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What Every Family Law Practitioner Should Know about the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005

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"Bankruptcy often follows divorce, and bankruptcy can wreak havoc on the expectations of a family law lawyer."[1] The impact of bankruptcy on domestic relations cases and judgments will be substantially reduced in bankruptcy cases filed on and after October 17, 2005, when most of the provisions in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 become effective. This article will review the changes in the bankruptcy law that most directly affect domestic relations.

I. Expansion of What Are Support Obligations - A New Bankruptcy Term: "Domestic Support Obligation"

The Bankruptcy Code historically has divided domestic relations obligations into two categories, "alimony, support and maintenance" and "non-support" obligations. The current Bankruptcy Code treats the former better than the latter in many respects, including discharge and the right to priority in distribution of the bankruptcy estate.

The 2005 Amendments expand the scope of the domestic relations obligations that get preferred bankruptcy and post-bankruptcy treatment by introducing a newly defined term, the "Domestic Support Obligation"("DSO"). § 101(14A).[2] The term is significantly broader than "alimony, support and maintenance."

A DSO is a debt that: (a) is "*owed to or recoverable by* a spouse, former spouse, or child of the debtor or such child's parent, legal guardian, or responsible relative; or a governmental unit;" (b) *"in the nature of alimony, maintenance or support* . . . of such spouse, former spouse, or child of the debtor or such child's parent," and (c) *established by* "reason of applicable provisions of a separation agreement, divorce decree," property settlement, court order or administrative determination. § 101(14A)(A)-(C)(emphasis added). Also, nongovernmental entities may recover support under this definition so long as the spouse, child, parent, legal guardian or other responsible relative has assigned the obligation voluntarily, for the purpose of collecting the debt. § 101(14A)(D). The treatment of DSOs during and after bankruptcy is explored below.

II. Effect of Bankruptcy on State Court Proceedings - The Automatic Stay

The automatic stay is fundamental to the bankruptcy process. It stops most creditor actions to collect debts from the debtor and protects property of the estate. § 362. Under existing law, the automatic stay does not apply to three types of domestic

relations proceedings against the debtor: (1) proceedings to establish paternity, (2) proceedings to modify support and (3) proceedings to collect support from property that is not property of the estate. § 362(b)(2). These exceptions are revised to substitute the broader DSO for the term "alimony, support and maintenance." In addition, the new law excepts from the automatic stay eight additional domestic relations proceedings and procedures:

1. child custody or visitation proceedings;
2. divorce proceedings, except to the extent that such proceeding seeks to divide property of the estate;
3. domestic violence proceedings;
4. withholding of income that is property of the estate or the debtor for payment of a DSO;
5. withholding, suspending or restricting a driver's, professional, occupational or recreational license under state law as specified by § 466(a)(16) of the Social Security Act;
6. reporting of overdue support owed by a parent to any consumer reporting agency as specified by § 466(a)(7) of the Social Security Act;
7. intercepting a tax refund as specified in §§ 464 and 466(a)(3) of the Social Security Act or under analogous state law;
8. enforcing a medical obligation as specified under Title IV of the Social Security Act; § 362(b)(2)(A)-(G). As a result of these changes, the automatic stay will not stay domestic relations litigation and collection efforts as frequently.

III. Discharge of Obligations in Bankruptcy

A. Chapters 7, 11, 12[3]

The primary objective of most individual bankruptcy debtors is to discharge as much debt as possible. At the inception of the Bankruptcy Code in 1979, domestic relations support obligations owed to a spouse, former spouse or child of debtor were nondischargeable.[4] The pertinent statute, § 523(a)(5), has been amended to expand the scope of what support obligations are nondischargeable. All debts defined as DSOs are nondischargeable. Thus, support obligations owed to a child's parent, legal guardian, responsible relative, a government agency or a nongovernmental entity that has been assigned the debt are all now nondischargeable. Property settlements and administrative determinations by governmental units have been added to the documents that can also be used to establish the existence of DSOs.[5] § 101(14A)(C)(i),(iii).

In 1994, Congress added property division and other non-support domestic obligations to the list of debts that are nondischargeable in a Chapter 7, 11 or 12 bankruptcy if certain conditions were met. The debt had to be owed to a spouse, former spouse, or child of a debtor in connection with a domestic relations proceeding and could not fit the definition of "alimony, maintenance or support." The debtor had to have the ability to pay the debt and the bankruptcy court had to find that the harm to the

debtor in paying the debt was less than the harm to the spouse or child if the debt went unpaid. § 523(a)(15). Section 523(a)(15) has been simplified and streamlined. The ability to pay and balancing test have been eliminated. Non-support domestic relations obligations are now on an equal footing with support obligations and are also nondischargeable. Additionally, the current short statute of limitations on commencing an adversary proceeding in the bankruptcy court to determine that such a debt is nondischargeable has been eliminated, § 523(c), Fed. R. Bankr. P. 4007(c), and there will no longer be a statute of limitations on § 523(a)(15) actions.

