

WHEN IS BANKRUPTCY THE RIGHT OPTION FOR YOUR ELDERLY CLIENTS?

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What is Bankruptcy?

A process designed to help individuals and businesses get protection from their creditors

- Right to file for bankruptcy is provided by federal law
- All bankruptcy cases are handled in federal bankruptcy court



What Are the Different Types of Bankruptcy Cases?

There are four types of bankruptcy cases individuals can file:

- *Chapter 7*, known as “straight” bankruptcy or “liquidation”
 - Requires individuals to give up property which is not “exempt”, so property can be sold to pay creditors
 - But most consumers who file chapter 7 keep all of their property except:
 - property which is very valuable, or
 - property subject to a lien which they cannot avoid or afford to pay

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- *Chapter 13* is a type of “reorganization” used by individuals
 - Consumer submits plan to pay all or portion of debts over a period of years using current income
 - Homeowner with mortgage default given time to get caught up, generally over longer period than under workout agreement
 - Unsecured debts (such as credit cards) may be paid either in full or a percentage of amount owed, over a 3 to 5 year period
 - Late charges and interest after chapter 13 filed do not have to be paid on unsecured debts

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- *Chapter 11*, known as “reorganization,” is used by businesses and a few individuals whose debts are very large
 - *Chapter 12* is for family farmers and fishermen
 - Most consumers file under either chapter 7 or chapter 13
 - Either type of case may be filed individually or by a married couple filing jointly



Unsecured and Secured Debts

□ **Secured Debts**

- The debtor has agreed to give a creditor rights in certain property as collateral to secure payment of a debt
- Most common are home mortgages and auto purchase loans
- Creditor can take property if borrower defaults on payment
- Liens created by a court judgment or statute (tax lien) can also create a secured claim.



Unsecured and Secured Debts

□ Unsecured debts

A debt not secured by an agreement that makes specific property collateral for payment of a debt

Credit card debt, medical bills are common examples

A court judgment can turn an unsecured debt into a lien on certain property, such as a home



What Can Bankruptcy Do

- ❑ Discharge of most debts and opportunity for fresh start
- ❑ Automatic stay of most creditor actions (including repossessions, garnishments, foreclosures, utility shut-offs and evictions)
- ❑ Lien avoidance or modification of certain secured debts
- ❑ Right to cure defaults
- ❑ Opportunity to repay some or all debts with affordable payments
- ❑ Opportunity to assert claims and defenses to creditor claims



What Bankruptcy Can Not Do

Bankruptcy does not cure every financial problem
Nor is it right step for every individual in financial
trouble

In bankruptcy, it is usually *not* possible to:

- ❑ Eliminate certain rights of “secured” creditors
- ❑ Discharge some types of debts, such as child support, most student loans, criminal fines, and most taxes
- ❑ Protect cosigners on debts (except in chapter 13 cases)
- ❑ Discharge debts that arise after bankruptcy is filed



Disadvantages of Bankruptcy

- ❑ Possible loss of nonexempt property
- ❑ Possible loss of secured collateral
- ❑ Impact on credit rating
- ❑ Concern over stigma and moral obligation to pay debts
- ❑ Concern about possible discrimination based on bankruptcy filing



Bankruptcy Opportunists

- Debt counselors who perform no services
- “Bankruptcy Petition Preparers”
- Others who encourage unnecessary or inappropriate bankruptcy filings



What Must Be Done Before Filing Bankruptcy?

Credit Counseling:

- ❑ Consumer must receive budget and credit counseling “briefing” from an approved agency **within 180 days *before*** bankruptcy case is filed
- ❑ Agencies are approved by the United States Trustee Program
- ❑ Briefing may be provided by in-person, telephone or Internet, and in individual or group session
- ❑ Consumers should be advised to complete counseling as soon as they think bankruptcy may be an option.



What are the First Steps in Filing a Bankruptcy?

- ❑ The first step involves completing some basic forms, including a three-page initial “petition”
- ❑ A number of other forms requiring disclosure of the consumer’s financial affairs must also be filed with the petition or shortly afterwards (usually within 15 days)
- ❑ It is important that all forms be filled out completely and accurately
- ❑ Bankruptcy is a legal proceeding with complicated rules and paperwork – it is difficult to complete without an attorney



Filing an Emergency Bankruptcy

- Voluntary Petition (Official Form 1)
- Counseling certificate or waiver request
- Mailing matrix listing names and addresses
for all creditors
- If filing fee not paid in full, application to pay
fee in installments or for fee waiver in
chapter 7



What Does It Cost to File Bankruptcy?

