

## Bankruptcy Abuse Prevention and Consumer Protection Act of 2005

# IMPACT ON THE FAMILY LAW PRACTITIONER

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### Introduction

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) was enacted April 20, 2005. Its enactment brought to an end a turbulent decade-long legislative reform initiative, the end product of which was described by Susan Jensen in "A Legislative History of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005," 79 *Am. Bankr. L.J.* 485, 485 (Summer 2005) as "one of the most comprehensive overhauls of the Bankruptcy Code in more than twenty-five years." This overhaul significantly changes consumer bankruptcy law by imposing many new requirements on debtors before bankruptcy relief will be granted. Included in the changes are significant modifications to the manner in which bankruptcy law and family law interact.

For the family law practitioner, knowledge of these changes is essential due to the frequency with which family law and bankruptcy issues overlap. We will outline the major changes to the Bankruptcy Code associated with family law, and note many new issues the family law practitioner must face as a result of BAPCPA's passage.

The list below briefly summarizes certain changes to the Bankruptcy Code most significant to a family lawyer:

- §101(14A) of the Bankruptcy Code is added to give a uniform definition to the term "domestic support obligation";
- §507(a)(1) of the Bankruptcy Code is amended to provide domestic support obligations a first priority claim among unsecured claims;
- §362 of the Bankruptcy Code is amended to expand the scope of the exceptions to the automatic stay for domestic support obligations, to include within the exception income



withholding orders, revocation of licenses, seizure of tax refunds and other common support collection techniques;

- §523(a) of the Bankruptcy Code is amended to broaden the scope of domestic support-related debts that are nondischargeable in a bankruptcy case;
- §547(c)(7) of the Bankruptcy Code is amended to broaden the scope of pre-petition payments on support debts that are not avoidable as preferences in a bankruptcy case; and
- The Bankruptcy Code is amended so that in order for a Chapter 11 or Chapter 13 debtor to obtain a confirmation of his plan with the accompanying discharge, that debtor must be current on all support payments.

## §101(14A): Definition of domestic support obligations

Under the Amended Code, a new term, “domestic support obligation,” is used whenever the Bankruptcy Code affects alimony, maintenance or child support payments. Section 101(14A) has been added to the Amended Code, which defines a “domestic support obligation” as a debt that accrues before, on or after the date of the order for relief, and which includes interest that accrues pursuant to applicable non-bankruptcy law. This definition broadens the scope of the obligations covered by the Bankruptcy Code, as it includes a debt owed to or recoverable by “(i) a spouse, former spouse, or child of the debtor, or such child’s parent, legal guardian or responsible relative; or (ii) a governmental unit.”

To qualify as a domestic-support obligation, the debt must be “in the nature of alimony, maintenance, or support (including assistance provided by a governmental unit) of such spouse, former spouse, or child of the debtor or such child’s parent, without regard to whether such debt is expressly so designated.” It must be “established or subject to establishment before, on, or after the date of the order of relief” pursuant to: (i) a separation agreement, divorce decree, or property settlement agreement; (ii) an order of a court of record; or (iii) a determination made in accordance with applicable nonbankruptcy law by a governmental unit. It does not apply to a debt assigned to a nongovernmental entity, unless it was assigned voluntarily by a spouse, former spouse, child or parent solely for the purpose of collecting the debt.

Prior to the implementation of BAPCPA, the former code defined these support-type obligations on a section-by-section basis, which led to some inconsistency throughout the former code. Now, under the amended code and with BAPCPA’s definition of domestic support obligation, there will likely be a uniform understanding of those family law debts and how those debts are addressed under the Bankruptcy Code.

