

AN ALFN WEBINAR PRESENTATION

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# ALFN ANSWERS WEBINAR

## Bankruptcy Hot Topics

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*Tuesday, August 18, 2020  
2:00-3:15 PM Central Time*

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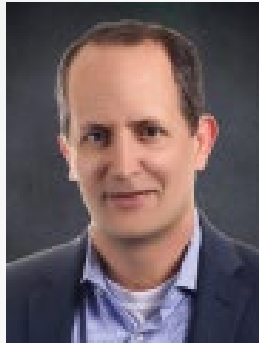
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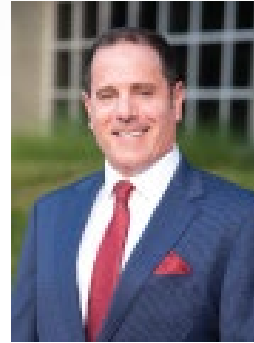
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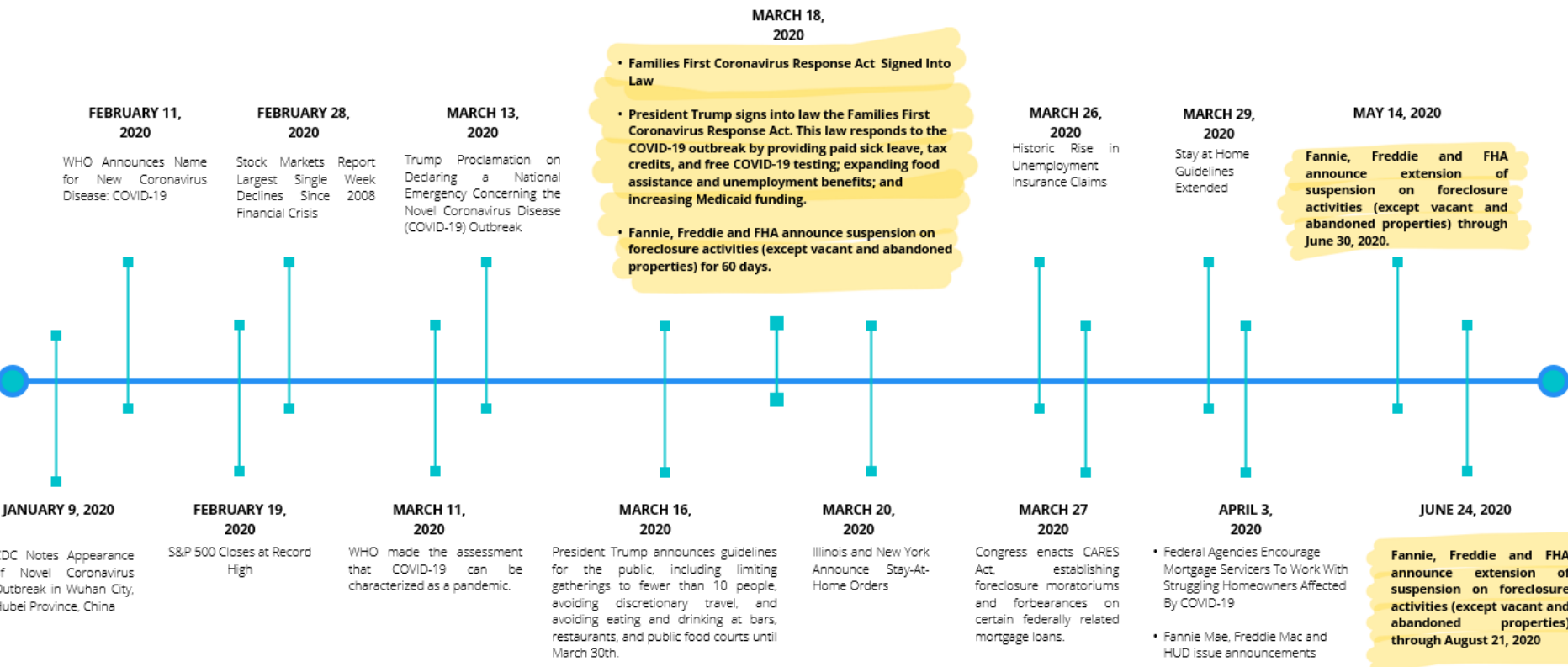


