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**Chapter 11 Basics for the Mortgage Lender**

*Friday, April 9, 2021*

*12:00-1:15 PM Central*

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# ALFN Webinar Presenters

## SPEAKER



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## Chapter 11 Basics for the Mortgage Lender

- What is Chapter 11? How are Creditors impacted?
- Chapter 11 cases are becoming more common with recent changes in the Bankruptcy Code and COVID. This session will review the most common types of Chapter 11 cases that Creditors may encounter. This session will highlight the important aspects of these cases. Panelists will also discuss the impact on Creditors drawing particular attention to the segments of each type of case that warrant heightened attentiveness by Creditors.

# Polling Question

How comfortable are you with Chapter 11s?

- a. Whiz Kid
- b. “B” Student
- c. Class Clown
- d. What’s Chapter 11, again?

# Chapter 11 Basics for the Mortgage Lender

## Highlights of Standard Chapter 11 Cases

- **Goals:** - Reorganization of debts/retain assets/keep business operating
- **Eligibility** – Primarily Businesses/Seldom Individuals due to cost/complexity
- **Petition** - Check box for Chapter 11 and then option to check Subchapter V
- **Debtors You May Encounter**
  - A wealthy individual who exceeds the debt limitations of Chapter 13
  - An individual or small business that owns multiple properties for investment purposes
- **Automatic Stay** – The filing of a case triggers an automatic stay (same as Chapters 7 & 13) (i) barring any act by creditors to enforce their rights and (ii) stay of any pending legal proceedings such as foreclosures or evictions.



## Highlights of Standard Chapter 11 Cases

- **Debtor In Possession (DIP)** –
  - Term that refers to the Debtor in a Standard Chapter 11 Case
  - Debtor permitted to manage their affairs without Trustee oversight
  - Trustee may only be appointed if the Debtor consents or the Court finds the Debtor is incompetent to manage its affairs (very rare)
- **Less Structure Than Chapter 13 (and Subchapter V)** – Standard Chapter 11 cases don't follow a predetermined process or timeline
  - No preset bar date to file proofs of claim
  - No preset deadline to file a plan of reorganization
  - No requirement to make current mortgage payments or cure arrearages
  - LIMBO

## Highlights of Standard Chapter 11 Cases

- **Strategy** – dealing with LIMBO
  - Treat like a Chapter 7 case
    - Equity/Payment Analysis
    - File Motion for Relief/Adequate Protection
  - Tie the Chapter 11 Debtor's Hands
    - Have rental proceeds from properties deemed "Cash Collateral"
    - Oppose or Limit the Debtor's use of Cash Collateral
  - Take Away the Debtor's Autonomy
    - Appoint Trustee or Receiver - Debtor incompetent or ignoring DIP responsibilities
- **Period of Exclusivity** – First 120 days of the case only the DIP can file Plan

## Highlights of Standard Chapter 11 Cases

- **The Confirmation Process** – Plan of Reorganization filed with the Court
  - **Disclosure Statement:**
    - Filed and read along with the Plan
    - Adequate information re: Debtor's finances/the Plan for voting
    - After Court approval, mailed out to creditors with Plan and Ballot
  - **Impaired:** Any modification of creditor's claim/rights
  - **Voting:**
    - Only Impaired Classes vote
    - Creditors grouped into classes.
    - Class can have 1 creditor (common with mortgages) or several
    - Voting on the Plan is tabulated by class. Class either Approves/Rejects
    - Class accepts if (i) at least 2/3 in dollar amount, and (ii) more than 1/2 in number vote for acceptance.

## Highlights of Standard Chapter 11 Cases

- **Objection to Confirmation** – In addition to voting against the Plan, creditors *can and should* file an objection to the Plan
- **Confirmation Methods**
  - **Easy Method:** All impaired classes vote to accept; or
  - **Cramdown Method:** 1 impaired class accepts and the Court overrules objections finding Plan is “fair and equitable” and does not “unfairly discriminate” (complex analysis)
    - Dissenting creditor has terms forced on them/loan rewritten
- **Treatment of Mortgage Claims**
  - No modification permitted on Debtor’s principal residence but....
  - Mortgages on investment properties can always be modified
    - Debtor can “cram down” new terms on servicer/investor

# Chapter 11 Basics for the Mortgage Lender

## Highlights of Standard Chapter 11 Cases

- **Common Confirmation/Objection Issues:**
  - **Absolute Priority Rule** – rejecting/objecting class (secured/unsecured) must be paid in full before a junior class (Debtor/Equity Holders) receives or keeps anything.
    - Work Around: Debtor contributes “new value”
  - **Best Interest of Creditors Test** - Plan must pay unsecured creditors at least as much as they would receive if the Debtor were liquidated in a Chapter 7
    - Work around: Pay unsecured creditors as low as 1%
  - **Sale Free and Clear of Liens** - Court allows sale of property “free and clear” of liens. Lien attach to proceeds. Lender consent or full payoff not required.



## Highlights of Standard Chapter 11 Cases

- **Common Objections/Confirmation Issues:**
  - **Undersecured Claim** – A secured claim where the fair market value of the collateral is less than total debt. \$100k mortgage on property worth \$75k. Debtor can split (bifurcate) claim in 2; secured claim of \$75k and unsecured claim of \$25k
  - **1111(b) Election**
    - A potential weapon for the undersecured mortgage creditor
    - Undersecured creditor elects to be treated as “fully secured”/No split
    - Debtor can pay the undersecured creditor the total amount of its claim (full payoff) over time **but** discounted down to its present value (i.e. interest is paid only on part of claim that would have been secured)
    - **KEY:** Undersecured creditor forfeits unsecured claim

## Highlights of Standard Chapter 11 Cases

- **Effect of Confirmation in Standard Chapter 11 Cases** –
  - *Once a Plan is confirmed Debtor and creditors are bound by its terms*
    - Engage Counsel immediately
    - Monitor the Case along with Counsel
    - Confer with Counsel immediately when Plan received
    - *VOTE against and OBJECT to any Plan that modifies your rights by the deadline!*
- **Discharge in Standard Chapter 11 Cases**
  - Business Debtor - Discharged upon confirmation
  - Individual Debtor - Discharged when all Plan payments complete
  - Confirmation + Discharge = Permanent modification of loan
  - Debtor released from any personal liability (debt becomes non-recourse)
  - Personal guaranty not generally extinguished in business case BUT.....

## Highlights of Subchapter V Chapter 11 Cases

- **Subchapter V** – part of the section of Chapter 11 applying to Small Businesses
- **Eligibility**
  - Person or entity with aggregate (secured and unsecured) debts of \$2,725,000.
    - Limit raised to **\$7,500,000** till 3/27/22 due to COVID
  - At least 50% of debt must be business or commercial debt
  - Debtor need not be presently engaged in business or incorporated
- **Sub V Debtors You May Encounter**
  - Individuals or Corporations that own multiple properties for investment
  - High net worth individuals who exceed the debt limits of Chapter 13 and want to avoid the high costs/delays of Standard Chapter 11



# Chapter 11 Basics for the Mortgage Lender

## Highlights of Subchapter V Chapter 11 Cases

- **Trustee**
  - Automatically appointed (unlike Standard Chapter 11/like Chapter 13)
  - Monitor Debtor's affairs/plan (like Chapter 13)
  - Investigate Debtor/filed claims (like Chapter 13)
  - Assist Debtor with facilitating development of consensual Plan (NEW)
  - Part Mediator/Financial Advisor
- **Timeline of Case**
  - "Fast Pass" through Chapter 11 (unlike Standard Chapter 11)
  - Court holds status conference within first 60 days
  - Deadline for Debtor to file a Plan is 90 days.
  - Only the Debtor can file a Plan

