

Where In The Bankruptcy Code Does It Say . . .



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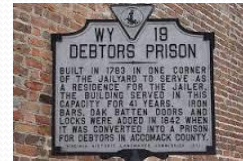
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Summary

- Cure “Arrearages” & Maintain Payments
- Pay “Outside the Plan”
- “Cramdown”
- “Strip Off” a Lien
- Pay Interest on Secured Claims
- No Interest on Arrearages?
- Plan “Feasibility”
- “Liquidation” Test
- Recovering a Repossessed Vehicle
- Dischargeability of Property Settlement Agreements/DSO’s

See accompanying written materials (“handouts”) for this webinar, available for download.



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“Arrearages” can be cured and regular mortgage payments can resume

- §§ 1322(b)(5) and (c)(1)
- Section 1322(b)(5) states that a plan may provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any secured claim on which the last payment is due after the date on which the final payment under the plan is due.

See Handouts, p. 3



What it means to pay a claim “outside the plan”

- “Outside the plan” is a misnomer; plan must provide for claims. More appropriately described as direct payments by debtor to creditor.
- 1322(b)(2) – plan may leave the rights of creditors unaffected (such as by paying a debt pursuant to the contractual terms).
- 1325(b)(5) – plan may provide for the maintenance of payments on any secured or unsecured claim that doesn’t mature until after the last plan payment is due. Examples:
 - Home mortgages
 - Student loans
- 1326(c) – unless the plan provides otherwise, the trustee shall make payments to creditors under the plan.
- It is within the bankruptcy court’s discretion whether to allow the debtor to make payments directly to creditors rather than having the trustee make the disbursements.

See Handouts, p. 5

A plan may “cram down” a secured claim to the value of the collateral

- 1322(b)(2) – plan may modify the rights of holders of secured claims . . .
- 1325(a)(5) – “with respect to each allowed secured claim provided for by the plan . . .”
- 506(a)(1) – an “allowed secured claim” is secured only to the extent of the value of the collateral; the remaining balance of the claim is unsecured.
- 506(a)(2) – value is “replacement value.”
- No “cram down”:
 - If the claim is “secured only by a security interest in real property that is the debtor’s principal residence” (1322(b)(2)); or
 - If the creditor has a purchase money security interest, the debt was incurred within 910 days prepetition, and the collateral is a motor vehicle acquired for the personal use of the debtor; or the collateral is “any other thing of value” and the debt was incurred within 1 year prepetition. (Unnumbered paragraph after 1325(a)(9)).

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Debtors can “strip off” a second lien and treat it as unsecured



- §§ 506 and 1322(b)(2)
- Strip or Cram Down v. Strip Off
- The Supreme Court in *Nobelman v. Am. Sav. Bank*, 508 U.S. 324 (1993), interpreted § 1322(b)(2) as precluding a “strip down” of a partially secured lien against a principal residence in Chapter 13.
- A number of circuit courts of appeal and bankruptcy appellate panels have weighed in since *Nobelman* and every circuit court that has addressed the issue has held that § 1322(b)(2)’s anti-modification provisions do not bar a Chapter 13 debtor from stripping off wholly unsecured liens on the debtor’s principal residence.

See Handouts, p. 10

Interest must be paid on secured claims

- § 1325(a)(5)(b)(ii)
- Creditor is entitled to an interest rate on the value of the allowed secured claim
- Equivalent to calculating the future value of a bank deposit or annuity with the amount of the allowed secured claim that is earning the annual interest rate compounded annually.
- The higher the interest rate, the more the debtor has to pay to the creditor.
- Courts have used various methods of determining what the interest rate should be, including: (1) formula; (2) coerced loan; (3) presumptive contract rate; and (4) and cost of funds.



