

**BANKRUPTCY REFORM FOR THE FAMILY LAW LAWYER:  
NEW CODE, NEW DAY**

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# BANKRUPTCY REFORM FOR THE FAMILY LAW LAWYER: NEW CODE, NEW DAY

## I. INTRODUCTION

### A. Scope Of Paper

On April 20, 2005, President Bush signed into law the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (the "Reform Act"). This ended an almost ten-year effort, primarily led by the banking and credit card interest, to substantially modify the United States Bankruptcy Code. While some of the provisions contained in the Reform Act became effective immediately, most of the changes to the Bankruptcy Code will take effect on October 17, 2005. The Reform Act is anticipated to have significant impact on how individuals seek (and obtain) relief from their debts in bankruptcy court.

The total impact of the Reform Act on the practice of bankruptcy law is beyond the scope of this paper. However, this paper will cover some of the basic changes impacting how individuals file for bankruptcy. The goal is to give the reader a flavor for how the Reform Act impacts individuals' rights when filing bankruptcy.

The second part of the paper will focus on how the Reform Act impacts specific issues where bankruptcy and family law coexist. In the opinion of the authors, the Reform Act makes the bankruptcy court a very unfavorable forum to attempt to escape family law obligations. In fact, the bankruptcy court may now be a more powerful forum than State court to enforce some family law obligations. Therefore, the changes discussed below will require family law attorneys to pay careful attention to what obligations they commit their clients to pay going forward.

### B. Sources And Acknowledgments

The authors wish to acknowledge the resources available on this topic including: *Family Law and Bankruptcy*, written by Diana S. Friedman and Joseph A. Friedman, presented at the State Bar of Texas' "Advanced Family Law Course" in August, 2000; *Dealing with Debt*, written by Carmen Rosita Rojo, presented at "Family Law on the Front Lines" in April 2001; *When the Wolf's at the Door: Pending Insolvency and Its Effect on Divorce*, written by Joseph A. Friedman and Ashley L. Amos, presented at State Bar of Texas in August 2001; *Dealing with Debt: Bankruptcy and Beyond*, written by Diana S. Friedman, Joseph A. Friedman and Ashley L. Amos, presented at "Family Law on the Front Lines" in March 2003; and *Synopsis of Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, written by Thomas J. Yerbich.

## C. Citation Convention

In order to keep references to the Bankruptcy Code clear between the old and new law, the old Bankruptcy Code references will be cited as "11 U.S.C. § \_\_\_\_ (2004)" and new Reform Act references will be cited as "11 U.S.C. § \_\_\_\_ (2005)." When no reference to a year is made, the referenced Bankruptcy Code Section was not materially changed by the Reform Act.

## II. THE "NEW" FILING FOR BANKRUPTCY

### A. Basic Bankruptcy Law

Bankruptcy law is codified under Title 11 of the United States Code, which is also referred to as the United States Bankruptcy Code. There are five different types of bankruptcy filings, specified by chapter, under the United States Bankruptcy Code. They are as follows:

- 1) Chapter 7 – Business entity and individual ;
- 2) Chapter 9 – Insolvent municipalities;
- 3) Chapter 11 – Reorganization of debt for mostly business entities;
- 4) Chapter 12 – Adjustment of debts with regard to the family farmer; and
- 5) Chapter 13 – Debtors propose a repayment plan.

Since Section 2.001(a) of the Texas Family Code defines lawful marriage as being between a man and a women, and the Reform Act's changes are in a large part focused on individual filings, the paper will concentrate on the types of bankruptcy relief available to individuals, as opposed to business entities.

The first significant impact of the Reform Act is the new limitations for individuals in order to qualify for bankruptcy relief. In the past, bankruptcy law's main theme was to provide a "fresh start" to honest debtors. Prior to the Reform Act, "there [was] a presumption in favor of granting the relief requested by the debtor." 11 U.S.C. § 707(b)(1) (2004). However, the Reform Act has modified the law by removing that favorable presumption, and replacing it with a specified test that obligates the court and the United States Trustee to inquire into the appropriateness of the relief requested by the debtor. In certain instances, the law now creates a presumption that the debtor is *abusing* the bankruptcy process! 11 U.S.C. § 707(2)(A) (2005).

Needless to say, the main theme may no longer be a "fresh start" for bankrupts. Instead, the Reform Act now protects the creditors from abusive filings by discouraging Chapter 7 (liquidation) filings, limiting exempt property (even if that property would be exempt under Texas law), and making a discharge much more difficult, expensive, and time consuming to obtain. In order to discuss how the Reform Act's changes impact family law clients, it is necessary for the reader to

become aware of the new “domestic support obligation” definition used in the Reform Act.

### B. New Definition-Domestic Support Obligation

A major change made in the Reform Act is the addition of the definition of “domestic support obligation.” The term domestic support obligation, (which is derived from the old non-dischargeable support language of 11 U.S.C. § 523(a)(5) (2004)), is defined as:

[A] debt that accrues before, on, or after the date of the order for relief in a case under this title, including interest that accrues on that debt as provided under applicable nonbankruptcy law notwithstanding any other provision of this title, that is

- A) 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;
- B) 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;
- C) established or subject to establishment before, on, or after the date of the order for relief in a case under this title, by reason of applicable provisions of –
  - 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; and
- D) not assigned to a nongovernmental entity, unless that obligation is assigned voluntarily by the spouse, former spouse, child of the debtor, or such child’s parent, legal guardian, or responsible relative for the purpose of collecting debt. 11 U.S.C. § 101(14A) (2005).

This broad definition appears to include any non-property division type of obligation that a family law client might incur during a divorce or SAPCR.

Consistent with the pre-Reform Act law under 11 U.S.C. § 523(a)(5) (2004), the new definition of a domestic support obligation establishes that such an obligation can be made via a separation agreement, divorce decree, or property settlement agreement. Furthermore, the Reform Act’s definition will also recognize child support established and/or enforced by the Office of the Attorney General or other governmental unit. 11 U.S.C. § 101(14A)(A)(ii) (2005).

The domestic support obligation also expands the old definition by addressing debts arising before or after filing and expressly permitting support claims to be asserted by governmental entities. 11 U.S.C. § 101(14A)(B) (2005). However, the definition excludes a support claim if it is assigned to a nongovernmental entity without the consent of the non-debtor’s spouse, unless the assignment is voluntary and only for purposes of collection. 11 U.S.C. § 101(14A)(D) (2005). Under this definition, it is unclear whether or not a “friend of court” or private company collecting child support under court order would be a governmental entity, or considered a voluntary assignment. Therefore, it is possible that these types of arrangements may possibly endanger the protections the Bankruptcy Code gives support obligations.

The most obvious use of domestic support obligation definition is to make support obligations non-dischargeable under 11 U.S.C. § 523(a)(5) (2004), just as they were in prior practice. Congress, however, has given domestic support obligation holders several more benefits related to enforcement of their claims in bankruptcy that are briefly outlined below, and discussed in more detail throughout this paper.