## Highlights of Subchapter V Chapter 11 Cases

- **Plan**
  - Much quicker and simpler process than standard Chapter 11
  - No Disclosure Statement. History of business operations, liquidation analysis and financial projections included in Plan
  - Classes vote with same rules on voting as Standard Chapter 11
- **Methods of Confirmation**
  - Consensual/Easy – all impaired classes vote to accept
  - Cramdown – does not require 1 impaired class to accept
    - Court may confirm if plan is “fair and equitable” and “does not discriminate unfairly” (same complex tests as Standard Chapter 11)
    - Debtor must commit all disposable income for 3-5 years
    - No Absolute Priority Rule - Debtor gets to retain ownership of all assets while paying less than 100% unsecured claims and without injecting “new value”

## Highlights of Subchapter V Chapter 11 Cases

- **Methods of Confirmation – Cramdown Continued**
  - 1111(b) election is still available to undersecured creditors
  - Best Interest of Creditors Test must be satisfied requiring all creditors to receive at least as much as they would if the Debtor were liquidated in Chapter 7
  - NEW: Feasibility Test – Requires Court to find that the Debtor can make all payments or there is a reasonable likelihood all payments can be made & with remedies for creditors if payments are missed
- **Loans on Debtor’s Principal Residence** – Can be modified (unlike in Chapter 13 and standard Chapter 11) provided:
  - Mortgage was not purchase money
  - Loan proceeds were used in connection with the Debtor’s business venture

## Highlights of Subchapter V Chapter 11 Cases

- **Effect of Confirmation of Plan** – (Similar to Chapter 11)
  - A confirmed Plan binds both the Debtor and Creditors to its terms
    - Engage counsel immediately
    - OBJECT and VOTE if impaired
- **Discharge** - (Similar to Chapter 11)
  - Business Debtor: Issued immediately upon confirmation
  - Individual Debtor: Issued upon completion of all plan payments
- **Overall Assessment vs. Standard Chapter 11** - a quicker, more structured, less costly, and more advantageous proceeding for Debtors provided they meet the eligibility requirements.

# Polling Question

How concerned are you about Subchapter V?

- a. Unbothered
- b. Meh
- c. Freaking Out
- d. Undecided- Ask Me Next Year

## HOW IS A CHAPTER 11 DIFFERENT FROM A CHAPTER 13??

Chapter 13 is for borrowers with stable income that meet specific debt limits.

Secured limit: \$1,257,850

Unsecured limit: \$419,275

\*Debt limits are updated every 3 years, next adjustment is April 2022\*

Chapter 11 can be filed by virtually anyone with no debt limit. However, these are expensive cases to file and are generally much more complex.





## WHAT TYPES OF DEBTORS DO WE SEE IN CHAPTER 11 CASES GIVEN THE HIGH DEBT LIMITS?

- Borrowers with high dollar homes
- Borrowers with multiple homes and investment properties

This is the most expensive type of bankruptcy and would not necessarily be the best option for a borrower of median income with a single family home looking for bankruptcy relief.

Where's the Magic 8 Ball when you need it??



## COVID AND CHAPTER 11

How does COVID impact a Chapter 11 case?

- Same concerns for debtors and creditors apply pre and post COVID – the questions around feasibility and valuations are more uncertain.
- CARES has been further extended. CARES also has temporarily increased the debt ceiling.



# MILESTONES IN CHAPTER 11 AND SUB V CASES

- First Day Motions
- Schedules and Statements
- Motions to Value
- Plan and Disclosure Statement
- Confirmation



# WHAT IS THE ROLE OF THE TRUSTEE IN A CHAPTER 11 AND SUB V – HOW IS THIS DIFFERENT THAN CHAPTER 13?

- Standard Chapter 11 cases generally have no trustee – the borrower operates as a Debtor In Possession, unless circumstances warrant the appointment of a Trustee.
- Appointment of a trustee is “for cause”
  - Fraud
  - Incompetence
  - Gross Mismanagement

# WHAT IS THE ROLE OF A TRUSTEE IN A SUB V CASE?

- Sub V Cases the Trustee is largely responsible for helping the borrower to develop the Plan and reach terms with Creditors. Think of them more as a mediator, but is that really what we are seeing?
  - What should be expected at the status conference?
  - Will SubV trustee operate more as a Chapter 13 trustee disbursing payments and utilizing NDC?
  - Are there pre and post petition payments due?

## WHAT DOCUMENTS SHOULD BE “RED HOT” INTERMS OF ATTENTION FOR A SERVICER?

- Notice of Proof of Claim Bar Date
- Motion for Use of Cash Collateral
- Motion to Value/Cramdown
- Disclosure Statement
- Plan



## If referral to counsel takes 10 days is this too long?

Short answer ----- YES

- Due to the short deadlines for some motions and/or some Ch 11s (i.e. Sub V) referral must be almost immediate
- More specifically – 1<sup>st</sup> Day Motions
  - Filed at or near the filing of the bk
    - Response deadlines are 14-21 days

# What are 1<sup>st</sup> Day Motions? What do you do?

Typical Attorney Answer ---- It depends!

- 1<sup>st</sup> Day Motions = Motions filed with the petition or near the petition date
  - Motion to Employ Counsel
  - Motion to Use Estate Property
  - Motion to Pay Wages
  
- What do you do?
  - Majority are irrelevant
  - Oppose Motion to Employ?

# What is Cash Collateral? Motion to Use Cash Collateral?

**Cash Collateral –income used for mortgage payments or other expenses**

## Motion for Use of Cash Collateral

- Can be 1<sup>st</sup> Day Motion
- If not, typically filed shortly after Motion to Employ is granted
- Must have court permission to use assets of the estate
  - Income whether salary or collected rents or other are assets of the estate
- Oppose?
  - Is it the principal residence? Rental?
  - Do you have equity?
  - What is the budget in the Motion?
  - Can cash flow be initiated?



# What are the challenges?

- Complex nature of Ch 11
- Extended length of these cases
- Negotiating terms early
- Payment of taxes and insurance
- Starting the flow of payments
- Terms similar to Ch 13
- Bad faith filing





