

Family Law and Bankruptcy

This paper will be divided into two sections. The first will be a general overview of the typical issues surrounding family law cases and what happens when a bankruptcy is filed. The second section will be an update on how the different sections of BAPCPA relating to domestic support obligations have been interpreted by the courts.

For simplicity, the family law topics will be generally divided into three parts, divorce, enforcements and establishment of support. The relevant bankruptcy sections will generally be found in 11 U.S.C. § 101(14A) and 11 U.S.C. § 362(b)(2). Section 101(14A) states:

The term “domestic support obligation” means 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;

© 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 the debt.

Section 362(b)(2) states the automatic stay is not in effect for the:

- (A) . . . the commencement or continuation of a civil action or proceeding—
 - (I) for the establishment of paternity;
 - (ii) for the establishment of 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;
- © 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;
- (D) of the withholding suspension, or restriction of a driver’s license, a professional or occupational license, or a recreational license, under State law, as specified in section 466(a)(16) of the Social Security Act;
- (E) of the reporting of overdue support owed by a parent to any consumer reporting agency as specified in section 466(a)(7) of the Social Security Act;
- (F) of the interception of a tax refund, as specified in sections 464 and 466(a)(3) of the Social Security Act or under an analogous State law; or
- (G) of the enforcement of a medial obligation, as specified under title IV of the Social Security Act.

D-I-V-O-R-C-E

The general issues surrounding a divorce and bankruptcy is what type of divorce is being sought and who are the parties to the divorce. Now, I know the second part of that sentence sounds particularly odd, but bear with me. It is assumed by most family law judges a motion to lift stay must be done prior to their granting a divorce if one of the parties is involved in a pending bankruptcy. This is not so.

If your client just wants to be divorced from their lovely spouse and does not seek any type of property division, the stay does not need to be lifted. This situation arises primarily when one spouse has not seen, heard from, or has cared where the other spouse has resided for a number of years. What prompts them to seek a divorce after years of peaceful non-cohabitation is their new significant other would like to give a go at this marriage thing and suddenly realizes they cannot marry as your client is still married to someone they have not seen in 10 years. So, in the interest of treating their new significant other as a foreclosure house that needs some renovation to make it more habitable, the push is to get them to straighten out their life in the form of a bankruptcy and a divorce. Think of it as a personal deep spring cleaning; sweep out the old debts and old relationships so this new one can flourish.

But, under § 362(b)(2)(iv) if there is not a property division, then there is no need to lift the stay. As a practical consideration, though, convincing a scared, leery of sanctions, state court judge, the stay does not need to be lifted will be difficult. The state court judge wants the protection of the stay being lifted to avoid any unpleasant treatment by the bankruptcy judge.

If there is to be a property division, then the stay must be lifted prior to the granting of a final decree. The thorny issue for you is that odd statement I made at the beginning of this section, who are the parties to the divorce? If it is your, at one time happy joint debtors, in your chapter 13 bankruptcy, then there may be ethical considerations for you to consider. Issues concerning how the property is to be divided; who will be responsible for paying the trustee fees; whether there will be one joint bankruptcy after the divorce or will there be two; and whether both will stay in the same chapters. Your continued representation of both debtors seeking a divorce in state court could prove impossible if they choose to sever their case with each ending up with their own bankruptcy. How do you reconcile classifications of debt in the new bankruptcies with the adverse effects for who is liable for what debt, innocent spouse liability under IRS regulation, discharge issues as to debts against each spouse, etc. Paying attention to

Texas Disciplinary Rules of Professional Conduct rules 1.05 and 1.06 will be necessary to determine if you need to withdraw as counsel of record. See also § 327 of the bankruptcy code that appears to not allow the parties to sign a waiver of conflict of interest that might allow you to continue to represent the parties under state law.

Establishment of Support, Paternity and Modification

Section 362(2)(b)(A)(I), (ii) and (iii) allow these suits to continue without any need to lift the automatic stay. Once again, as a practical matter, the state court judge may want the stay lifted just to feel safe and secure. The primary issue in these state court actions is what type of classification should a state court award of attorney fees be under the bankruptcy code. Your debtor would like the classification to be one of a debt that can be discharged, while the creditor is trying valiantly to turn their judgement for attorney fees into a Domestic Support Obligation (DSO).

Under pre-BAPCPA cases, federal bankruptcy law, rather than state law, determined if a debt was in the nature of alimony, maintenance or support and did classify judgements for attorney fees as alimony, maintenance and/or support. See *In re Hudson*, 107 F.3d 355 (5th Cir. 1997). In *Hudson*, a state court law suit for paternity became highly convoluted with a secondary suit for fraud being brought when Mr. Hudson decided to go to another court to set aside an irrevocable trust to his children as he was being tried in a paternity suit. The judge in the paternity suit became creative and also determined the jury trial on the issue of paternity should be made more interesting when he allowed the jury to ask written questions of all the witnesses. Needless to say, the attorney fees rapidly became quite high in the case. The Fifth Circuit Court allowed a state court judgement for attorney fees to stand as child support even though there was some evidence certain elements of the judgement included fees for the fraud action.