#### 1. Protection Of Domestic Support Claim Holders

The Reform Act now offers extensive protection for holders of domestic support claims which make bankruptcy virtually useless to those trying to avoid paying their domestic support obligations. With respect to domestic support obligations, the Bankruptcy Code (after the Reform Act becomes effective) provides that:

- a) Domestic support obligations are not dischargeable under any Chapter of the Code, 11 U.S.C. § 523(a)(5) (2005);
- b) Domestic support obligations are payable as a first priority claim in Chapter 7, subject only to the administrative costs of a trustee to the extent that the trustee administers assets that can be used to pay support costs, 11 U.S.C. §§ 507(a)(1)(C) (2005);

- c) Post-petition domestic support obligations must be paid on a current basis after filing a Chapter 11, 12 or 13 case, under penalty of denial of confirmation and/or dismissal of case, 11 U.S.C. §§ 1112(b)(P), 1208(c)(10), and 1307(c)(11);
- d) All domestic support obligations, even those owed prior to filing, must be paid under the plan in a Chapter 11, 12 or 13 case before a discharge is granted, 11 U.S.C. §§ 1141(d)(5), 1228(a) and 1328(a) (2005);
- e) The Automatic Stay does not apply to the collection of domestic support obligations to the extent collection is pursued against property that is not property of the estate and to the extent of existing wage withholding orders to remain in place, 11 U.S.C. § 362(b)(2) (2005);
- f) Payment of domestic support obligations are exempt from the trustee's avoidance powers in Chapter 5 of the Code, 11 U.S.C. § 547(c)(7) (2005); and
- g) Exempt property is liable to satisfy domestic support obligations *notwithstanding any State or Federal law to the contrary*. 11 U.S.C. § 522(c)(1) (2005); (overruling *In re Davis*, 170 F.3d 475 (5<sup>th</sup> Cir. 1999)).

This last point may make bankruptcy courts a better forum than State court for collection of support obligations. The significance of this change cannot be overstated, and it is discussed in full in Section III. However, before analyzing how bad bankruptcy is for debtors who owe on domestic support obligations, we will first describe how much harder Congress has made it for everyone to file bankruptcy.

### C. New Debtor's Duties And Prerequisites To Filing Bankruptcy

The Reform Act imposes new requirements for individuals before they are qualified to have their debt discharged. For example, an individual must attend a class from an accredited counseling agency within 180 days before the filing of the petition. 11 U.S.C. §§ 109(h) and 521(b) (2005). The debtor must then file a certificate of completion with the court under penalty of dismissal or denial of discharge. *See* 11 U.S.C. § 727(a)(11) (2005).

The prospective debtor must also file a statement of financial affairs, and provide copies of recent tax returns in order to obtain any relief. 11 U.S.C. § 521(e)(2)(A) (2005). Further, if requested by the trustee, the debtor must also establish his identity by providing a photo identification. 11 U.S.C. § 521(h) (2005). If the debtor

fails to provide any of the information under section 521, the case could be dismissed. 11 U.S.C. 521(i) (2005).

Generally, these are a few examples of how the Reform Act makes filing for bankruptcy relief more complicated. The Reform Act also took specific efforts to make it very difficult for individuals to file Chapter 7.

### D. Chapter 7 – Not The Easy Way Anymore

Chapter 7 bankruptcies are commonly thought of as a “liquidation” filing. Prior to the Reform Act, a debtor could simply turn over to the Chapter 7 Trustee his property that was not exempt under Texas’ favorable exempt property statutes (which in reality often meant surrendering nothing), and could thereby eliminate most of his obligations to pay unsecured debts. The process took about 120 days from filing to discharge. Further, it only required the debtor to attend a 10 minute meeting of creditors.

With the enactment of the Reform Act, Congress has restricted the number of people who can qualify for relief under a Chapter 7 by requiring the courts to apply an objective test as to whether the debtor has the “means” to pay something to his creditors over time. These tests are an effort to force more debtors to file for relief under Chapter 13, which requires payments over time through an approved payment plan.

#### 1. Presumption Of Abuse (“The Means Test”)

Section 707(b) has been amended to expand the grounds for the dismissal or conversion of a Chapter 7 case if an individual fails to satisfy a new “Means Test”. The Means Test is considered by many supporters of the Reform Act to be the heart of the Act. On the other hand, critics have noted that if Congress did any more to “protect” consumers, they might find themselves sleeping in cardboard boxes.

The failure to satisfy the Means Test allows both creditors and the United States Trustee to seek dismissal or conversion of a Chapter 7 filing to Chapter 11 or 13. 11U.S.C. §707(b) (2005). This has changed from prior law in which only the United States Trustee or the court, on its own motion, could seek dismissal due to a bad faith filing. The Reform Act also created an income level at which it is presumed that the debtor's filing is abusive. If abuse is presumed, the debtor could be required to participate in a five-year repayment plan under a Chapter 13 proceeding in order to obtain a discharge. 11 U.S.C. § 707(b) (2005).

To further discourage legal counsel from advising clients about filing Chapter 7 bankruptcies, Congress added provisions that allow creditors and the United States Trustee to seek sanctions against the debtor's lawyer if a Chapter 7 filing is found abusive. 11 U.S.C. 707(b)(4) (2005).

To determine if a debtor is eligible for Chapter 7 requires an analysis of the debtor's income, the debtor's allowable expenses (based on Internal Revenue Service guidelines), and the applicable State Median Income (based on census data as adjusted by Consumer Price Index data).

Basically, if a debtor's monthly net income exceeds the applicable median income by more than \$100.00, to \$166.66 (depending on amount of debt), the Means Test will be failed. Therefore, the debtor's filing is presumed to be abusive. 11 U.S.C. § 707(b)(1) (2005).

A brief discussion on how these numbers were obtained is discussed below. However, hopefully the United States Trustee will publish median income tables for their Districts prior to enactment, so that lawyers will not need to become mathematicians and statisticians.

## 2. Median Family Income

The median family income is based on the number of people in the household as follows:

- a) For a debtor in a household of one person, the median family income of the applicable State for one earner;
- b) For a debtor in a household of 2 to 4 individuals, the highest median family income of the applicable State for a family of the same or fewer persons; and
- c) For a debtor with more than 4 individuals in her household, the highest median family income in the applicable State for a family of four or fewer individuals, plus \$525.00 per person for each individual in excess of four. 11 U.S.C. § 704(b)(2)(A)-(B) (2005).

Under the Reform Act, "median family income" is calculated from the data collected by the Census Bureau for the most recent year. 11 U.S.C. § 101 (39A) (2005). However, if it is not calculated in the current year, it will be calculated on prior year's data and will be adjusted annually by the increase in the Consumer Price Index for all urban consumers during the period occurring between the most recent and current year. *Id.* If the debtor's current monthly income (discussed below) exceeds the applicable median income, the Means Test is applied to determine if the filing is possibly abusive.

