BANKRUPTCY
AND
YOUR FAMILY LAW CASE

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I. GENERAL BANKRUPTCY

To understand how a bankruptcy impacts a divorce or post-decree family law matters, a general understanding of basic bankruptcy is necessary. There are generally two types of bankruptcy that interact with obligations arising from a dissolution action and/or a dissolution decree. A Chapter 7 is a straight liquidation process. Any and all assets owned by the debtor on the date of filing can become property of the bankruptcy estate. Any debts existing on the date of filing are typically subject to a discharge. Usually, earnings of a debtor after the date of filing are not important in a Chapter 7 proceeding.

A Chapter 13 is an opportunity for a debtor to repay creditors over a period of time. All debts that exist on the date of filing constitute obligations to be dealt with under the Chapter 13 plan. Those debts fall into several categories. The treatment a debt is afforded under the plan typically depends upon the category of that debt.

Priority debts include costs of the administration of the bankruptcy, tax obligations, and (under the new BAPCPA) domestic support obligations. The second category of debt is secured debt. Common examples of secured debt dealt with in a Chapter 13 are a mortgage obligation or a vehicle repayment. Under certain circumstances, those obligations are able to be modified by the Chapter 13. Finally, the lowest category of debt is the unsecured debt.

The debtor is responsible for proposing a plan to the Bankruptcy Court. The ongoing earnings of the debtor during the term of the plan are under control of the Bankruptcy Court and it is the debtor's obligation to propose a repayment plan utilizing the greater percentage of his disposable income during the term of the plan. The debtor typically makes weekly or monthly payments to the Chapter 13 Trustee. The trustee collects those funds and at periodic intervals distributes monies to the various creditors pursuant to the terms of the confirmed plan.

Assets owned by the debtor on the date of filing are important because to have a plan confirmed, the plan must provide creditors with at least what they would receive under a Chapter 7 liquidation. If a debtor has assets in excess of his exemptions, that value must be paid to the creditors under the Chapter 13 plan.

Assuming the debtor is able to get a plan confirmed and fully fund and complete the plan, certain debts receive a discharge as a result of that Chapter 13. Under 11 USC §1328, subject to certain exceptions, the Court will discharge the bulk of the debtor's unsecured debt.

The best relief to a debtor is to obtain a Chapter 7 discharge. Nevertheless, there are a number of reasons why a debtor may choose to file a Chapter 13. One significant reason arises from the enactment of BAPCPA. Specifically, in order to qualify for a Chapter 7 case, the debtor must pass what is known as the "means test." The means test measures the income of the debtor against national IRS standards for living expenses. The scope of this seminar does not warrant a detailed analysis of the means test, however if a debtor makes too much money per year and does not pass the means test that debtor likely will only be allowed to file a Chapter 13. Additionally, if a debtor has past obligations or mortgage arrearages, a Chapter 13 provides a very effective remedy of relief for that debtor. Likewise, if a debtor has a child support arrearage, that child support arrearage can be paid under the Chapter 13 plan. Finally, as will be discussed in more detail later, certain non-support

related domestic support obligations may be able to be discharged in a Chapter 13 that would not be able to be discharged in a Chapter 7.

II. AUTOMATIC STAY

One of the significant benefits of filing a bankruptcy is the invocation of the automatic stay. Regardless of the chapter under which relief is sought, the automatic stay becomes effective as of the moment of filing.

The automatic stay is designed to protect the status quo of the debtor during the course of the bankruptcy proceedings and to prevent virtually all collection efforts by creditors against the debtor unless and until the Bankruptcy Court orders otherwise. The automatic stay prevents:

1. The commencement, or continuation of any Court proceedings.

2. Execution by a judgment creditor against the debtor or property of the bankruptcy estate (such as wage garnishment, bank garnishment, execution sales).

3. Any action to obtain property of the debtor or exercise control over the property of the debtor (repossession of automobiles).

4. Any act to create, perfect, or enforce a lien against a property of the debtor.

5. Any act to collect, assess, or recover any claim against the debtor that arose prior to the date of filing (stops harassing debt collection calls).

6. And generally, any action whatsoever to enforce any kind of claim that existed prior to the date of filing against the debtor.

There are certain enumerated actions which are not prevented or stopped as a result of the automatic stay. These are contained in 11 USC § 362 (b).

The provisions of the automatic stay generally continue to prevent any action against property of the estate (such as repossession or mortgage foreclosure) until that property is no longer property of the bankruptcy estate. Additionally, with respect to any direct activity against the debtor, the stay continues until the earliest of :

1. the time the case is closed;
2. the time the case is dismissed; or
3. the time the discharge is granted or denied.

Additionally, in the event the creditor believes that the stay is applicable to action the creditor would like to initiate, that creditor may file what is known as a Motion for Relief from Stay and in such motion request either a termination, annulment, modification, or further conditioning of the stay. To be successful, the party in interest must show that there is a lack of adequate protection to the interest of the moving party and if the action is against property of the estate (such as mortgage foreclosure), that the debtor did not have any equity in the property and that the property is not

necessary to an effective reorganization of the debtor. Relief from the stay is to be granted by the Court thirty (30) days after such a request unless, after notice and a hearing, the Court orders the stay continued in some format until a final hearing.

BAPCPA provided certain amendments to § 362 which are of significant importance to family law attorneys. A copy of the amended language is attached as Exhibit A. Under 11 USC §362(b)(2), the filing of the petition does not operate as a stay with respect to the following:

1. The commencement or continuation of a civil action or proceeding
   a. for the establishment of paternity;
   b. for the establishment or modification of an order for domestic support obligations;
   c. concerning child custody or visitation;
   d. for the dissolution of marriage, except to the extent that such proceedings seeks to determine a division of property that is property of the estate; or
   e. regarding domestic violence.

