

A Few Words About Bankruptcy

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Divorce & Bankruptcy

Often, family law and bankruptcy seem to go together. Either upon splitting up, the spouses can't pay the family debts, or one spouse seeks to use bankruptcy as a weapon against the other spouse, or the other spouse's lawyer.

Bankruptcy's effect on family law issues

For those divorcing or divorced, the bankruptcy issues generally fall into three categories:

Support/Discharge, payment and the automatic stay

Property Settlement: what happens to debts between spouses

Liability to others who is liable for the debts at divorce

Filing together

Sometimes, one or both spouses can **benefit** from a bankruptcy filing:

dischargeable debts are eliminated, leaving more money for the payment of on going expenses, including support.

taxes can be paid, without interest, or even discharged where sufficiently old. More on taxes in bankruptcy

the divorce is simplified by the elimination of much of the family debt

Do we have to file together?

When Only One Spouse Files

When only one spouse files, the legal worlds of state family law and federal bankruptcy law may collide. The bankruptcy courts are left to sift through the wreckage.

Where there are non exempt assets, a bankruptcy filing by one spouse pulls *all* the community property into the bankruptcy estate and assures that the available assets are used to pay debts now. Most Chapter 7 cases, though, are no asset cases in which no distribution is paid to creditors because all of the assets are exempt.

The 2005 amendments to the Bankruptcy Code made debts arising in a divorce non dischargeable in Chapter 7, without any action required by the non debtor spouse. As a result, debts to even up the distribution of marital assets or obligations to hold the other spouse harmless from existing debts survive a Chapter 7 discharge. These obligations remain dischargeable in Chapter 13.

Child and spousal support debts in bankruptcy

Child support, alimony, family support: it is all non dischargeable in bankruptcy. Nonetheless, if you owe back support, bankruptcy might help you get control of your support obligations by eliminating other creditors who compete for your dollars or by creating a Chapter 13 plan for the cure of support arrears.

Bankruptcy might also provide a forum in which any disputes about what is owed or has been paid can be determined. A bankruptcy judge won't revisit support orders made by a family law court, or modify support for the future, but might sort out accounting issues as to the amounts owed.

In Chapter 13, support is a priority claim, which must, by law, be paid **in full** over the life of the Chapter 13 plan. Support has a higher priority than even taxes. The automatic stay protects you from all creditor action to collect back debts while you propose and perform on a Chapter 13 plan.

Don't be an ostrich!

Too often, the financially stressed spouse who should be paying support can't for reasons of job loss, illness, etc. The biggest mistake you can make is not attempting to get the court ordered support modified to fit the current circumstances. The current order will control what is owed each month, **now and forever**, until it is changed. It is virtually impossible to get a court to retroactively modify a support order, or to get any governmental agency collecting back support to compromise.

So, if circumstances have changed and you truly can't pay at the ordered level, go back to court to get it adjusted. Sticking your head in the sand on this issue is a mistake that will follow you forever until paid.

Bankruptcy and support claims

The Bankruptcy Code attempts to protect the rights of children and former spouses to collect support: whether it is called family support, alimony, or child support, the bankruptcy code makes it non dischargeable in bankruptcy. The recipient spouse does not have to do anything for the debt to be excluded from the discharge.

The automatic stay, which stops other court proceedings when a bankruptcy is filed, does not apply to actions to establish or modify a support order or to collect support from post petition wages.

Wage orders that deduct *current* support from the debtor's wages are not generally affected by the bankruptcy filing. Wage orders that collect *past due* support arguably are stayed in Chapter 7 and certainly stayed in Chapter 13.

Also, support is a priority claim for purposes of payment from the estate. Thus in a Chapter

13, payment of past due support is paid before unsecured creditors, and even before taxes. The recipient spouse must file a proof of claim to receive payment. Chapter 13 frequently works well for both the paying spouse (who is protected from other creditors while paying back support) and for the recipient spouse (who gets regular payments from the trustee made by the debtor voluntarily).

Bankruptcy and the division of property and debts in a pending divorce

The issues raised when one spouse in a divorce action files bankruptcy are complex and vary somewhat depending on the property and family laws of the state.

In general, the filing of a bankruptcy stops all court proceedings against the debtor; brings into the bankruptcy estate all property of the debtor and all community property of the debtor and his spouse; and upon entry of a discharge, relieves the debtor of personal liability for all dischargeable debts.

