Prevention of Post-Bankruptcy Issues

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Your Debtor has completed bankruptcy and now you get a phone call from them that goes something like this, "A creditor, that you told me was included in my bankruptcy, is harassing me. They told me they are going to garnish my wages. You need to take care of this." Are you able to get the creditor to stop harassing your client? If you have one of the following situations, the answer is no.

Situation 1. The silent dangers of cure and maintain.

In March of 2010, Judge Fines authored an Opinion in a case called *In re Bryant*, 430 B.R. 516 (Bankr. C.D.Ill, 2010). Chapter 13 debtor owned a 2001 Saturn, which she desired to keep. At the time of filing, she was in arrears on her Saturn in the amount of $816.66. The Debtors Plan provided for "The Trustee to cure defaults... Creditors shall retain their liens" Essentially the Debtor would "cure and maintain" the vehicle. The Plan was confirmed and the Trustee cured the $816.66 arrearage. If we concluded the story here, we would say and they all lived happily ever after, however, at some point the Debtor fails to make the post-petition payments. The Creditor was unhappy with the lack of payments and filed a Motion for Relief from Stay, which was unopposed by the Debtor, an Order was entered, and the Saturn met its ultimate demise. Without any further Modification, the Debtor's Plan proceeded to discharge. After the Discharge was entered, the Creditor filed suit to collect the remaining balance owed on the Contract. The Debtor filed an adversary seeking sanctions for violation of the discharge injunction pursuant to 11 U.S.C. § 524.

The Court looked at the interplay between four different statutes 11 U.S.C. §§ 1322(B)(5), 1327(a), 1328(a), and 1329. The court found that the Debtor's Plan provided for the cure and maintenance of payments under 11 U.S.C. §1322(b)(5) which states "Notwithstanding paragraph (2) of this subsection, provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due."

Next the Court looked to the effect of confirmation pursuant to 11 U.S.C. § 1327 and found that the confirmation of the Plan bound both the Debtor and the Creditor, specifically, that the Debtor was bound by the Plan to make the Post petition payments when they became due. The Court cited *In re Harvey*, 213 F.3d 318, 323 (7th Cir. 2000) where the 7th Circuit indicated that "No party to a bankruptcy plan proceeding can be expected to envision every foreseeable circumstance that could require a court to construe a particular plan provision." The Court indicated that the Debtor could have filed a response to the Motion for Relief, the

Debtor could have sought a provision in the Order that would have affected the secured claim or its treatment under the Plan, or the Debtor could have filed a Motion to Modify the Plan pursuant to 11 U.S.C. § 1329.

The Discharge pursuant to 11 U.S.C. § 1328(a) provides the Debtor with a "discharge of all debts provided for by the plan or disallowed under section 502 of this title, except any debt- (1) provided for under section 1322(b)(5);" Since the Plan provided for the payment of the Saturn through 1322(b)(5), the Debtor failed to make the required payments, and the Debtor failed to ensure that the Plan was modified prior to the entry of the discharge, the Debtor was liable for the unpaid post-petition contractual payments owed to the Creditor.

Judge Gorman reviewed a similar situation in *In re St. Pierre,* 2012 WL 1835448 (Bankr. C.D.Ill 2012), in which a deficiency claim was filed by Wells Fargo. The Trustee sought to dismiss the case, however, since no Motion to Modify had been filed, there was no change to the terms of the Plan which bound the Debtors and Wells Fargo. Ultimately, the Motion to dismiss was denied. In a footnote Judge Gorman indicated that some courts do not allow the surrender of a property through a Motion to Modify. If 11 U.S.C. §1329 is limited to the four purposes listed in 1329(a) (to increase or decrease a claim, extend or reduce time for payments, alter the amount of a claim to take into account payments outside of the Plan, and reduce the amounts paid based on the purchase of health insurance,) then you have one opportunity to counsel your client to surrender the vehicle. Which leaves me with a big question, did the Debtors complete all of their Plan payments? It seems to me the answer might be no. The Plan required the payment to the Creditor directly and 11 U.S.C. §1328 (a) states "as soon as practicable after completion by the debtor of all payments under the Plan." After the sale of the vehicle and successful completion of the Plan, is the remaining deficiency balance discharged?

It is important to remember that this applies anytime the Debtor cures an arrearage through the Plan and elects to maintain the payments with at least one payment being due after the final payment is due. Since more lenders are willing to enter into 72 month car loans, this will become a bigger issue. If you are in a jurisdiction where surrender is not allowed after the Plan has been confirmed, then make sure to advise your client, through a letter at the onset of the case, what will happen if they fail to make the payments. In reviewing motions for relief from stay, you may want to dust off the plan and determine if the Debtor was curing a delinquency and maintaining plan payments, as the payments that are contractually due after confirmation are not discharged, unless you take an affirmative step to modify the plan. Typically, the Orders that are entered on the Motion for Relief from stay do not contain language to protect your client. If after the Order is entered, you realize that your client may still be liable for the contractually due post-petition payments, file a Motion to Modify which surrenders the property, gives the creditor ample time to file a deficiency claim, and allows you to sleep better at night knowing you won't be sued to cover 29 years worth of contractual payments.