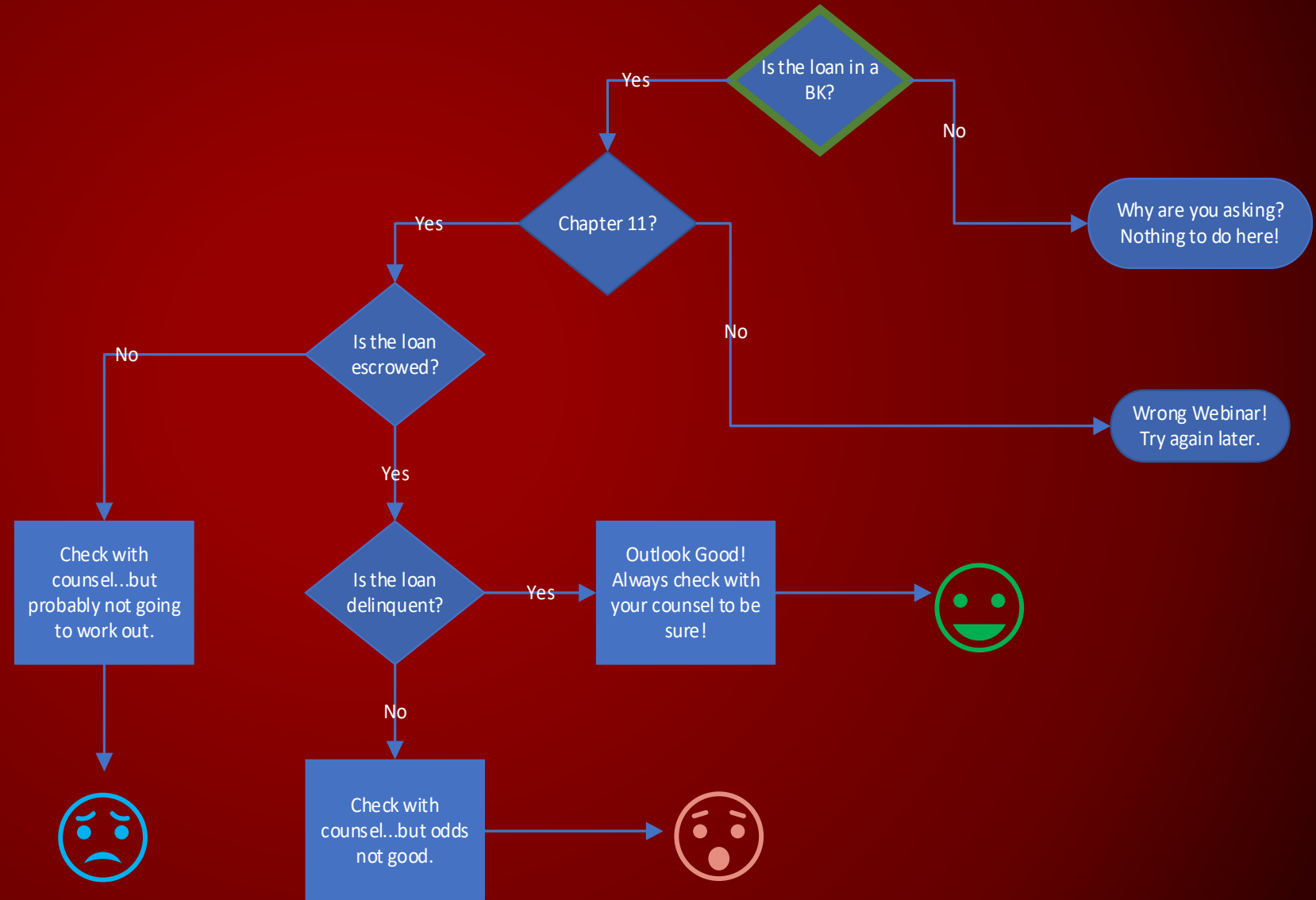
# When can the servicer expect to be paid post-filing?

Typical Attorney Answer ---- It depends!

- Motion for Use of Cash Collateral
- Motion to Value
- Disclosure Statement
- Plan
- Motion for Relief from the Automatic Stay
- Is a Motion to Dismiss the answer?

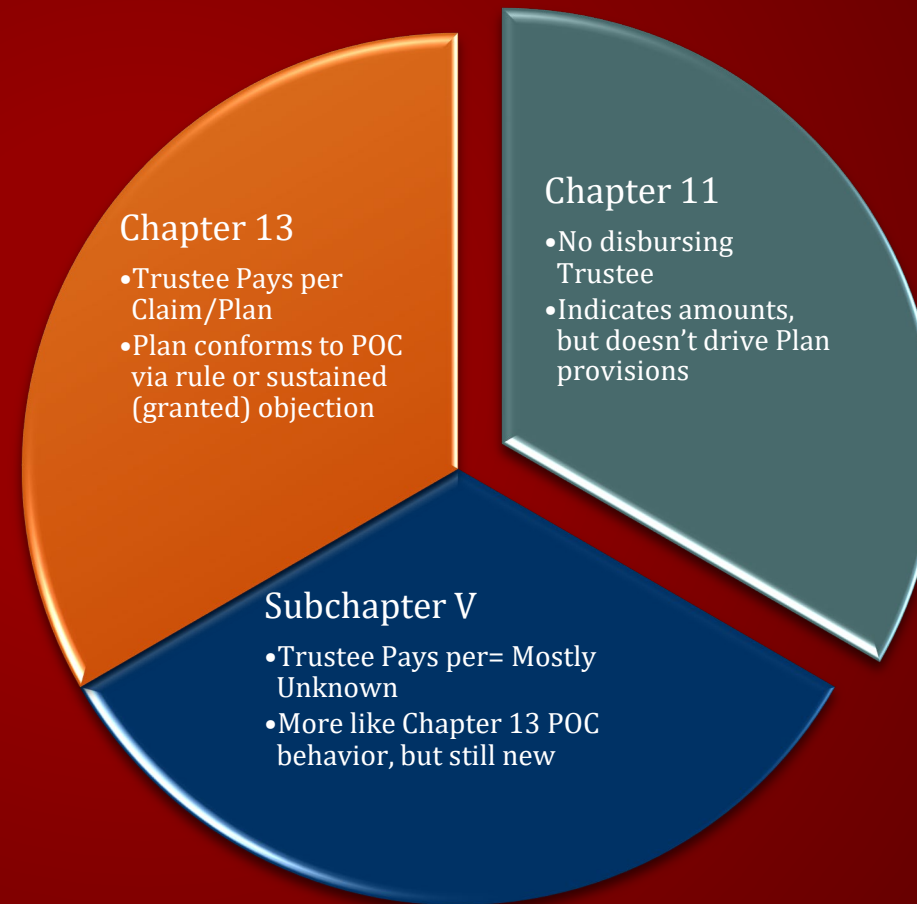
# Motion for Adequate Protection- *Where is My Money?*

- What is it?
  - A motion filed by a Creditor to ensure their interest in the collateral is protected from loss.
- When is this most commonly needed in Chapter 11 cases?
  - Post-Petition, Pre-Confirmation Escrow Disbursements.
- Why not post-petition payments?
  - Treatments are being decided and with many creditors impacted, post-petition mortgage payments may not be the highest priority at this stage.