Further, the filing of bankruptcy relief does not prevent:

1. The collection of a domestic support obligation from property that is not property of the estate (remember that post-filing earnings of a debtor do not constitute property of the estate in a Chapter 7).

2. The withholding of income that may be property of the estate for payment of a domestic support obligation.

3. The withholding, suspension, or restriction of a driver's license, a professional occupational license, or a recreational license under state law as specified in §466(a)(16) of the Social Security Act.

4. The reporting of overdue support owed by a parent to any consumer reporting agency.

5. The interception of a tax refund.

6. The enforcement of a medical obligation (as specified under Title IV of the Social Security Act.)

The impact of the automatic stay will be discussed more fully, however it is relatively safe to say that when Congress implemented these changes, it intended to send a message that the filing of a bankruptcy does not provide an immediate halt to most family law actions. The sole exception would be the distribution of property in connection with a dissolution when that property was property of the bankruptcy estate.

III. PROPERTY OF THE ESTATE

Immediately upon filing a petition for relief under the United States Bankruptcy Code, an estate is created. Under §541, any interest the debtor has in property either beneficially or actually, constitutes property of the bankruptcy estate. Once the debtor files for relief, the debtor has

absolutely no power or authorities to transfer, sell, encumber, or in any way dispose of property of the estate.

Additionally, upon filing the petition for relief, a trustee is appointed with respect to every Chapter 7 and Chapter 13 case. In a Chapter 7 case, the trustee stands in the shoes of the debtor. The trustee is charged with the responsibility of investigating the affairs of the debtor. This is typically fulfilled by the debtor appearing at a First Meeting of Creditors. That first meeting usually is scheduled about thirty (30) days after the date the bankruptcy is filed. The meeting is presided over by the trustee, and it is the obligation of the debtor to provide the trustee with all information requested by the trustee.

Essentially, the trustee's obligations are twofold. First of all, the trustee is charged with the responsibility of determining what assets the debtor has (property of the estate) which can be seized and liquidated. The trustee then reviews claims filed by creditors and distributes any proceeds received as a result of the bankruptcy estate to those creditors pursuant to an order of the Court. The second prong of the trustee's inquiry concerns whether or not the debtor has complied with the provisions of the Bankruptcy Code or if the debtor is engaging in bad faith, unscrupulous conduct, and/or criminal conduct. In such a case, the trustee will typically refer the case to the United States Trustee's Office or the United States Attorney's Office for further proceedings.

While the general rule is that all property owned by the debtor on the date of filing constitutes property of the estate, certain property is allowed to be retained by the debtor pursuant to the exemption statutes. The federal Bankruptcy Code sets forth exemptions, however Congress granted to each state, the power to opt out of the federal exemptions. Indiana has done so. Consequently, any bankruptcy filed in Indiana is governed by the Indiana exemption. A complete copy of the Indiana Exemption Statute is found at IC §34-55-10-2. Additionally, please be aware that there are significant other exemption statues scattered throughout the Indiana Code. Essentially, a debtor filing in Indiana is allowed to protect the following:

1. Up to $17,600 of equity in the debtor's principal residence;

2. Up to $9,350 in personal property;

3. Up to $350 in cash, bank accounts, and intangibles;

4. All interest in real estate owned as tenants by the entireties except to the extent that certain joint debts are to be discharged;

5. Any interest in an educational IRA; and

6. Any interest in a tax qualified retirement account (including IRA's, 401(k)'s, defined benefit plans).

In the event of a joint filing, each debtor may claim the above exemptions.

By claiming property that is exempt, this property is determined to not constitute property of the bankruptcy estate. Any assets which exceed the debtor's exemptions do constitute property of the bankruptcy estate. Upon determining assets, the trustee will then seek to administer those assets

and reduce them to cash. If the trustee determines that insufficient assets exist to warrant an administration, a no asset report is filed with the Court.

IV. DISCHARGE

The point of filing a Chapter 7 bankruptcy is to obtain a discharge of indebtedness. Pursuant to 11 USC §524, a bankruptcy discharge:

1. Voids any judgment that imposes personal liability against the debtor;

2. Serves as an injunction against any act or attempt to enforce or collect the debt as a personal liability of the debtor; and

3. Serves as an injunction against any act or attempt to enforce or collect a debt from property of the debtor.

There are a number of reasons enumerated in 11 USC §727(a) which prevent a debtor from getting a general discharge of his indebtedness. The bulk of these involve some type of dishonesty or bad faith on the part of the debtor. There is typically a presumption in a bankruptcy that the debtor is entitled to a fresh start and consequently, denial of a discharge in general is not a common occurrence.

Also within the context of a Chapter 7 bankruptcy, any creditor has the right to assert that although the debtor is entitled to a general discharge, the debtor is not entitled to discharge the debt of that particular creditor. The exceptions to the dischargability of a individual debt are contained in Section 523 of the Bankruptcy Code. There are two portions of Section 523 that specifically deal with family law obligations. Both deal with domestic support obligations, and as such, attention first must focus upon the definition of what a domestic support obligation entails. The term "domestic support obligation" (DSO) is defined in 11 USC § 101(14A).

In general, a DSO is a debt owed to a spouse which is in the nature of alimony, maintenance, or support, and which is established by agreement or Court order in connection with a family law litigation. To qualify as a DSO, the debt may not be assigned to a non-governmental entity. Although many debts involved in a Chapter 7 bankruptcy are those that exist prior to the date of filing, a DSO can mean a debt that accrues prior to the date of filing or after the date of filing. (This becomes important in the context of a Chapter 13). Additionally, although interest accruing on unsecured obligations or under secured obligations typically ceases as of the date of filing, interest on a DSO continues to accrue after the date of filing.

To qualify as a DSO, the obligation must be owed to, or recoverable by, a spouse or former spouse, or a child of the debtor, or that child's parent, legal guardian, or responsible relative, or a governmental unit. This is an extremely broad definition and includes virtually every type of arrangement under which a child is cared for by a non-parent family member. Additionally, Congress intended to protect the right of governmental entities to collect child support in the event the party to whom the domestic support obligation was originally owed has assigned that right to the government (Title IV-D).