- Chapter 7 filing fee now \$299 and \$274 for chapter 13
- Approx. \$50 for credit counseling briefing and \$50 for education course
- Attorney fees have gone up since 2005
- New pressures on *pro bono* programs



What Will Happen After Filing?

- In most chapter 7 cases, consumer only has to go to a proceeding called the **“meeting of creditors”**
- The meeting of creditors gives the bankruptcy trustee and any creditor who chooses to attend a chance to ask questions about consumer’s financial affairs
- Few creditors attend in consumer cases



A KEY BANKRUPTCY CONCEPT

Automatic Stay:

Filing bankruptcy instantly creates an “automatic stay”

- ❑ Temporarily stops most all creditor actions to collect debts
- ❑ Actions stayed include starting or continuing a legal proceeding, dunning calls and letters
- ❑ Stops foreclosure sales, repossessions, wage garnishment, utility shutoffs,
- ❑ Creditor liable for damages/sanctions if violates stay



Limited Exceptions to Stay

- ❑ **Most Common Examples:**
- ❑ Criminal actions and proceedings
- ❑ Enforcement of domestic support obligations
- ❑ Enforcement of police or regulatory powers
- ❑ Limits on automatic stay for repeat filers (one or more case dismissed in prior year)



Question No. 1

- Which of the following acts related to pre-bankruptcy debt would *not* violate the automatic stay:
 - Lender enters default judgment against debtor in state court foreclosure case
 - Creditor holds up a sign in front of debtor's home, saying, "A deadbeat lives here."
 - Debtor sues mortgage servicer for violating debt collection statute
 - Mortgage servicer accidentally allows computer generated dunning letters to be sent to debtor



Answer to Question 1

- (C)The Debtor may sue a mortgage servicer for violating a debt collection statute. The automatic stay only applies to bar actions by the creditor.



Questions?



Why Exemptions Are Important

- The Bankruptcy Estate (all debtor's interest in wide range of property)
- Property Exempted from the Estate
 - Two Exemption Schemes
 - Federal
 - State (and federal non-bankruptcy law)
 - Generally, debtor may choose scheme unless state has “opted out” of the federal exemptions



Federal exemptions

- ❑ Homestead: \$20,200
- ❑ Motor Vehicle: \$3,225
- ❑ Household Goods and Furnishings: \$10,775
- ❑ “Wildcard” exemption: \$10,125 up to unused portion of homestead
- ❑ Most government benefits



State Exemptions (Connecticut)

- ❑ Homestead: \$75,000
- ❑ Motor Vehicle: \$1,500
- ❑ Household Goods and Furnishings: necessary food, furniture, bedding , and appliances
- ❑ “Wildcard” exemption: \$1000 in any property
- ❑ Most government benefits



Question No. 2

- Homeowner's residence is subject to first mortgage with \$120,000 current loan balance, second mortgage with \$35,000 balance. Fair market value of property is \$175,000. Applicable state homestead exemption applies: \$20,000.
- Will homeowner face an exemption problem in Chapter 7 bankruptcy?

- Yes

- No



Another Key Bankruptcy Concept

Fresh Start:

Goal of bankruptcy to provide help with existing debts and give consumer a second chance financially

Two key elements to bankruptcy fresh start:

- **Discharge:** Elimination of the legal obligation to pay a debt
- **Exemptions:** Property which the law allows a bankruptcy debtor to keep



Nondischargeable Debts

Common debts *not* dischargeable in Chapter 7 and Chapter 13

- Certain taxes
- Unlisted debts
- Most debts for domestic support obligations
- Most fines and penalties owed to govt.
- Most student loans



Other Nondischargeable Debts

- Debts that *may* not be dischargeable in chapter 7
 - Debts incurred by fraud – 523(a)(2)
 - Debts incurred through fraud as fiduciary, embezzlement, larceny
 - Willful and malicious injury to person or property (but property injury debt may be dischargeable in chapter 13)



Nondischargeable Debts in Chapter 13

- Dischargeable in Chapter 13 but not in Chapter 7
 - Property settlement from divorce
 - Willful or malicious injury to *property*.