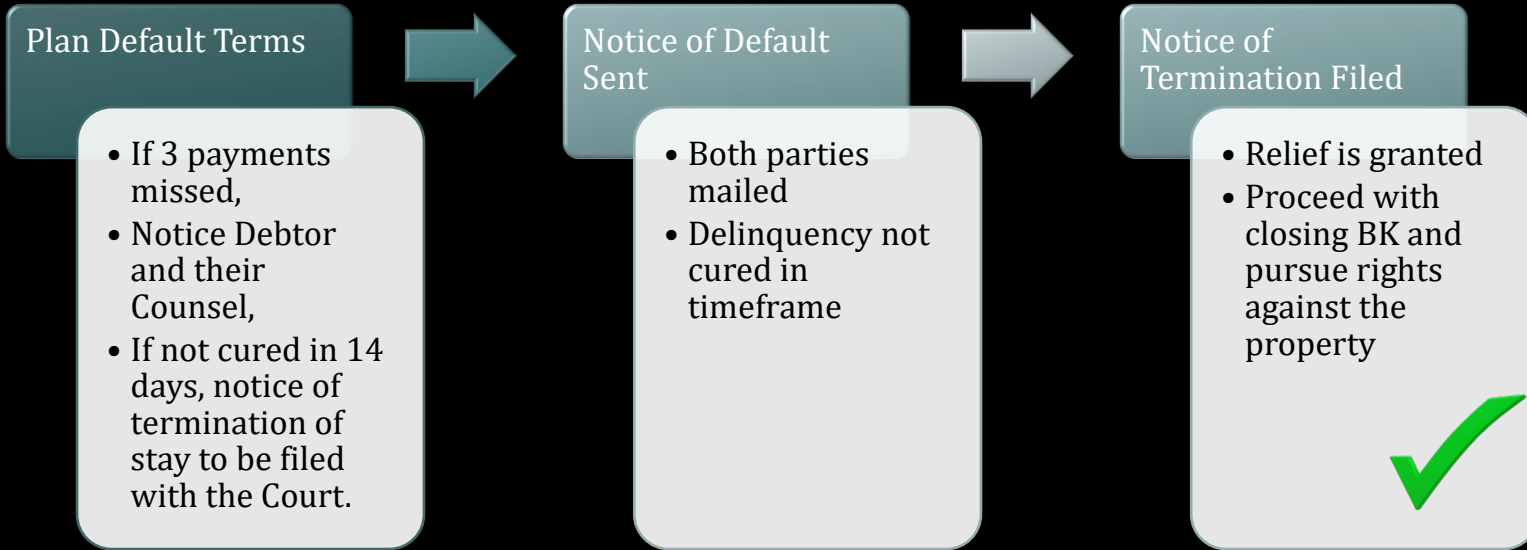


# Plans and POCs- *How Do They Correlate? Do I Care?*

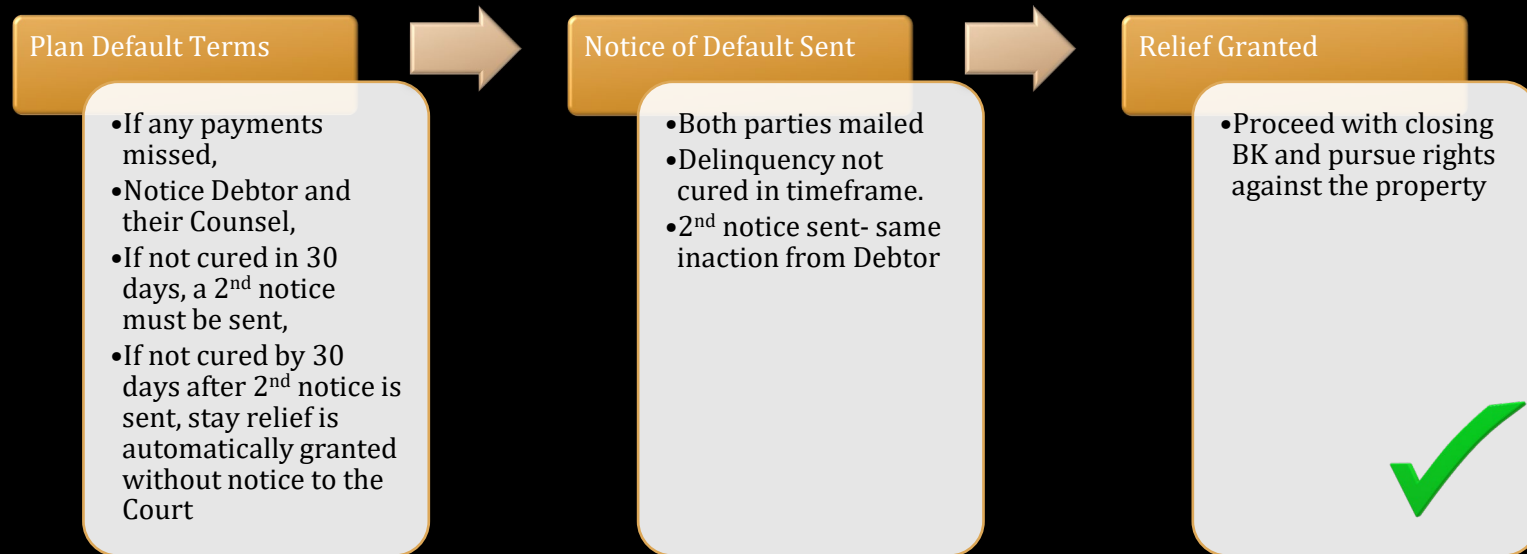
- *Does the POC even Effect the Plan?*
  - Full Chapter 11s-
    - No. It's a good indicator to the Debtor of amounts due, but will not drive the Plan as it may in a Chapter 13.
  - Subchapter V:
    - *Kind of.* With a Trustee involved, the POC will behave more like it does in a Chapter 13, but whether Trustees will pay per Claim or Plan is not set in stone today like Chapter 13s. Also, all treatments in full 11s are possible too.
  
- *How can I make this work for me?*
  - Full 11s Suggestion-
    - Use POC filing date to review if treatment is settled. If not, assess the possibility of reaching out to Debtor's counsel for negotiation or advisement of intention.
  - Subchapter V Suggestion-
    - If the Plan amounts are incorrect, you must object!
      - As directed by counsel...of course.



## Example 1



## Example 2



# Notice of Default- *The Exit Strategy*

### *What is it?*

- A notice to the Debtor, Debtor's Counsel, and sometimes the Court that informs the parties that a Creditor has not received payments per the Plan
- Most of the time, this is the path toward stay relief in Chapter 11 cases if a Debtor defaults
- Terms are highly varied case-by-case

### *How do you know what the terms are?*

- Generally located in the Plan
- If not in Plan, objection should be filed to make sure these terms are clear
- Terms are negotiable, so best to coordinate with your local counsel on which terms are not acceptable based on business needs

### Pre-Confirmation

- Surrender
- Claim not in BK
- Party of No Interest

### Post-Confirmation

- Delinquent and Default Terms Allow/Require

### Subchapter V

- Similar to Chapter 13 parameters, but Plan controls.

## Motion for Relief- *Get Me Outta Here!*

Is it possible to file a Motion for Relief pre-Confirmation in a Chapter 11? When?

Post-Confirmation?

What about Subchapter V?





# What to Do Before a Plan is Filed? *I'm Tired of Waiting!*



## Proactive Benefits



Faster Resolutions



Better Inventory Movement



Payments Received Faster



Relief Obtained Faster



Better Risk Mitigation



Lowers Servicing Costs

# Polling Question

What are the biggest servicing challenges you experience with Chapter 11s?

- a. Monitoring
- b. Notices of Default
- c. Closing Requirements
- d. Treatment Negotiation
- e. Other

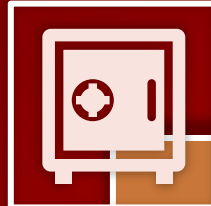
# What is an 111(b) Election and Why Should I Care?

## Definitions to Know



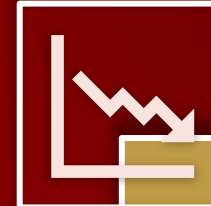
### Secured Debt

- The lien was properly perfected pre-petition.



### Wholly Secured

- Enough equity exists in the collateral to fully pay the lien amount owed on the date of filing.



### Partially (or Under) Secured

- The *market* value of the collateral is less than what is owed on the lien.
- Be careful of cramdown appraisals here! “Liquidation Value” may not be allowed in all districts!

Now on to the good stuff...what to do!



# What is an 1111(b) Election and Why Should I Care?



## What is the election really?

- The election under 11 U.S.C. § 1111(b)(2) is a potential weapon for an undersecured creditor being crammed down in a plan. The creditor can elect to be “fully secured” with no bifurcation of the claim into secured and unsecured parts, but with certain tradeoffs. The creditor is paid the total amount of its claim after it is discounted to the present value.



## Who can file?

- Any secured creditor may file an 1111(b) election, *unless* the property is of inconsequential value or to be sold under the plan or under 11 U.S.C. § 363.



## When and how do you file?

- Careful here, the election may be filed at any time prior to conclusion of the hearing on the disclosure statement, or at “such later time as the court may fix.” It must be made in writing and signed, but can also be made at the hearing on the disclosure statement (this is not a recommended best practice). A written election should be made before the DS hearing.



## No Take Backs! Why?

- Courts have held that once a creditor has timely made a Section 1111(b) election, it may not withdraw that election provided that the plan under which the election was made has not been materially amended.

# What is an 1111(b) Election and Why Should I Care?

## What happens if the debt is only partially secured?

- The proposed Chapter 11 Plan states the lien will be crammed down, or bifurcated, into secured and unsecured portions, with separate plan treatment for both.
  - For our example, the market value will be \$100,000 and the lien amount on the date of filing was \$160,000.
  - Plan proposes to pay \$100,000 as secured debt and the remaining \$60,000 as a general unsecured creditor (paid at 5%, or \$3,000).



