

BANKRUPTCY PETITIONS? BE PREPARED!

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Certain steps should be taken to protect the Association in the event of the filing a Bankruptcy proceeding by one of the Owners. Procedures should be in place in the event that the delinquent owner has no other choice than to file for Bankruptcy. It is possible that those procedures will never be used, but prudent planning is always advised.

When an Owner does file for Bankruptcy, it will most likely affect the amount and way the Association can collect delinquent assessments, which he or she owes, and alters the steps and procedures normally taken in collecting the same.

There are steps that the Association can take and steps that cannot be taken when an Owner files Bankruptcy. It is advisable to contact the licensed Collection Agency used by the Association and the Association's attorney when the Association becomes aware of the filing. This is recommended even if the notice is not in writing, but is heard by way of another owner. Any notices should be immediately forwarded to both of the above parties.

Types of Bankruptcy

Chapter 7 - Straight Bankruptcy – This type of bankruptcy is called “straight bankruptcy or liquidation”. It involves the prompt sale and conversion of all the individual's or corporations non-exempt property to cash and payment to the creditors to the extent that it is possible. It can be either voluntary (started by the debtor himself) or involuntary (started by the debtor's creditors.)

The Bankruptcy laws establish the order in which creditors are paid. Where the Association is in order of creditors will affect whether it is paid what is owed and, if so, how much. Typically, an Association receives a small percentage of the amount it is owed when an owner chooses this type.

Chapter 11 - Business Reorganizations – This type is called a “reorganization” because it is designed to allow for an orderly payment to creditors that enables a corporation to continue. Chapter 11 involves the development of a plan to pay off debts in a timely manner. Once a judge approves a plan as “fair and equitable,” it is binding and discharges all debts not provided for under the plan.

Creditors usually receive more of what they are owed under a Chapter 11 than a Chapter 7. However, they don't necessarily receive all they are owed.

Chapter 13 – Wage Earner's Plan - This type is used to reorganize personal or non-corporate debt. A plan is submitted to a judge for paying off all or nearly all of the debt over a specified period of time. Chapter 13 sets limits to the amount of debt that can be involved and the time period for repaying it. Creditors do not have to agree to the plan.

Under Chapter 13, any insolvent debtor who is a wage earner (earns wages, salary, or commissions) can formulate and file a plan with the court that provides the debtor with additional time to pay-off unsecured creditors. The debtor's plan must provide that future earnings will be subject to the supervision and control of the trustee until these debts are satisfied. A plan made in good faith and acceptable to the unsecured creditors will be confirmed by the court. Should the wage earner ultimately be unable to pay the debts, Chapter 7 liquidation is still an available alternative.

The Trustee is a person appointed by the Bankruptcy Court to take charge of debtor estate, to collect assets, to bring suit on debtor's claims, to defend actions against it, and otherwise administer debtor's estate; he has power to examine debt, to initiate actions to set aside preferences, etc.

Again, a creditor has more of a chance of being repaid under Chapter 13 than Chapter 7.

What Should You Do?

It is extremely important that the Association has a formal written Collection Policy, which is distributed to all owners at least once a year, advisedly with the budget annually and to all new owners with the other rules provided in escrow. The Collection Policy must be in compliance with the Association documents, which can also provide for remedies outside of the courts.

A Collection Policy should establish a clear policy, which educates the owners of their obligations and the consequences of not meeting those obligations on time. If the Owners are informed about their obligations and the consequences of not meeting them, they are more likely to avoid delinquent payments.

The Collection Policy will, however, provide a checklist of timeframes and steps to be taken for Management or the Association to remain consistent with all Owners. It is important to treat the Board, Committee and "*really nice people*" equally as the largest number of claims submitted against the Directors and Officer insurance is for inconsistent actions of the Association.

Following the checklist will enable the Association to be a "secured" creditor prior to the owner filing either type of Bankruptcy. A Secured Creditor is one who has been given a special pecuniary (monetary) assurance of payment of his debt. The lien has been placed on the property prior to the owner filing for Bankruptcy, which means the "debt is not exposed to danger; safe; so strong, stable or firm as to insure safety and financial security." (Black's Law Dictionary – Sixth Edition)

It is easy to see then why the Association should follow their Collection Policy consistently and reached the Secured Creditor portion of their policy quickly for the added protection should the Owner file for Bankruptcy.

Please keep in mind that the owner must pay his post petition (written request to the court for an order after notice) payments. If the Owner does not pay the Post Petition Assessments, the Association can ask the Bankruptcy Judge for authority to proceed with the foreclosure of the property. The assessments that are levied after the filing can be treated as any other homeowner and the process should be followed to include late fees, etc.

(This information has been provided to help individuals understand the different types of Bankruptcy's that Owners can file. It is not meant to replace legal advice during the proceedings and should not persuade the use of the appropriate professional help during the proceedings.)