lien that would otherwise survive the debtor's discharge. To so interpret § 522(f)(1) would be to grant the debtor not merely the benefit of his exemption in the homestead property but also all the benefits of ownership beyond the exemption amount . . . .[190]

Thus, purporting to adhere to the plain meaning of the statute, the court partially adopted the reasoning of the carve-out approach.[191]

The court, however, continued its analysis and departed from the carve-out approach in its interpretation of the word "avoid."[192] As opposed to the carve-out approach's nullification of the portion of the lien found to impair the exemption, the court here viewed the issue in terms of priority.[193] The court reasoned that "to avoid can be to go around as well as declare a nullity."[194] Thus, the court held that those judicial liens that impaired the exemption assumed a subordinate position to that of the exemption.[195]

The court in *Bellenoit v. Avco Leasing Services* further developed the subordination approach.[196] In 1992, in *Bellenoit*, the United States Bankruptcy Court for the District of Massachusetts held that the portion of the judicial lien that impaired the debtor's exemption was

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[186] *See id.*
[187] *See id.*
[188] *See D'Amelio*, 142 B.R. at 9–10.
[189] *See id.* at 10 (quoting *Cerniglia*, 137 B.R. at 722 (citing *Dewsnup*, 502 U.S. at 410)).
[190] *Id.* (quoting *Cerniglia*, 137 B.R. at 725).
[191] *See id.*
[192] *See id.*
[193] *See D'Amelio*, 142 B.R. at 10.
[194] *Id.*
[195] *See id.*
[196] 157 B.R. at 186–90.

subordinated to the exemption.[197] The debtor and his wife owned a home as tenants-by-the-entirety.[198] This residence was valued at $285,200 and was subject to an unavoidable mortgage of $268,000.[199] Thus, the debtor's equity in the property was $8600—debtor's one-half interest in the $17,200 of equity remaining in the property owned by debtor and his wife as tenants-by-the-entirety.[200] Moreover, the debtor claimed a homestead exemption of $7900, thereby leaving only $700 in equity to which a $600,000 judicial lien could attach.[201]

The court expressly agreed with the *D'Amelio* court.[202] Nevertheless, the court noted that the conclusion in *D'Amelio* did not provide an answer as to *which* liens impair a debtor's exemption.[203] While the court in *D'Amelio* merely concluded that the judicial liens are subordinated to the exemption, here, the court expanded on the reordering concept introduced in *D'Amelio*.[204] The court explained that lien avoidance begins with the lien, or the part thereof, that consumes the last portion of equity to which the exemption could attach.[205] For example, here there remains $8600 in equity and the debtor claims a $7900 homestead exemption.[206] The judicial liens therefore would first attach to the $700 that existed above the $7900 and then the homestead exemption would attach to the final remaining $7900 of equity.[207] Any remaining value of the judicial liens would be subordinated to the exemption.[208] In effect, the court noted that the lien "is split to make room for the debtor's exemption."[209] Thus, the court concluded that the lien was partially avoided by displacement.[210]

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[197] *See id.* at 189–90.

[198] *See id.* at 186.

[199] *See id.*

[200] *See id.* at 186–87.

[201] *See Bellenoit*, 157 B.R. at 187. *But see id.* at 187 n.3 (stating that it is unclear whether debtor is claiming $7900 as exemption or merely saying that amount is the equity from which his exemption may be taken).

[202] *See id.* at 187; *see also D'Amelio*, 142 B.R. at 10.

[203] *See Bellenoit*, 157 B.R. at 187 (citing *D'Amelio*, 142 B.R. at 10).

[204] *See id.* at 187–88 (citing *D'Amelio*, 142 B.R. at 10).

[205] *See id.* at 188.

[206] *See id.*

[207] *See id.*

[208] *See Bellenoit*, 157 B.R. at 188.

[209] *Id.* at 188.

[210] *See id.* at 187, 189–90.

III. Congressional Response: The 1994 Amendments to the Code

Recognizing the ongoing confusion surrounding the interpretation and application of § 522(f)(1), Congress amended the Code in 1994 by adding § 522(f)(2).[211] This new provision was designed to provide a definition for § 522(f)(1)'s phrase "impair an exemption."[212] Section 522(f)(2) provides:

> For the purposes of this subsection, a lien shall be considered to impair an exemption to the extent that the sum of
> (i) the lien;
> (ii) all other liens on the property;
> (iii) the amount of the exemption that the debtor could claim if there were no liens on the property;
> exceeds the value that the debtor's interest in the property would have in the absence of any liens.[213]

Specifically, with the addition of § 522(f)(2), Congress intended to avoid the above-illustrated confusion by providing a "simple arithmetic test" to determine whether a lien impairs an exemption.[214]

In the legislative history to the 1994 Amendments, Congress makes clear that § 522(f)(2) was solely intended to be a clarification amendment.[215] As the House report explains, "[b]ecause the Bankruptcy Code does not currently define the meaning of the words 'impair an exemption' in § 522(f), several court decisions have, in recent years, reached results that were not intended by Congress when it drafted the Code."[216] In the House report, Congress addressed three particular areas plagued by confusion and explained that certain decisions would be overruled by this clarification amendment.[217]

The first area of confusion that Congress intended to clarify by the 1994 Amendments involved the first fact pattern—no equity in the

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[211] *See* 140 Cong. Rec. 10,752, 10,769 (1994); *see also* 11 U.S.C. § 522(f)(1)–(2) (1994).

[212] 140 Cong. Rec. at 10,769.