Market Value (at confirmation): \$100,000

Lien Amount: \$160,000

# What is an 1111(b) Election and Why Should I Care?

To Elect or Not to Elect? Let's Try the Math for *NOT* making the election.



## Cramdown Payout

Plan proposes a cramdown to \$100,000.00 at 5.0% over 30 years:  $\$100,000.00 \times 5\%$  over 30 years = 360 P&I payments of \$536.82, resulting in a **total of \$193,255.78 paid over the 30-year term.**

*Also...*the creditor retains the ability to vote as both a secured and unsecured creditor under the bifurcated claim, and can block rights in one or both categories.

## 1111(b) Payout

1111(b) election pays \$160,000.00 at 0.0% over 30 years: results in 360 P&I payments of \$444.45, resulting in a **total of \$160,000 paid over the 30-year term.**

# What is an 111(b) Election and Why Should I Care?

**To Elect or Not to Elect? Let's Try the Math for YES, make the election.**



**Most importantly:  
 Creditor loses the  
 ability to vote on  
 the plan.**

## Prong 1: Claim = \$160,000

To Satisfy: The present value of the stream of payments must be at least equal to the value of the claimant's lien.

160,000.00 at 0.0% over 30 years = \$160,000.00 (360 payments of \$444.45)



## Prong 2: Value = \$160,000

To Satisfy: The total of the payments must at least equal the total allowed claim of the claimant.

Present value of \$160,000.00 at 5.0% over 30 years = \$82,791.00



The second prong is not satisfied, therefore the plan would need to pay \$160,000.00 over 30 years at 1.30% to reach a present value of \$100,027.64 (360 payments of \$536.97), with a future value of \$193,309.20.

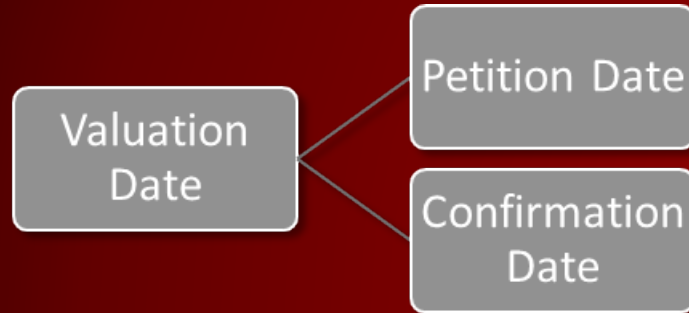


# What is an 1111(b) Election and Why Should I Care?

	No 1111(b) Election	1111(b) Election
Bifurcation of Claim Section 506(a)	Claim equal to value of collateral. Claim bifurcated into secured and unsecured portions	Claim equal to full amount of Creditor's Claim. No Claim bifurcation.
Recourse/Unsecured Claim	Has recourse against borrower regardless of whether loan was recourse or non-recourse prior to filing.  Has an unsecured deficiency claim.	Loan is non-recourse.  Unsecured deficiency claim waived.
Unsecured Voting Right	Has right to vote as an unsecured creditor due to the deficiency claim.  Has ability to block confirmation as an unsecured creditor.	No right to vote as an unsecured creditor.  No blocking right.
Unsecured Distribution	Will receive distribution under the Plan as an unsecured creditor.	Foregoes distribution as an unsecured creditor
Confirmation Rights	Can raise unsecured creditor objections, such as absolute priority rule and unfair discrimination.  Can raise secured creditor objections such as feasibility etc.	Unable to raise objections in the capacity as an unsecured creditor.  Can raise objection as a secured creditor such as feasibility etc. based on modified payment structure.
Cramdown Treatment-Deferred Payments	Retention of lien Deferred payments having present value equal to collateral value (interest)	Retention of lien Deferred payments having value to total amount of unsecured claim (no interest)
Recovery From Collateral	No right to future increases in collateral value; on sale, recovery limited to collateral value as of confirmation less principal payments received.	Entitled to future increases in collateral value up to total amount of allowed claim; on sale, entitled to allowed claim less payments received.

# Considerations for a Cramdown

- What is the valuation date used for the cramdown?
  - There is differing law on what valuation date is used for a cramdown:

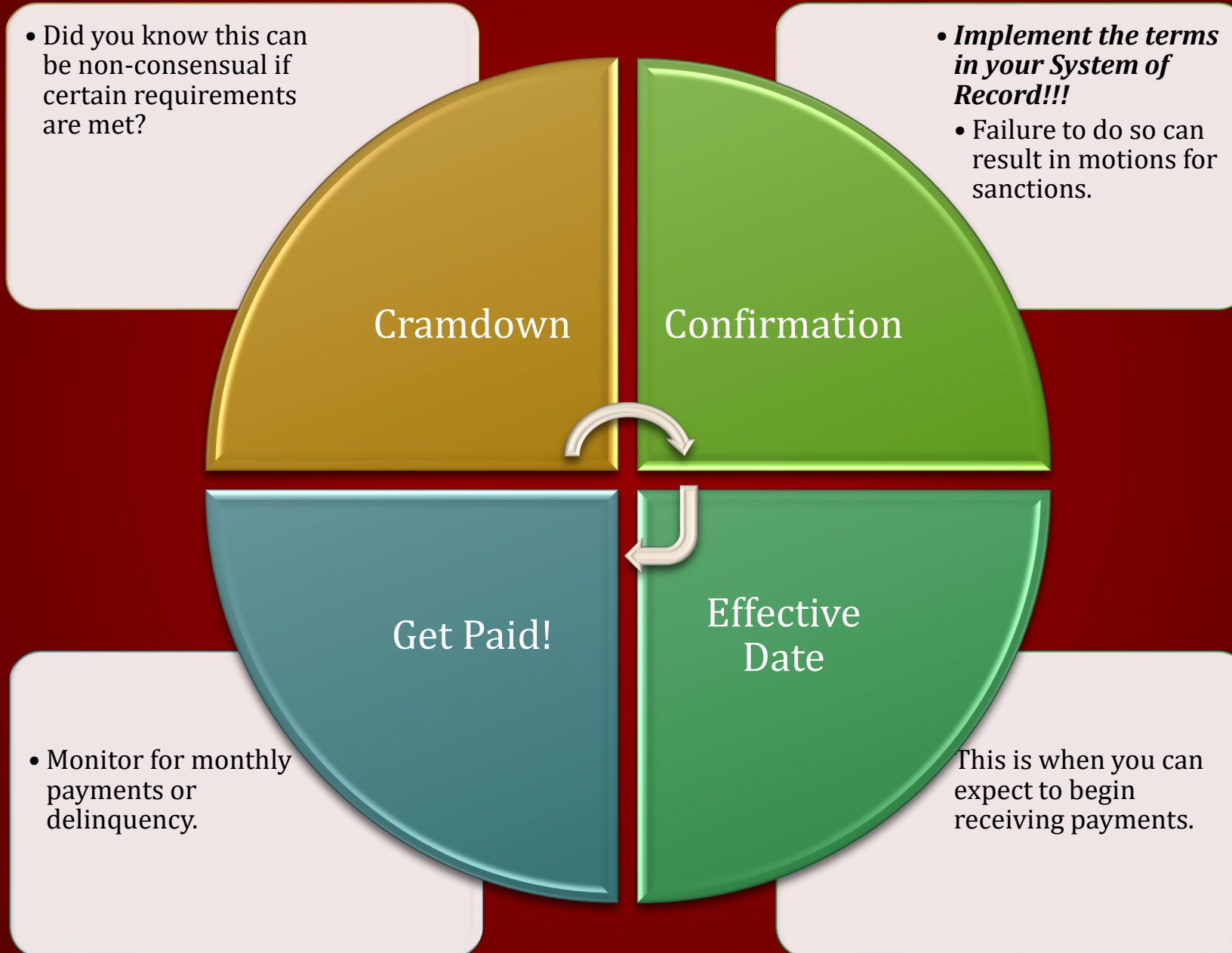


- Some Circuits use the petition date, which appears to be more of a minority.
- Most Circuits use date of confirmation (which is also generally followed by the Ninth Circuit).