## 3. Current Monthly Income

The term "current monthly income" is now defined as the average monthly amount received by the debtor (and the spouse if filing jointly) from all sources during the prior six months and ending on the last day of the month proceeding the filing date. 11 U.S.C. § 101(10A) (2005). This definition also includes all amounts regularly contributed by others for household expenses

such as child support. *Id.* However, the definition excludes Social Security payments or payments received by victims of war crimes, crimes against humanity, and/or terrorism. *Id.*

## 4. Allowable Expenses

"Allowable expenses" are now codified in the Reform Act. Specifically, the general amount of allowable expenses is determined by referring to both National and Local standards, along with reference to the Collection Financial Standards issued by the Internal Revenue Service. 11 U.S.C. § 707(b)(2)(A)(ii) (2005). Specific allowable expenses include:

- a) Debtor's expenses for payment of priority claims (like priority child support and alimony claims). 11 U.S.C. § 707(b)(2)(A)(iv) (2005).
- b) Necessary health insurance, disability insurance and health savings plans. 11 U.S.C. § 707(b)(2)(A)(ii) (2005).
- c) Expenses to maintain safety under the Family Violence Prevention and Services Act. *Id.*
- d) Expenses for the care of an elderly or chronically ill or disabled member of the household. *Id.*
- e) Up to \$1,500.00 (per year) for expenses of dependent minor children to attend a private or public elementary or secondary school. *Id.*
- f) Actual expenses for utilities in excess of the allowance specified in the Collection Financial Standards. *Id.*
- g) An additional 5% of the National Standards for food and clothing if reasonable and necessary. *Id.*

## 5. Calculations For The Means Test - Presumption Of Abuse

The Means Test is designed to determine if a debtor has the means to pay something toward general unsecured claims over a period time.

If the debtor's income exceeds the applicable median income, and the debtor has after all allowable expenses:

- a) less than \$100.00, no presumption of abuse;
- b) \$100.00, presumption of abuse arises, unless debt exceeds \$24,000;
- c) by \$150.00, presumption of abuse arises, unless debt exceeds \$36,000;
- d) by \$166.66; presumption of abuse arises, unless debt exceeds \$39,998.40;
- e) by more than \$166.66, presumption of abuse always arises.

11 U.S.C. § 707(b)(1)-(2) (2005).

#### 6. Putting It All Together--Dismissal Or Conversion

Generally, creditors have two options to request a dismissal or conversion of the debtor's case. First, if a debtor's income is above the applicable median and the Means Test has been failed, the creditor will have standing to seek dismissal or conversion. 11 U.S.C. § 707(b)(7) (2005). The second option for the creditor to seek dismissal or conversion is created if under the totality of the circumstances it is evident that the filing is abusive since no presumption of abuse arose under the Means Test, or if the Means Test has been successfully rebutted. 11 U.S.C. § 707(b)(3) (2005). From a procedural point, the United States Trustee must review all materials submitted by the debtor and file a statement no later than 10 days after the meeting of the creditors. 11 U.S.C. § 704(b)(1) (2005). The statement shall proclaim whether abuse is presumed under the Means Test. *Id.* If abuse is presumed, the trustee must file a motion to dismiss or convert the bankruptcy within 30 days after the filing of the statement. *Id.* Even if the Means Test is passed, the court or United States Trustee, may still seek dismissal on general grounds based on the totality of the circumstances. 11 U.S.C. § 707(b)(3) (2005).

One might question how a bankrupt debtor can afford to defend litigation based on an "abusive filing" when the debtor only has \$100.00 above the "minimum expenses" needed to live. However, Congress was not so inclined. Instead, unless the debtor can rebut the presumption of abuse, or qualifies for an exception, the court must dismiss, or (with the consent of the debtor) convert the Chapter 7 case to a Chapter 11 or Chapter 13 proceeding. 11 U.S.C. § 707(b)(1) (2005).

#### 7. Rebuttal Of Presumption Of Abuse

The presumption of abuse may be rebutted only by establishing exceptional circumstances such as a serious medical condition or a call to active duty in the armed forces. 11 U.S.C. § 707(b)(2)(B) (2005). In order to establish these special circumstances, the debtor is required to itemize each additional expense or adjustment and to provide documentation along with a detailed explanation. *Id.*

#### 8. Exceptions To Presumption Of Abuse

There is a specific exception with regard to the presumption of abuse in that the presumption does not apply to a disabled veteran whose indebtedness was incurred primarily during a period when on active duty or performing a homeland defense activity. 11 U.S.C. § 707(b)(2)(D) (2005).

In addition, the court may not dismiss a case under those circumstances if the debtor establishes by a preponderance of the evidence that the bankruptcy is necessary so that the debtor can satisfy a claim for a

domestic support obligation. 11 U.S.C. § 707(c)(3) (2005).

#### 9. Conclusion

Needless to say, the Reform Act has substantially altered the ability of individuals to seek quick relief in a Chapter 7 proceeding. Instead, the Reform Act pushes individuals to seek relief from payout plans under Chapter 13 and Chapter 11.

#### **D. Chapter 13: The New Preferred Chapter For Individuals**

The Chapter 13 bankruptcy is commonly referred to as the "payment plan bankruptcy". This proceeding generally allows for the discharge of both secured and unsecured debts after the debtor has made regular payments under an approved plan for 3 to 5 years.

Prior to the Reform Act, on a national basis, Chapter 7 insolvency proceedings were more commonly used by individual debtors. However, due to the substantial revisions to Chapter 7 (discussed above), it is predicted that the Chapter 13 will now be the only viable proceeding for the majority of modest income debtors. However, the Reform Act, also changed several aspects of Chapter 13 proceedings which directly impact family law clients.

##### 1. Support Payments Protected In Chapter 13

Under the Reform Act, domestic support creditors are protected from delays in receiving post-filing support payments by several mechanisms, as follows:

- a) Chapter 13 proceedings may be dismissed or converted if the debtor fails to make any domestic support payments that are due after the filing of the bankruptcy. 11 U.S.C. § 1307(a)(11) (2005). Therefore, it is imperative that the family law attorney, protecting the rights of the creditor spouse, pay particular attention to the payments made by the debtor during the pendency of the bankruptcy.
- b) During the confirmation hearing, the debtor must present evidence that he is current on all post petition domestic support payments. 11 U.S.C. § 1325(a)(8) (2005). Obviously, if you are representing a domestic support creditor who has not been paid, it is important to appear at the confirmation hearing and let the court know about the debtor's failure to keep current on a post petition basis.