[213] *See* 11 U.S.C. § 522(f)(2).

[214] 140 Cong. Rec. at 10,769. The legislative history to § 522(f)(2) states, "because the Bankruptcy Code does not currently define the meaning of the words 'impair an exemption' in section 522(f), several court decisions have, in recent years, reached results that were not intended by Congress when it drafted the Code. This amendment would provide a simple arithmetic test to determine whether a lien impairs an exemption . . . ." 140 Cong. Rec. at 10,769.

[215] *See* Schmidt, *supra* note 32, at 1053; *see also* 140 Cong. Rec. at 10,769.

[216] 140 Cong. Rec. at 10,769.

[217] *See id.* Congress explicitly addressed three areas that would be overruled by the amendment; however, for purposes of this note, I will only address the first two areas. *See id.*

property beyond the unavoidable encumbrances.[218] Purporting to follow the majority of courts, Congress took the position that a judicial lien could impair an exemption where there remained no equity in the property above any unavoidable encumbrances, reasoning that a debtor has equitable rights in the property, such as a possessory interest.[219] Congress explained that a debtor is entitled to exempt these residual interests.[220] Congress stated that to follow the minority of courts that have held that the *unavoidable encumbrance* impaired the exemption and therefore, the judicial lien could not be avoided, would inhibit a debtor's fresh-start.[221] Congress further explained that if the judicial lien is not avoided, any post-bankruptcy appreciation in the property would accrue for the benefit of the creditor, thereby threatening to deprive a debtor of his exemption.[222] Thus, Congress stated that a judicial lien can impair an exemption where there exists no equity in the property beyond the unavoidable encumbrances and therefore, the lien can be avoided.[223] In effect, Congress adhered to the complete avoidance approach adopted by the court in *Cravey* and rejected the "not impair" approach, as followed by the courts in *Simonson* and *Bovay*.[224]

The second area of confusion that Congress endeavored to clarify involves the second fact pattern—no equity existing beyond the unavoidable encumbrances and exemption.[225] Congress overruled those cases adhering to the carve-out approach, including *Chabot*.[226] Congress agreed with the majority of courts that have found that, where there is no equity beyond the unavoidable encumbrances and exemption, the judicial lien is avoided in its entirety.[227] Congress explained that the avoidance of the entire lien in such situations preserves the debtor's exemption after bankruptcy.[228] In rejecting the minority view that adopts the carve-out approach—as illustrated by *Chabot*—Congress reasoned that the carve-out approach threatens the debtor's fresh-start.[229] Congress stated that any equity created in the property

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[218] *See id.*; *see also supra* notes 68–118 and accompanying text.
[219] *See* 140 CONG. REC. at 10,769.
[220] *See id.*
[221] *See id.*
[222] *See id.*
[223] *See id.*
[224] *See* 140 CONG. REC. at 10,769; *see also supra* notes 68–118 and accompanying text.
[225] *See* 140 CONG. REC. at 10,769; *see also supra* notes 120–210 and accompanying text.
[226] *See* 140 CONG. REC. at 10,769; *see also supra* notes 137–78 and accompanying text.
[227] *See* 140 CONG. REC. at 10,769.
[228] *See id.*
[229] *See id.*; *see also supra* notes 137–78 and accompanying text.

as a result of mortgage payments made from the debtor's post-bankruptcy income—income that the fresh-start is supposed to protect for the debtor—would accrue for the benefit of the lienholder.[230] Moreover, Congress explained that the debtor's fresh-start would be further endangered because the judicial lien may prevent the debtor from selling his home prior to paying the judicial lienholder.[231] Thus, concerned with preserving the debtor's exemption and fresh-start, Congress rejected the carve-out approach.[232] Although Congress expressly addressed the confusion surrounding the first and second fact patterns, it did not address those situations involving the third fact pattern.[233]

IV. Post-Amendment Judicial Approaches to the Interpretation and Application of § 522(f)(1)

A. *Overview*

In the legislative history to the 1994 Amendments, Congress explicitly rejected the not impair and carve-out approaches, but it did not expressly address the subordination and full avoidance approaches.[234] Nevertheless, no court has applied the subordination approach since the passage of the 1994 Amendments to the Code, and a few courts have even gone so far as to reject this approach expressly.[235] On the other hand, following the 1994 Amendments to the Code, some courts have continued to adhere to the full avoidance approach, while other courts began adopting a new approach—the "entire lien avoidance" approach.[236] Thus, despite the 1994 Amendments, courts have never-

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[230] *See* 140 Cong. Rec. at 10,769.

[231] *See id.*

[232] *See id.*

[233] *See id.*

[234] *See id.*

[235] *See, e.g., In re* Donahue, 205 B.R. 661, 662 (Bankr. D. Mass. 1997). In 1997, in *Donahue*, the United States Bankruptcy Court for the District of Massachusetts held that the judicial lien was avoided by nullification, and not merely subordinated to the exemption. *See id.* The court explained that although the 1994 amendments did not apply to that case, the court could consider the legislative history. *See id.* In viewing the legislative history, the court rejected the creditor's argument that *Bellenoit* requires the subordination of the judicial lien. *See id.*; *see also* Bellenoit v. Avco Leasing Serv., 157 B.R. 185, 185 (Bankr. D. Mass. 1992). Rather, the court held that the lien was voided and not subordinated. *See Donahue*, 205 B.R. at 662.