The bankruptcy court and the state court now have concurrent jurisdiction to determine whether such a debt is nondischargeable.[6] Counsel will need to remember that the change in the law does not eliminate the need to obtain a judgment determining the debt to be nondischargeable to prevent any claims that post-bankruptcy collection efforts violate the discharge injunction.[7] § 524(a). The bankruptcy trustee is not a necessary party in a nondischargeability action because administration of the estate is not affected by the scope of the discharge the debtor obtains.

While the nondischargeability action can be commenced in the bankruptcy court without relief from stay, In re Roxford Foods, 12 F.3d 875, 878 (9th Cir. 1993), relief from the automatic stay should be obtained if the action is going to be filed in the state court before the automatic stay terminates. § 362(c).

B. Chapter 13

Chapter 13 cases are filed by individual debtors who meet their bankruptcy obligations by voluntarily performing a debt payment plan. Under current law, a Chapter 13 debtor who completes his or her plan[8] discharges non-support domestic obligations. The amendments do not change this. Thus, the domestic relations practitioner will want to remember that bankruptcy can still substantially alter how much may be collectable on a property or debt division judgment that is not support.

Collection of an unsecured non-support domestic obligation during a Chapter 13 will be limited by how much is payable under the Chapter 13 plan. Such plans last only three to five years and there are often numerous priority and secured debts to pay, leaving little left for unsecured debts, including non-support domestic obligations.

IV. Changes in the Bankruptcy Code that "Encourage" Debtors to Perform their DSOs

A. Chapter 11, 12 and 13 debtors cannot confirm a plan or obtain a discharge without being current on all DSOs that become due after debtor files bankruptcy.

Chapter 11, 12 and 13 cases involve debt repayment plans that often last several years. The new law "encourages" such debtor's performance of post-bankruptcy filing DSOs ("postpetition DSO") in two ways. First, Chapter 11, 12 and 13 debtors will not be

able to confirm a repayment plan unless the debtor has paid all DSOs that became due postpetition. §§ 1129(a)(14), 1225(a)(7), 1325(a)(8). Second, in Chapters 12 and 13, the new law requires debtors to certify that all postpetition DSOs have been paid in order to receive a discharge, which typically is not granted for three to five years after a case is filed. §§ 1228(a), 1328(a).

B. A Chapter 11, 12 or 13 debtor who fails to pay postpetition DSOs may not be able to stay in bankruptcy.

The amendments expressly provide that failure of a Chapter 11, 12 or 13 debtor to pay a postpetition DSO is cause for dismissal of the bankruptcy case or conversion to Chapter 7 liquidation. §§ 1112(b)(4)(P), 1208(c)(10), 1307(c)(11). Generally, such conversion or dismissal will only occur if an interested party brings the default to the court's attention through a motion to dismiss or convert.

V. Treatment of DSOs in the Administration of Bankruptcy Cases.

Under the Amendments, DSOs have advanced from the seventh priority to the first priority in the distribution of the bankruptcy estate. § 507(a)(1). Only the bankruptcy trustee and the trustee's agents will be paid ahead of a DSO. § 507(a)(1)(C). This is a practical recognition that it is necessary to pay the trustee if there is going to be any distribution. This provision will likely discourage attorneys from providing bankruptcy representation to debtors with substantial DSOs, unless attorney fees are paid in full before the case is filed.

Generally, a Chapter 11, 12 or 13 plan must provide for payment in full of priority claims in order to be confirmed. §§ 1129(a)(9)(B), 1222(a)(2), 1322(a)(2). There is a limited exception in Chapters 12 and 13 for DSOs assigned to governmental units, but only if the debtor proposes a five year plan dedicating all disposable income. §§ 507(a)(1)(B), 1222(a)(4), 1322(a)(4). The payment is usually made in installments, often over several years. This is not changed by the amendments.

As a general rule, trustees have the power to avoid preferential transfers that were made by a debtor to a creditor within 90 days before a bankruptcy petition was filed. § 547(b). Current bankruptcy law excepts from this rule transfers made as payments of domestic relations support obligations. The new amendments have expanded the types of domestic relations support obligations that a trustee may not avoid under § 547(c)(7) by substituting the term DSO for "alimony, maintenance and support." See § 547(c)(7).