The family court *cannot* assign marital debts to the debtor after he has received a discharge and cannot make orders dividing the property of the debtor while the property is property of the estate. The family court *can* divide the property that the debtor exempts; after the exemption is allowed, that exempt property is no longer property of the estate.

The family court can continue to hear and decide issues relating to fixing support. Some courts will require an order from the bankruptcy court, specifically finding that motions to establish or modify support are outside the bankruptcy stay. See Relief from stay.

If you become involved in such a proceeding, get advice from an experienced bankruptcy lawyer. Find a lawyer.

Bankruptcy and enforcement of marital settlement agreements

The 2005 amendments to the Bankruptcy Code recently made non support obligations created in connection with a divorce or separation nondischargeable in Chapter 7 *without any action on the part of the non debtor spouse*. 11 U.S.C. 523 (a)15. Those same obligations ***are*** dischargeable in a Chapter 13.

Effect of listing a marital debt on the schedules

Just because a creditor is listed by the debtor on the bankruptcy schedules does not make the creditor's claim dischargeable. The debtor is **required** to list all debts on the schedules, even debts that are acknowledged to be non dischargeable. So, listing a debt to a spouse or former spouse does not show either an intent or perhaps the power to discharge the debt.

The dischargeability of the debt depends on the nature of the debt (support, property division, lien for equalizing payment, etc.). Support is non dischargeable without action on the part of the receiving spouse.

If you know about the bankruptcy, whether from the court or through the grapevine, you are charged with finding out what is going on and taking steps to protect your interests, if necessary.

How is my spouse affected if I file bankruptcy alone?

. Since a bankruptcy can be filed by one spouse without the other, this is one of the most common bankruptcy questions. There are several aspects of the answer.

A bankruptcy filing by one spouse does not bring the other spouse into bankruptcy. Neither does the bankruptcy of a spouse give the non filing spouse the full protection of the automatic stay or the bankruptcy discharge.

Joint debts

If you and your spouse are jointly liable to a creditor, the bankruptcy of one spouse does not relieve the other of paying the debt. Upon a bankruptcy, the creditor may look to the other spouse for payment, unless the bankruptcy case is under Chapter 13. If the debt is a consumer debt to be paid 100% through the Chapter 13 plan, the co debtor is protected by the codebtor stay in §1301.

Generally, marriage alone doesn't make both spouses personally liable for a debt. Liability on contracts such as home loans and credit cards arises by agreement between the creditor and the debtor. Only persons who signed the loan or credit application are liable for the debt.

A joint tax return, however, makes both spouses liable for the total of the tax due.

If you have joint debts, you can expect the bankruptcy to be noted in some way on the credit record of the non filing spouse. There is uncertainty in the law at the moment as to whether it is proper to mention the bankruptcy of one debtor on the credit report of a debtor who is not in bankruptcy.

Joint property

If you and your spouse own property together, that property may be included in the bankruptcy estate and be potentially available to pay creditors. In community property jurisdictions such as California, both halves of the community property comes into the estate: all of the community property is available to pay community creditors and any other creditors of the spouse who has filed. So the filing of one spouse could have significant impact on the other.

Community property discharge

When one spouse files bankruptcy in a community property state, the marital community enjoys the protection of the filing spouse's bankruptcy discharge. Section 524 of the Bankruptcy Code provides that any community property that the filing spouse and the non filer acquire after the bankruptcy is protected from creditors of the non filer who held a claim against the non filing spouse as of the date of the filing.

A creditor with a claim against the non filing spouse can only collect its debt from the separate property of the non filing spouse.

Creditors, despite the fact that the community property discharge has existed since at least the passage of the Bankruptcy Code in 1978, have a hard time believing that someone in a community property state gets the benefit of their spouse's bankruptcy discharge, but that's the law.

Credit reports

Each person has (or is supposed to have) a separate credit file for credit reporting purposes. Your debts, if yours alone, are not supposed to show in your spouse's credit file. Similarly, your bankruptcy should not show in your spouse's file if you have no joint debts.

Even so, it pays to monitor your credit file, since credit reporting, like so much else in life, does not always follow the law.

Future credit

The bankruptcy of one spouse will have some effect on the credit worthiness of the non filing spouse *if* they apply jointly in the future for a loan. The loan grantor will consider the credit rating of both applicants in making a lending decision. More on post bankruptcy credit.