[236] *See, e.g.*, East Cambridge Sav. Bank v. Silveira, 1998 WL 175119, at *4, 6 (1st Cir. Apr. 21, 1998); *In re* Finn, 211 B.R. 780, 784 (B.A.P. 1st Cir. Sept. 5, 1997); East Cambridge Sav. Bank v. Silveira, Memorandum & Order, 1, 7 (No. 96–11388-WGY) (D. Mass. 1997), vacated and remanded, 1998 WL 175119 (1st Cir. Apr. 21, 1998); *In re* Ryan, 210 B.R. 7, 13 (Bankr. D. Mass. 1997).

theless adopted different interpretations of the statutory language, the legislative history and the policy objectives behind the Code.[237] Consequently, the confusion surrounding § 522(f) persists, causing courts to continue to struggle over how to interpret and apply this provision.[238]

B. *The* Gonzalez *Saga*

A clear illustration of the confusion that continues to surround § 522(f)(1) is the *Gonzalez* saga.[239] In 1993, prior to the 1994 Amendments to the Code, in *In re Gonzalez*, the United States Bankruptcy Court for the District of Massachusetts followed the carve-out approach, holding that the debtor could avoid the judicial lien in the amount of the claimed exemption.[240] The debtor's property was valued at $129,100 and was encumbered by a $106,000 mortgage.[241] Moreover, the debtor claimed a $4235 homestead exemption.[242] Thus, there remained $18,865 in equity to which a $300,000 judicial lien could attach.[243] Adhering to a strict reading of the statutory language, the court explained that the word "extent" in § 522(f)(1) means "range . . . over which something extends."[244] Thus, the court reasoned that the judicial lien could only be avoided to the extent of the claimed exemption—$4235.[245] The court held that the remainder of the judicial lien that exceeded the existing equity—the unsecured portion—was subordinated to the unavoidable encumbrances and exemption.[246]

On appeal, in 1996, in *Gonzalez v. First National Bank of Boston*, the United States District Court for the District of Massachusetts held that the debtors were entitled to completely avoid the judicial lien.[247] Because the case commenced before the adoption of the 1994 Amendments to the Code, the court explained that the 1994 Amendments did not apply to this case.[248] Nevertheless, the court announced that the legislative history "is enlightening and relevant."[249] The court noted

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[237] *See, e.g.*, *Silveira*, 1998 WL 175119, at *4, 6; *Finn*, 211 B.R. at 784; *Silveira*, Memorandum & Order, at 7; *Ryan*, 210 B.R. at 13.

[238] *See, e.g.*, *Finn*, 211 B.R. at 784; *Silveira*, Memorandum & Order, at 7; *Ryan*, 210 B.R. at 13. *But see Silveira*, 1998 WL 175119, at *4.

[239] *See In re* Gonzalez, 191 B.R. 2, 4 (Bankr. D. Mass. 1996) ("*Gonzalez II*"); *In re* Gonzalez, 149 B.R. 9, 12 (Bankr. D. Mass. 1993) ("*Gonzalez I*").

[240] *Gonzalez I*, 149 B.R. at 11–12.

[241] *See id.* at 10.

[242] *See id.*

[243] *See id.*

[244] *Id.* (citing WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY (1986)).

[245] *See Gonzalez I*, 149 B.R. at 10.

[246] *See id.* at 11–12.

[247] *Gonzalez II*, 191 B.R. at 3–4.

[248] *See id.* at 3.

[249] *Id.*

that the legislative history directly rejected the carve-out approach, as adopted by the court in *Chabot*.[250] Thus, the *Gonzalez* court reversed the lower court's ruling, reasoning that the result was in direct contradiction to Congress's intent.[251] Rather, the court concluded that the entire judicial lien could be completely avoided.[252] The court, however, did not explain whether it was applying the full avoidance or entire lien avoidance approach.[253]

C. *Current Judicial Approaches—Full Avoidance vs. Entire Lien Avoidance*

As the *Gonzalez* cases illustrate, courts disagree over the meaning of the statutory language, the legislative history to the 1994 Amendments and the policy objectives behind the Code.[254]

1. The Full Avoidance Approach

Following the 1994 Amendments to the Code, some courts have continued to adhere to the full avoidance approach, thereby completely avoiding any portion of a judicial lien that exceeds the quantity of equity remaining in the property.[255] In 1998, in *East Cambridge Savings Bank v. Silveira*, the United States Court of Appeals for the First Circuit adopted the full avoidance approach, holding that the debtor could avoid only partially the judicial lien.[256] The debtor sought to avoid a $209,500 judicial lien on his home, which was valued at $157,000.[257] The home was subject to a $117,680 mortgage and the debtor was entitled to a $15,000 homestead exemption.[258] Thus, there remained $24,320 in equity after the mortgage and exemption.[259]

Purporting to adhere to the plain language of the statute, the court explained that the statutory language supports the application

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[250] *See id.* at 3–4 (quoting 140 CONG. REC. 10,752, 10,769 (1994)).

[251] *See id.* at 4.

[252] *See Gonzalez II*, 191 B.R. at 3–4.

[253] *See id.* In making its calculations, the court used the liquidation value of the property, rather than the standard fair market value. *See id.* Under the liquidation valuation, there remained no equity beyond the unavoidable encumbrances and exemption, whereas, under a fair market evaluation, there did remain some equity. *See id.*

[254] *See, e.g.*, *Finn*, 211 B.R. at 784 (applying full avoidance approach); *Silveira*, Memorandum & Order, at 7 (adhering to entire lien avoidance approach); *Gonzalez II*, 191 B.R. at 3–4 (unclear whether applying full avoidance or entire lien avoidance approach). *But see Silveira*, 1998 WL 175119, at *4 (adopting the full avoidance approach).