Carefully review the appraisal used to cramdown the lien. Some attorneys use a “liquidation value” which is not allowed in most districts: *In re Lam*, 211 B.R. 36, 38 (B.A.P. 9th Cir. 1997) (“Based on the current fair market value of the Debtors' real property, the fourth deed of trust held by Thrift is wholly unsecured.”).

Pursuant to your request, [REDACTED] has inspected the above captioned property on January 14, 2017, as requested, for the purpose of estimating the liquidation value (defined within). It is understood that the intended user of this report is [REDACTED]. The intended use of this appraisal report is to provide a liquidation value for financial planning proceedings. This appraisal is not intended for use in estimating replacement cost for insurance purposes, establishing a value for extensions of credit, or any use in a federally related transaction.

# What is the Effective Date of a Cramdown?





# Payment Issues After a Cramdown

- Make sure the “new” crammed-down payment clarifies how it is divided between principal, interest, taxes and insurance. This is commonly missed in objections!
  - Most chapter 11 plans simply state the terms (4.0% at 30 years) and the “payment amount” (i.e. \$1,234.00 per month).
  - An issue arises later when the servicer tries to change the escrow portion of the payment, and the debtor seeks sanctions since the stated payment locked the loan into not only a permanent P&I but *also* into a permanent T&I.

Class	Name of Creditor	Collateral	Regular Monthly Payment	Estimated Arrears	Interest Rate on Arrears	Monthly Payment on Arrears
1E	Wells Fargo Bank, National Association (serviced by Ocwen Loan Servicing LLC)	705 E. Fifth St, Calexico, CA 92231	\$2,191.16	\$10,467.43	3%	\$188.09

Class	Name of Creditor	Collateral	Regular Monthly Payment	Estimated Arrears	Interest Rate on Arrears	Monthly Payment on Arrears
	Towd Point Mortgage Trust / Select Portfolio Servicing, Inc.  (1 <sup>st</sup> Mortgage Loan)	8451 Tiger Lily Dr., San Ramon, CA 94582	\$2,195.04 (P&I)  \$1,301.84 (Taxes and insurance)  = \$3,496.88	\$3,611.29	0.00	\$601.88

commence making the regular ongoing monthly payments commencing with the July 1, 2020 monthly payment in the amount of \$14,881.41 for principal, interest, taxes, and insurance. The maturity date is re-set to June 1, 2060.

- Once a plan is confirmed, these terms are binding even if the case is later dismissed or converted.

# Administrative Closure of a Case

## Who Files This?

- The Debtor

## What is It?

- A motion filed to administratively close a chapter 11 bankruptcy prior to completion of the plan and before seeking a discharge.

## Why is It Filed?

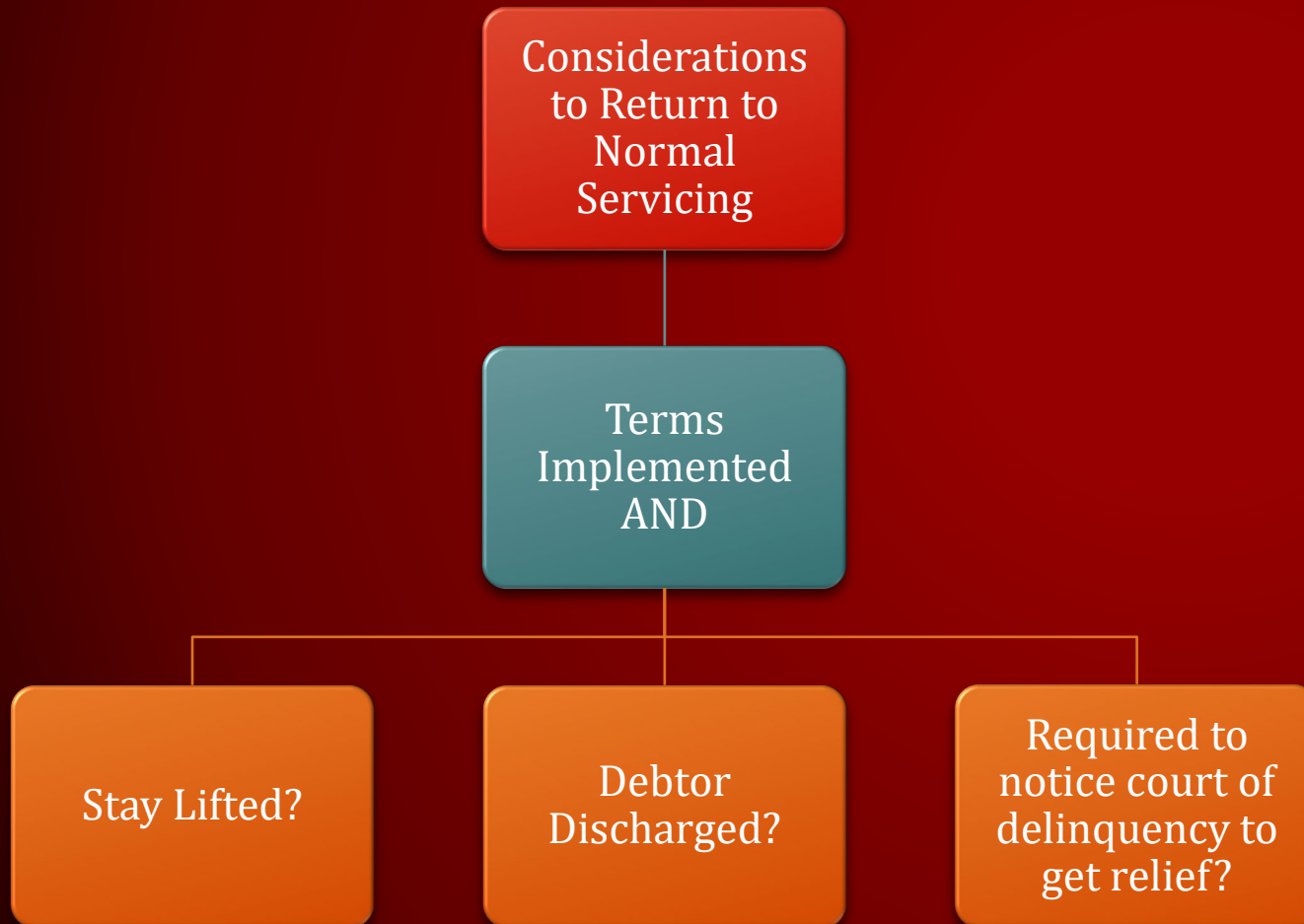
- This is done to alleviate payment of quarterly fees to the U.S. Trustee, and to avoid filing status reports and appearing at status conference hearings.

## When Does this Happen?

- Usually filed once plan is confirmed and performance has commenced, with the intention to reopen the case at the conclusion of “x” years to request entry of a discharge. BUT...
- Some districts allow it, but some do not.

# Administrative Closure of a Case

- What happens to servicing of the loan? Can it be returned to regular servicing?
  - Yes and No.
    - Returning the loan to regular servicing may run afoul of the automatic stay, the confirmation order and/or the discharge injunction.