##### 2. Interest On Non-Dischargeable Claims

Under a Chapter 13 bankruptcy, the payment plan must provide for the payment of interest on non-dischargeable claims, provided that the debtor has

sufficient disposable income to pay all other unsecured claims in full. 11 U.S.C. § 1322(b)(10) (2005). Since domestic support obligations are non-dischargeable, they are eligible for this treatment. Accordingly, review of the plan by the domestic support creditor is critical to determine if they can earn interest on past due support.

### 3. Debtor's Payments

Generally, the debtor must start making plan payments no later than thirty days from the filing of the petition. 11 U.S.C. § 1326(a)(1) (2005).

This rule reduces the amount of lag time between the start of the plan payments.

### 4. Confirmation Hearing And Discharges

At the confirmation hearing, the debtor must certify that he is keeping all of his post-petition domestic support obligations current. 11 U.S.C. § 1325(a)(8) (2005). As such, the confirmation hearing is an excellent opportunity to bring non-payment of domestic support obligations to the court's attention. Therefore, the domestic support creditor will want to pay careful attention to noticed dates for plan confirmation.

Generally, the confirmation hearing for approval of the payment plan is set after the meeting of the creditors. The meeting of the creditors typically occurs between 20 and 50 days after the Chapter 13 petition is filed. 11 U.S.C. § 341 (2005) and BANKR. R. 2003(a). The confirmation hearing must be held no less than 20 days, and no more than 45 days, after the date of the creditors meeting. 11 U.S.C. § 324(b) (2005). Therefore, the soonest that a domestic support creditor should expect a confirmation hearing would be about 40 days after the filing of the Chapter 13 bankruptcy.

In order for the plan to be approved at the confirmation hearing, it must provide for the full payment of pre-petition arrearages on domestic support obligations. 11 U.S.C. § 1325(a)(8) (2005). If it does not, the domestic support creditor should object. *Id.*

Moreover, for the debtor to obtain a discharge, the debtor must certify at the end of the plan process that all payments of the domestic support obligation as required by the plan have been completed. 11 U.S.C. § 1328(a) (2005). If it does not, the domestic support obligation creditor should again object. Since discharge occurs only after the debtor completes his plan payments, domestic support obligation creditors will need to monitor the debtor's Chapter 13 proceeding from beginning to end.

### 5. Notice Regarding Domestic Support Claims Under Chapter 13

The Reform Act now requires the United States Trustee (or a qualified individual appointed by the United States Trustee) to provide written notice to the holder of a domestic support claim of their right to use

the services of the State child support enforcement agency for assistance in collecting child support both during and after the insolvency proceedings. 11 U.S.C. § 1302(b)(6) (2005). Further, at the same time, written notice will be provided to such State child support agency of the claim and it will include in the notice the name, address and telephone number of the holder. 11 U.S.C. § 1302(d) (2005). Similar notice obligations to support creditors are also contained in Chapter 7 (11 U.S.C. § 704(a)(10) (2005), Chapter 12, 11 U.S.C. § 1202(b)(6) (2005), and 11 U.S.C. § 1106(a)(8) (2005)

If the debtor is able to obtain a discharge under a Chapter 13 insolvency proceeding, the trustee will provide written notice to such holder and to the State child support enforcement agency that the discharge was granted along with the last known address of the debtor and any last known information regarding the debtor's employer. 11 U.S.C. § 1302(d)(1)(C). The notice will also include the name of each creditor that holds a claim that has not been discharged, or if the debt was reaffirmed by the debtor. *Id.*

The purpose of this last provision is to allow the holder, or the State child support enforcement agency, the ability to request from the listed creditors information they may have about the debtor. 11 U.S.C. § 1302(d)(2)(B) (2005). This built in requirement to give information to the holder of a domestic support claim allows the information to be used for the pursuit of any future non-payment. This is important as many family law clients have limited financial resources in tracking down the location of the payor/debtor.

### 6. Modification Of Plan After Confirmation

The Reform Act has now codified the possibility of a reduced payment under the plan by giving a credit for the amount paid by the debtor to purchase health insurance. However, the insurance must be for the debtor and any dependent of the debtor (if the dependent does not otherwise have health insurance coverage). 11 U.S.C. § 1329(a)(4) (2005).

This health insurance exception benefits the debtors and their dependents. With the current increases in the rates of health insurance, this is a safety valve used to relieve some of this financial pressure.

## E. Chapter 11 As An Alternative

The current belief is that debtors who do not qualify for a Chapter 7 will probably proceed under Chapter 13. However, the benefits of a Chapter 13 are limited with regard to higher wage earners (*i.e.*, doctors, lawyers and other professionals). Specifically, under a Chapter 13 there are debt limitations for undisputed, unsecured obligations to be no more than \$307,675.00, and secured debts which cannot exceed \$922,975.00. 11 U.S.C. § 109(e) (2004). This may require higher wage earners to

file a Chapter 11—a proceeding requiring reorganization of the debt that was used by businesses in the past.

In order to accommodate individuals in Chapter 11 proceedings, Congress added several provisions which ultimately have the effect of making a Chapter 11 proceeding look more like a Chapter 13. A few examples would include making post-petition wages part of the property of the estate, and requiring the debtor to meet the disposable income distribution test for confirmation of the payment plan. 11 U.S.C. §§ 1115, 1129(a)(15) (2005).

Because Chapter 11 filings are relatively complex (and individual filings have been rare under the old Bankruptcy Code), the authors anticipate substantial litigation in the future. Although these issues are beyond the scope of this paper, one of the more interesting issues scholars have begun to identify is whether the use of involuntary Chapter 11 filings will violate the 13<sup>th</sup> Amendment to the United States Constitution prohibiting involuntary servitude. All the authors can say is “stay tuned.”

#### F. Not Filing At All

The final alternative for individuals is not to file bankruptcy at all. With the changes to exempt property law (discussed below), certain Texas debtors, and particularly those with domestic support obligations and significant exempt property, may be better served by not filing bankruptcy at all. Instead, these debtors will potentially seek advice on maintaining a “judgment proof” status. On the other hand, domestic support creditors may begin to use involuntary petitions to force non-paying ex-spouses into bankruptcy.

### III. SPECIFIC BANKRUPTCY ISSUES IN THE FAMILY LAW PLACE

There are several bankruptcy law issues that routinely appear in family law cases. Under the old Bankruptcy Code, you may have been aware that a bankruptcy filing stayed certain family law cases, prohibited the discharge of support obligations, and in certain instances banned the discharge of property settlement obligations.

Under the new Reform Act, the law has (1) reduced the ability of debtors to use the automatic stay to postpone collection of support; (2) in this expanded the ability of spouses, ex-spouses and children to collect support obligations; and (3) it provides for a complete bar to the discharge of any obligations under a divorce decree in a Chapter 7, 11, or 12 proceeding.