## §507(a)(1): Priority of domestic support obligations

Under the amended code, §507(a)(1) of the Bankruptcy Code is amended to accord first priority status to allowed unsecured claims for domestic support obligations that, as of the bankruptcy petition date, are owed to or recoverable by a

spouse, former spouse, or child of the debtor, or the parent, legal guardian, or responsible relative of the child. First priority status is granted without regard to whether such claim is filed by the claimant or by a governmental unit on behalf of such claimant, on the condition that funds received by such unit be applied and distributed in accordance with non-bankruptcy law. In contrast, under the former code, allowed unsecured claims for debts owed to a spouse or former spouse for alimony, maintenance or support of a spouse or child had seventh priority unsecured status.

The change impacts the priorities, which determine the order in which claims are paid from the property of the bankruptcy estate. In addition to elevating the priority of domestic support obligations under the amended code, what is included as a domestic support obligation is expanded. By elevating domestic support obligations to first priority status, these obligations have priority over all unsecured claims in a bankruptcy case, including most administrative claims. Administrative claims include professional fees incurred during a bankruptcy case. However, in the context of confirming a Chapter 13 plan, under the

amended code, courts continue to hold that administrative claims, including professional fees, must be paid either before or concurrently with the payments to other creditors. See 11 U.S.C. §1326(b)(1). Thus, in a Chapter 13 case, administrative claims may be paid in full prior to domestic support obligations, as long as the deferred payment of domestic support obligations will include full payment during the life of the Chapter 13 plan.

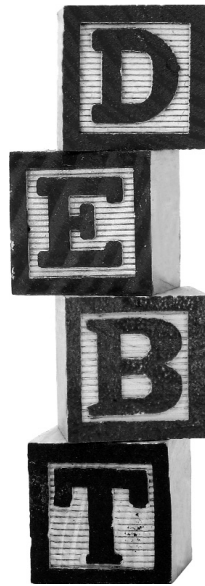
Unless a domestic support creditor agrees to accept a lesser payment, that creditor will be fully paid before other unsecured creditors, as long as there are sufficient assets in the estate to allow a distribution to unsecured creditors.

## §362: Automatic stay and exceptions thereto

Generally, upon the commencement of a bankruptcy proceeding, all prior judgments and enforcement actions against the debtor are stayed automatically. However, the Bankruptcy Code enumerates certain exceptions to this general rule. Prior to the implementation of BAPCPA, under §362(b)(2) of the former code, relevant examples of such exceptions to the automatic stay were for actions or proceedings (1) for the establishment of paternity; or (2) for the establishment or modification of an order for alimony, maintenance or support.

BAPCPA makes several revisions to the automatic stay provisions of the Bankruptcy Code, all of which appear to broaden the scope of the exceptions to the automatic stay for support-related proceedings. First, BAPCPA replaces the reference to “alimony, maintenance or support” in §362(b)(2)(A) with the term “domestic support obligations,” which is broader than the former reference in the former code.

Second, BAPCPA adds to the exceptions to the automatic stay actions or proceedings concerning: (1) child custody or visitation; (2) the dissolution of a marriage (except to the extent such proceeding seeks division of property that is property of the estate); and (3) domestic violence.



Third, BAPCPA permits as an exception to the automatic stay the “withholding of income that is property of the estate or property of the debtor for payment of a domestic support obligation under a judicial or administrative order.”

Fourth, BAPCPA authorizes the reporting of overdue support owed by a parent to any consumer-reporting agency pursuant to section 466(a)(7) of the Social Security Act.

Fifth, BAPCPA permits the interception of tax refunds as authorized by sections 464 and 466(a)(3) of the Social Security Act or analogous state law.

Finally, BAPCPA allows medical obligations, as specified under Title IV of the Social Security Act, to be enforced notwithstanding the automatic stay.

These changes could have a significant impact on child support collection practices. A common procedure used in collecting support payments is an income withholding order. Under the former code, the withholding of a debtor’s income was barred by the automatic stay upon the filing of a bankruptcy petition if the debtor’s income was property of the bankruptcy estate. Now, after the implementation of BAPCPA, under the amended code, the use of income withholding orders is expressly excepted from the automatic stay.