[255] *See, e.g.*, *Silveira*, 1998 WL 175119, at *4; *Finn*, 211 B.R. at 784; *Ryan*, 210 B.R. at 13.

[256] 1998 WL 175119, at *4.

[257] *See id.* at *1.

[258] *See id.*

[259] *See id.*

of the partial lien avoidance approach.[260] The court reasoned that if Congress had intended the provision to be a "all-or-nothing" matter, it would not have used the word "if" in lieu of the phrase "to the extent that."[261] The court further reasoned that partial lien avoidance comports with the statute's intended purpose.[262] Introducing hypothetical scenarios, the court explained that the entire lien avoidance approach would lead to results that "seemed arbitrary and unfair."[263] Particularly, the court explained that it would be arbitrary to allow a $30,000 lien to remain intact where there existed $30,000 in equity, but to avoid the entire lien if the amount was increased by only $1—totalling $30,001.[264] Thus, the court adopted the partial lien avoidance approach and allowed the debtor to avoid only $185,180—the portion of the lien that impaired his exemption.[265]

Moreover, in 1997, in *In re Ryan*, the United States Bankruptcy Court for the District of Massachusetts held that a debtor could only partially avoid a judicial lien.[266] The debtor's property was valued at $140,000 and was subject to a $38,021.08 mortgage.[267] Moreover, the debtor claimed a $10,161 homestead exemption.[268] Thus, there existed $91,817.92 in equity beyond the unavoidable encumbrance and exemption to which a $290,596.79 judicial lien could attach.[269]

Adhering to a strict reading of the statutory language of § 522(f)(2), the court reasoned that the phrase "to the extent" allows only partial lien avoidance—avoidance to the extent of the impairment that results from the application of the arithmetic formula.[270] The court explained that "[t]he formula set forth in § 522(f)(2)(A) is straightforward and easily applied."[271] At the same time, however, the court conceded that the legislative history is confusing and suggests that Congress intended entire lien avoidance.[272] Nevertheless, the court explained that where the statutory language is unambiguous, the plain

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[260] *See id.* at *2.

[261] 1998 WL 175119, at *2.

[262] *See id.* at *3.

[263] *See id.* at *3 n.3.

[264] *See id.*

[265] *See id.* at *4, 6.

[266] 210 B.R. at 13.

[267] *See id.* at 8.

[268] *See id.*

[269] *See id.*

[270] *See id.* at 10, 12–13.

[271] *Ryan*, 210 B.R. at 10.

[272] *See id.* at 10–11. Judge Feeney explained, "[t]he commentary about the *Chabot* case contained in the legislative history suggests that partially secured liens should be avoided in their entirety . . . ." *Id.* at 11.

language governs, irrespective of the legislative history.[273] The court concluded that § 522(f)(2) only requires avoidance of the portion of the judicial lien which impairs an exemption, as determined by that section's arithmetic formula.[274] Consequently, the court determined that the lien was partially avoided in the amount of $198,778.87—the amount in excess of the quantity of equity remaining in the property.[275]

Likewise, in 1997, in *Federal Deposit Insurance Corp. v. Finn*, the United States Bankruptcy Appellate Panel of the First Circuit ("BAP") followed the full avoidance approach.[276] In *Finn*, the BAP overruled the federal district court's avoidance of a judicial lien in its entirety and instead, held that the debtor could only partially avoid the lien.[277] The debtor owned a home that was valued at $225,000.[278] The home was encumbered by several mortgages and liens: a first mortgage of $66,965.34, a second mortgage of $87,932, a first judicial lien of $1,300,000 and a second judicial lien of $766,552.63.[279] Moreover, the debtor claimed a $15,700 homestead exemption.[280]

Adhering to a strict reading of the statutory language of § 522(f)(2), the court reasoned that the arithmetic formula compelled partial lien avoidance.[281] On the other hand, the court noted that the legislative history was confusing because Congress alluded to cases that did not support the correlating fact patterns.[282] Nevertheless, the court stated that "review of the analysis of the legislative history is not necessary where the plain meaning of the statute is conclusive."[283]

Moreover, the court reasoned that partial avoidance of the lien is consistent with bankruptcy policies.[284] First, the court explained that the full avoidance approach preserves the exemption and allows post-bankruptcy appreciation to accrue for the benefit of the debtor.[285] Second, the court stated that the full avoidance approach provides certainty and definiteness by setting judicial liens at a fixed amount.[286]

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[273] *See id.* at 12 (citing United States v. Ron Pair Enters., Inc., 489 U.S. 235, 242 (1989)).

[274] *See id.* at 12–13.

[275] *See id.*

[276] 211 B.R. at 784.

[277] *See id.*

[278] *See id.* at 780–81. The valuation of the home is the debtor's valuation. *See id.* at 780–81 & n.1.

[279] *See id.* at 781.

[280] *See id.*

[281] *See Finn*, 211 B.R. at 782–83.

[282] *See id.* at 782.

[283] *See id.*

[284] *See id.* at 783.

[285] *See id.*

[286] *See Finn*, 211 B.R. at 783.