#### A. The Automatic Stay - No Longer a Refuge for Non-Payers of Support

##### 1. Automatic Stay

Upon the filing of a bankruptcy petition, and without further notice, an automatic stay is immediately created. 11 U.S.C. § 362(a). The purpose of the automatic stay is to afford the debtor immediate protection from collection efforts upon the debtor and his property. The automatic stay generally remains in place until the case was closed, dismissed, or the debtor was discharged. 11 U.S.C. § 362(c)(2). While the automatic stay precludes collection efforts against a debtor, a creditor may seek to modify or terminate the automatic stay by filing a motion to lift the stay. 11 U.S.C. § 362(d).

Previously, the Bankruptcy Code provided limited exceptions from the stay to allow certain family law related actions to proceed. For example, support orders could be entered or modified, and collection of support from property (that was not property of the estate, *i.e.*, post-petition earning in Chapter 7 cases were all permissible). 11 U.S.C. § 362(b)(2) (2004).

In the past, many family practitioners had a difficult time getting State court judges comfortable with proceeding with any family law case without an order modifying the stay. The Reform Act has created new exceptions to the automatic stay that substantially limit the applicability and duration of the stay with regard to domestic support obligations and other family law matters. The Reform Act’s explicit language should give judges greater comfort to act on many types of family law cases.

##### 2. New Exceptions To The Automatic Stay As To Certain Family Law Matters

The Reform Act has attempted to limit the application of the automatic stay in a number of family law matters, involving domestic support obligations and custody issues. However, the family law attorney is cautioned to carefully read the code and applicable case law to determine whether the automatic stay impacts his case.

The “new and improved” section 362(b)(2) provides that the automatic stay does not apply to any of the following family law situations:

- A) of the commencement or continuation of a civil action or proceeding -
  - i) for the establishment of paternity;
  - ii) for the establishment or modification of an order for domestic support obligations
  - iii) concerning child custody or visitation;
  - iv) for the dissolution of a marriage, except to the extent that such proceeding seeks to

- determine the division of property that is property of the estate; or
- v) regarding domestic violence;
- B) of the collection of a domestic support obligation from property that is not property of the estate;
- C) with respect to 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 or a statute. 11 U.S.C. § 362(b)(2) (2005) (emphasis added).

The Reform Act makes clear that a family law case dealing with child custody, visitation, or domestic violence is not subject to being stayed by a bankruptcy filing. In the context of the enforcement of domestic support obligations, and obtaining a divorce, the analysis is much more complex. To a large extent, as was the case prior to the Reform Act, whether the pursuit of support or a divorce violates the automatic stay will turn on whether the litigation involves the property of the "estate." Nevertheless, the Reform Act has at least eased some of the burdens of bankruptcy upon domestic support obligation creditors.

### 3. "Estate" Defined

The filing of a bankruptcy petition automatically creates an "estate" pursuant to section 541(a). The estate includes all of the debtor's legal and equitable interests in property from the commencement of the case. 11 U.S.C. § 541(a)(1). However, this is subject to the debtor's right to exempt property from the estate pursuant to 11 U.S.C. § 522. While most property acquired by a debtor after the bankruptcy petition is filed is not property of the estate, certain "windfalls" that are acquired within 180 days are property of the estate. 11 U.S.C. § 541 (a)(5). Examples of these "windfalls" would include property obtained: (1) by bequest, devise or inheritance; (2) property from a property settlement agreement with the debtor's spouse, or of an interlocutory or final decree; or (3) benefits of a life insurance policy or death benefit plan. *Id.* In addition, property of the estate includes any interest in property that the estate acquires after commencement of the case, (*i.e.*, through a legal action such as an avoidance lawsuit). 11 U.S.C. § 541(a)(7).

Property of the estate also includes proceeds, products, offspring, rents or profits from property of the estate, but it excludes earnings from services performed by an individual debtor after commencement of the case. 11 U.S.C. § 541(a)(6). In Chapter 11, 12 and 13 cases, the debtor's post-petition earnings, and property acquired post-petition, are included as property of the estate. *See* 11 U.S.C. §§ 1115, 1207, and 1306 (2005).

As was the case under the law in Chapter 7 proceedings, a debtor's post-petition earnings, and property acquired after filing, remain available to satisfy enforcement of support claims without relief from the automatic stay. 11 U.S.C. § 362(b)(2).

However, the Reform Act now makes clear that wage withholding orders are not effected by the automatic stay even if wages are part of the property of the estate. 11 U.S.C. § 362(b)(2)(C) (2005). Thus, a bankrupt can no longer use her bankruptcy filing to avoid or suspend wage withholding orders used to secure child support, no matter under which type of proceeding is filed.

### 4. Other Actions Not Stayed In Family Law Cases

The Reform Act has also made clear that the stay will not impact the relatively new ability under Texas law to seek the suspension of the debtor's drivers license, professional license, or recreational licenses for the failure to pay child support. TEX. FAM. CODE ANN. § 232.004 (Vernon 1999), and 11 U.S.C. § 362(b)(2)(D) (2005). Further, reporting the delinquent amount to a credit reporting agency along with the interception of tax refunds are also not effected by the Automatic Stay. 11 U.S.C. § 362(b)(2)(E-F) (2005).

The Reform Act also allows an enforcement action being brought for a medical obligation (specified under Title 4 of the Social Security Act) to proceed without regard to the Automatic Stay. 11 U.S.C. § 362(b)(2)(G) (2005).

### 5. Termination Of Stay Upon Motion

Notwithstanding the expanded scope of exceptions to the stay, because a divorce in Texas necessarily involves division of property, and such property may be property of the estate, relief from the stay may be needed in certain family law matters. In a case filed by an individual under Chapter 7, 11, or 13, the automatic stay automatically terminates 60 days after a motion to lift the stay is filed, unless a final decision upon the case is rendered within 60 days (or the 60 day period is extended by agreement of the parties or the court for cause). 11 U.S.C. § 362(e)(2) (2005).

Generally, bankruptcy courts are willing to grant relief from the stay to allow divorces to be completed. However, the court will usually require the parties to return to the bankruptcy court for the enforcement of the decree as it impacts the bankruptcy estate and other creditors.

## B. Texas Property Exemptions And The Reform Act

### 1. Exempt Property

Both Federal bankruptcy law and State law recognize certain property as exempt from the claims of

creditors, (who do not have direct liens against the exempt property). With respect to Texas debtors, the Bankruptcy Code gives the debtor a choice between a specified list of Federal exemptions and the exemptions provided by State law. However, the Reform Act has substantially curtailed, and as it relates to domestic support obligations, entirely eliminated the right to exempt property for a bankrupt debtor.

## 2. Texas Exempt Property

In the past, when a debtor qualified to exempt property under Texas law, they were usually well served. The Texas Constitution provides protection of a debtor's homestead from seizure by creditors. In 1999, Texas expanded an "urban" homestead to up to ten (10) acres of land in one or more contiguous lots. The exempt property also included the improvements on such land, provided that the land and improvements were used as a home or combined home and business. TEX. PROP. CODE. ANN. 41.002 (Vernon 2000).

