

What Every Board Member and Community Association Manager Should Know about Bankruptcy in These Incredibly Difficult Financial Times

This article was adapted by David Swedelson and Alyssa Klausner of Swedelson & Gottlieb from an article entitled "What Every Lawyer Should Know about Bankruptcy after 2005 and in These Incredibly Difficult Financial Times" *By Catherine E. Bauer, Assistant United States Attorney, Los Angeles. Published in the Los Angeles County Bar Update Newsletter, November 2008 Edition*

1. Bankruptcy still exists. Everyone and his or her brother seem to have recently stumbled upon a truth that bankruptcy lawyers have known since 2005: Bankruptcy did not go away with enactment of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. BAPCPA did create a "means test" for filing Chapter 7 (the bankruptcy procedure that discharges the delinquent owner's debts and obligations that predated the bankruptcy filing and is contrasted from a Chapter 11 or 13 filing which reorganizes the debts that are still paid over time), and it did make some fairly major changes to bankruptcy law, but debt relief is still available to most individuals and entities who are experiencing financial woes. This means that owners can still and often do file for Chapter 7 Bankruptcy or are forced by the Court into a Chapter 7 because they have no income or assets sufficient to reorganize their debts. The reality is that if the owner is in Chapter 7, and there is no equity in the property, then it is unlikely that the association will recover the delinquent assessments, and sometimes, that delinquent owner will be able to keep the home.

2. Bankruptcy won't modify a home mortgage. We are living in very strange and dire economic times. The fact is that many owners cannot afford to pay their loan payments and the assessment fees levied by their associations. Possible solutions for dealing with the subprime mortgage mess have included changing bankruptcy law to allow bankruptcy judges the ability to alter home mortgages. But, as of this writing, it is still the case that bankruptcy judges cannot modify the terms of home mortgages. However, if they can make a deal with the lender and pay their loan but are having trouble with their assessment payments, a community association can discount the balance owed as a last resort before foreclosure. A wage earning owner (someone with regular income) can file a Chapter 13 bankruptcy and pay past due payments over time through a plan (while continuing to make their regular monthly payments). Unfortunately, a Chapter 13 bankruptcy is not a realistic option for those owners with subprime mortgages since typically the problem is that their loan payments have increased and they can't afford to make the loan payments.

3. The automatic stay is now only semi-automatic. A stay is a hold on debt collection action against an owner who has filed bankruptcy. BAPCPA changed the automatic stay into a semi-automatic stay. A debtor gets one old-fashioned automatic stay to stop a foreclosure, but the good news is that multiple bankruptcy cases do not lead to multiple automatic stays. This eliminates the problem of owners filing multiple bankruptcies to avoid rescheduled foreclosure sales.

4. Financial education is now a mandatory part of bankruptcy. BAPCPA added a requirement that owners that have filed bankruptcy (called debtors) are required to attend a personal financial management course to receive a discharge of debts. (This is in addition to the credit counseling course that must be completed to file bankruptcy in the first place.) The financial management class must be taught by one of the organizations approved by the Office of the United States Trustee. If a certificate of attendance at a financial management course is not filed before the bankruptcy case is closed, the debtor does not receive a discharge. While it is possible to reopen a case to file the necessary certificate, this requires payment of a hefty fee.

Without a discharge, a debtor/owner remains personally liable for debts as if a bankruptcy had not been filed.

5. Get friendly with a lawyer that knows bankruptcy. Bankruptcy filings are way up. In the Central District of California, filings for 2009 exceeded the historical average of 61,000 per year by many thousands. Unfortunately, Southern California is, by far, the district with the most bankruptcy filings in the nation. At Swedelson & Gottlieb, we are prepared to assist those associations that have owners in bankruptcy by filing the appropriate claim forms, making motions for relief from the stay (so that the association can foreclose) and/or monitoring the bankruptcy and advising the board and management as to their options.