Thus, the court held that, pursuant to § 522(f)(1), the debtor could avoid only that portion of the judicial lien that exceeded the debtor's equity in the property.[287]

2. The Entire Lien Avoidance Approach

At the same time, following the 1994 Amendments, some courts adopted a new approach—the "entire lien avoidance" approach.[288] Under this approach, courts adhere to a strict reading of the statutory language.[289] Courts following this approach explain that § 522(f) mandates that a lien is either avoided in its entirety or fully survives bankruptcy.[290]

The entire lien avoidance approach is illustrated by *East Cambridge Savings Bank v. Silveira*.[291] In 1997, in *Silveira*, the United States District Court for the District of Massachusetts held that, pursuant to § 522(f)(1), the entire lien was avoided.[292] In *Silveira*, the debtor sought to avoid a $209,500 judicial lien on his home, which was valued at $157,000.[293] The home was subject to a $117,680 mortgage and the debtor was entitled to a $15,000 homestead exemption.[294] Thus, there remained $24,320 in equity after the mortgage and exemption.[295]

Adhering to a strict reading of the statutory language, the court avoided the $209,500 lien entirely, reasoning that § 522(f)(2) mandates the avoidance of the entire lien if that lien impairs an exemption to any extent.[296] The court explained, "Congress set forth a clear formula which, if satisfied, requires the avoidance of the lien."[297] Moreover, the court reasoned that the legislative history to the 1994 Amendments to the Code likewise mandate entire lien avoidance.[298] Specifically, the court referenced a passage from the legislative history in

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[287] *See id.* at 784.

[288] *See, e.g., Silveira*, Memorandum & Order, at 7; *see also Finn*, 211 B.R. at 785 (DeJesus, J., dissenting).

[289] *See, e.g., Silveira*, Memorandum & Order, at 5; *In re* Thomsen, 181 B.R. 1013, 1016 (Bankr. M.D. Ga. 1995); *see also Finn*, 211 B.R. at 785 (DeJesus, J., dissenting).

[290] *See, e.g., Finn*, 211 B.R. at 785 (DeJesus, J., dissenting); *Silveira*, Memorandum & Order, at 5; *Thomsen*, 181 B.R. at 1016.

[291] Memorandum & Order, at 5–7. Although United States Court of Appeals for the First Circuit vacated the decision in this case, the theory expounded by the court remains important because similar issues are bound to arise in other circuits that have not yet decided, for themselves, which approach is correct. *See Silveira*, 1998 WL 175119, at *6.

[292] *See Silveira*, Memorandum & Order, at 7.

[293] *See id.* at 1, 3–4 nn.1–2.

[294] *See id.* at 1, 3–4 n.2.

[295] *See id.*

[296] *See id.* at 5, 7.

[297] *Sileiva*, Memorandum & Order, at 5.

[298] *See id.* at 5–6.

which Congress rejected the not impair approach.[299] The court explained that Congress also implicitly rejected the full lien avoidance approach in this passage.[300] Without providing any reasoning, the court merely stated, "[p]articularly relevant is the following excerpt where the House Report rejects the partial avoidance approach [here referred to as the full avoidance approach] . . . ."[301] The court then cited the passage in which Congress expressly rejected the not impair approach.[302]

In addition to garnering support from the statutory language and the legislative history to the 1994 Amendments, the court also explained that the entire lien avoidance approach furthers the Code's fresh-start policy.[303] Particularly, the court noted that the entire lien avoidance approach protects a debtor's interest in the property after bankruptcy because any future increase in the value of the property accrues for the benefit of the debtor.[304] Thus, the court concluded that, pursuant to § 522(f)(1), the entire lien was avoided.[305]

Similarly, in a dissenting opinion in *Finn*, Judge DeJesus argued in favor of adopting the entire lien avoidance approach.[306] Judge DeJesus agreed with the lower court's opinion and argued that the entire lien should be avoided.[307] In addition, Judge DeJesus referenced a long passage from *In re Thomsen* to support his position that § 522(f)(1) mandates the avoidance of the entire lien where the lien impairs an exemption in any amount.[308] Particularly, he emphasized *Thomsen*'s explanation that "[a] lien is an absolute entitlement. Property is either subject to a lien, or not."[309] Judge DeJesus implicitly reasoned that a

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[299] *See id.* at 6.

[300] *See id.* at 5–6.

[301] *Id.* at 5–6.

[302] *See Silveira*, Memorandum & Order, at 6.

[303] *See id.* at 7.

[304] *See id.*

[305] *See id.*

[306] *See Finn*, 211 B.R. at 784–85.

[307] *See id.* at 784; *see also supra* notes 265–76 and accompanying text for discussion of the facts and the majority opinion in *Finn*.

[308] *See Finn*, 211 B.R. at 784–85 (quoting *Thomsen*, 181 B.R. at 1016). In *Thomsen*, the United States Bankruptcy Court for the District of Georgia held that the entire judicial lien could be avoided pursuant to § 522(f)(1). *See* 181 B.R. at 1016. In *Thomsen*, there did not exist any equity beyond the unavoidable encumbrances and exemption. *See id.* at 1017. In reviewing § 522(f)(2) and the legislative history to the 1994 Amendments to the Code, the court explained that there is confusion over whether the entire lien avoidance or full avoidance approach is the correct approach under § 522(f)(1). *See id.* at 1016. Nevertheless, the court did not have to answer the question because there was no remaining equity in the property; therefore, under either approach, the entire lien would be avoided. *See id.* Thus, the court concluded that the lien was avoided in full pursuant to § 522(f)(1). *See id.*

[309] *Finn*, 211 B.R. at 785 (citing *Thomsen*, 181 B.R. at 1016).