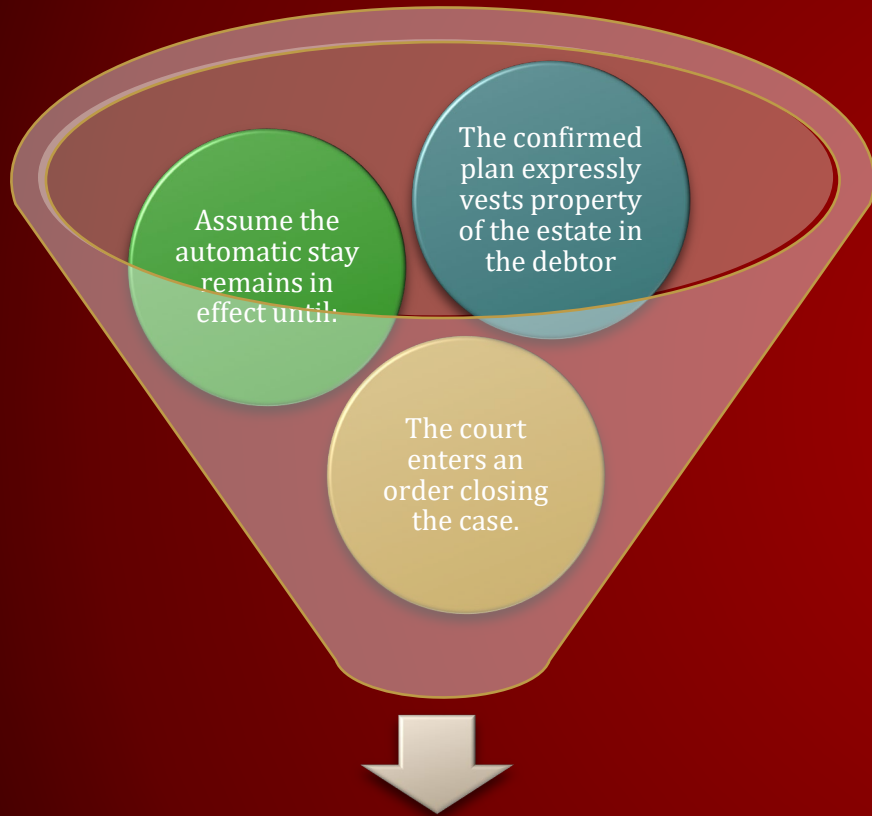


When Might I Need to Pay to Reopen the Case?

- Remedies Under the Plan
  - Dismiss/Convert
  - Relief Motion/MFR
  - Seek Clarification

The cost to reopen a case is expensive. Most districts have a filing fee of over \$1,000.00.

# Administrative Closure of a Case



**Best Practice**





# What Happens When There is a Default?

(c) Material Default Defined. If Debtor fails to make any payment, or to perform any other obligation required under the Plan, for more than 10 days after the time specified in the Plan for such payment or other performance, any member of a class affected by the default may serve upon Debtor and Debtor’s attorney (if any) a written notice of Debtor’s default. If Debtor fails within 30 days after the date of service of the notice of default either: (i) to cure the default; (ii) to obtain from the court an extension of time to cure the default; or (iii) to obtain from the court a determination that no default occurred, then Debtor is in Material Default under the Plan to all the members of the affected class.

(d) Remedies Upon Material Default. Upon Material Default, any member of a class affected by the default: (i) may file and serve a motion to dismiss the case or to convert the case to Chapter 7; or (ii) without further order of the court has relief from stay to the extent necessary, and may pursue its lawful remedies to enforce and collect Debtor’s pre-confirmation obligations.

(e) Claims not Affected by Plan. Upon confirmation of the Plan, and subject to Part 5(c), any creditor whose claims are left unimpaired under the Plan may, notwithstanding paragraphs (a), (b), (c), and (d) above, immediately exercise all of its contractual, legal, and equitable rights, except rights based on default of the type that need not be cured under section 1124(2)(A) and (D).

E. Material Default Defined. If Debtor fails to make any payment required under the Plan, or to perform any other obligation required under the Plan for more than 14 days after the time specified in the Plan, the affected creditor may serve upon Debtor and Debtor’s attorney (if any) a written notice of default. The Debtor is in material default under the Plan if the Debtor fails within 21 days of the service of such notice of default, plus 3 additional days if served by mail, either: (i) to cure the default or (ii) to obtain from the court an extension of time to cure the default or a determination that no default occurred.

- The confirmed plan will outline default remedies. These are rarely contained in the order confirming the plan. Stipulate to terms in advance, if possible.

A creditor or party in interest may bring a motion to convert or dismiss the case under §1112(b), after the Amended Plan is confirmed, if there is a default in performing the Amended Plan. If the Court orders, the case converted to Chapter 7 after the Amended Plan is confirmed, then all property that had been property of the Chapter 11 estate, and that has not been disbursed pursuant to the Amended Plan, will re-vest in the Chapter 7, estate. The automatic stay will be re-imposed upon the re-vested property, but only to the extent that relief from stay was not previously authorized by the Court during this case.

# What is The Discharge And What Does it Mean?

## Corporations, LLCs, Non-Individuals

### Discharge is at Confirmation

- A discharge here is valid even if the debtor later *fails* to fulfill its obligations under the Chapter 11 plan.
- All pre-confirmation debt is also discharged.

#### 8. FINAL DECREE

Once the estate has been fully administered as referred to in Bankruptcy Rule 3022, the Reorganized Debtor shall file a motion with the Court to obtain a final decree to close the case.

## Individuals

### Granted Separately by the Court

- This will happen after all payments under the Plan have been satisfied.

#### 6(a) Discharge.

Debtor shall not receive a discharge of debts until Debtor makes all payments due under the Plan or the Bankruptcy Court grants a hardship discharge.

## Confirmation Order

### Read to see if it Contains information about the Debtor's Discharge

- The order will not always contain the plan terms or discharge terms, and often only recites the requirements for confirmation and that they have been met.

#### 1. DISCHARGE

Debtor is not eligible for a discharge when the plan is completed by virtue of having received a discharge in a prior chapter 7 case on February 8, 2016, Case No.: 2:15-bk-26460-RK.

## What is The Discharge And What Does it Mean?

- What if it was a corporation that filed, but the obligor is an individual that has not filed BK?
  - There is no automatic stay stopping creditor action against a non-debtor: guarantors, co-obligors, partners of debtor partnerships, officers or directors or employees of a corporate debtor, or the non-debtor spouse of an individual Chapter 11 debtor are not protected. But...
  - In exceptional cases where it is conclusively shown that success of the Chapter 11 case depends upon protecting non-debtor persons or entities, the bankruptcy court can separately enjoin creditors from proceeding against them until a plan is confirmed. This usually requires some act by the debtor with notification to all affected creditors.



# What is The Discharge And What Does it Mean?

- Continued: What if it was a corporation that filed, but the obligor is an individual that has not filed BK?
  - 11 U.S.C. § 524(a)(2) provides only for the discharge of the debts of the Debtor, but not a non-debtor co-borrower or obligor, which is supported by § 524(e) (providing that there is no release of the personal liability of a third-party non-debtor). The bankruptcy court does not have the authority to release the liability of non-debtors.
  - All communications required under non-bankruptcy law are to still be sent to the non-discharged borrower, and can also be sent to the discharged borrower for “informational” purposes.
    - It is best practice to have a “bankruptcy disclaimer” on all correspondences, sent to all parties, in a prominent font in a prominent location, and do not provide tear-off/payment coupons or return envelopes.
  - Tax forms can still be sent to both parties.

# What is The Discharge And What Does it Mean?

- What about credit reporting?