Reaffirmation Basics

- *Made* before discharge
- Required disclosures given
- Filed with the Court
- Accompanied by Attorney Declaration
- Not rescinded by later of discharge or 60 days after filing
- Unrepresented debtor must attend hearing and receive warnings and court approval of agreement (exception for real property)



Question No. 3

- Homeowner in default on mortgage gets chapter 7 bankruptcy discharge. Which of the following is true:
 - Debtor gets to keep home, discharge wipes out the mortgage
 - Debtor gets to keep home subject to mortgage, discharge wipes out any arrearage
 - Discharge wipes out unpaid interest only
 - Discharge wipes out obligation to pay any deficiency left after foreclosure



Answer to Question 3

- (d) The chapter 7 discharge wipes out the former homeowner's obligation to pay for any deficiency left after sale. The chapter 7 discharge does not affect the mortgage lien on the property.



Questions?



What About Homes, Cars and Other Secured Property?

Bankruptcy usually does not eliminate a creditor's lien or security interest on property

Despite chapter 7 filing, secured creditor may be able to foreclose on a home or other property, usually after the bankruptcy case.

Chapter 13 has more options for dealing with secured creditors

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Four Ways to Deal With a Secured Claim in Chapter 13

- ❑ Cure a pre-bankruptcy payment default (e.g, pay the mortgage arrearage over time) while the stay and a repayment plan are in effect
- ❑ Remove or reduce a lien
- ❑ Pay a lien in full over time, modify terms
- ❑ Do nothing about the lien



Chapter 13 Basics

- ❑ Must file a Chapter 13 plan: describe treatment of secured, unsecured, “priority” debts
- ❑ Length of Plan: 3 to 5 years
- ❑ Role of chapter 13 trustee
- ❑ Court must review and “confirm” the plan
- ❑ “Feasability” determination made by judge



Who Can File Chapter 13?

A Person With “Regular Income”

- “Individual whose income is sufficiently stable and regular to enable such individual to make payments under a plan under chapter 13.” 11 U.S.C. § 101(30)
- Social Security, public benefits, child support income generally ok.
- Debt limitations \$1,010,650 secured; \$336,900 unsecured.



Curing a pre-bankruptcy mortgage default in chapter 13

- mortgage arrearage, including reasonable pre-petition foreclosure costs, can be cured within “reasonable time”
- plan shall also provide for “maintenance of payments” while case pending



Curing Mortgage Arrears

What Must Be Paid?

- Attorney's fees and interest on arrears
- “if it is proposed in a plan to cure a default, the amount necessary to cure the default shall be determined in accordance with the underlying agreement and applicable nonbankruptcy law.” 11 U.S.C. § 1322(e).



When is it too late to file?

- General federal rule: “ a default with respect to . . . a lien on the debtor’s principal residence may be cured . . . until such residence is sold at a foreclosure sale that is conducted in accordance with applicable nonbankruptcy law.” 11 U.S.C. § 1322(c)(1).



Modification of Mortgage in Chapter 13

- General rule: Bankruptcy Code permits modification of secured claims in chapter 13

“Modification” can include changing terms of obligation, including interest rate, repayment period, reduce debt to value of collateral

- Exception: debtor can modify claims “other than a claim secured *only* by a security interest in *real property* that is the *debtor’s principal residence*” 11 U.S.C. § 1322(b)(2)

Mobile Homes

- Loans on mobile homes that are considered personal property under state law are not subject to the anti-modification provision