To qualify as a DSO, the character of the obligation must be in the nature of alimony, maintenance, or support regardless of whether there is a specific designation that the obligation is alimony, maintenance, or support. This clause has created a substantial amount of litigation in the past and will likely create additional litigation in the future. (Query: Is payment of a joint credit card pursuant to a divorce decree considered to be in the nature of alimony, maintenance, or support? What about attorney fees owing to counsel for one of the parties?)

The obligation must also have been established under a separation agreement, a divorce decree, a property settlement agreement, an order of the Court of record, or a determination made in accordance with applicable non-bankruptcy law by a governmental unit. The law does not specifically state that a separation agreement or a property settlement agreement must first be approved by a Court in order to qualify as a DSO.

Finally, to qualify as a DSO, the obligation fails to retain its characterization as a DSO under bankruptcy law if the debt is assigned to a non-governmental entity unless the obligation was voluntarily assigned by the DSO recipient for the purpose of collecting the debt. This would certainly appear to encompass a Title IV-D prosecutor enforcing a child support obligation as well as an assignment by the support recipient to a collection agency or other type of debt collection service.

Under the code, two types of DSO are considered non-dischargeable. Under prior law, 11 USC §523(a)(5) provided that obligations in the nature of support, maintenance, or alimony were non-dischargeable. Under BAPCPA, the general discharge in Chapter 7 does not discharge an individual debtor from any debt "for a domestic support obligation." Although the language is slightly different under the new law, the effect is still the same.

In addition to debts in the nature of support, alimony, or maintenance, 11 USC §523(a)(15) also excepts from the general discharge, debts "to a spouse, former spouse, or a child of the debtor, and not of the kind described in paragraph (5) that is incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree, or other order of the Court of record, or a determination made in accordance with state or territorial law by a governmental unit." This is a significant deviation from pre-BAPCPA law. Prior to October of 2005, it was generally accepted that debts in the nature of child support, maintenance, or alimony were non-dischargeable. Unfortunately, this is not the only type of obligation ordered to be paid pursuant to family law litigation. The obligation of one spouse to pay debt obligations such as mortgages, car loans, medical bills, and credit cards do not fall under the exclusion from discharge under 523(a)(5). Under the old law, it was necessary that a spouse file an adversary complaint in the Bankruptcy Court to determine that property settlement obligations were non-dischargeable. Failing to file such a lawsuit allowed those debts to be discharged. In the event a former spouse filed a Complaint to determine the non-dischargeability of property settlement obligations, the Court invoked a balancing test to determine if discharging the debts would impose a greater hardship on the non-filing spouse or the debtor. This provision created substantial litigation and negotiations because a determination of the dischargeability of property settlement obligations was a factual determination to be made by the Judge on a case by case basis. It also imposed a sense of urgency on the creditor spouse to hire an attorney and file a Complaint to determine the dischargeability of those debts within sixty days after the first date set for the First Meeting of Creditors.

Although the old law provided an opportunity for the creditor spouse to contest the

dischargeability of property settlement obligations, the remedy was of very little benefit. The cost the creditor spouse incurred in retaining counsel and proceeding in Federal Bankruptcy Court was significant. Even if the creditor spouse were to convince the Bankruptcy Judge that the debt should not be dischargeable, there was no guarantee that the debtor spouse would actually pay the third-party creditors. Hence, additional litigation was typically necessary.

In connection with BAPCPA, Congress substantially streamlined the process with respect to property settlement obligations. Any debt a spouse is ordered to pay in connection with a divorce proceeding, even though not characterized as support, alimony, or maintenance, is considered non-dischargeable pursuant to new sub-section 15.

Under the old law, either party could file a Complaint to determine the dischargeability or non-dischargeability of support related claims at any time. If a party intended to contest the discharge of property settlement obligations, that adversary complaint had to be filed within the sixty day time period after the first scheduled First Meeting of Creditors. Failure to do so meant that debts under sub-section 15 were in fact discharged by the general discharge. This statute put the burden on the creditor spouse to initiate the adversary proceeding within this very brief time limitation or forever be bound with a determination that the debts were, in fact, discharged. BAPCPA has changed this. Under 11 USC §523(c)(1), debts falling under sub-section 15 (property settlement debts) do not have the requirement of an adversary proceeding to be discharged. By removing sub-section 15 from 523(c)(1), Congress has elevated property settlement debts to those of support, alimony, and maintenance as unquestionably non-dischargeable obligations. This is a significant change which family practitioners need to contemplate.

Simply categorizing a debt in a property settlement agreement or order will not assure that the debt will be treated in that fashion in the bankruptcy proceeding. Debts to a spouse, former spouse, or child alimony, maintenance or support will be non-dischargeable if the liability is truly in the nature of alimony, maintenance or support. *In re Goin*, 808 F.2d 1391 (CA7 1987). The liability would be determined non-dischargeable only when it is actually for support or maintenance of the former spouse or child of the debtor. The bankruptcy courts will look beyond the labels used by the parties to determine the intent of the parties and whether the obligations created are to remain the nature of alimony, maintenance or support. *In re Reines*, 142 F. 2d 970 (7th Cir. 1998); *In re Garrard*, 151 B.R. 598 (Bankr. M.D. Fla. 1993). The bankruptcy courts may actually hold evidentiary hearings to determine whether the debt is for alimony, maintenance or support regardless of how that debt is identified in the dissolution court proceeding.