	<b>All Borrowers Filed Bankruptcy Chapter 7, 11 or 12</b>
Month BK Filed	<ul style="list-style-type: none"> <li>• CII = A, B or C (Petition for Chapter 7, 11 or 12 Bankruptcy)</li> <li>• Account Status = status at time of petition</li> <li>• Payment History = first character based on previous month's status plus prior history</li> <li>• Current Balance = outstanding balance amount</li> <li>• Scheduled Monthly Payment Amount = contractual monthly payment amount</li> <li>• Amount Past Due = dependent on status</li> <li>• Date of Account Information = current month's date</li> </ul> <p><b>Note: Authorized Users (ECOA Code 3) on accounts included in a bankruptcy petition should either be terminated (ECOA Code T) or deleted (ECOA Code Z) from the account because they are not contractually liable for payments.</b></p>
Months Between Petition Filed & BK Resolution (Reaffirmation of Debt, Lease Assumption, Discharged, Dismissed, Withdrawn)	<ul style="list-style-type: none"> <li>• CII = Blank (previous petition value reported is retained) or CII = A, B or C</li> <li>• Account Status = status at time of petition</li> <li>• Payment History = increment first position with value 'D' (plus history reported prior to bankruptcy filing)</li> <li>• Current Balance = outstanding balance amount</li> <li>• Scheduled Monthly Payment Amount = contractual monthly payment amount</li> <li>• Amount Past Due = dependent on status</li> <li>• Date of Account Information = current month's date</li> </ul>
Reaffirmation of Debt or Lease Assumption	<ul style="list-style-type: none"> <li>• CII = R (Reaffirmation of Debt) or 2A (Lease Assumption)</li> <li>• Account information as it applies going forward</li> </ul>
BK Discharged	<ul style="list-style-type: none"> <li>• CII = E, F or G (Discharged through BK Chapter 7, 11 or 12)</li> <li>• Account Status = status at time of petition</li> <li>• Payment History = increment first position with value 'D' (plus prior months' history)</li> <li>• Current Balance = outstanding balance amount</li> <li>• Scheduled Monthly Payment Amount = contractual monthly payment amount</li> <li>• Amount Past Due = dependent on status</li> <li>• Date of Account Information = current month's date</li> </ul> <p><b>Note: After reporting the discharge CII for all Filers, discontinue reporting the account.</b></p>

## If all borrowers filed bankruptcy:

	<b>All Borrowers Filed Bankruptcy Chapter 7, 11 or 12</b>
Reaffirmation of Debt Rescinded	<ul style="list-style-type: none"> <li>• CII = V (Chapter 7 Reaffirmation of Debt Rescinded)</li> <li>• Account Status = status at time of petition</li> <li>• Payment History = increment first position based on previous month's Account Status, plus prior history</li> <li>• Current Balance = outstanding balance amount</li> <li>• Scheduled Monthly Payment Amount = contractual monthly payment amount</li> <li>• Amount Past Due = dependent on status</li> <li>• Date of Account Information = current month's date</li> </ul> <p><b>Note: After reporting CII 'V' for all Filers, if the bankruptcy has been discharged, discontinue reporting the account. If the bankruptcy has not yet been discharged, continue reporting the account and Filers with the applicable CIIs.</b></p>
BK Dismissed	<ul style="list-style-type: none"> <li>• CII = I, J or K (BK Chapter 7, 11 or 12 Dismissed )</li> <li>• Account information as it applies going forward</li> </ul>
BK Withdrawn	<ul style="list-style-type: none"> <li>• CII = M, N or O (BK Chapter 7, 11 or 12 Withdrawn)</li> <li>• Account information as it applies going forward</li> </ul>

# What is The Discharge And What Does it Mean?

- Continued: What about credit reporting?

	<b>Filer(s) and Non-filer(s)</b>
Month BK Filed	<ul style="list-style-type: none"> <li>CII for Filer(s) = A, B or C (Petition for BK Chapter 7, 11 or 12)</li> <li>CII for Non-filer(s) = Blank</li> <li>Account Status = applicable status for consumer(s) who did <u>not</u> file Bankruptcy</li> <li>Payment History = first character based on previous month's status plus prior history</li> <li>Current Balance = outstanding balance amount</li> <li>Scheduled Monthly Payment Amount = contractual monthly payment amount</li> <li>Amount Past Due = dependent on status</li> </ul> <p><b>Note: Authorized Users (ECOA Code 3) on accounts included in a bankruptcy petition should either be terminated (ECOA Code T) or deleted (ECOA Code Z) from the account because they are not contractually liable for payments.</b></p>
Months Between Petition Filed & BK Resolution (Reaffirmation of Debt, Lease Assumption, Discharged, Dismissed, Withdrawn)	<ul style="list-style-type: none"> <li>CII for Filer(s) = Blank (previous petition value reported is retained) or CII = A, B or C</li> <li>CII for Non-filer(s) = Blank</li> <li>Account Status = applicable status for consumer(s) who did <u>not</u> file Bankruptcy</li> <li>Account information as it applies going forward for the Non-filer(s)</li> </ul>
Reaffirmation of Debt or Lease Assumption	<ul style="list-style-type: none"> <li>CII for Filer(s) = R (Reaffirmation of Debt) or 2A (Lease Assumption)</li> <li>CII for Non-filer(s) = Blank</li> <li>Account information as it applies going forward</li> </ul>
BK Discharged	<ul style="list-style-type: none"> <li>CII for Filer(s) = E, F or G (Discharged through BK Chapter 7, 11 or 12)</li> <li>CII for Non-filer(s) = Blank</li> <li>Account information as it applies going forward for the Non-filer(s)</li> </ul> <p><b>Note: After reporting the discharge CII for the Filer(s), discontinue reporting the Filer(s).</b></p>

## Not all borrowers filed bankruptcy:

	<b>Filer(s) and Non-filer(s)</b>
Reaffirmation of Debt Rescinded	<ul style="list-style-type: none"> <li>CII for Filer(s) = V (Chapter 7 Reaffirmation of Debt Rescinded)</li> <li>CII for Non-filer(s) = Blank</li> <li>Account information as it applies going forward for the Non-filer(s)</li> </ul> <p><b>Note: After reporting CII 'V' for the Filer(s), if the bankruptcy has been discharged, discontinue reporting the Filer(s). If the bankruptcy has not yet been discharged, continue reporting the account and Filer(s) with the applicable CIIs.</b></p>
BK Dismissed or Withdrawn	<ul style="list-style-type: none"> <li>CII for Filer(s) = I, J or K (Dismissed through BK Chapter 7, 11 or 12) or M, N or O (Withdrawn through BK Chapter 7, 11 or 12)</li> <li>CII for Non-filer(s) = Blank</li> <li>Account information as it applies going forward</li> </ul>

# What is The Discharge And What Does it Mean?

- Continued: What about credit reporting?

It is noted that case law and other authorities are very mixed on the topic of how credit reporting on mortgage debt is affected by a bankruptcy discharge.

For example, NOLO.com states that after discharge, *all* debts must be reported as having a zero balance and must further indicate that it was included and/or discharged in a bankruptcy. (<http://www.nolo.com/legal-encyclopedia/can-debts-discharged-bankruptcy-appear-my-credit-report.html>).

Other proprietary websites, blogs, and articles promulgate differing opinions on reporting of secured debt, and run the gamut from showing the debt as fully paid to reporting the full balance as due and owing despite a discharge.

Both extremes seem excessive, if not unwise, and the better reasoned result may lie somewhere in between.

Adding to the confusion, some articles distinguish between whether the mortgage debt is for a primary or non-primary residence.

The best way to handle reporting is to follow the CDIA Guide.



# What is Needed to Close a Bankruptcy in The System?

## Implementation

- Update the system of record as soon as the Plan is Confirmed.
- The system can also be updated if there is a stipulated agreement that provides for immediate implementation of the terms.



## Default

- Know how to monitor for *and* handle defaults under the Plan.
- Ensure that defaults are handled in strict adherence of the confirmed plan.
  - If the plan calls for notice to be sent via certified mail or a notice be filed with the court first, etc.



## Discharge or Admin Close?

- Release from bankruptcy only if there is a clear understanding of where the loan itself is at with respect to the confirmed plan, automatic stay, default, the discharge injunction, and bankruptcy court retention of jurisdiction over certain acts.

## Webinar Wrap-Up

### Questions

If you have a question regarding today's presentation, please contact the ALFN or any of the presenters directly.

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