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# COVID – TIMELINE OF IMPACTS ON MORTGAGE SERVICING



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# RELEVANT PORTION OF CARES ACT ON MORTGAGE SERVICING

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## FORECLOSURE MORATORIUM

The foreclosure moratorium applies to all federally-back mortgage loans which are defined by loans purchased by Fannie Mae and Freddie Mac, insured by HUD, the VA, or the USDA, or directly made by the USDA. The moratorium runs to May 18, 2020 (now extended through August 31, 2020). During that time, a servicer of a federally-back mortgage loan cannot (1) initiate a judicial or non-judicial foreclosure, (2) notice and conduct a foreclosure hearing, or (3) conduct a foreclosure sale or execute a foreclosure-related eviction. The Act does not exempt foreclosure proceedings commenced before its enactment.

## FORBEARANCE PROVISIONS

Borrowers with a federally-back mortgage loan may contact their servicer and request forbearance if they are experiencing financial hardship due to the COVID-19 emergency. The hardship can be direct or indirect and forbearance can be requested regardless of delinquency status. Proof of hardship is based solely on an attestation from the borrower. A servicer cannot require additional documentation. The Act states the forbearance "shall" be granted for up to 180 days and "shall" be extended at borrower's request for an additional 180 days. During the forbearance period, the servicer cannot charge or collect any fees, penalties, or interest beyond what could be charged if the borrower made all payments timely.

## INCOME FOR CHAPTER 7 AND CHAPTER 13

The CARES Act has amended the definition of "Income" in the Bankruptcy Code to ensure that any COVID-19 related payments are excluded from the calculation of both disposable income and current monthly income for purposes of filing a Chapter 7 or Chapter 13 bankruptcy.

## PLAN PAYMENT MODIFICATION

Chapter 13 debtors with already confirmed plans are permitted to modify if experiencing a material financial hardship due the pandemic, which includes extending plan payments for up to seven years after the initial plan payment was due. This applies to any Chapter 13 case in which the plan was confirmed prior to the enactment of the CARES Act.

## SMALL BUSINESS REORGANIZATION ACT (AKA SUBCHAPTER 5 BANKRUPTCY)

Per the CARES Act, an enhancement to the Small Business Reorganization Act (aka Subchapter 5 Bankruptcy) was added, which raises the eligibility debt limit from \$2,725,625 to \$7.5 million for the length of one year. This provision was added in hopes to allow more small businesses to take advantage of the Small Business Reorganization Act (Subchapter 5) during this economic downturn. After one year, the debt limit for cases that fall under Subchapter 5 will return to \$2,725,625 without an extension by Congress.



# LOSS MITIGATION TREATMENTS RELATED TO COVID

## LOSS MITIGATION TREATMENTS:

### INITIAL PHASE

#### FORBEARANCE ARRANGEMENT

An arrangement wherein the mortgage servicer agrees to abstain from taking negative action (e.g. collection attempts, proceed with or initiate foreclosure, proceed with a Motion for Relief, or report negatively to credit bureaus) against the borrower if the borrower elects not to tender payments during the pendency of the forbearance arrangement.

**(UP TO 12 MONTHS)**



### NEXT STEPS

#### DEFERRAL

A deferral is defined as an arrangement between the servicer and the borrower wherein the servicer agrees to extend payments to the end of the loan. These payments could result in a balloon payment or in extension of the loan term.

#### LOAN MODIFICATION

An agreement between the servicer and the borrower to change the terms (e.g. interest rate, term, capitalization and/or extension of past due payments) of the underlying loan.

# INDUSTRY LETTER TO CHAPTER 13 TRUSTEES

On April 22, 2020, 8 mortgage servicers and 3 Bankruptcy Law Firms issued a memo to the NACTT and the NCBJ Liaison Subcommittee setting forth best practices around how the Participating Mortgage Servicers will manage Chapter 13 cases where the debtor enters into a forbearance arrangement[1] related to COVID-19 and resulting issues that the NACTT should consider addressing along with the mortgage servicing industry.