The amendments have imposed a new duty on Chapter 7, 11, 12 and 13 trustees to send certain notices to DSO claimants. Trustees are now required to give DSO claimants and child support enforcement agencies two different notices at different times in the case. Both notices contain information that will assist DSO claimants in the collection of their DSOs from the estate and the debtor. See § 704(c)(1), § 1106(c)(1), § 1202(c)(1) and § 1302(d)(1).[9]

In administering bankruptcy cases in Oregon, the exemptions available under Oregon law and non-bankruptcy federal law apply. The amendments provide that exempt property is liable for DSOs and that this provision preempts any state law to the contrary. § 522(c)(1). Thus, the bankruptcy trustee may be able to liquidate the debtor's homestead and other exempt property to satisfy a DSO, even though state law may not allow liquidation of such property.[10]

VI. Domestic Relations Attorneys May Be Debt Relief Agencies Subject to Bankruptcy Code Requirements

The Bankruptcy Code now regulates the conduct of "debt relief agencies" (hereafter DRA). A DRA includes "any person who provides any bankruptcy assistance to an assisted person in return for the payment of money or other valuable consideration . . . ." § 101(12A). The term "bankruptcy assistance" is not defined, but a number of commentators have suggested that it is far broader than just attorneys who provide actual bankruptcy services; it includes attorneys who counsel financially distressed clients about their options. "[A] domestic relations attorney (who is being paid) who discusses options for his or her ('assisted person') client [in dealing with debt beyond the client's ability to pay as required] before, during or after a dissolution proceeding, probably is a DRA."[11]

Attorneys who are DRAs are restricted in giving certain types of advise to their clients (§ 526), must provide specific disclosures to the client (§ 527), and must comply with certain requirements with respect to their advertising and fee agreements (§ 528). While a discussion of the detailed restrictions is beyond the scope of this article, lawyers should be aware that DRAs are prohibited from advising a client to incur more debt. § 526(a)(4). A domestic relations lawyer who is a DRA should consider how to comply with the DRA requirements before counseling the client regarding new debt that commonly results from many dissolution decrees, e.g., suggesting that the client pay fees by credit card or that the client obtain a loan from a relative.

Conclusion

The bankruptcy amendments will significantly reduce, but hardly eliminate, the impact that a bankruptcy filing will have on domestic relations obligations and proceedings. Financially overburdened domestic relations clients will need to be advised how limited their bankruptcy options will be before undertaking obligations in a dissolution decree. Attorneys giving such advice need to consider whether they are DRAs, and if so, they must comply with the restrictions applicable to DRAs.

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1. Robert Vanden Bos and Ann Chapman, *Bankruptcy and Family Law*, 21 OREGON STATE BAR CONTINUING LEGAL EDUCATION: FAMILY LAW § 21.1 (2002).

2. All statutory references are to the Bankruptcy Code (11 U.S.C.), as amended by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, unless otherwise indicated.

3. Debts that are nondischargeable under § 523(a) are nondischargeable in Chapter 7, 11, and 12. §§ 523(a), 727(b), 1141(d), 1228(a).

Chapter 7 is liquidation by an individual, partnership or corporation, §§ 701-784; Chapter 11 is reorganization by a business or individual, §§ 1101-1174; Chapter 12 is the family farmer reorganization chapter, §§ 1201-1231.

4. A debt "to a spouse, former spouse, or child of the debtor, for alimony to, maintenance for or support of such spouse or child, in connection with a separation agreement, divorce decree or other order of a court of record" is currently dischargeable. § 523(a)(5)(prior to 2005 amendment).

5. Under existing law, separation agreements, divorce decrees and court orders can be used to establish nondischargeable support obligations. § 523(a)(5)(prior to 2005 amendment).

6. "Non-bankruptcy courts have concurrent jurisdiction to determine dischargeability on grounds other than those contained in paragraphs (2),(4),(6) and (15) of Code § 523(a)." 4 William L. Norton Jr., NORTON BANKRUPTCY LAW AND PRACTICE § 47:67 (March 2005 Supplement). Under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, paragraph (15) has been eliminated from the previous sentence. See § 523(c)(1), as amended.

7. After discharge, an injunction protects a debtor against a creditor's further efforts to recover a discharged debt as a personal liability of the debtor. 4 Lawrence P. King, COLLIER ON BANKRUPTCY ¶ 524.02 (15th ed. Rev. 2005).

8. If a debtor obtains a Chapter 13 discharge after completing a plan, the debtor is able to discharge some debts that would be nondischargeable in Chapters 7, 11 or 12. § 1328(a). This is commonly referred to as the "superdischarge," but the amendments substantially eviscerate the superdischarge. If a Chapter 13 debtor is unable to complete his or her Chapter 13 plan and is granted a hardship discharge under § 1328(b), all of the § 523(a) exceptions to discharge apply. §§ 523(a), 1328(b).

9. The new notice duties of Chapter 7, 11, 12 and 13 trustees are identical, except for the Chapter 7 trustee, who has an additional duty to inform the DSO claimant of his or her rights to payment of the DSO. § 704(c)(1)(A)(iii).

10. ORS 18.398 provides that a homestead exemption may be denied under certain circumstances when the judgment being collected is for child support.

11. Richard J. Parker, "New Obligations of Debtor's Counsel," *Vol. XXIV, No. 3, Oregon Debtor-Creditor Newsletter,* p. 5 (Fall 2005).