A clause in a property settlement whereby a debtor waives the benefit of a discharge is invalid against public policy. *In re Markizer*, 66 B.R. 1014 (Bankr. S.D. Fla. 1986). Any agreement to waive the benefit of a discharge in a bankruptcy proceeding is void and the bankruptcy courts will not give those clauses any effect. See also *In re Kriger*, 2 B.R. 19 (Bankr. Ore. 1979). While written agreements may provide evidence of whether the debt is non-dischargeable, the bankruptcy courts will look for extrinsic evidence to determine whether the obligation is in fact non-dischargeable. *In re Hart* 130 B. R. 817 (Bankr. N.D. Ind. 1991); *In re Yeates*, 807 F.2d 874 (10th Cir. 1986). The bankruptcy court must attempt to ascertain the parties intentions in determining whether an obligation created in a divorce court setting is dischargeable in bankruptcy. Determining whether the obligation is non-dischargeable in the bankruptcy forum is an issue to be determined by federal

bankruptcy law and not by state law. *In re Hart,* 130 B.R. 817 (Bankr. N.D. Ind. 1991); *Shaver v. Shaver,* 736 F.2d 1314 (9th Cir. 1984). State law should be looked to by the bankruptcy court to provide guidance as to whether the award is in the nature or characterizes property settlement, eventually dischargeable, or an award of support, alimony or maintenance and, therefore, non-dischargeable. Bankruptcy courts cannot simply ignore well developed state law of domestic relationships. However the bottom line is that federal law and not state law controls the determination of dischargeability in the bankruptcy forum.

If the issues of support and property settlement have been litigated in the dissolution proceeding, those decisions may be binding upon the bankruptcy court. The Supreme Court and numerous court of appeals have concluded that collateral estoppel is applicable in non-dischargeability proceedings. *Kelly v. Robinson,* 479 U.S. 36; 107 S. Ct. 353 (1986); *Klingman v. Levinson,* 831 F. 2d 1292 (7th Cir. 1987).

When presented with a non-dischargeability issue, the bankruptcy court needs to look to the preclusion laws of the state to determine the preclusive affect of the state court decree. *In re Hart,* 130 B.R. 817 (Bankr. N.D. Ind. 1991). Under Indiana law, issue preclusion or collateral estoppel bars relitigation of a particular issue which was adjudicated in a prior action. *Starzensky v. City of Elkhart,* 87F.2d 872 (CA 7 1996); *Studio Art Theater of Evansville, Inc. V. City of Indianapolis, Ind.,* 76 F.3d 128 (CA 1996). In Indiana to establish preclusion, a party must show (1) the issues sought to be precluded must be the same as involved in a prior litigation; (2) determination of the issue must have been actually litigated; (3) determination of the issue must have been essential the final judgment; and (4) the party against whom issue preclusion is invoked must have been fully represented in the prior action. *Gentry v. Duckworth* 65 F.2d 555 (CA-7 1995).

Generally, a state court judgment will be *res judicata* on that issue in the bankruptcy proceeding. See *In re Dempster,* 182 B.R. 790 (Bankr. M.D. Ill. 1995). If a state court, in the course of the dissolution, determines factual issues using legal standards applicable to the Bankruptcy Code, the findings in the state court will be binding in non-dischargeability cases. See *In re Maurice,* 138 B.R. 890 (Bankr. N.D. Ill. 1992).

In regard to issue preclusion and *res judicata,* a distinction must be maintained between debtors' ability to contractually waive their rights to discharge certain obligations and the debtor's ability to enter into an agreement which stipulates as to the underlying facts that the bankruptcy court may rely upon to determine if the debts are non-dischargeable. The debtor cannot contract or waive the rights to a discharge or the dischargeability of certain debts; the debtor can stipulate as to the facts or be held to the facts determined in a prior forum upon which a bankruptcy court make a decision.

A growing trend exists whereby the Rooker-Feldman Doctrine is advanced as precluding the bankruptcy court from revisiting or interpreting decisions made or settlements reached in prior state court litigation. The Rooker-Feldman Doctrine is premised upon two Supreme Court cases, *Rooker v. Fidelity Trust Co.,* 263 U.S. 413 (1923) and *District of Columbia Court of Appeals, et. al. v. Feldman,* 460 U.S. 462 (1983). These two cases interpret 28 U.S.C. §1257 which provides that the district court shall be a court of original jurisdiction. The Rooker-Feldman Doctrine stands for the proposition that "district courts do not have subject matter jurisdiction over challenges to state court

decisions and judicial proceedings." *Charchenko v. City of Stillwater*, 47F. 2d 981, 983 (CA 8 1995). Therefore, under the Rooker-Feldman Doctrine, the lower federal courts lack jurisdiction to engage in appellate review of state court determinations. The Rooker-Feldman Doctrine is based on the principal "that district courts have only original jurisdiction; the full appellate jurisdiction over judgments of state courts in civil cases lies in the Supreme Court of the United States." *Gash Assoc. v. Village of Rosemont, Illinois*, 995 F.2d 726, 728 (CA 7 1993). The Rooker-Feldman Doctrine precludes a federal action if the relief requested would effectively reverse the state court decision or void the state court ruling.

The Rooker-Feldman Doctrine was embraced in the Southern District of Indiana by the Honorable Frank J. Otte in the case *Bratton v. Daw, (In re: Bratton,* Chapter 13 Case No. IP-98-133-FJO-13, Adversary No. 98-136 (Bankr. S.D. Ind. December 7, 1998) upheld on appeal on other grounds IP-98-1743-C-B/S (S.D. Ind. May 21, 1999). The parties in *Bratton* had entered into a property settlement agreement in a prior dissolution proceeding. The property settlement agreement provided that husband was to pay $175,000.00 to the ex-wife. In the "Miscellaneous Section" of the property settlement agreement language was inserted categorizing the $175,000.00 obligation in the nature of child support. At trial, the ex-wife's attorney acknowledged that classifying the $175,000.00 as support was customary language he asserted in property settlement agreements in an effort to protect his clients in the event of future bankruptcies. The support provisions of the property settlement agreement required the husband to pay the ex-wife monthly support obligations of approximately $920.00 and he was current on those support payments up through the time of trial.