## BEST PRACTICE #1:

**NOTICE OF FORBEARANCE:** When entering into a COVID-19 related forbearance arrangement with a borrower, mortgage servicers should notify the court of the arrangement utilizing a form similar to one of two examples attached as Exhibits A (Modified PCN Approach) and B (Notice on the Docket Approach). This notice should be served on the Chapter 13 Trustee, Debtor’s Counsel and Debtor. The notice should include:

- Months included in the Forbearance Arrangement.
- A statement that the debtor has been directly or indirectly impacted by COVID-19.
- A statement that it is the Debtor’s responsibility to work with the creditor to determine how the forbearance payments will be cured upon expiration of the forbearance arrangement (e.g. through a modified plan, agreed order, loan modification, or deferral). Note, under the CARES Act, some debtors will be eligible for up to a 2 year extension of their Chapter 13 Plan term if the case was confirmed prior to the enactment of the Act. There is nothing within these notices that requires the creditor to offer any of these additional arrangements.

Note: Debtors will not be charged for any fees or costs associated with this notice.

## BEST PRACTICE #2:

**PAYMENT CHANGE NOTICES (PCNS):** A payment change notice, under Rule 3002.1, is not required to be filed in connection with the forbearance arrangement since the agreement is not causing the payment amount to change. However, for those mortgage servicers that are utilizing Exhibit A (Modified PCN Approach) in response to a forbearance arrangement, it is important to note that this form will only be utilized to facilitate the filing of the Notice of the Forbearance Arrangement and should not be an actual change of the ongoing mortgage payment amount. It is important to note that PCNs will still be filed if the payment amount changes during the pendency of the forbearance arrangement (such as an ARM or escrow change).



# BEST PRACTICES CONTINUED



## BEST PRACTICE #3:

**PERIODIC STATEMENTS:** Servicers will continue to send periodic billing statements during the pendency of the forbearance arrangement in accordance with the CFPB Regulations and applicable law.



## BEST PRACTICE #4:

**LOCAL RULES:** Servicers will comply with any other local rule applicable to COVID-19 related notices or other similar requirements.



## BEST PRACTICE #5:

**DOWNSTREAM LOAN MODIFICATIONS AND DEFERRALS:** Servicers will comply with existing expectations and localized requirements around entering into loan modifications and deferrals with Chapter 13 debtors.



# WHERE ARE WE NOW?

## AS OF JUNE 23, 2020:

Residential Delinquencies on Residential Mortgages  
Hit Highest Levels since November 2011

Mortgage Borrowers who are more than 30 days  
delinquent increased to 4.3 Million in May from 3.4  
Million in April

More than 8% of all mortgages are currently in  
foreclosure or past due (as reported by Black Knight)

*The above figures all include borrowers who are in an  
active forbearance.*

# OF BORROWERS WHO MADE  
PAYMENTS WHILE IN A FORBEARANCE  
PLAN:

**46% IN APRIL**  
**28% IN MAY**  
**15% IN JUNE**

% OF LOANS IN FORBEARANCE:

PRE-COVID-19 SHUTDOWN: **0.25%**  
6/22/2020: **8.48%**

# WHAT NEXT? - POST FORBEARANCES

Forbearance payments are due and owing at the end of the forbearance term.

## WATERFALL OF ISSUES:

Did the borrower make all forbearance payments?

- If **yes**, borrower is current and no issues.
- If **no**, borrower must pay all payments or find another way to cure the payments.

**If borrower didn't make the payments, the following might be available to the borrower:**

- Loan Modification
- Deferral



**HOWEVER, THE BELOW ITEMS MUST BE CONSIDERED:**

- Will FHA and FHFA require to prove ability to pay?
- Will FHA and FHFA require borrower to prove prior hardship?
- What if borrower can't make payments?
- How will pre-COVID related delinquencies be addressed?

# Polling Question #1

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Do you anticipate a deluge of Bankruptcy filings as a result of the pandemic?

- a) Yes
- b) No
- c) Depends on government intervention

# BANKRUPTCY CASE LAW UPDATE

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**Rose v. Select Portfolio Servicing, Inc., 945 F.3rd 226 (5th Cir. 2019); cert. denied, 2020 WL 3492660**

- **Issue:** If a petition by an individual under Chapters 7, 11 or 13 has been dismissed within one year, does the stay terminate automatically 30 days after a new filing only as to property of the debtor or as to both property of the debtor and the estate?
- **Holding:** Section 362(c)(3)(A) only terminates the automatic stay as to property of the debtor, but not as to property of the estate.