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Whether interest must be paid on arrearage claims

- 1322(e) – the amount necessary to cure the default is determined by –
 - Underlying contract, AND
 - Applicable nonbankruptcy law.
- Interest must be paid on arrearages only if authorized by both the note/mortgage and state law.
- Interest might be required on components of an arrearage claim such as fees and costs, depending on the loan agreement and state law.



See Handouts, p. 14



Plan must be “feasible”

- 1325(a)(6) – debtor must be able to make payments under the plan and comply with the plan.
- Whether debtor can afford payments sometimes implicates eligibility under section 109(e) – only an “individual with regular income” (defined in 101(30)) may be a chapter 13 debtor.
- A corollary to 1325(a)(6) is that the plan must be adequately funded to pay, within a maximum of 5 years (1322(d)):
 - Priority claims in full (1322(a)(2));
 - Secured claims (other than long-term debts) (1325(a)(5)); and
 - General unsecured claims as necessary to satisfy:
 - liquidation test (1325(a)(4)); or
 - disposable income test (1325(b)).

See Handouts, p. 17

Plan must meet a “liquidation test”

- § 1325(a)(4)
- “Best interest of creditors test” or “liquidation test”
- Unsecured creditors must receive at least the present value of what they would have received under a Chapter 7 liquidation.
- Requires calculation



See Handouts, p. 19

Debtors may recover a car that was repossessed prepetition . . .

- § 541 – Property of the estate:
 - All legal or equitable interests of the debtor.
 - Property rights are determined by state law.
- Debtor can seek return of repossessed car:
 - only if debtor still has some interest (e.g., right of redemption) under state law that becomes property of the estate;
 - not if ownership interest in the car has been transferred to the creditor prepetition under state law.
- § 542(a) – An entity in possession of property the trustee can use under § 363 must deliver the property to the trustee.
- However, per § 1303, the debtor has, exclusive of the trustee, the right to use property under § 363.
- Also, per § 1306(b), the debtor remains in possession of property of the estate (unless the plan provides otherwise). (cont'd)

See Handouts, p. 20

... and creditor's failure to turn over car to debtor violates the automatic stay

- Therefore, reading §§ 542, 363, and 1303 together, debtor is entitled to possession.
- § 362(a)(3) – prohibits a creditor from exercising control over property of the estate.
- In most jurisdictions, creditor must turn over the car to the debtor upon request, then may seek adequate protection per § 363(e) (such as proof of insurance) or request termination of the automatic stay.
- Retaining possession of car = exercising control over property of the estate
- Failure to turn over car upon request can give rise to damages for violation of the automatic stay.

See Handouts, p. 20



Debtors can discharge divorce-related property settlement claims



- § 523(a) and § 1328(a)(2)
- Domestic support obligations (“DSO”) include alimony (spousal support), maintenance, and child support.
- Debts from a division of assets from a property settlement agreement are not a DSO.
- To be classified as a DSO, the debt must be for actual support or maintenance, meaning that courts will look beyond the label the parties have given to a particular debt and consider various factors under state law: (1) the agreement's language; (2) the parties' financial positions when the agreement was made; (3) the amount of the division; (4) whether the obligation ends upon death or remarriage of the beneficiary; (5) the frequency and number of payments; (6) whether the agreement waives other support rights; (7) whether the obligation can be modified or enforced in state court; and finally (8) how the obligation is treated for tax purposes.

(cont'd)

See Handouts, p. 24

Debtors can discharge divorce-related property settlement claims



- 523(a)(5) makes DSO debts nondischargeable.
- 523(a)(15) makes property settlement debts nondischargeable.
- But 523(a) only applies to discharges under certain specific code sections; it does not apply to 1328(a) discharges.
- A discharge under 1328(a) (when debtor completes plan payments) only excepts 523(a)(5) DSO debts from discharge.
- 523(a)(15) property settlement claims can be discharged under 1328(a).
- If the debtor gets a “hardship discharge” under 1328(b), both 523(a)(5) DSO claims and 523(a)(15) property settlement claims are nondischargeable.

See Handouts, p. 24

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