The ex-wife asserted that the Rooker-Feldman Doctrine precluded the bankruptcy court from interpreting the property settlement agreement and classifying the debt as property settlement. Judgment dated December 7, 1998 upheld on appeal May 21, 1999. *Bratton v. Daw*, IP98-1743-C-B/S upheld on other grounds. Notwithstanding that the property settlement agreement was drafted by the ex-wife's counsel and should be construed against the ex-wife; and notwithstanding that the settlement agreement was an agreement and not a decision by the court, the bankruptcy court still held that the Rooker-Feldman Doctrine applied. The decision underscores that counsel must be exceedingly cautious in allowing language to be inserted in a property settlement agreement which classifies the nature of obligations. (Query: Wouldn't this entire debt be non-dischargeable in a Chapter 7 under new §523(a)(15) whether or not it was called support or maintenance? What about in Chapter 13?)

If a debt is truly in the nature of alimony, support or maintenance, the debt is non-dischargeable pursuant to 11 U.S.C. §523(a)(5). The state court dissolution action has concurrent jurisdiction with the bankruptcy forum to address these issues. If the debt falls within 11 U.S.C. §523 (a)(5), the debt is non-dischargeable. If there is a gray area as to whether the debt asserted truly is in the nature of alimony, support, or maintenance, the non-filing spouse may want to initiate a motion in the state court dissolution proceed, for a determination as to whether the debt is nondischargeable under 11 U.S.C. §523(a)(5). The state court may be more inclined to protect its prior decision and find the debt in the nature of support.

The mere statement or labeling of a debt as in a nature of alimony, support or maintenance in a decree does not render such for purposes of §523(a)(5). The courts must look at the totality of the circumstances and all facts involved prior to making a determination as to the identity of the debt. Included on a list of factors to be considered are the following:

1. If the obligation terminates on death or remarriage of either spouse;

2. Whether the payments balance disparate income;

3. Whether the obligation is payable in a lump sum or installments over a period of time;

4. Whether the parties intended to create an obligation of support;

5. Whether the assumption of a debt has the effect or providing the support necessary to insure the daily needs of the former spouse and any children; and

6. Whether an assumption of a debt is effective providing support necessary to insure a home for the spouse or minor children.

The courts must weight the factors, not just tally them to determine the true nature of the debt. *In Re Calhoun*, 715 F. 2d 1103 (6th Cir. 1983).

V. CHAPTER 13

For a debtor spouse looking for bankruptcy relief, there is very little promise under Chapter 7 after BAPCPA. The only realistic opportunity is for a debtor spouse to look to the provisions of Chapter 13 for some type of limited relief. Remember that under Chapter 13, the debtor must pay to the creditors an amount equal to the equivalent creditors would receive in a Chapter 7 liquidation. A Chapter 13 is available to an individual with regular income and may also include a debtor that is self-employed and incurs trade credit in the production of income through that business. 11 U.S.C. §1304(a). If a Chapter 13 debtor proposes a plan which is confirmed by the Bankruptcy Court and that debtor substantially completes the plan, the debtor may be entitled to a discharge with respect to certain unpaid debts which could include property settlement debt obligations. One significant problem is that the debtor's plan devotes the future disposable income of the debtor to payment of pre-existing debt obligations. Prior to October, 2005, that plan would have a maximum of three years. Now, a Chapter 13 is presumed to have a plan term of five years. For individuals who have been plagued with debt obligations, exerting the discipline to make planned payments for sixty months is an enormous burden.

In proposing a plan, the debtor is not allowed to prefer one class of creditor against another if those classes fall within the same category of debts. If your creditor spouse was obligated to make mortgage payments for the non-creditor spouse and children and has failed to do so, a Chapter 13 may provide an appropriate remedy. If the plan is confirmed and the mortgage arrearage cured, the non-creditor spouse may not be adversely affected. Under 11 U.S.C. § 1301, the automatic stay in a Chapter 13 is applicable to protect a co-debtor. This protection is subject to certain enumerated exceptions, however the co-debtor's stay could protect the non-filing creditor spouse if the debtor were proposing a Chapter 13 plan to cure mortgage arrearages required to be paid by that debtor under a divorce decree.

In proposing a Chapter 13 plan, the debtor has always been required to pay priority claims during the term of the plan. The BAPCPA has substantially impacted this obligation as a result of the new

priority afforded to domestic support obligations. The type of debts entitled to priority in bankruptcy proceedings are set forth in 11 U.S.C. §507. Priority debts typically included costs of administration of the bankruptcy action, wage claims, and taxes. As a result of BAPCPA, the first priority debt now applies to DSO's. The new §507 provides:

The following expenses and claims have priority in the following order:

(1) First:

(A) Allowed unsecured claims for domestic support obligations that, as of the date of the filing of the petition in a case under this title, are owed to or recoverable by a spouse, former spouse, or child of the debtor, or such child's parent, legal guardian, or responsible relative, without regard to whether the claim is filed by such person or is filed by a governmental unit on behalf of such person, on the condition that funds received under this paragraph by a governmental unit under this title after the date of the filing of the petition shall be applied and distributed in accordance with applicable non-bankruptcy law.

(B) Subject to claims under subparagraph (A), allowed unsecured claims for domestic support obligations that, as of the date of the filing of the petition, are assigned by a spouse, former spouse, child of the debtor, or such child's parent, legal guardian, or responsible relative to a governmental unit (unless such obligation is assigned voluntarily by the spouse, former spouse, child, parent, legal guardian, or responsible relative of the child for the purpose of collecting the debt) or are owed directly to or recoverable by a governmental unit under applicable non-bankruptcy law, on the condition that funds received under this paragraph by a governmental unit under this title after the date of the filing of the petition be applied and distributed in accordance with applicable non-bankruptcy law.