# BANKRUPTCY CASE LAW UPDATE

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## ***Roman Catholic Archdiocese of San Juan, Puerto Rico vs. Acevedo Feliciano, 140 S. Ct. 696 (2020)***

- **Issue:** Can a bankruptcy court make an order *nunc pro tunc* (i.e. retroactive)?
- **Holding:** A bankruptcy court may make an order *nunc pro tunc* only if the court announces its ruling without immediate entry of an order due to inadvertence.

# BANKRUPTCY CASE LAW UPDATE

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## Bobka v. Toyota Motor Credit Corp., 2020 U.S. App. Lexis 24338 (9th Cir.)

- **Issue:** Does the assumption of a lease of personal property survive discharge if the lease was not reaffirmed?
- **Holding:** The assumption of a lease of personal property does survive discharge even though the lease was not reaffirmed.

# BANKRUPTCY CASE LAW UPDATE

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## Derham-Burk v. Mrdutt (In re Mrdutt), 600 B.R. 72 (B.A.P. 9th Cir. 2019)

- **Issue:** Are direct mortgage payments made by a Chapter 13 debtor consider to be “payments under the plan”?
- **Holding:** Direct mortgage payments made by a Chapter 13 debtor are considered “payments under the plan”.

# BANKRUPTCY CASE LAW UPDATE

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## In re Simmons, Case No. 14-10757 (Bankr. S.D. Ga. Sept. 30, 2019)

- **Issue:** Does a debtor's default on post-petition mortgage payments, standing alone, constitute a material default that justifies dismissal?
- **Holding:** A debtor's default on post-petition mortgage payments, standing alone, does not constitute a material default that justifies dismissal.



# SMALL BUSINESS REORGANIZATION ACT OF 2019

## CHAPTER 11'S NEW SUBCHAPTER V

- Created to free small businesses from the burdens, costs and complexities of a traditional Chapter 11 reorganization case
- Became effective on February 19, 2020
- Congress fused concepts from Chapter 12 and 13 cases with concepts of Chapter 11 to create a “fast pass” reorganization for small businesses
  - Streamlined procedures
  - Greater flexibility to restructure debts
  - Greatly reduced costs
  - Wider availability
  - Enhanced even more by the CARES ACT in March, 2020

# SMALL BUSINESS REORGANIZATION ACT OF 2019

## THE SUBCHAPTER V BORROWER

### Eligibility:

- Person or entity with aggregate (secured and unsecured) non-contingent debts up to \$7,500,000 (adjusted up from \$2,725,000 for 1 Year)
- At least 50% of their pre-petition debt arose from commercial or business activity
- Debtor need not be presently engaged in the business activity when filing

### Candidates:

- **YES:** Individuals or businesses that own multiple (residential or commercial) properties for investment
- **MAYBE NOT:** High income individual borrowers who exceed the debt limitations of Chapter 13
- **NO:** Single Asset Real Estate Entities

# SMALL BUSINESS REORGANIZATION ACT OF 2019

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## SUBCHAPTER V HIGHLIGHTS

**Trustee:** appointed automatically, investigates the debtor, investigates claims, monitors the financial affairs of the Debtor, monitors the plan and acts as a conduit for plan payments just like the Chapter 13 Trustee; **BUT**

- Also charged with “facilitating the development of a consensual plan of reorganization”
- Part Mediator/Financial Advisor

### Timeline of Case:

- **First 60 Days:** court holds status conference to make sure the case is moving toward resolution
- **90 Days From Filing:** deadline for Debtor to file plan. May only be extended for circumstances beyond the Debtor’s control.
- Only the Debtor may propose a plan
- **120-150 Days:** Confirmation. Start to finish 4-6 months

# SMALL BUSINESS REORGANIZATION ACT OF 2019

## SUBCHAPTER V HIGHLIGHTS

### ○ Plan

- No Disclosure Statement. Instead Debtor must include history of business operations, liquidation analysis, and financial projections in plan
- **2 Methods of Confirmation**
  - **Consensual** – all classes of claims vote to accept
  - **Non-Consensual/Cramdown** – does not require 1 class to accept like traditional Chapter 11.
    - Allows Court to confirm if it finds Plan does not “discriminate unfairly” and is “fair and equitable”
    - Requires that the Debtor commit all disposable income for a minimum of 3 and maximum of 5 years
    - Requires unsecured creditors receive more than they would in a Chapter 7 liquidation case
    - Debtor gets to retain ownership of business/ all assets