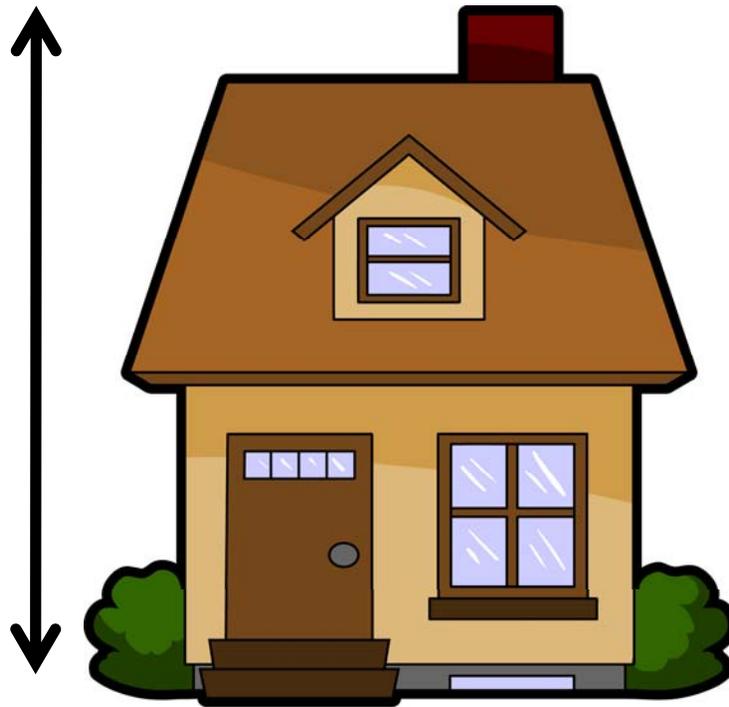
Multi-family Buildings

- Modification permitted when other real property, such as rental units, is part of security interest

