

BANKRUPTCY MYTHS, REALITIES AND DECISION MAKING

We haven't written about bankruptcy (BK) issues for quite some time. Unfortunately, the current economic climate has resulted in an escalating number of bankruptcies by residents. Deciding what course of action to take when a resident files BK is difficult because it is almost certainly to be a no win proposition. A resident's BK is almost certain to be a money-losing proposition. Some managers hesitate to make a decision to avoid the inevitable costs that are incurred when a resident files BK. As we will explain, in almost all instances a BK is going to cost the community money, and putting off decisive action at that start is a gamble that rarely pays off, and almost always results in bigger losses.

But before we discuss BK decision-making, let's review some basics. First, when a resident files BK, an automatic stay immediately goes into effect. The automatic stay is analogous to an instant force field surrounding the resident. This force field protects the resident from all creditors, including you the resident's landlord. Once you have been notified that the automatic stay is in place, you cannot take any action against the resident to collect the rent, or to enforce the lease for non-payment until you lower the force field.

You can only lower the force field by obtaining a court order. This order is called Relief from the Automatic Stay. To obtain a court order granting you relief from the automatic stay, you must file a Motion for Relief from the Automatic Stay. Once the automatic stay goes into effect up to the time you obtain a court order granting you relief from the automatic stay, you must cease all eviction action against the resident. If you served a three-day demand for rent and the resident has not paid, you can't file a case. If we have filed an eviction case for you, we must halt the court process. You face substantial liability, both in fines and for damages, including attorneys' fees, if you continue to process an eviction or try to collect the rent when the automatic stay is in place.

The cost to file motion for relief from stay is Six Hundred dollars, which includes

the One Hundred Fifty dollar filing fee. Once the motion is filed, the court sets a preliminary hearing date around thirty days from the date of filing. The resident must file a response a week before the hearing to contest the motion. If the resident doesn't file a response, no hearing takes place, but we are required to file a certificate of non-contested matter with the court, and the court orders relief from the stay. If the resident files a response, then on the date of the hearing the court conducts a brief non-evidentiary hearing regarding the evidence that would be submitted at a formal hearing. Both sides submit witness and exhibit lists showing what the evidence will show. If the court determines there is a genuine dispute, then the matter gets set for a final hearing where testimony will be required. If the court determines there is no issue, the court grants relief from the stay. If the resident does not contest, you are not required to appear.

Residents rarely contest motions for relief from stay. Further, in the few instances that the resident does contest a motion for relief, the matter is almost always resolved in the landlord's favor at the initial non-evidentiary hearing. Only in the rarest of cases does the court set a motion for relief for a final formal hearing usually because the resident is unable to demonstrate a legitimate dispute. A legitimate dispute will only exist if there is a factual question regarding the validity of the amount owed, or a challenge to title of the property, or on certain subsidized properties a tenant can put the arrearage into a bankruptcy plan and remain in the property.

Generally, residents can file either a Chapter 7, or a Chapter 13 bankruptcy. A Chapter 7 resident bankruptcy filing will wipe out all past due money owed to you, including rent, owed as of the date the BK petition is filed. A Chapter 13 is a reorganization plan. If a resident files a Chapter 13, you may get paid some money, but don't hold your breath. If you do get paid under a Chapter 13, the resident's Chapter 13 plan usually will only pay a fraction of what is owed to any individual creditor. In order to get paid, you may have to file what is called a "proof of claim". As a creditor of the resident, the BK court will notify you if you are eligible to file a proof of claim, and the applicable deadline for filing.

You should verify that the resident obtained a "discharge" after the resident has

filed BK. While not too common, some resident BK cases get dismissed prior to discharge. In order for the debt to be wiped out, the debt must be discharged. Sometimes the resident files his BK without an attorney, and then fails to file the necessary paperwork with the court. Sometimes a resident is a serial bankruptcy filer and the BK court ends up dismissing the case for abuse of the system. In either case, the resident's bankruptcy case gets dismissed prior to discharge. If a resident's bankruptcy case is dismissed, the resident's debts, including any debt to you, is not discharged, and you may collect the debt. Thus, you should not write off a resident debt until verification of discharge. If you are uncertain as to whether a debt has been discharged, you should contact us for assistance.