A homestead is considered "urban" if located within a municipality and able to receive certain services, set forth in the statute, such as police, electricity, and/or sewer services. Homesteads that do not qualify as "urban" are classified as "rural". Rural homesteads are up to two-hundred (200) acres, along with all improvements thereon, if it is used by a family as their home. A single adult is entitled to one-hundred acres (100) for the purpose of his or her home. It is interesting to note that no distinction is made between a family and an individual is made for the urban homestead classification. Furthermore, pursuant to Article 16 § 50 of the Texas Constitution, the homestead is exempt from:

. . . the payment of all debts except for the purchase money thereof, or a part of such purchase money, the taxes due thereon, or for work and material used in constructing improvements thereon, and in this last case only when the work and material are contracted for in writing, with the consent of both spouses, in the case of a family homestead, given in the same manner as is required in making a sole and conveyance of the homestead.

TEX. CONST. art. 16 § 50.

While Texas law does not focus on the value of the homestead, the Reform Act artificially creates limits on Texas law by having monetary caps in some circumstances.

First, in order to even have the option of using the Texas' homestead election, a Texas citizen must have resided in the State for 730 days prior to the filing for

bankruptcy. 11 U.S.C. § 522(b)(3) (2005). If the debtor cannot meet the domiciliary requirements, the debtor will be forced to use his prior State or Federal exemptions. *Id.*

The Reform Act then limits the Texas homestead exemption by only allowing the debtor to hold as exempt no more than \$125,000.00, of the debtor's interest in a homestead acquired within the 1,215 days (approximately 3 1/3 years) prior to filing for bankruptcy relief. 11 U.S.C. § 522(p) (2005). However, this limitation does not apply to the residence of a family farmer, or to equity transferred from a prior residence in the same State acquired prior to the 1,215-day period. 11 U.S.C. § 522(p)(2)(A) (2005). Notably, the cap applies to equity "acquired" during the 1,215 day period and as such, it not only includes down payments or extra equity pay downs, but normal loan payments as well.

The Act also imposes a hard cap on State exemptions for certain "bad debtors." In no event, may the debtor exempt more than \$125,000.00, under a State homestead exemption if the debtor has been convicted of a felony, or owes on a debt arising from a violation of the Federal Securities Exchange Act, or money is owed from an intentional or reckless tort involving bodily injury and/or death, or a RICO violation. 11 U.S.C. § 522(q) (2005). However, the hard cap with regard to felons does not apply to the extent that the interest is reasonably necessary for the support of the debtor and/or the debtor's dependents. 11 U.S.C. § 522(q)(2) (2005).

Finally, Federal law also reduces the State homestead exception by the amount of the value of the exemption that is attributable to any property disposed of by the debtor during the preceding ten years. However, the debtor must have had the intent to hinder, delay or defraud a creditor, and the property disposed of was not exempt at the time of the disposition. 11 U.S.C. § 522 (o) (2005).

While the changes to Texas homestead laws are meaningful to all Texas residents, family law lawyers will be even more surprised at how Congress eliminated all protections of Texas exempt property law as to domestic support obligations. In doing so, Congress reversed the panel decision in *In re Davis*, 170 F.3d 475 (5<sup>th</sup> Cir. 1997).

## 3. Exempt Property And Domestic Support Obligations

The Reform Act reverses the Fifth Circuit's *en banc* ruling in the *Davis* case. *In re Davis*, 170 F.3d 475 (5<sup>th</sup> Cir. 1997). In the *Davis* case, the non-debtor, ex-wife, sought an order in bankruptcy court requiring the debtor spouse to execute a deed conveying his homestead to her. This would enable her to enforce the parties' consent order regarding the debtor's obligation for non-dischargeable alimony, maintenance, and child support under section 523(a)(5). The bankruptcy court held that

the ex-wife could not levy on the homestead, which the debtor had exempted under State law, and the district court affirmed that decision.

Initially, the Fifth Circuit first ruled that the lower courts were wrong citing the (former) 11 U.S.C. § 522(c) of the Bankruptcy Code, which stated that exempt property may be levied upon for the collection of support obligations. *In re Davis*, 105 F.3d 1017 (5<sup>th</sup> Cir. 1997).

However, upon rehearing *en banc*, the Fifth Circuit affirmed the decisions of the lower courts, holding that Section 522(c) of the Bankruptcy Code did not preempt the debtor's State-law rights. *In re Davis*, 170 F.3d 475 (5<sup>th</sup> Cir. 1997). Thus, according to the *en banc* ruling, the debtor was allowed to exempt his residence valued at \$500,000.00, despite the creditor spouse's claim for over \$250,000.00, child support and maintenance.

Under the Reform Act, Section 522(c)(1) of the Bankruptcy Code has been modified to make clear that notwithstanding other laws to the contrary, a debtor's exempt property will be subject to liability for domestic support obligations. 11 U.S.C. § 522(c)(1) (2005).

As to a result of this change, bankruptcy now becomes a super-charged collection tool for creditors holding domestic support obligations. When this power is coupled with the ability of the creditor spouse to argue certain obligations were intended to be support, (as has been done in discharge litigation under the old section 523(a)(5) and which is discussed in more detail below), it is easy to foresee involuntary bankruptcy petitions by alimony and child support creditors in bankruptcy court in the future.

### C. Avoiding Payment And Discharge Of Family Law Obligations: Harder Than Ever Before

#### 1. The Discharge

The discharge sought by a debtor in a bankruptcy proceeding is generally the primary reason that an individual files a bankruptcy case. The discharge operates as an injunction that prohibits creditors from holding onto pre-petition debts and attempting to collect upon those debts at a later time. 11 U.S.C. § 524(a); *see also* 11 U.S.C. §§ 727, 1141, 1328.

Debtors who file Chapter 7 cases receive a discharge approximately 120 days after filing, absent litigation contesting the discharge. Debtors who complete Chapter 13 plans, generally receive discharges within three to five years.

The Reform Act has made it much more difficult to discharge debts arising under agreements and orders reached in family law cases. Thus, from the perspective of a family law practitioner, the availability and the impact of a possible future discharge granted in bankruptcy must be carefully considered when a client agrees to take on obligations as part of the property division.

#### 2. Non-Dischargeability Of "Other Obligations" Awarded In A Divorce Decree

In the past, certain debts awarded in a divorce proceeding, other than alimony, maintenance or support obligations were non-dischargeable in Chapter 7, 11 and 12 cases unless: (a) the debtor lacked the ability to pay such debt from future income; or (b) the discharge of such debt will result in a benefit to the debtor that outweighs the detrimental consequences to the spouse, former spouse or child of the debtor. 11 U.S.C. § 523(15) (2004). As one can imagine, there was much ground for litigation under the law, along with complicated schemes for switching burdens of proof. These legal issues have all been eliminated by the Reform Act.

