

When Bankruptcy Beckons

**Hang on to
your fee
by knowing
the rules**

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In the midst of a divorce proceeding, it is not unusual for one or both spouses to file for bankruptcy. When your client's spouse files for bankruptcy, the clock begins to run on your client's rights. Protecting those rights not only helps your client but protects your fee as well. To safeguard these rights, you first need to understand how bankruptcy works.

The automatic stay

A bankruptcy filing creates an injunction against creditors known as the automatic stay. In general, the automatic stay enjoins creditors from commencing or continuing litigation, enforcing judgments, obtaining possession of a debtor's property (e.g., foreclosure or repossession), perfecting or enforcing liens, collecting claims, and setting off debts.

Although broad in scope, the automatic stay has certain important family law exceptions. It does not stay the commencement or continuation of an action or proceeding for the establishment of paternity or the establishment or modification of alimony, maintenance, or support. Thus, a spouse's bankruptcy filing does not bar judicial proceedings to determine the amount of alimony, maintenance, or support a spouse in bankruptcy should pay.

Whether the collection of alimony, maintenance, or support is stayed is not always clear. The automatic stay does not prohibit the collection of alimony, maintenance, or support

from property that is not property of the estate. The tricky part is determining what constitutes "property of the estate." One entire section of the bankruptcy code (11 U.S.C. § 541) is devoted to defining this term. The definition can depend on the chapter under which a bankruptcy is filed. For example, wages earned after the bankruptcy filing are property of the estate in chapter 13, but not in chapters 7 or 11. If you incorrectly assess what constitutes property of the estate and consequently violate the automatic stay, you can be sanctioned. The bankruptcy court has authority to impose punitive damages for willful violations of the automatic stay.

It is good practice to file a motion seeking relief from the automatic stay before attempting to collect alimony, maintenance, or support so that you are not subsequently accused or found to have willfully violated the automatic stay. For the same reason, it is also a good idea to seek relief from the automatic stay to continue with any state court domestic relations proceeding or any appeals. The motion should describe the steps you intend to take to collect alimony, maintenance, or support, and the assets you intend to attach to enforce these claims. The bankruptcy code guarantees a hearing within 30 days of filing a motion for relief from stay, so you will lose little time in filing the motion.

In filing for bankruptcy, the goal of any debtor is to be discharged (or legally absolved) of debts. Debts for alimony, maintenance, or support cannot be discharged in bankruptcy. Debts incurred in the course of a divorce or separation proceeding that are not in the nature of alimony, maintenance, or support (e.g., monetary award, property settlement) can be discharged unless a complaint to determine the dischargeability of the debt is timely filed; the debtor does not have the ability to pay the debt; and the discharge of the debt would result in a benefit to the debtor that is not outweighed by the detrimental consequences to the spouse, dependent, or child of the debtor. 11 U.S.C. § 523(a)(15).

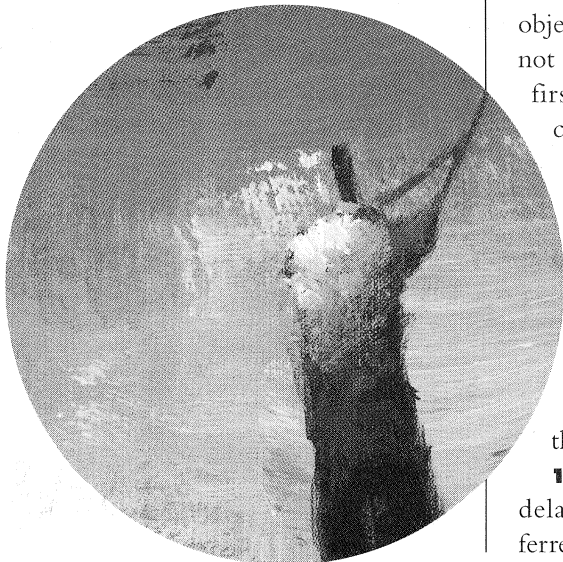
It is not always clear in a domestic relations case whether a debt, such as an award of attorney's fees or a requirement to pay for educational expenses, is in the nature of alimony, maintenance, or support. To protect your client, file a complaint to determine the dischargeability of all domestic relations debts that are not clearly alimony, maintenance, or child support. Although there is no

deadline for filing a complaint to determine the dischargeability of a debt for alimony, maintenance, or support (which cannot be discharged), there is a deadline for filing a complaint to determine whether all other types of debts arising out of a divorce or separation proceeding can be discharged. Under chapters 7 and 11, such complaints must be filed within 60 days following the first date set for the spouse's meeting of creditors. 11 U.S.C. § 532(c)(1); Bankruptcy Rule 4001(c).