Situation 2. Interest on a non-dischargeable claim

In July of 2011, Judge Perkins authored an Opinion *In re Kreps*, 2011 WL 2749584, (Bankr. C.D.Ill. 2011). The Debtor owed back child support to his ex-wife. The Illinois Department of Children and Family Services filed a claim seeking a priority claim in the amount of $7,439.75 and an unsecured Non-Priority claim in the amount of $10,782.21. The Debtors' eventually modified their Plan to pay the priority portion of the claim in full. The Trustee paid the priority portion of the claim in full without interest and the Debtor received a discharge. After the entry of the discharge, the Department of Healthcare and Family Services continued to pursue the Debtor for the interest that accrued post-petition on the priority portion.

The Court reviewed a 9th Circuit Court of Appeals *In re Foster,* 319 F.3d 495 (9th Cir. 2003), which had very similar facts. In *Foster*, the Debtor owed $8,918.78 for his back child support. The child support was paid in full during the plan; however, no post-petition interest was paid. On January 31, 2000, the Debtor received his discharge, on February 2, 2000; the Ventura County District Attorney sent a wage garnishment to the Debtors employer seeking $100.00 per month until the full $2,006.75 of interest had been paid. The Court looked to 11 U.S.C. § 502(b)(2) and stated that because the interest was unmatured at the time of filing, the County could not have objected to the Plan. Since the debtor did not pay the interest during the Plan, the under lying obligation is non-dischargeable, the interest that accrues on that obligation is also non-dischargeable

The Court in *Kreps* agreed with the opinion in *Foster* Court and held that "to the extent that child support arrearages are non-dischargeable in chapter 13, the arrearages continue to accrue interest as provided by state law. The postpetition interest is the liability of the debtor personally, not of the estate, is not subject to discharge in the case and is collectable thereafter. "The Court further held that "section 1327(a) has no effect on a debtor's continuing liability for payment of the unmatured interest that accrues postpetition."

Pursuant to 11 U.S.C. §1322(b)(10), the plan may "provide for the payment of interest accruing after the date of the filing of the petition on unsecured claims that are nondischargeable under section 1328(a), except that such interest may be paid only to the extent that the debtor has disposable income available to pay such interest after making provision for full payment of all the allowed claims." This means the only way you can pay interest through the Plan is to pay in full the other allowed unsecured claims.

Currently priority federal tax claims accrue interest at a rate of three percent. If a debtor owed $10,000.00 for a federal tax claim, using a simple amortization, over a sixty month plan, assuming the debtor pays on time and the Trustee disburses an equal amount to the federal tax claim each month, the debtor would owe approximately $781.21 after receiving their discharge. If the $10,000.00 was owed on a nondischargeable claim that instead accrued interest at a statutory rate of nine percent, using the same simple amortization, then the debtor after discharge would owe approximately $2,455.01.

The scary part is that this applies to all non-dischargeable claims. You can provide for the principle to be paid, but you cannot pay the interest, unless you pay all of the unsecured creditors in full. So the interest owed on all of your debtor's non-dischargeable tax claims, student loan claims, Domestic Support Obligation, etc., survive the chapter 13 plan. [1] The idea of bankruptcy is to provide a fresh start, but how fresh is the start if you are immediately encumbered by several years worth of post-petition interest on the nondischargeable claims. What would be more troubling to me, if I was a debtor, would be if my attorney never disclosed the interest issue. The Internal Revenue Service is aware that the interest is not dischargeable and does frequently pursue debtors for the interest. As illustrated in the hypothetical above, interest on the claims can become substantial and if the Debtor is unaware, that may result in several unhappy phone calls. The good news is that I don't receive any of those phone calls. The bad news is that your office, and my boss, will receive those angry and disgruntled debtor's phone calls.

Even scarier is in order to receive a discharge, the Debtor, pursuant to 11 U.S.C. §1328(a), must certify "that all amounts payable under such order or such statute that are due on or before the date of the certification … have been paid." There is an exception that allows for the court to approve a written waiver of discharge, but there is no guarantee that the Court will enter the waiver. In the event that the court does allow the waiver of discharge, you will want to ensure that the waiver is narrowly tailored to address your specific priority interest claim. What information do you request from the debtors to verify that they are completing Form 283 correctly? If the Debtor has failed to pay the post petition interest, then they cannot certify that they have paid all such amounts that became due between the filing of my bankruptcy petition and today as the unmatured interest became due after filing and was not paid. What is your liability if you file a certification with the court and you know that the Debtor was not making post-petition interest payments, because the Debtor did not know to make them?

The take away, although the plan may not be able to provide for the interest payment, unless you pay all of the other unsecured claims in full, you can run an amortization to determine the amount of interest that will accrue during the pendency of the Plan, so that, upfront, you can inform the Debtor, in writing, the amount they will still owe upon the completion of the Plan. Better yet, you could advise the Debtor to make a monthly payment to the entity which represents the interest payment so they might have a small amount they owe upon completion of their plan.

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[1] The Internal Revenue Service pursues interest for the following claims:

1. Trust Fund Taxes. Section 507(a)(8)(C)
2. Taxes on returns that were not filed before the bankruptcy or are late filed after two (2) years before the date of the bankruptcy petition. Section 523(a)(1)(B)
3. Taxes for which the debtor made a fraudulent return or taxes that the debtor willfully attempted to evade or defeat. Section 523(a)(1)(C) (The fraud penalty is dischargeable but the tax and interest is not dischargeable.)