One would think after BAPCPA, the issue of who would be entitled to claim a DSO classification would be clear and concise. Not so. *In re Lauderdale*, 2006 WL 2633859, S. D. Tex. 2006, the Court held attorney fees for an *ad litem* should be classified as a DSO. A quick check of § 101(14A) which defines who can claim a DSO debt very noticeably does not include *ad litem*s.

In our neck of the woods, you also have choices. In an adversary proceeding, 07-04040, *Loe, Warren, Rosenfield, Katcher, Hibbs, & Windsor, P.C. v. Brooks*, 371 B.R. 761 (Bankr.N.D.Tex. 2007), Judge Lynn found a law firm does not fall under any of the classifications of DSO debtors in § 101(14A) and § 523 (5) and (15) and their debt was dischargeable. The fees were in regards to a divorce proceeding where the law firm was awarded the judgement for the fees in their name and not in the ex-spouse's name.

However, in a February 1, 2008 opinion by Judge Houser, in 06-35493-BJH-13, *In re Jeffrey Todd Van Dermark*, 2008 WL 319107 (Bankr. N.D. Tex.), issued a somewhat different ruling. The issue in *Van Dermark* revolved around a Georgia divorce court ruling for attorney's fees. In that Georgia divorce proceeding, the Court awarded attorney fees to the law firm representing the wife in the law firm's name only. Seems very similar to the above situation in *Brooks*, so a similar result should occur, right? That would be too easy. The facts in *Van Dermark* differ from *Brooks* in that the ex-spouse in *Van Dermark* paid the attorney fees to the Georgia law firm. She then filed a proof of claim as a DSO creditor in the bankruptcy court, claiming an assignment of the law firm's judgement had been made. An objection to the ex-spouse's claim was made by the debtor in that it should not be treated as a DSO obligation. The actual written assignment was not made by the law firm until days before the hearing on the objection to claim. Judge Houser found the law firm's claim assigned to the ex-spouse should be allowed as a DSO obligation. So, you might have to check which court you are in to determine the status of a claim for attorney fees in a family law case.

Enforcement

An enforcement action in family law creates all sorts of problems in a bankruptcy case. The first determination needs to be what type of enforcement is being sought. Contempt can be either coercive or punitive. If it is punitive, it is treated as a criminal action and is exempt from the automatic stay under § 362(b)(1). If it is coercive in nature, the automatic stay will protect the debtor and stay the enforcement proceeding. The problem is trying to determine which type of contempt is being sought against your debtor. Usually, both types of contempt, punitive and coercive, are pled. If your debtor was sentenced to a term certain without any hope of being released prior to the end of their sentence, then the enforcement is punitive. If the sentence end date is conditioned with an amount of funds that need to be paid prior to release, then the enforcement is coercive.

There is also two secondary issues regarding enforcement proceedings. The first is § 362(b)(2)(B) regarding collection from property not in the bankruptcy estate. Texas generally has very broad exemptions as to what is eligible to be seized for the satisfaction of a debt. Unless, it is a child support debt. About the only thing protected under Texas exemption laws regarding child support debts is the actual homestead. So all the property that has been listed as exempt in the schedules is fair game for collection and enforcement proceedings in state court. And because of the unique supremacy clause, it appears as you could argue even the homestead would be subject to seizure by a DSO claimant as it is not property that is part of the bankruptcy estate.

The second issue regards medical enforcement. With provisions providing payment of medical insurance, actual medical support and unreimbursed medical expenses in most divorce decrees, many debtors have medical support obligations. Section 362(b)(2)(G) allows for a suit for enforcement of a medical obligation regardless if it is punitive or coercive. If the enforcement suit is limited to just medical enforcement, and there is an order placing the debtor in jail, bankruptcy relief to get out of jail may not be an option as with an enforcement action for child support.

In this case, as with an enforcement action limited to punitive contempt, the only option you might have to get your debtor out of jail would be to plead under the equity powers of the court, that it will be impossible for your debtor's plan to succeed if they are in jail.

BAPCPA Interpretations

Attorney Fees

In re Bellamy, 379 B.R. 86, (Bankr. D. Md. 2007). Court considered order payment of bankruptcy attorney fees in light of DSO claims. Although they determined DSO claimants might be entitled to payment prior to bankruptcy attorney fees, since the debtor's attorney was providing ongoing services, allowed the trustee to escrow 20% of the allowed fees pending completion of the case or further orders of the Court.

Bad Faith

In re Miller, 07-32080, 2007 WL 4563445 (Bankr. W.D. Ky. Dec. 21, 2007). Debtor had prior bankruptcy case where ex-spouse's claim was determined to be nondischargeable. In new ch. 13 case plan only proposed payment to ex-spouse of 10%. Court found proposed plan was made in bad faith.