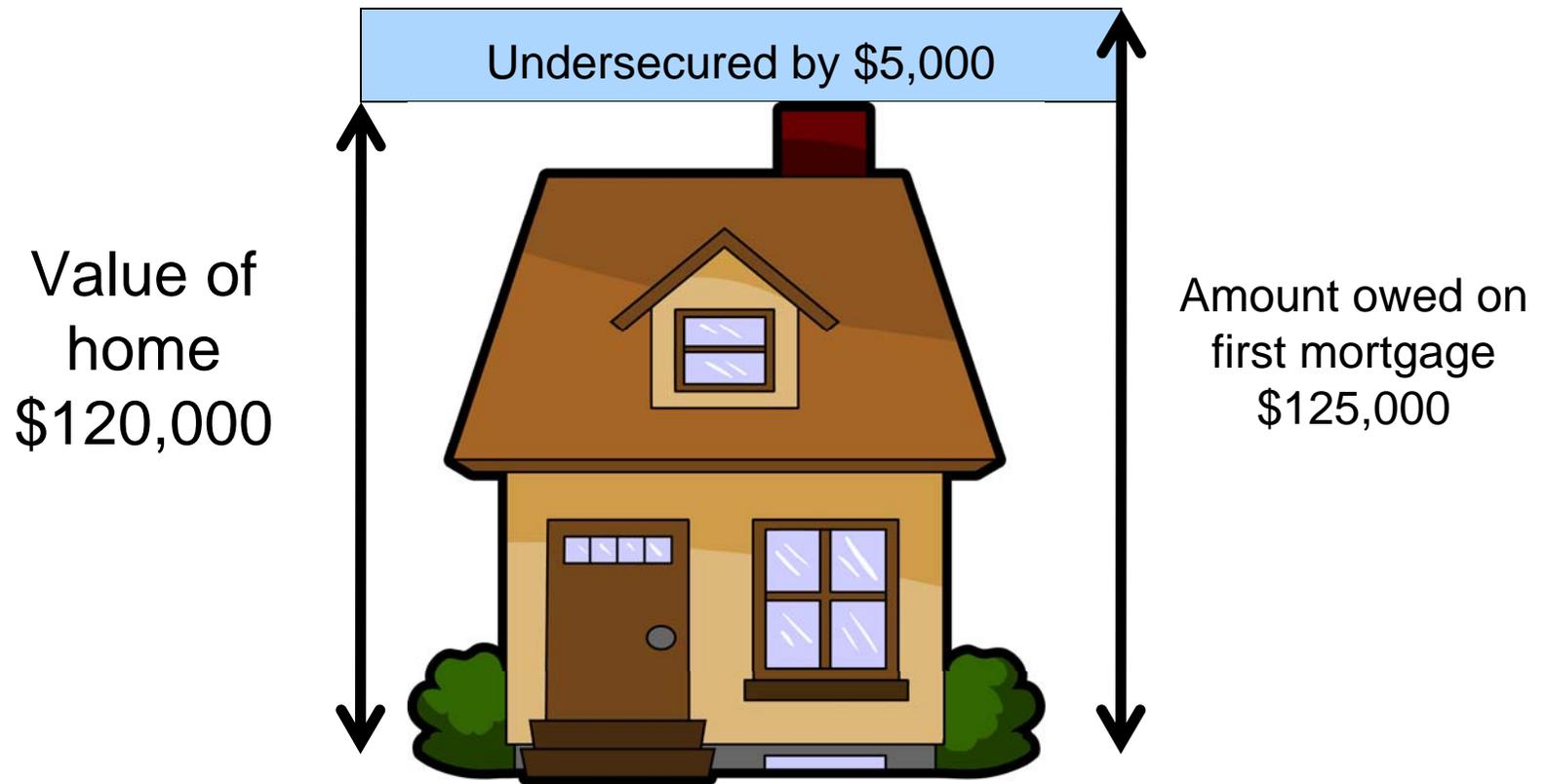


Underwater Mortgages

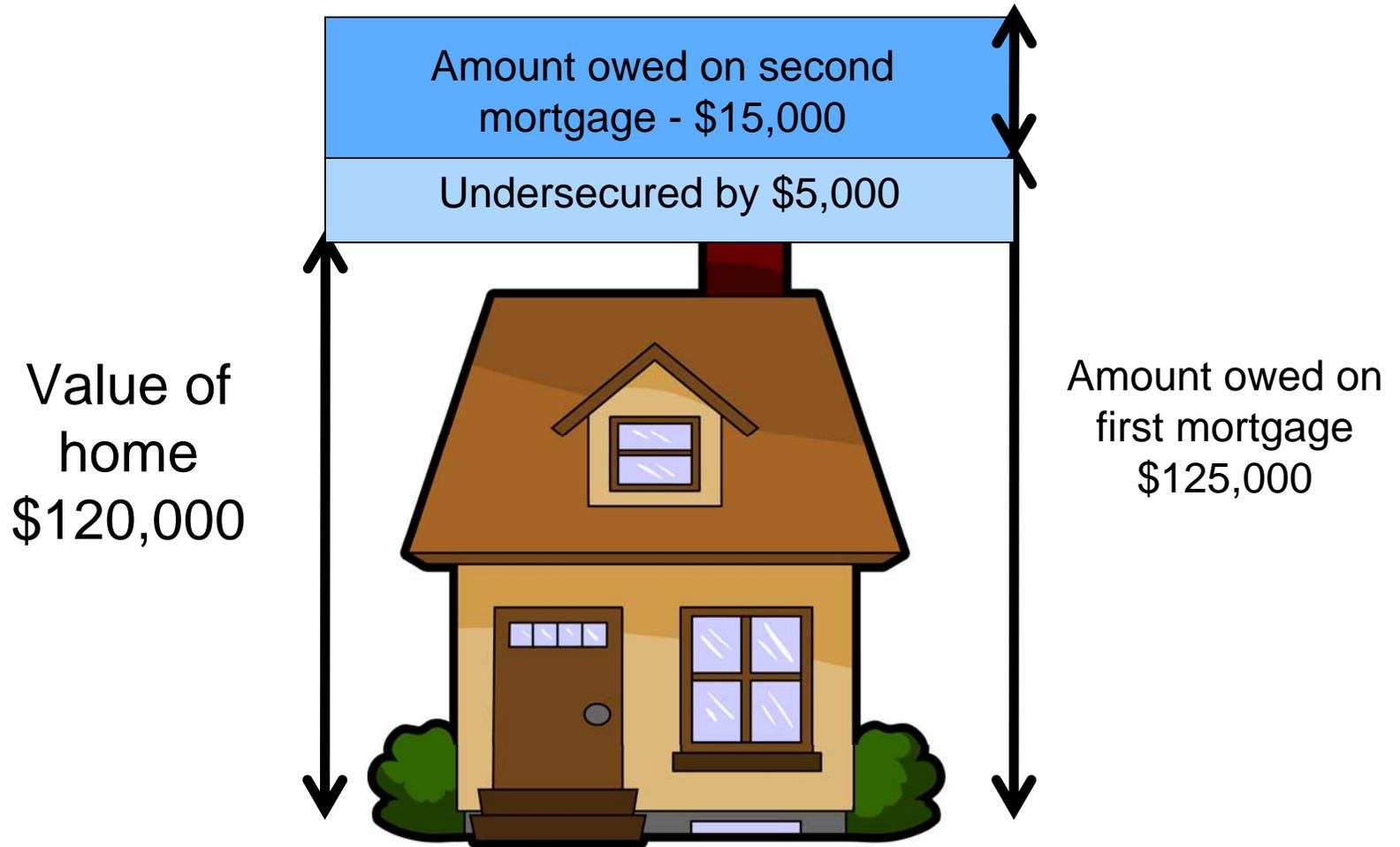
Value of
home
\$120,000



Underwater Mortgages



Underwater Mortgage





Modification

Anti-modification does not apply to loans with short remaining terms

- Final payment due during life of Ch.13 plan
- Loan may be modified - § 1322(c)(2)



Lien Avoidance

- ❑ Judgment liens are imposed on property without consent or agreement of owner
- ❑ A bankruptcy debtor can often avoid a judgment lien against property.
- ❑ Needs a simple motion filing
- ❑ Can do this in Chapter 13 and Chapter 7



Dismissal or conversion of chapter 13 case

- ❑ A chapter 13 case is completely voluntary
- ❑ Possible to convert case to chapter 7, receive chapter 7 discharge
- ❑ Dismissal (voluntary or involuntary) restores pre bankruptcy foreclosure status



When chapter 13 is most helpful

- ❑ Curing default in mortgage
- ❑ Modifying mobile home loan payments
- ❑ Removing junior liens on underwater properties
- ❑ Bringing legal claims against a creditor
- ❑ Eliminating unsecured debts so consumer can focus on mortgage



Bankruptcy and Loan Modification Programs

- HMP (federal/Treasury) loan mod program
 - Borrowers in bankruptcy are not automatically eliminated from consideration

- FHA insured loans
 - HUD Mortgagee Letter 2008-32 (10/17/2008)

 - Other lender modification programs



Does Bankruptcy Affect the Consumer's Credit?

- Bankruptcy can stay on consumer's credit report for **ten years**, rather than normal seven years for other credit information
- Bankruptcy usually does not make credit record any worse, if there have already been numerous reports of defaults

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- ❑ Some creditors will lend to recent bankruptcy filers since they know all or most of consumer's past debts have been discharged and consumer can not get a discharge in another chapter 7 case for a period of **eight years**
 - ❑ Bankruptcy may be problem in getting approved for conventional home mortgage