The new language of section 523(a)(15), again specifically refers to obligations arising under divorce decrees, separation agreements, other orders of a court of record, or a determination made in accordance with State or territorial law that are not domestic support obligations. However, the Act has deleted the former requirement that the Court consider whether the debtor lacked an ability to pay, or the harm caused to the spouse creditor caused by granting a discharge. With this balancing test removed, and the bar to discharge domestic support obligations under section 523(a)(5), a debtor filing under Chapters 7, 11 and 12, cannot discharge any obligations arising from orders or agreements entered into during divorce or SAPCR proceedings. *See, e.g.* 11 U.S.C. § 1141(d)(2) (2005). However, debtors in Chapter 13 cases remain able to discharge non-domestic support obligations. 11 U.S.C. § 1328(a)(2).

#### 3. Non-Dischargeability Of Domestic Support Obligations

As in the past, child support obligations remain non-dischargeable in bankruptcy. 11 U.S.C. § 523(a)(5) (2005).

However, by grafting the old Bankruptcy Code section 523(a)(5) language into the definition of the domestic support obligation (as discussed above), Congress also applied an extensive body of case law under which bankruptcy courts examined the intent of the parties and/or the State court at the time when the agreement or order was entered. The purpose of the analysis was to determine if the obligations were intended to actually be support.

Generally, the analysis under the old § 523(a)(5) started with an understanding that Federal bankruptcy law, not State law determined what constituted support. *See, e.g., In re Paneras*, 195 B.R. 395, 400 (Bankr. N.D. Ill. 1996); *Bonheur v. Bonheur (In re Bonheur)*, 148 B.R. 379, 382 (Bankr. E.D.N.Y. 1992). This approach remains in the new definition of domestic support obligation. 11

U.S.C. § 101(14A) (2005). Further, the Court can determine if an obligation is “in the nature of alimony, maintenance, or support, without regard to whether such debt is expressly so designated.” *Id.* The authors anticipate that courts will continue to examine the parties intent under the case law developed under the old section 523(a)(5) by looking at both child support and other obligations created under family law orders and agreements.

#### a. Child Support

Bankruptcy courts have given the term “child support” broad construction. For example, bankruptcy courts have held that a debtor’s agreement to pay for four years of college for his child was in the nature of child support and non-dischargeable. *See, e.g., In re Brown*, 74 B.R. 968 (Bankr. E.D. Conn. 1987)(the debtor’s obligation to pay for a child’s higher education was non-dischargeable despite fact that debtor was no longer obligated to support the child under state law).

Thus, even in Texas, where court-ordered child support obligations usually ends when a child turns 18 and graduates from high school, a properly drafted agreement or order containing an agreement for payment of a child’s higher education may preclude the debtor spouse from discharging this obligation. However, to avoid discharge, the obligation should clearly find that it benefits the child. *In re Brown*, 74 B.R. at 973.

Another advantage of having the determination under Federal law is that a valid property settlement agreement renders a contractual support obligation non-dischargeable in bankruptcy, even where the court has decreased the court-ordered support obligation. For example, in *Ruhe v. Rowland*, 706 S.W.2d 709 (Tex. App.-Dallas 1986, no writ), the husband contractually agreed to pay \$750.00 per month in support. Later, the husband had his court-ordered support obligation reduced to \$350.00. When the husband was sued in contract for the difference, the resulting judgment was held to be non-dischargeable. *Id.*

The fact that the bankruptcy court may look beyond the language of the decree or property settlement to determine if the obligation is, in reality, one for support of the child, does not always work in favor of the creditor spouse. For example, *In re Rhodes*, 44 B.R. 79 (Bankr. D. N.M. 1984), the court found that lump-sum payment that denominated as child support was in reality compensation for a spouse’s share of the community estate, and hence dischargeable.

Practitioners should note that the discussion above has been focused on analysis of the dischargeability of obligations created by an original divorce decree. The analysis as to the dischargeability of obligations arising under a judgment relating solely to child support, including the award of attorneys’ fees, is much less

complex under current case law in the Fifth Circuit. *See, e.g. In re Hudson*, 107 F.3d 355, 357 (5th Cir. 1997) (because the ultimate purpose of a proceeding on child support is to provide support for the child, attorneys’ fees awarded in connection are also in the nature of child support, and thus non-dischargeable). *See also, In re Cheng*, 163 F.3d 1138 (9th Cir. 1998)(expenses incurred in a child custody dispute in which the court appointed a guardian for the child were not dischargeable).

Thus, when State court awards in a modification proceeding both child support and attorneys’ fees to the non-debtor spouse, the bankruptcy court has found as a matter of law the attorneys’ fee award was non-dischargeable. 11 U.S.C. § 523(a)(5), *In re Fulton (Whipple v. Fulton)*, 236 B.R. 626 (Bankr. E.D. Tex. 1999); accord *In re Dvorak (Dvorak v. Carlson)*, 986 F.2d 940, 941(5th Cir. 1993).

#### b. Spousal Support Obligations

As with child support, the question of whether a debt actually constitutes alimony, maintenance or support, and is therefore non-dischargeable, has always been considered a question of federal bankruptcy law, and not State law. *In re Biggs*, 907 F.2d 503 (5th Cir. 1990); *Kessel v. Kessel (In re Kessel)*, 261 B.R. 902 (Bankr. E.D. Tex. 2001).

Bankruptcy courts frequently have found payments ordered to former spouses to be non-dischargeable support obligations, even in Texas, which until recently had no court ordered alimony. Thus, a debt or obligation awarded pursuant to a decree of divorce may be categorized as alimony, support or maintenance by the bankruptcy court if they find that the intent of the court or the agreement was for it to be support. *See, e.g., In re Davidson*, 947 F.2d 1294, 1296 (5th Cir. 1991); *In re Nunnally*, 506 F.2d 1024, 1027 (5th Cir. 1975).

While State law does not govern the determination of non-dischargeability, it may serve as a guide to determine the nature of the obligation. *Champion v. Champion (In re Champion)*, 189 B.R. 516 (Bankr. D.N.M. 1995). Thus, the mere fact that an obligation is designated as alimony does not necessarily mean that it is alimony if a decree or property settlement agreement designates payments as alimony. *Smith v. Smith (In re Smith)*, 97 B.R. 326 (Bankr. N.D. Tex. 1989). On the other hand, if the debtor spouse treats such payments as alimony for tax purposes, the debtor spouse will be estopped from seeking to discharge the obligation. *In re Davidson*, 947 F.2d 1294, 1296; *Stebbins v. Seibert (In re Seibert)*, 2002 WL 1482728 (N.D. Tex. 2002)(debtor estopped from asserting that payments be deducted pre-petition from income taxes as alimony were not in the nature of alimony).