(C) If a trustee is appointed or elected under section 701, 702, 703, 1104, 1202, or 1302, the administrative expenses of the trustee allowed under paragraphs (1)(A), (2), and (6) of section 503 (b) shall be paid before payment of claims under subparagraphs (A) and (B), to the extent that the trustee administers assets that are otherwise available for the payment of such claims.

As a result of this modification, the highest level of priority is afforded to DSO's where 507(a)(1)(A) provides the highest class of priority to domestic support obligations owing directly to an individual. Immediately thereafter in 507(a)(1)(B) are all claims for domestic support obligations owed directly to a governmental entity (such as Title IV-D). This distinction is important in determining the contents of a plan proposed by the debtor.

Pursuant to 11 U.S.C. §1322 (a)(2), the Chapter 13 plan must "provide for the full payment, in deferred cash payments, of all claims entitled to priority in §507 of this title, unless the holder of a particular claim agrees to different treatment of such claim." Since DSO's are entitled to priority under §507, the traditional plan must provide for payment of all child support obligations to be paid in full during the term of the plan. A carve out is provided in §1322(a)(4) for child support that is being collected by a governmental entity rather than the creditor spouse. That section states that "notwithstanding any other provision of this section, a plan may provide for less than full payment of all amounts owed for a claim entitled to priority under §507(a)(1)(B) only if the plan provides that all of the debtor's projected disposable income for a five year period beginning on the date that the first

payment is due under the plan will be applied to make payments under the plan." As a result, the debtor must pay child support owed directly to a spouse or other individual, however if the debt is owed to a governmental entity, and the debtor devotes his entire disposable income to a five year plan, those amounts owing to the governmental entity need not be paid in full in order for the plan to be confirmed.

The ability of a debtor to obtain a discharge under Chapter 13 is specified in §1328. A new provision added by BAPCPA requires that after the debtor has completed all payments owed to the plan, the debtor must file a certification that all amounts payable under a domestic support order that were due on or before the date of the certification (including pre-petition obligations) have been paid. This is a significant change from former law and again underscores the importance Congress has placed upon payment of child support and DSO's. 11 U.S.C. §1328(a). Under 1328 (a)(2), certain debts are specifically excluded from the Chapter 13 discharge. Section 523(a)(5) debts (child support, alimony, and maintenance) are not discharged by the Chapter 13 discharge. Noticeably absent from the list of debts not subject to discharge in this paragraph are debts falling under §523(a)(15). Those are the property settlement obligations. Consequently, if the debtor confirms and completes a Chapter 13 plan, property settlement obligations not paid in full under the plan should be eligible for a discharge under Chapter 13. Herein lies the controversy concerning whether debt obligations are in the nature of support or maintenance. If so, the debt is not discharged. If the debt is truly a property settlement obligation, the debt will likely be discharged.

The code does provide some remedy to a Chapter 13 debtor who is operating under a confirmed plan but finds that he is unable to complete the plan payments. Under §1328(b), after a judicial determination by the Bankruptcy Court that the debtor was unable to complete payments due to circumstances beyond the debtor's control and that the debtor paid at least the equivalent that creditors would have received under a Chapter 7 and that a modification of the plan is not practical, the Court may grant a discharge. Nevertheless, under §1328(c), the hardship discharge specifically excepts from that discharge, any debt "of a kind specified in §523(a) of this title." 11 U.S.C. §1328(c)(2). This section does not differentiate between the (a)(5) or the (a)(15) exceptions under §523 and consequently, it appears that the hardship discharge does not discharge the debtor from either child support related obligations [§523(a)(5)] or property settlement obligations [§523(a)(15)]. Consequently, the only relief afforded to a debtor with respect to property settlement obligations is the successful completion of a confirmed Chapter 13 plan.

VI. ASSORTED BANKRUPTCY/DIVORCE ISSUES

The enforcement of family law orders and judgments occupies a significant amount of time family lawyers spend in a day to day practice. The choice of remedy typically becomes whether or not a contempt action is appropriate or the creditor/spouse must enforce his or her rights pursuant to T.R. 69 proceedings supplemental to execution. In Article I, §22 of the Indiana Constitution, there is a proscription against imprisonment for debt. Nevertheless, "child support obligations have long been enforceable by contempt in Indiana." *Pettit v. Pettit* 626 NE 2d 444, 445 (Ind. 1993) An action for contempt can be divided into civil contempt or criminal contempt. Criminal contempt is aimed at vindicating the public authority of the Court and is typically not applicable in cases involving enforcement of domestic obligations. Civil contempt is for the benefit of a party who has been injured or damaged by the failure of another to conform to a Court Order issued for the private benefit of the aggrieved party. *Duemling v. Fort Wayne Community Concerts, Inc.* 188 NE 2d 274

(Ind. 1963). In *Thomas v. Woolen* 266 NE 2d 20 (Ind. 1971) special damages and attorney fees were recoverable in connection with the finding of civil contempt. The Court found there was no limitation on the assessment of damages both to compensate the injured party and to coerce the offending party.

Nevertheless, contempt proceedings are not allowed to enforce the payment of a sum certain of money whether it is payable in installments or in a lump sum. In *Bahre v. Bahre* 230 NE 2d 411 (Ind. 1967), the Indiana Supreme Court opined that the party could not be held in contempt of court for his failure to pay attorney fees arising out of a divorce proceeding. However, in *Mosser v. Mosser* 729 NE 2d 197 (Ind. App 2000) attorney fees pursuant to a provisional order were allowed to be enforced by contempt. Additionally, in *State Ex Rel Shaunki v. Endsley* 362 NE 2d 153 (Ind. 1977), the Indiana Supreme Court was faced with the issue of whether an alimony judgment constituted a simple money judgment or whether it could be collected through contempt proceedings. The Court stated "unquestionably there are some aspects of a divorce or marriage dissolution decree that properly may be the subject of a Court order, but the payment of the sum of money, whether in a lump sum or installments, as an incident of settling the property rights of the parties, is not among them." In this case, the ex-wife was entitled to a money judgment for a distribution of property in the sum of $35,000. The Court determined that whether or not this payment was to be made in installments or in a lump sum, contempt proceedings were inappropriate.