 - ❑ But most lenders will still provide mortgage if consumer has reestablished good credit for period of **two to four years** after discharge



Question No. 4

- Homeowner in default files chapter 13 case, cures mortgage default under terms of plan and gets chapter 13 discharge. Which of the following is true:
 - The mortgage is wiped out
 - The homeowner will be liable for a deficiency if foreclosed in the future
 - The mortgage is reinstated under original terms as if no default had ever occurred
 - The lender can now foreclose based on the pre-bankruptcy default



Answer to Question 4

- (c) The mortgage is reinstated to the pre-default status quo. The debtor may pay off the mortgage debt according to the note and mortgage's original terms.



New Requirements Under 2005 Amendments

- ❑ Credit/debtor education counseling (before and after filing)
- ❑ Means testing and safe harbor
- ❑ New documentation requirements (pay stubs, tax returns)
- ❑ New limits on repeat filers



Means Testing

- ❑ Consumer with income above median must fill out form that compares monthly income with actual and assumed expenses in variety of categories
- ❑ Some expenses are based on IRS collection guidelines
- ❑ If form shows that consumer should have certain amount left over to pay unsecured creditors, bankruptcy court may decide consumer can not file chapter 7 case, unless there are “special circumstances”



What is Current Monthly Income?

- Monthly average of all income (whether or not taxable) received by debtor during 6 month period ending on last day of calendar month before bankruptcy filed - § 101(10A)
- Does not include payments under Social Security Act.



Safe Harbor From Means Test Is Debtor Below Median?

- Below median income debtors are not subject to the Means Test
- Annualize debtor's current monthly income
 - Multiply CMI by 12.
- Compare to “median family income” for debtor's state based on debtor's “household” size.



Median Income Figures: New York State Example

- Eligibility for Safe Harbor For Cases Filed as of 3/15/2009:
 - One Earner: \$ 46,523
 - Two People: \$ 57,006
 - Four People: \$ 83,036