Similar to many areas of the law, the internet has created many myths regarding bankruptcy. These fall under the "I heard it was the law" category. Let's take a moment to address some common myths.

A resident can exclude me from his bankruptcy. This is false. A resident can elect to re-affirm the debt to you after the resident has filed BK, as part of the process. However, if a resident promises to re-affirm a debt to you (the rent he owes), and doesn't, there is nothing you can do.

A resident can only file bankruptcy once every seven to eight years, my applicant just filed 3 years ago, and thus I don't have to worry about the applicant going BK on me. This is partially true. A resident can only obtain a discharge once every seven to eight years. However, a resident can file many times during this period. As noted above, some residents are frequent filers. These residents start the process, but don't complete it.

A resident can live in my unit rent-free after filing. This is false. If a resident obtains a BK discharge, this only discharges rent due at the time the BK petition was filed. Any rent due after a resident files bankruptcy is a "post-petition" obligation. Post-petition obligations are not discharged in bankruptcy. You would still have to get relief from the automatic stay to evict a resident for failure to pay post-petition rent, but the resident owes it, and at some point you can collect it.

Only bad persons, or deadbeats file bankruptcy. This is false. Donald Trump

and Chrysler filed BK. Sure, many residents abuse the bankruptcy system. However, bankruptcy is a legitimate tool that many residents are forced to use because of circumstances beyond their control. Further, more and more residents are filing bankruptcy and paying their rent.

If your resident files bankruptcy, these are the steps to be taken. First, respect the force field. Don't demand rent, or attempt to evict the resident. The court can and will fine you, and will award damages, including attorneys' fees if you ignore the automatic stay. While you can't take action until you get relief from the automatic stay, you are free to talk to the resident to ascertain the resident's intentions. So ask the resident, do you plan on staying, are you planning on paying the rent, and when? You can also talk to the resident (verify) the resident's total debt, why the resident filed, and resident's current income. Knowing these answers gives you the knowledge you need to make an informed decision about whether you should move for relief from the automatic stay.

If you don't like the resident's answers, you don't believe the resident, the resident is ignoring you, or refusing to pay rent, you file a Motion for Relief from Stay to get the force field lowered. The biggest mistake is delaying this decision. Landlords and managers delay making this decision for several reasons. You can't get a hold of the resident, or you want to avoid the legal fees that will be incurred to lower the force field. Another big mistake in making this decision is placing too much faith in the resident's word when it is not warranted, and without scrutinizing the resident's ability to perform.

For example, July's rent is due, Ronnie Resident hasn't paid and is now late. Right before you are about to post your rent demands, Ronnie gives you notice that he has filed bankruptcy. You attempt to contact Ronnie, but he doesn't return your phone calls, and otherwise avoids you. A couple of weeks go by, you finally talk to Ronnie. Despite being late eight times in the last two years, Ronnie swears on his mother's grave he will pay you next week, and will be current next month. You ask Ronnie about his debts and his job, but he doesn't want to talk about them. Next week comes and goes, and Ronnie doesn't pay you. It's now almost August, and Ronnie owes July and will owe August rent in a couple of days.

You finally decide that Ronnie is not credible, and you must get relief from the automatic stay. We promptly file a Motion for Relief from the Automatic Stay, but this process takes thirty days. After the bankruptcy court grants you relief, Ronnie still refuses to pay or move. You have to end up evicting Ronnie. Clearly, based on these facts, you would have been better off immediately filing for relief from stay. Delaying or putting off filing for relief from stay to avoid legal costs has resulted in a bigger loss for the property. A poor payment history, and a refusal to promptly communicate or provide information are red flags. When you see these red flags, you are almost always better off immediately filing a Motion for Relief from Stay with the bankruptcy court.

Not filing for relief from stay is a gamble. You are betting that you will be better off not filing because you save the legal costs, and that the resident will either pay or move before you could have the resident out if you went through the court process. Some clients have taken this gamble and won. Others have taken this gamble and lost. The key point is that it is a gamble, and you should only place this bet after carefully assessing the probability of your resident either paying, or voluntarily moving. If you don't want to gamble on the resident and have decided to move for relief from the stay, you should take immediate action because delaying usually results in a bigger loss.