Even though contempt is typically not applicable to collect a sum certain of money, the creditor/spouse may enforce its obligations as provided for in proceedings supplemental to execution under T.R. 69. Consequently, money judgments are to be enforced pursuant to proceedings supplemental rather than contempt. *Cowart v. White* 711 NE 2d 523 (Ind. 1999).

Contempt powers have been allowed to enforce obligations to transfer property from one spouse to the other. *State Ex Rel Dale v. Superior Court of Boone County* 299 NE 2d 611 (Ind. 1973).

The Indiana Supreme Court case of *Cowart v. White* should be consulted in connection with all divorce related enforcement proceedings in which a bankruptcy is involved. The Indiana Supreme Court engaged in a scholarly yet practical analysis of the interaction between Mr. Cowart and Ms. White resulting from their divorce decree and the subsequent bankruptcy filing of Mr. Cowart. The court held that the dissolution court could enforce duties to sell and divide property imposed by the dissolution decree through contempt proceedings without violating the bankruptcy injunction created as a result of the §524 discharge in favor of Mr. Cowart. The Court determined that the initial determination should be whether or not the obligation to pay a fixed sum of money was discharged in the bankruptcy. If it was, no further enforcement could take place. If the debt obligation was not discharged, then if it was an obligation to pay a sum of money, it should be enforceable through proceedings supplemental but not through contempt. Finally, if the obligation did not include a requirement to pay a fixed sum of money, it became the proper subject for contempt proceedings and then a determination should be made as to what orders of contempt the Court had the power to issue including payment of money as punishment for the contempt.

Mr. Cowart was obligated to sell two parcels of real estate and to divide the proceeds with his former wife. He failed to do so, and the Court determined that his ongoing obligation to sell and divide the proceeds of the sale did not constitute a debt as determined by the Bankruptcy Code. The

Court referred to the bankruptcy case of *Peterson v. Peterson* decided by the United States Bankruptcy Court in the Western District of Missouri in 1991 (133 BR 508). The Court conducted an analysis of the obligations and determined that if a payment obligation is directly linked to the sale of property, the obligation is more likely to be part of a property division and therefore dischargeable. Additionally, an obligation to pay an amount in a lump sum or over a short period of time is more likely to be considered property settlement. Since this case was prior to BAPCPA, the Court conducted an analysis of whether or not certain obligations were in the nature of support and maintenance and therefore, non-dischargeable. The Court determined that certain obligations were non-dischargeable and that others had been discharged by Mr. Cowart's bankruptcy discharge.

The decision is also informative with respect to the issue of the dischargeability of an attorney fee award. Again, deciding the facts under old law, the Court held that an obligation to pay attorney fees could be non-dischargeable in bankruptcy if it was in the nature of maintenance or support. The Court cited the cases of *In Re: Balvich*, 135 BR 327 (Bankr. ND Ind. 1991) and *In Re: Kanabe* 8 BR 53 (Bankr. SD Ind. 1980). The Court determined that the trial Court had looked at the financial resources of the parties and determined that if attorney fees were not based on the financial needs of the parties, they constituted a Property Settlement Agreement which would be dischargeable. Under BAPCPA, attorney fees would be non-dischargeable regardless of the nature of the obligation unless a Chapter 13 was involved. The Cowart court remanded the issue of attorney fees to the trial court. If the obligation to pay attorney fees survive the bankruptcy, the Court specifically asserted that T.R. 69 was available to Ms. White to enforce the obligation. Again, contempt proceedings are not allowed to enforce a money judgment obligation.

Finally, the Court was asked to review the Trial Court's order requiring Mr. Cowart to pay money damages as a result of his failure to sell the real estate and divide the proceeds with Ms. White. The Supreme Court held that once a party had been determined to be in contempt, money damages could be awarded to compensate the aggrieved party for injuries incurred as a result of a contempt. In determining the amount of damages, the inconvenience and frustration suffered by the aggrieved party are to be taken into account.

On New Year's Eve of 2003, the Indiana Court of Appeals rendered its decision in *Dawson v. Dawson* 800 NE 2d 1000 (Ind. App. 2003). The former husband was required to pay a second mortgage on the marital residence. The Court analyzed whether T.R. 69 or contempt proceedings were appropriate and determined that the Trial Court was entitled to use its contempt powers to enforce an order that requires performance instead of payment of a fixed sum to coerce a party into compliance with an underlying order or decree. The Court of Appeals cited *Cowart* as controlling authority. The husband filed an action for bankruptcy in 1999 but did not list his obligation to pay the second mortgage as a debt. Nevertheless, he became unable to meet that obligation. Judge David of the Boone Circuit Court found the husband to be in violation of the obligation of the second mortgage and apparently found that this was a willful violation of the Court order because he ordered Mr. Dawson to serve 90 days in jail unless he purged himself of contempt either by satisfying or refinancing the second mortgage. The Court of Appeals determined that the sanction was appropriate as a result of Mr. Dawson's "persistent contemptuous conduct."

The issue of contempt was also dealt with in the Indiana Court of Appeals in *Burrell v. Lewis* 743 NE 2d 1207 (Ind. App. 2001). In that case, the Court determined that the father's filing of a bankruptcy action did not stay enforcement by the mother of her claim for collection for child

support. The Court determined that the stay did not prevent the Trial Court from exercising jurisdiction to hear the contempt motion and to award attorney fees and costs to the mother, notwithstanding the pending bankruptcy.