Moreover, under the amended code, a debtor’s driver’s license, professional or occupational license or recreational license can be withheld, suspended or restricted as a result of the debtor’s failure to pay a domestic support obligation without regard to the automatic stay. Further, the Amended Code adds an exception to the automatic stay to allow support creditors to seize tax refunds, which should make it less troublesome for support creditors to collect from debtors in bankruptcy cases.

The legislative history behind the addition of the foregoing provisions included the following:

“This key provision will mean that support deducted from an employee’s wages by an employer and paid to the support creditor will not be interrupted. This provision applies to both the ongoing support obligations and support arrears. In addition, other means of enforcement will remain available after the filing of a bankruptcy petition. Such enforcement tools include: (1) the revocation or non-renewal of drivers, professional and recreational licenses; (2) the reporting of overdue support to credit reporting agencies; (3) the interception of tax refunds to pay support arrears; and (4) the collection of medical support obligations.” Stmt. of Phillip L. Strauss, Dep’t of Child Support Svcs., San Francisco, reprinted in *22-4 Am. Bankr. Inst. J.* 6 (May 2003).

As a result, the changes to the automatic stay provisions of the Bankruptcy Code implemented by BAPCPA will likely have a profound effect on support creditors in receiving payment from debtors upon the filing of a bankruptcy case.

## **§523(a)(5) & (15): Nondischargeability of certain debts**

Other important changes to the family law practitioner brought about by BAPCPA are those made to §§523(a)(5) and 523(a)(15) of the Bankruptcy Code, which address the nondischargeability of debts in a bankruptcy case. Generally, one of the

major benefits a consumer debtor seeks by filing for bankruptcy is obtaining a clean slate by receiving a discharge of all pre-petition debts upon the completion of the bankruptcy case. Under §523 of the Bankruptcy Code, however, certain debts maybe excepted from discharge and would need to be paid even upon the completion of the bankruptcy case.

Under the former code, §523(a)(5) excepted from discharge all domestic obligations for support, alimony or maintenance to a spouse, former spouse or child of the debtor. Further, under the former code, non-support obligations and property distribution obligations also were excepted from discharge under certain circumstances. However, under the former code, a debtor maintained the ability to seek to discharge non-support obligations and property distribution obligations.

Under the amended code, all domestic support obligations, as defined in §101(14A), are excepted from discharge. Further, under the amended code, all debts to a spouse, former spouse or child incurred in the course of a divorce or separation, whether or not designated as a “domestic support obligation,” are excepted from discharge in a bankruptcy case.

To summarize the implications of the changes to §523, a recent treatise on the effects of BAPCPA states that the impact of the changes to §§523(a)(5) and (15) are as follows:

“Essentially, the combination of amended §§523(a)(5) and (15) would be to exclude from discharge all marital and domestic relations obligations, whether support in nature, property division, or hold-harmless, provided that they were incurred in the course of a divorce or separation or established in connection with a separation agreement, divorce decree, or other order of a court of record or a determination made in accordance with state or territorial law by a governmental unit.” Hon. William Houston Brown & Lawrence Ahern III, *2005 Bankruptcy Reform Legislation with Analysis*, 32 (2005).

However, while BAPCPA does add some certainty into the discharge arena where it did not exist before, questions may still arise in certain cases.

For example, under the former code, several courts had ruled that attorney fees arising out of divorce proceedings owed by the debtor to a former spouse were dischargeable notwithstanding §523. While it appears that the changes made by BAPCPA to §§523(a)(5) and (15) cause these types of debts to fall within the nondischargeability provisions, these sorts of issues that fall along the edges of the amended code will still most likely have to be decided by the courts in the coming months and years.