lien does not have a numerical sum and therefore, rejected the ability of the majority to bifurcate a lien.[310] Specifically, Judge DeJesus quoted *Thomsen*, in which the court stated, "the concept of bifurcation of the lien, rather than the debt that it secures, is heretofore unknown."[311] Alluding to *Thomsen*, Judge DeJesus noted that in addition to the carve-out approach, which the amendments rejected, and the claims bifurcation approach of § 506, the only remaining approach is entire lien avoidance.[312] Thus, Judge DeJesus concluded that where a judicial lien is found to impair an exemption to any extent, § 522(f)(2) mandates complete avoidance of the lien.[313]

V. Analysis

Although the 1994 Amendments to the Code were intended to clarify § 522(f)(1), they have not produced such a result.[314] Rather, following the 1994 Amendments, courts have continued to interpret and apply § 522(f) differently, even when addressing the same fact pattern.[315] Through the passage of the 1994 Amendments, Congress only managed to produce a limited amount of clarity with its express rejection of the not impair and carve-out approaches and its implicit rejection of the subordination approach.[316]

The legislative history does explain that in situations involving the first fact pattern—no equity existing beyond the unavoidable encumbrances—a judicial lien does impair an exemption, thereby rejecting the "not impair" approach.[317] Moreover, in the legislative history, Congress interpreted the phrase "to the extent" as not meaning to the extent of the allowable exemption, thereby rejecting the carve-out approach.[318] In addition, although Congress did not expressly discredit the subordination approach, it implicitly rejected it by broadly interpreting the Code's fresh-start policy.[319]

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[310] *See id.* at 784–85.

[311] *Id.* at 785.

[312] *See id.*

[313] *See id.*

[314] *See* 140 Cong. Rec. 10,752, 10,769 (1994); *see, e.g.*, *In re* Finn, 211 B.R. 780, 784 (B.A.P. 1st Cir. Sept. 5, 1997); East Cambridge Sav. Bank v. Silveira, Memorandum & Order, 1, 7 (No. 96-11388-WGY) (D. Mass. 1997), *vacated and remanded*, 1998 WL 175119 (1st Cir. Apr. 21, 1998). *But see* East Cambridge Savings Bank v. Silveira, 1998 WL 175119, at *4, 6 (1st Cir. Apr. 21, 1998).

[315] *See, e.g.*, *Finn*, 211 B.R. at 784; *Silveira*, Memorandum & Order, at 7; *In re* Ryan, 210 B.R. 7, 12 (Bankr. D. Mass. 1997); Gonzalez v. First Nat'l Bank of Boston, 191 B.R. 2, 3–4 (Bankr. D. Mass. 1996) ("*Gonzalez II*").

[316] *See* 140 Cong. Rec. at 10,769.

[317] *See id.*

[318] *See id.*

[319] *See id.* at 10,769.

Despite this limited clarity, courts have continued to differ over whether to apply the full avoidance or entire lien avoidance approach.[320] Nevertheless, as recognized by the First Circuit, the full avoidance approach is the only approach which comports with the statutory language, the legislative history to the 1994 Amendments and the policy objectives behind the Code; therefore, it is the approach courts should follow when interpreting and applying § 522(f)(1).[321] Whereas the entire lien avoidance approach results in a windfall for debtors, the full avoidance approach strikes an appropriate balance between the interests of failed debtors and their creditors.[322]

A. *The Confusion Surrounding the 1994 Amendments to the Code*

The legislative history to the 1994 Amendments is confusing in many respects.[323] For example, Congress misinterpreted the holding in *Gonzalez*.[324] Congress stated that *Gonzalez* fit into the first fact pattern—no equity beyond the unavoidable encumbrances.[325] In *Gonzalez*, however, there was equity in the debtor's property in the amount of $23,100.[326] Moreover, Congress was purporting to overrule the not impair approach when it referred to *Gonzalez*.[327] The court in *Gonzalez*, however, applied the carve-out approach.[328] Thus, Congress cited a case to serve as an illustration for a position that it did not represent.[329]

Despite the confusion caused by such mischaracterizations, Congress did explain that the not impair and carve-out approaches were overruled.[330] Moreover, Congress expressed its broad interpretation of the Code's fresh-start policy and its related view that any post-bankruptcy appreciation should accrue for the benefit of the debtor.[331]

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[320] *See, e.g.*, *Finn*, 211 B.R. at 784–85; *Ryan*, 210 B.R. at 12–13; *see also Silveira*, Memorandum & Order, at 5.

[321] *See* 11 U.S.C. § 522(f) (1994); *Silveira*, 1998 WL 175119, at *4; 140 CONG. REC. at 10,769; *see also supra* notes 120–36, 255–87 and accompanying text.

[322] *See supra* notes 120–36, 255–313 and accompanying text.

[323] *See* 140 CONG. REC. at 10,769; *see also Silveira*, 1998 WL 175119, at *5 (noting that cases cited in legislative history do not fit examples discussed); *Finn*, 211 B.R. at 782 (same); *Ryan*, 210 B.R. at 9 ("[A]lthough the legislative history states that the amendment was intended to overrule these decisions, the hypothetical scenarios do not present the facts or the issues in the cases cited.").

[324] *See* 140 CONG. REC. at 10,769; *see also In re* Gonzalez, 149 B.R. 9, 12 (Bankr. D. Mass. 1993) ("*Gonzalez I*").

[325] *See* 140 CONG. REC. at 10,769.

[326] *See Gonzalez I*, 149 B.R. at 10.

[327] *See* 140 CONG. REC. at 10,769.

[328] *See Gonzalez I*, 149 B.R. at 10–12.