The issue was also addressed in *Mitchell v. Mitchell*, 871 NE 2d 390 (Ind. App. 2007). The trial Court was not precluded from enforcing the terms of a hold harmless agreement by contempt. The Court recited that *Coleman v. Coleman*, 539 NE 2d 34 (Ind. App. 1989) and Dawson had decided that judgments requiring one party to pay the other party a fixed sum of money were not enforceable by contempt. In this case, contempt could be used to enforce an obligation for the ex-husband to pay and hold ex-wife harmless from payment of the mortgage and credit card debts because they were not fixed sums of money.

VII. PROPERTY OF THE BANKRUPTCY ESTATE

Certain issues have arisen as to whether or not some marital property could constitute property of the bankruptcy estate if one party files bankruptcy. A bankruptcy trustee in the Northern District of Indiana asserted that a child support arrearage was a sum certain of money owed by the father to the mother. When the mother filed bankruptcy, the trustee asserted that the support arrearage judgment was property of the bankruptcy estate and that the trustee took over this right. The trustee asserted that collection of the support arrearage was his obligation for the benefit of the unsecured creditors of the bankruptcy estate. The Indiana Supreme Court determined that the child support was not an asset of the mother and therefore was not property of the bankruptcy estate. The right to collect a support arrearage belongs solely to the mother and the bankruptcy trustee had no claim to it. *Warsco v. Hambright* 735 NE 2d 844.

A recent bankruptcy case from Florida should cause divorce attorneys some concern. Both parties had lived apart for many years. They had negotiated a Property Settlement Agreement which apportioned the bulk of the property to the wife. Prior to the divorce court approving and ordering the Decree of Dissolution, the husband filed bankruptcy. The bankruptcy court for the Middle District of Florida determined that since ownership of the property had not vested in the wife as a result of an enforceable divorce decree, all property was potentially property owned by the husband and therefore property of the bankruptcy estate. *In Re: Hoyo* 340 BR 100 (MDFLA 2006). Presumably, the bankruptcy trustee would have to determine what interest the debtor/husband had in the jointly owned marital property. Then a determination would have to be made whether or not the husband had proper exemptions with respect to any of that property. Finally, if any property remained as non-exempt, presumably it would be property of the bankruptcy estate which could be sold and used to pay the debts of the husband. This is a convoluted fact scenario that in practice would likely not result in a substantial recovery for the trustee, however certainly must have created nightmares for the divorce lawyers.

Two recent bankruptcy cases have dealt with the issue of fraudulent transfers as a result of a divorce decree. A bankruptcy trustee of one spouse has the right to file adversary proceedings to set aside what amount to fraudulent transfers. *In Re: Knippen* 355 BR 710 (ND Ill. 2006), the parties engaged in substantial child related litigation. Once the child related matters were resolved, the parties were able to effectively enter into an agreed property settlement. The husband received certain property including a business which ostensibly had no value. The wife received the marital

residence subject to a first and second mortgage. The wife then sold the marital residence to a family member. The family member paid the sum of $200,000 of which approximately $155,000 went to pay the first and second mortgages. The remaining money went to the former wife to use for living expenses. To this point, the facts seem quite consistent with what Indiana practitioners encounter. Nevertheless, the bankruptcy trustee took the position that this transfer provided the wife with greater equivalent value than the husband received. The trustee asserted that an equal division of property was contemplated by the Property Settlement Agreement, however as a result in a significant equity in the real estate, the wife received more assets than the husband. The bankruptcy court ultimately determined that the trustee should have a judgment against the former wife "as well as the transferees" for the sum of $20,000 which represented the extra value the wife received as a result of receiving title to the real estate. This is an extremely harsh result and the court stated that the court took no pleasure in such an award, but felt that the decision was legally sound. From a review of the decision, it appears that the husband did not present any evidence whatsoever concerning a valuation with respect to the business transferred to him. Presumably, had he (or his ex-wife) been able to convince the bankruptcy judge that the property distribution was, in fact, an equal distribution, a different result would have been achieved. Nevertheless, this case illustrates the far reaching effect a bankruptcy can have on divorce proceedings.

When confronted with a similar case, the Bankruptcy Court for the District of Oregon determined that there was no fraud, either actual or constructive, involved in the Property Settlement Agreement between debtor/husband and his former wife and as a result denied the trustee's action to set aside the Property Settlement Agreement as a fraudulent transfer. *In Re: Bledsoe* 350 BR 513 (D. Oregon 2006).

VIII. HOLD HARMLESS/INDEMNIFICATION

Many divorces result in one spouse being obligated to make payments on joint obligations. The payor/spouse is to then hold the other spouse harmless from any non-payment. Under prior Indiana law, if a debtor listed his former spouse as a creditor pursuant to the hold harmless agreement, not only would the debts to third parties discharged but also the obligation to the former spouse pursuant to the hold harmless was discharged. On June 5, 2007, the Bankruptcy Court for the Eastern District of Arkansas rendered a decision in *In Re: Douglas*. In this case, the parties were divorced in Arkansas in February, 2006 and the debtor filed his petition for Chapter 7 relief in June, 2006. Pursuant to the divorce decree, debtor was ordered to pay joint credit cards and vehicle debts in the divorce. He listed those obligations as creditors in his bankruptcy action. His ex-wife filed an adversary proceeding under BAPCPA and asserted that the debt obligations were domestic support obligations and as a result non-dischargeable. The court decided that "the joint debts which the State Court ordered debtor to pay in his divorce from Plaintiff, are non-dischargeable in this Chapter 7 bankruptcy." What meaning in a practical sense this decision has is hard to say. Certainly, the creditor is not able to enforce its debt obligation against the debtor because of his discharge. If the creditor asserts claims against the ex-wife, it would seem logical that she would only have claims against her former husband under the hold harmless agreement after she paid the third-party creditor. Future cases decided under BAPCPA will need to determine the actual effect of divorcing spouses in Indiana.