The final significant change to the dischargeability provisions of the Bankruptcy Code relates to the timing requirements for filing nondischargeability complaints. Under the former code, complaints under §523(a)(5) could be filed at any time, but complaints under §523(a)(15) could only be filed within 60 days of the date of the first meeting of the creditors. Under the Amended Code, just as under §523(a)(5), complaints under §523(a)(15) can be filed at any time, “and the debtor’s discharge would automatically exclude both (a)(5) and (a)(15) debts from discharge unless a complaint for determination is filed.”

## **§547(c)(7): Protection of domestic support claims against preference actions**

Under the Bankruptcy Code, payments made (1) to or for the benefit of a creditor; (2) on account of a debt of the debtor; (3) while the debtor was insolvent; (4) on or within 90 days before the filing of the petition; and (5) that enables the creditor to receive more than she would under a Chapter 7 proceeding, is an avoidable transfer that can be recovered by a debtor or a trustee appointed for the debtor. The former code, however, contained an exception to a debtor's or trustee's ability to avoid and recover payments made by a debtor to a spouse, former spouse or child for alimony, maintenance or support.

The implementation of BAPCPA has changed the Bankruptcy Code so as to except from avoidance and recovery any payment made by a debtor that falls within the term "domestic support obligation," as defined in §101(14A).

Thus, after BAPCPA, under §547(c)(7) of the amended code, all domestic support payments made by a debtor within 90 days prior to the filing of the bankruptcy will remain with the support creditor and cannot be avoided.

## **Requirements for obtaining confirmation and discharge in cases involving domestic support obligations**

One other significant change to the Bankruptcy Code put in place by BAPCPA is the establishment of self-executing checkpoints within the Bankruptcy Code to ensure continuing payment of domestic support obligations by debtors. For example, BAPCPA added a new provision to the Bankruptcy Code, providing that if a Chapter 13 debtor fails to make any payment on a domestic support obligation that first became payable post-petition, the support creditor may move to have the case converted to a chapter 7 or to have the bankruptcy case dismissed entirely. Additionally, a Chapter 13 debtor may not obtain a discharge of debts at all unless the debtor certifies he has paid off all domestic support obligations. Finally, BAPCPA amends the Bankruptcy Code to require a Chapter 11 debtor demonstrate that it is current on domestic support

obligations in order to confirm a Chapter 11 plan. Since confirmation of a plan is a requisite predecessor to a Chapter 11 discharge, the requirement that all post-petition Chapter 11 debts be paid in full limits the debtor's ability to obtain a discharge. Moreover, in Chapter 11 bankruptcy cases, a support creditor has the power to require payment in full of all domestic support obligations on the effective date of the plan.

## **Miscellaneous BAPCPA provisions affecting family law issues**

BAPCPA also amends the Bankruptcy Code to require trustees in Chapter 7, 11, 12 and 13 cases to provide certain notices to child support claimants and governmental enforcement agencies. For example, the amended code now requires trustees to provide written notice to a domestic support creditor of the right to use the services of a state child support enforcement agency established under §§464 and 466 of the Social Security Act in the state where the support creditor resides for assistance in collecting child support during and after the bankruptcy case. The amended code requires this notice (i) include the address and telephone number of the agency; and (ii) explain the claimant's right to payment under the applicable chapter of the Bankruptcy Code. Moreover, if the debtor is granted a discharge, the trustee must then notify both the child support claimant and the state agency that the debtor was granted a discharge, as well as provide them with the debtor's last known address. Further, the trustee must also provide the name and address of the debtor's last known employer and the name of each creditor holding a debt that is not discharged or that was reaffirmed.

Finally, BAPCPA amends the Bankruptcy Code to make exempt property liable for nondischargeable domestic support obligations, notwithstanding any contrary provision of applicable non bankruptcy law.

## **Conclusion**

BAPCPA has made significant changes to consumer bankruptcy law. The changes aim to prevent debtors from using the bankruptcy system as a way to avoid support obligations, while at the same time attempting to ease the support creditor's ability to obtain payments. ©