[329] *See* 140 CONG. REC. at 10,769; *see also Gonzalez I*, 149 B.R. at 10–12.

[330] *See* 140 CONG. REC. at 10,769.

[331] *See id.*

Thus, the legislative history does provide some guidelines for courts to consider when interpreting and applying § 522(f).[332]

B. *The Full Avoidance Approach: The Correct Approach*

The full avoidance approach is the only approach that garners support from the statutory language, the legislative history to the 1994 Amendments and the policy objectives behind the Code.[333] A strict reading of § 522(f)(2) provides support for the full avoidance approach.[334] Courts following this approach merely plug the appropriate numbers into the "simple arithmetic" formula and avoid that portion of the lien.[335] As Judge Federman wrote, "[t]he guiding purpose behind the revision is to leave the debtor with a total of mortgage debt, judicial liens26

and homestead exemptions equal to the value of the property at the time of the bankruptcy."[336]

At the same time, the full avoidance approach comports with Congress's intent, as propounded by the 1994 Amendments to the Code.[337] In the 1994 Amendments, Congress broadly interpreted the Code's fresh-start policy and explained that any post-bankruptcy appreciation should accrue for the benefit of the debtor.[338] Thus, the full avoidance approach furthers the Code's fresh-start policy by preserving the debtor's exempt property and allowing any post-bankruptcy appreciation to accrue for the benefit of the debtor.[339] Moreover, the full avoidance approach furthers the Code's other policy objective of helping to protect some of the rights of creditors by preserving the secured portion of their liens.[340] Thus, the full avoidance approach strikes a balance between the Code's fresh-start policy and its goal of protecting some of the rights of creditors.[341]

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[332] *See id.*

[333] *See* 11 U.S.C. § 522(f); 140 CONG. REC. at 10,769; *see also supra* notes 28–63 and accompanying text.

[334] *See* 11 U.S.C. § 522(f)(2)(1994); *see also Silveira*, 1998 WL 175119, at *2; *Finn*, 211 B.R. at 783–84; *Ryan*, 210 B.R. at 12–13.

[335] *See Silveira*, 1998 WL 175119, at *2; *Finn*, 211 B.R. at 783–84; *Ryan*, 210 B.R. at 12–13.

[336] *See* Judge Arthur B. Federman, *The Bankruptcy Reform Act of 1994*, 51 J. MO. BAR 105, 106 (Mar./Apr. 1995).

[337] *See* 140 CONG. REC. at 10,769.

[338] *See id.*

[339] *See, e.g., Finn*, 211 B.R. at 784; *Ryan*, 210 B.R. at 7.

[340] *See, e.g., Finn*, 211 B.R. at 784; *Ryan*, 210 B.R. at 7; *see also supra* notes 28–63 and accompanying text.

[341] *See supra* notes 28–63 and accompanying text.

C. *The Implicit Rejection of the Subordination Approach*

Adhering to a strict reading of the statutory language of § 522(f)(1), the word "avoid" can be interpreted to mean either to nullify or to subordinate.[342] Due to the statutory ambiguity, one must turn to the legislative history for clarification.[343] Although Congress did not expressly reject the subordination approach in the legislative history to the 1994 Amendments to the Code, it implicitly rejected this approach.[344] In the legislative history, Congress did express its view that post-bankruptcy appreciation should accrue for the benefit of the debtor in order to fulfill the Code's fresh-start policy.[345] In overruling both the not impair and carve-out approaches, Congress expressly stated its concern that under those approaches post-bankruptcy appreciation would go to the benefit of the creditor.[346] In particular, in overruling *Chabot*, Congress explained that a major flaw with the carve-out approach was that any equity created by mortgage payments would go to the benefit of the judicial lienholder.[347] Congress stated that the fresh-start policy was supposed to protect the debtor.[348] Thus, given Congress's broad interpretation of the fresh-start policy, the subordination approach—which leaves any post-bankruptcy appreciation to the creditor—is contrary to Congress's intent.[349]

Moreover, courts following the subordination approach apply faulty reasoning in their reliance on *Dewsnup v. Timm*.[350] Although *Dewsnup* reaffirmed the pre-Code rule that liens on real property generally survive bankruptcy, it qualified this position by explaining that such liens only survive when the Code does not provide otherwise.[351] Section 522(f), however, does provide otherwise.[352] Moreover, the Court in *Dewsnup* expressly stated that its holding was narrowly limited to the facts of that case.[353] In sum, the legislative history clearly

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[342] *See* 11 U.S.C. § 522(f)(1) (1994); *see, e.g.*, *Finn*, 211 B.R. at 784; *Ryan*, 210 B.R. at 12–13; Bellenoit v. Avco Leasing Serv., 157 B.R. 185, 188 (Bankr. D. Mass. 1992); *In re* D'Amelio, 142 B.R. 8, 10 (Bankr. D. Mass. 1992).

[343] *See generally* United States v. Ron Pair Enters., Inc., 489 U.S. 235, 242–46 (1989).

[344] *See* 140 CONG. REC. at 10,769.

[345] *See id.*

[346] *See id.*

[347] *See id.*

[348] *See id.*

[349] *See* 140 CONG. REC. at 10,769; *see also supra* 179–210 and accompanying text.

[350] Dewsnup v. Timm, 502 U.S. 413–19 (1992); *see Bellenoit*, 157 B.R. at 188; *D'Amelio*, 142 B.R. at 10.

[351] *See Dewsnup*, 502 U.S. at 419–20.

