

## Chapter 15 – Creditors Rights and Bankruptcy

### Laws Assisting Creditors

- Liens
  - A claim against specific property to satisfy a debt
  - Mechanic's liens
  - Artisan's liens
  - Judicial liens
    - **Attachment** refers to a court-ordered seizure of property before a judgment is obtained; prejudgment remedy
    - Writ of attachment
    - Writ of execution
  
- Garnishment
  - Permits a creditor to collect a debt by seizing property or wages of the debtor held by a third party
  - Procedures – can be a prejudgment remedy
  - Laws limiting the amount of wages subject to garnishment
  
- Creditors' Composition Agreements
  - Creditors take less than owed on a liquidated debt.
  - Binding on those who agree because consideration given by each depending on one another.
  
- Suretyship and Guaranty
  - Suretyship
    - Promise by a third person to be responsible for the debtor's obligation to the creditor.
    - Suretyship is an express contract between the surety and the creditor.
    - Creditor can demand payment from surety at any time after debt is due.
  
  - Guaranty
    - Third person making the guaranty is *secondarily* liable.
    - Guarantor is liable only after the principal debtor defaults.
  - Actions that release the surety and the guarantor
    - Material modification
    - Surrender of property
    - Payment of tender of payment
  - Defenses of the surety and the guarantor
    - Incapacity
    - Statute of limitations
    - Fraud
  
  - Rights of the surety and the guarantor
    - Right of subrogation
    - Right of reimbursement

- Right of contribution

### **Mortgages**

- Fixed-Rate Mortgages
- Adjustable-Rate Mortgages
- Creditor Protection
  - Require mortgage insurance
  - Record the mortgage
  - Include contract provisions
- Mortgage Foreclosure
  - Ways to avoid foreclosure
    - Forbearance
    - Workout agreement
    - Short sale
  - Foreclosure procedure
  - Redemption rights
    - Debtor's legal right to repurchase, or buy back, property before a foreclosure sale

### **Protection for Debtors**

- Exempted Real Property
- Exempted Personal Property
  - Most often exempt:
  - Household furniture
  - Clothing and personal possessions
  - Vehicle for transportation
  - Certain classified animals
  - Equipment debtor uses in business or trade

### **Bankruptcy Law**

- Bankruptcy proceedings are under authority of U.S. District Courts.
- Types of Bankruptcy Relief
  - Chapter 7 provides for liquidation proceedings
  - Chapter 11 governs reorganizations
  - Chapters 12 and 13 provide for adjustment of debts by persons with regular incomes
- Special Requirements for Consumer-Debtors

### **Chapter 7—Liquidation**

- Most familiar type of bankruptcy
- Ordinary, or straight, bankruptcy
- Debtor turns over all assets to a bankruptcy trustee.
- Trustee sells nonexempt assets and distributes proceeds to creditors.
- Voluntary Bankruptcy
  - Prior to filing, debtor(s) must receive credit counseling within 180 days of filing, and submit certificate.

- Consumer-debtor must confirm accuracy of contents; attorney must file affidavit informing debtor about other chapters.
  
- Chapter 7 schedules
  - A list of both secured and unsecured creditors, their addresses, and the amount of debt owed to each.
  - A statement of the financial affairs of the debtor.
  - A list of all property owned by the debtor, including property claimed by the debtor to be exempt.
  - A listing of current income and expenses.
  - A certificate of credit counseling (as discussed previously).
  - Proof of payments received from employers within sixty days prior to the filing of the petition.
  - A statement of the amount of monthly income, itemized to show how the amount is calculated.
  - A copy of the debtor's federal income tax return for the most recent year ending immediately before the filing of the petition.
  
- Tax returns during bankruptcy
- Substantial abuse and the means test
  - To determine whether debtor's petition will be dismissed under Chapter 7
  - The Basic Formula
  - Applying the means test to future disposable income
- Additional grounds for dismissal
- Order for relief
  
- Involuntary Bankruptcy
  - Occurs when creditors force debtor into bankruptcy proceedings
- Automatic Stay
  - Suspension of all actions by creditors against the debtor or debtor's property
- Estate in Property
  - Community property
  - Property transferred in a transaction voidable by the trustee
  - Proceeds and profits from the property of the estate
  
- The Bankruptcy Trustee
  - Duties for means testing
    - To determine whether there is substantial abuse. Must file statement within 10 days after 1<sup>st</sup> meeting with creditors.
  - The trustee's powers
    - Trustee has the right to 'strong arm' creditors to return debtor's property to trustee.
  - Voidable rights
  - Preferences
  - Fraudulent transfers
  
- Exemptions

- Debtor is entitled to exclude certain property from bankruptcy
- States can pass legislation precluding debtors from using federal exemptions within the state.
- The Homestead Exemption
  
- Creditors' Meeting
- Creditors' Claims
- Distribution of Property
  - Distribution to secured creditors
  - Distribution to unsecured creditors
  
- Discharge
  - Exceptions to discharge
    - Claims for back taxes accruing within 2 years prior to bankruptcy
    - Claims for amounts that the debtor borrowed to pay federal or nondischargeable taxes
    - Certain government fines
    - Claims by creditors who were not notified of bankruptcy
    - Domestic-support obligations and property settlements made from separation or divorce
    - Claims that arose from a debtor's driving while intoxicated
    - False representations and misuse of funds
  
  - Objections to discharge
    - Court may deny discharge of debts based on debtor's conduct
    - The debtor's concealment or destruction of property with the intent to hinder, delay, or defraud a creditor
    - The debtor's fraudulent concealment or destruction of financial records
    - The grant of a discharge to the debtor within 8 years before the petition was filed
    - The debtor's failure to complete the required consumer education course
    - Proceedings in which the debtor could be found guilty of a felony
  
- Reaffirmation of Debt
  - An agreement between a debtor and creditor in which the debtor voluntarily agrees to pay a debt dischargeable in bankruptcy

### **Chapter 11—Reorganization**

- Most commonly used by organizations
- Creditors and debtor create a plan under which the debtor pays a portion of the debts and is discharged of the remainder.
- Congress established "fast-track" Chapter 11 procedure
  
- Debtor in Possession
  - A debtor who is allowed to continue in possession of the estate in property (business) and to continue business operations
- The Reorganization Plan

- Filing the plan
- Acceptance of the plan
- Confirmation of the plan
- Discharge

**Bankruptcy Relief under Chapter 12 and Chapter 13**

- Chapter 12—Family Farmers and Fishermen
  - Filing the petition
  - Content and confirmation of the plan
- Chapter 13—Individuals' Repayment Plans
  - Filing the petition
  - Good faith requirement
  - The repayment plan
  - Discharge