# SMALL BUSINESS REORGANIZATION ACT OF 2019

## SUBCHAPTER V HIGHLIGHTS

- **Plan Confirmation (continued)**
  - Requires finding that the Debtor can make all payments or there is a reasonable likelihood all payments can be made with remedies for creditors if payments can't be made
  - **Claims Secured by Debtor's Principal Residence**
    - Unlike Chapter 13 and conventional Chapter 11 these claims can be modified provided:
      - Mortgage was not purchase money
      - Loan proceeds were used in connection with the Debtor's business venture
  - **Discharge**
    - Consensual Plan – upon confirmation
    - Cramdown Plan – upon completion of all plan payments

# SMALL BUSINESS REORGANIZATION ACT OF 2019

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## IMPACT ON DEFAULT MORTGAGE PORTFOLIOS

- **Less standard Chapter 11 Filings as more borrowers engaged in some form of business will look to elect the quicker and less expensive option of Subchapter V**
- **Impact on Chapter 13 filings should be minimal due to the requirements for business related debt**



## Polling Question #2

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Have you been involved in a Subchapter V filing?

- a) Yes
- b) No
- c) No but I am looking forward to my first one.

# IN REM RELIEF AND THE CO-DEBTOR STAY

- **Automatic Stay:** Section 362(a) of the Bankruptcy Code provides that the filing of a bankruptcy petition operates as a stay against the commencement or continuation of a mortgage foreclosure action against the **Debtor**
- **Co-Debtor Stay:** Section 1301 of the Bankruptcy Code provides that the filing of a bankruptcy petition under Chapter 13 will prevent a creditor from commencing or continuing a mortgage foreclosure action against any individual that **cosigned** a mortgage with the Debtor, so long as that mortgage is classified as a “consumer debt”.
  - Virtually all mortgages involved in Chapter 13 proceedings are consumer debts/subject to the Co-Debtor Stay.
  - Virtually all mortgage foreclosure actions are subject to the Co-Debtor Stay
    - Exception: Co-Debtor Stay will not apply if the foreclosure proceeding is completely “in rem”



# IN REM RELIEF AND THE CO-DEBTOR STAY

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- **Relief from The Automatic Stay and Co-Debtor Stay:**
  - The Automatic Stay and the Co-Debtor Stay are separate/operate completely independent of each other
  - The Bankruptcy Code has separate provisions/procedures for mortgage creditors when seeking Relief from the Automatic Stay and the Co-Debtor Stay
  - Generally both stays must be lifted before a loan can be removed from bankruptcy and placed in foreclosure if one of the borrowers are in a pending Chapter 13 Case
  - Separate Motions/Separate Orders may even be required



# IN REM RELIEF AND THE CO-DEBTOR STAY

- **2005 Amendments Aimed at Repeat Filers/Scammers**
  - **Repeat Filers – Section 362 (c)(3) and (4)**
    - 1 Prior Filing within year of filing: Automatic Stay expires after 30 Days;
    - 2 Prior Filings within year of filing: No Automatic Stay
  - **Scammers – Section 362 (d)(4)**
    - Codification of “In Rem” Relief
    - Courts get authority to lift the automatic stay as to a particular property no matter who files if the filing was part of a scheme to delay, hinder or defraud through:
      - Transfer of all or part ownership
      - Multiple filings involving the same property
  - *Burden shifts to Debtor to petition to get an automatic stay*
  - *No changes made to the Co-Debtor Stay*

# IN REM RELIEF AND THE CO-DEBTOR STAY

- **The Co-Debtor Stay Conundrum**
  - **Issue:** Can a lender with “In Rem” relief or no Automatic Stay in effect under 2005 Amendments proceed directly to foreclosure sale?
    - When presented with the issue of whether the Co-Debtor Stay needed to be lifted in addition to the Automatic Stay (via the repeat filer/scammer provisions) most Courts have said **YES**.
    - Not many cases/cases are very fact specific
  - **Best Practice:**
    - Include a request for prospective Co-Debtor Relief with every In Rem Motion under Section 362 (d)(4)
    - Motions to Annul the Automatic Stay and/or Co Debtor Stay and Validate Foreclosure Sales will depend on the facts but are risky.

# WEBINAR WRAP-UP: QUESTIONS & ANSWERS

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July 16-19, 2023 – Park Hyatt Beaver Creek Resort, Beaver  
Creek, CO

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*Thank you for attending this ALFN webinar presentation.*

## **WEBINAR CONCLUSION**

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