Moreover, the assumption of marital debts may be in the nature of support even if a decree or agreement

provides for express support elsewhere. *See Kubik v. Kubik (In re Kubik)*, 215 B.R. 595 (Bankr. D. N.D. 1997)(husband's obligation to pay obligations related to marital homestead non-dischargeable support in light of award of marital resident to non-debtor spouse for purposes of raising minor children). Ultimately, the bankruptcy court will separately examine each obligation in the context of the particular facts of each case. *See, e.g. Sanders v. Lanare (In re Sanders)*, 187 B.R. 588 (Bankr. N.D. Ohio 1995).

The burden of proof rests on the non-debtor spouse to establish that the debt in question is actually in the nature of alimony, maintenance or support for the purpose of nondischargeability. *Bell v. Bell (In re Bell)*, 189 B.R. 543 (Bankr. N.D. Ga. 1995). *See generally, Grogan v. Garner*, 111 S.Ct. 654 (1991)(creditor seeking determination that debt is non-dischargeable has the burden of proof by preponderance of the evidence). However, bankruptcy courts have differed on how § 523(a)(5) will be construed. *See In re Champion*, 189 B.R. at 520 (support under § 523 construed broadly) compare with *In re Bell*, 189 B.R. at 547 (section 523 construed narrowly).

Bankruptcy courts, under the guidance of the various courts of appeals, have developed a non-exhaustive list of evidentiary factors to assist them in determining whether an obligation is truly in the nature of alimony, maintenance or support:

- a. the parties' disparity in earning capacity;
- b. the relative business opportunities of the parties;
- c. the physical condition of the parties;
- d. the educational background of the parties;
- e. the probable future financial needs of the parties;
- f. the benefits each party would have received had the marriage continued.

*See, e.g. In re Kessel*, 261 B.R. at 908; *In re Billingsley*, 93 B.R. 476 (Bankr. N.D. Tex. 1987); *In re Benich v. Benich (In re Benich)*, 811 F.2d 943 (5th Cir. 1987); *In re Nunnally*, 506 F.2d 1024 (5th Cir. 1975). In the case of a contested divorce, the bankruptcy court will examine the intent of the family law court as well as the evidence adduced in support of the decree. *In re Chapman*, 189 B.R. at 518 (interpreting Texas decree). To determine the "true" nature of payments, courts have examined whether payments to provide alimony continue when the recipient dies or remarries and whether the obligation is to be paid in installments. *In re Ingram*, 5 B.R. 232 (Bankr. N.D. Ga. 1980). If the obligation continues regardless of remarriage or death, courts often find that the debt is dischargeable. *See In re Kaufman*, 115 B.R. 435 (Bankr. E.D.N.Y. 1990). Furthermore, at least one

court has noted that if the property settlement awards virtually all the property to one spouse, and also provides for periodic payments to that spouse, such payment must be in the nature of support. *In re Smith*, 97 B.R. at 329.

One important issue which has arisen in connection with the issue of whether obligations to the non-debtor spouse under a divorce decree or property settlement are actually in the nature of support has been the award of attorneys' fees to the non-debtor spouse. Several bankruptcy courts have considered whether attorneys' fees pursuant to a divorce decree awarded directly to the non-debtor spouse's law firm are in fact entitled to discharge because such a debt is not a debt owing to "a spouse, former spouse, or child of the debtor," as required by the express language of § 523(a)(5). The Fifth Circuit held in *Joseph v. J. Huey O'Toole, P.C. (In re Joseph)*, 16 F.3d 86 (5th Cir. 1994), that a debtor's obligation to pay his wife's attorneys' fees was a non-dischargeable debt so long as it was in the nature of alimony, maintenance or support. Accordingly, *In re Miller*, 55 F.3d 1487 (10th Cir.), cert. denied, 516 U.S. 916 (1995) (applying plain language of statute would elevate form over substance). However, other courts have not been as kind to counsel. *See Hartley v. Townsend (In re Townsend)*, 177 B.R. 902, 904 (Bankr. E.D. Mo. 1995) (court awards of attorneys' fees directly to the attorney, and not to the "spouse, former spouse or child" are dischargeable debts); *Newmark v. Newmark (In re Newmark)*, 177 B.R. 286 (Bankr. E.D. Mo. 1995) (same). Accordingly, counsel should be aware that the award of attorneys' fees directly to her law firm may create an issue regarding dischargeability in a subsequent bankruptcy filing.

#### c. Reform Act

With domestic support obligations now being payable by seizure of what was otherwise exempt property under Texas law, one can see the increased importance of how the bankruptcy court characterizes family law obligations. Accordingly, family law practitioners will want to undertake careful consideration in drafting documents that clearly evidence their clients' intent.

#### d. Dischargeability - Drafting With Discharge In Mind

When drafting agreements and orders to be used in marital litigation there are four major concepts that need to be respected to avoid a possible future discharge.

In the authors' opinions, the practitioners will not find success by placing simple declarations of non-dischargeability in documents. Instead, divorce orders and agreements will provide the greatest protection only if there are references to the existence and importance of the factors related to non-dischargeability under section 523(a)(5) (set forth

above). Second, when possible, divorce documentation should include a statement of intent as to whether an obligation is to provide for spousal and/or child support.

Third, when possible, payment obligations should run to a spouse rather than to a third party creditor as the definition of domestic support obligation continues to exclude assigned obligations. 11 U.S.C. § 101(14A); see *In re Townsend*, 177 B.R. at 904. In the case of third party debt, the decree or agreement incident to divorce should require the spouse charged with paying the marital obligation to indemnify and hold the other spouse harmless for payments made to the third-party creditor as part of the support obligation. *Cf. Stegall v. Stegall (In re Stegall)*, 188 B.R. 597, 598 (Bankr. W.D. Mo. 1995)(no debt to former spouse exists as to marital debt as decree lacked hold harmless or indemnification provisions; therefore, discharge exception of § 523(a)(15) not applicable); *Salyers v. Richardson (In re Richardson)*, 212 B.R. 842 (Bankr. E.D. Ky. 1997).

Fourth, when possible, terminate payments upon death or remarriage, as courts are more likely to find such payments in the nature of support.

Conversely, counsel representing the payor spouse will want to document when obligations are intended to be a property settlement. While these obligations may not be dischargeable except in a Chapter 13 proceeding, but the property settlement obligations will not be enforceable against exempt property. 11 U.S.C. § 522(c)(1) (2005).

#### IV. CONCLUSION

The interaction of bankruptcy, creditor rights and family law is a complex and difficult subject. This paper has attempted to highlight the changes the Reform Act has made to the Bankruptcy Code and how those changes will impact the family law practitioner. Given the fact that many of the changes have not yet faced judicial scrutiny, practitioners would be wise to keep a close eye on the case law for future developments.