[352] *See* 11 U.S.C. § 522(f).

[353] *See Dewsnup*, 502 U.S. at 416–17.

illustrates that Congress intended the word "avoid" to mean nullify.[354] Thus, courts following the subordination approach inaccurately interpret and apply § 522(f)(1).[355]

D. *Flaws with the Entire Lien Avoidance Approach*

Courts following the entire lien avoidance approach likewise apply faulty reasoning.[356] The entire lien avoidance approach, the opposite extreme from the subordination approach, clearly does not result from a strict reading of the statutory language.[357] Courts following this approach ignore the phrase "to the extent" and act as though the phrase means "if."[358] Although the court in *Silveira* reasoned that a strict reading of the statutory language mandates the entire avoidance of a judicial lien that impairs an exemption to any extent, it offered no justification for such a reading.[359]

One might argue, however, that the legislative history does suggest that Congress intended entire lien avoidance.[360] In explaining the purpose of the addition of § 522(f)(2), the record states "[t]his amendment would provide a simple arithmetic test to determine *whether* a lien impairs an exemption . . . ."[361] Although the actual statutory language uses the phrase "to the extent," one may argue that the legislative history behind the provision suggests that the provision was merely intended to determine "whether" a lien impaired an exemption, not the extent of the impairment.[362]

On the other hand, the legislative history to the 1994 Amendments to the Code does not require the application of the entire lien avoidance approach.[363] Although courts following the entire lien avoidance approach explain that the legislative history supports such an approach, they cite passages where Congress referred to either the first or second fact pattern.[364] In the legislative history, Congress never addressed the third fact pattern—where equity remains beyond the

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[354] *See* 140 CONG. REC. at 10,769.

[355] *See Bellenoit*, 157 B.R. at 188; *D'Amelio*, 142 B.R. at 10.

[356] *See, e.g.*, *Silveira*, Memorandum & Order, at 5–7; *see also Finn*, 211 B.R. at 784–85 (DeJesus, J., dissenting).

[357] *See supra* notes 288–313 and accompanying text.

[358] *See In re* Corson, 206 B.R. 17, 22 (Bankr. D. Conn. 1997).

[359] *See Silveira*, Memorandum & Order, at 5–6.

[360] *See* 140 CONG. REC. at 10,769.

[361] *Id.* (emphasis added).

[362] *See id.*; *see also* 11 U.S.C. § 522(f)(2).

[363] *See* 140 CONG. REC. at 10,769.

[364] *See id.*; *see also Silveira*, Memorandum & Order, at 6.

unavoidable encumbrance and exemption.[365] Thus, the legislative history offers little guidance for determining whether Congress intended full or entire lien avoidance.[366] Nevertheless, because the statutory language is clear, one should not even consider the legislative history with respect to this issue.[367]

In addition to being contrary to the plain statutory language, the entire lien avoidance approach is inconsistent with the policy objectives behind the Code.[368] Although under the entire lien avoidance approach post-bankruptcy appreciation goes to the benefit of the debtor, this approach goes too far.[369] The entire lien avoidance approach fails to consider the Code's other policy objective of helping to protect the rights of creditors.[370] Thus, the entire lien avoidance approach results in a windfall to debtors, giving them a "head start," rather than a "fresh-start."[371]

Moreover, the entire lien avoidance approach has the potential of producing arbitrary results and makes a judicial determination of the value of the property extremely critical.[372] For example, if there is a $40,000 judicial lien and the court determines that the value of the property is such that there remains $40,000 in equity beyond the unavoidable encumbrances and the exemption, then the entire lien would survive bankruptcy. On the other hand, if the court determines that the value of the property is such that there remains $39,999 in equity beyond the unavoidable encumbrances and the exemption, then the entire lien would be avoided.

In addition, support for the entire lien avoidance approach is wrongly garnered from *Dewsnup*.[373] Although the United States Supreme Court prohibited lienstripping in *Dewsnup*, the Court expressly narrowed its holding to the facts of that case.[374] Also, the Court was dealing with § 506(d), as well as with a deed of trust, a type of lien that assumes a higher priority position than a judicial lien.[375]

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[365] *See* 140 CONG. REC. at 10,769.

[366] *See id.*

[367] *See Ron Pair*, 489 U.S. at 242–45.

[368] *See supra* notes 27–62 and accompanying text.

[369] *See supra* notes 277–302 and accompanying text.

[370] *See supra* notes 36–62 and accompanying text.

[371] *In re* Chabot, 100 B.R. 18, 22 (Bankr. C.D. Cal. 1989) (citing Polk County Fed. Sav. & Loan Ass'n of Des Moines v. Weathers (*In re* Weathers), 15 B.R. 945, 951 (Bankr. D. Kan. 1981)).

[372] *See Silveira*, 1998 WL 175119, at *3 n.3.

[373] 11 U.S.C. §§ 502(d), 506(d), 522(f)(1) (1994); *see Dewsnup*, 502 U.S. at 410.

[374] *See Dewsnup*, 502 U.S. at 410.

[375] *See id.*

Conclusion

In sum, the strict statutory language of § 522(f)(1), the legislative history to the 1994 Amendments to the Code and the policy objectives behind the Code mandate the application of the full avoidance approach. This approach strikes an appropriate balance between relieving failed debtors of some of the hardships resulting from overwhelming debt obligations and protecting the rights of unfortunate creditors. In addition, the adoption of the full avoidance approach will help provide the clarity and predictability that debtors, creditors and their attorneys need in order to plan their future relationships.

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