You waive your right

In chapter 13 cases, the court sets the deadline for filing such complaints. 11 U.S.C. § 532(c)(1); Bankruptcy Rule 4001(d). Be aware that if you are mistaken in your belief that a debt is in the nature of alimony, maintenance, or support, and do not timely file a complaint to determine the dischargeability of the debts by the deadline, you will forever waive your right to have the debts declared nondischargeable.

By filing your complaint before the deadlines, you give your client two opportunities to have the court declare a domestic relations debt nondischargeable. The first opportunity is to have the court declare the debt to be in the nature of alimony, maintenance, or support. If you succeed, you win and the case is over.



If you lose on the alimony, maintenance, or support argument, you can still argue that the debt should not be discharged because the debtor has the ability to pay the debt and discharge of the debt would result in detrimental consequences to the spouse, dependent, or child of the debtor, which are not outweighed by the benefit to the debtor. (In many jurisdictions, the debtor is required to plead as an affirmative defense an inability to pay the domestic relations debt. See *Collins v. Hesson (In re Hesson)*, 190 B.R. 229 (Bankr. D. Md. 1995); *King v. Speaks (In re Speaks)*, 193 B.R. 436, 441 (Bankr. E.D. Va. 1995). (Debtor also must affirmatively plead that discharge of the debt would result in benefit to debtor that outweighs detrimental consequences to the spouse, dependent, or child of the debtor.) If you fail to file your complaint by the deadlines, you waive the opportunity to make this alternative argument.

In addition to asking the court to determine the dischargeability of debts arising out of domestic relations proceedings, your client may have the right to object to the discharge of all of the spouse's debts. To prevail on such an objection, you must prove that the debtor intentionally perpetrated a fraud in the bankruptcy case. In a chapter 7 case, a complaint objecting to discharge must be filed not later than 60 days following the first date set for the meeting of creditors. Bankruptcy Rule 4004(a). In a chapter 11 case, the complaint must be filed no later than the first date set for the hearing on confirmation of the plan of reorganization. Bankruptcy Rule 4004 (a). Three common grounds for objecting to discharge are that the spouse has:

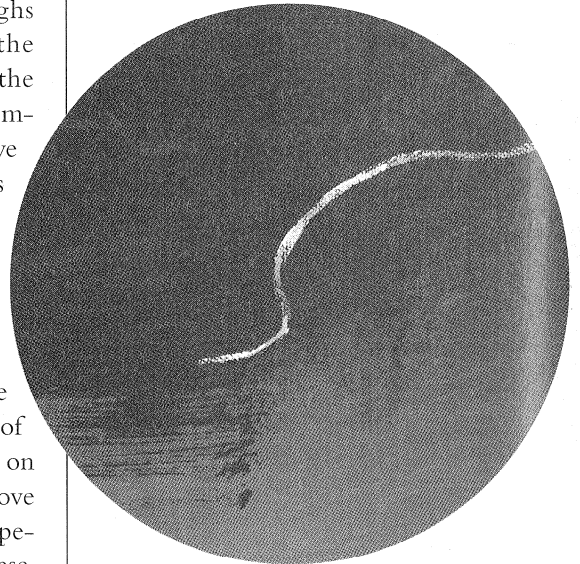
1. With the intent to hinder, delay, or defraud creditors, transferred, removed, destroyed, mutilat-

ed, or concealed property within one year before the date of the bankruptcy filing; or after the bankruptcy case has been filed. 11 U.S.C. § 727(a)(2).

2. Concealed, destroyed, mutilated, falsified, or failed to keep or preserve information from which the spouse's financial condition could be ascertained. 11 U.S.C. § 727(a)(3).

3. Knowingly and fraudulently made a false oath or account in the bankruptcy case. 11 U.S.C. § 727(a)(4)(A).

If your complaint is based on allegations that the debtor concealed property, you should add a second count that the debtor made a false oath by not disclosing the concealed



assets in the bankruptcy schedules. Keep in mind that if you prevail on an objection to discharge, you have done a favor for all of the other creditors whose debts now will not be discharged. In seeking to collect your debt, you will place yourself in competition with them. Success on an objection to discharge may confer an emotional rather than financial victory for your client.

File proof of claim

For your client to receive money in a chapter 7 or chapter 13 case, he or she must file a "proof of claim" in the bankruptcy court. The proof of