DSO Obligations

In re Forgette, 379 B.R. 623 (Bankr. W.D.Va. 2007). Divorce decree ordered debtor to pay a third party. Ex-spouse filed proof of claim in bankruptcy to receive payment to 3rd party (car creditor) as she was liable as it was a joint debt. Court ruled ex-spouse had no standing as divorce decree ordered payment to 3rd party and not her.

Child Support Liens

Faillace v. Moriarty 324 B.R. 243 (Bankr. M. D. Pa. 2004). Recording of Divorce Decree with \$150,000.00 obligation in county records operated as a lien on debtor's real estate that had priority over any subsequent judgement liens.

Partial Discharge

In re Munck, 02-41690, 2007 WL 4354418 (Bankr. D. Kan. Dec. 7, 2007). State of Kansas child support division filed proof of claim for reimbursement support only, not court ordered child support. Was attempting to get the funds paid by the Kansas on behalf of the debtor's children through various aid programs. Plan that was confirmed provided for this debt to be discharged. Kansas did not object. Kansas bound by confirmed plan.

DSO Priority Claims

In re White, 07-03870 2008 WL 682422 (Bankr. S. D. Miss. Mar. 7, 2008). Debtor attempted to put post petition arrears in plan. Did not have any prepetition arrears. Court held anticipated post petition DSO payments are not proper to be put in plan.

In re Johnson, 07-51275, 2008 WL 553221 (Bankr. M.D.N.C. Feb. 27, 2008). Plan did not provide for mortgage payments that were part of a hold harmless provision in debtor's divorce decree. The Court found the payments on the mortgage were in the nature of maintenance and support of his children and must be provided for payment in full in the plan.

In re Sprouse, 2008 WL 544999 (Bankr. D. Neb. Feb. 25, 2008). Ex-spouse of debtor claimed debt in a divorce decree was a DSO claim. Court examined the divorce decree and determined the provision was a property settlement agreement and was not entitled to DSO status.

In re Poole, 383 B.R. 308 (Bankr. D.S.C. 2007). Ex-spouse claimed certain debts and attorney fees were a DSO obligation and wanted the Court to enforce a hold harmless clause in the divorce decree. The Court examined the divorce decree and determined the division of debts was a property settlement, the payments were to be made to 3rd parties and the debts were not DSO obligations. Court found insufficient evidence to support ex-spouse's claim division of debts was in the nature of support or alimony.

In re Hernandez, 07-40470 2007 WL 3998301 (Bankr. E.D. Tex. Nov. 15, 2007). Court found post petition interest that accrues on a DSO is not entitled to priority status and is not recoverable under the chapter 13 plan.

In re Eichwedel, 06-81327, 2007 WL 2212396 (Bankr. C.D. Ill. July 30, 2007). Court found obligation for child support was a DSO and it continued to accrue interest until paid in full under Illinois law.

In re Reid, 06-50147, WL 2077572 (Bankr. M.D.N.C. July 19, 2006). Court found under state law the DSO accrued interest. Court then found the plan "must provide for the payment of any interest accruing pursuant to nonbankruptcy law on any claims for domestic support obligations."

In re Van Nice, 07-60080, 2007 WL 2178069 (Bankr. D. Mont. July 26, 2007). Court found divorce decree that required debtor to make best effort to pay children's college expenses was a DSO and the entire amount of the college expenses had to be paid through the plan in full.

In re Lepley, 07-20344, 2007 WL 2669128 (Bankr. W.D. Mo. Sept. 6, 2007). Court examined divorce decree to determine if debt was a DSO obligation. Divorce decree's characterization is not binding, but it is a starting point.

In re Knox, 07-11082, 2007 WL 1541957 (Bankr. E.D. Tenn. May 23, 2007). Divorce decree stated allocation of credit card debt would be nondischargeable under § 523(a)(15). Court examined the divorce decree and determined the allocation of debt was a property settlement and not a DSO obligation.

Stay Violations

Florida Dept of Rev. V. Omine, 485 F.3rd 1305 (11th Cir.2007). State of Florida child support division attempted numerous times to collect child support arrears outside of the plan through either wage withholding or threatened interception of income tax refunds. State filed a proof of claim in debtor's bankruptcy. Court found Florida violated the automatic stay, did not have sovereign immunity and was sanctioned.

In re Gellington, 363 B. R. 497 (Bankr. N.D. Tex. 2007) Texas Attorney General filed proof of claim for child support and plan was to pay arrears through the plan. Texas AG then issued wage withholding for both the current support and arrears. Court found the current support wage withholding order did not violate the automatic stay. Court did find the withholding order for arrears did violate the automatic stay. Did not issue sanctions as Texas AG agreed to promptly refund the funds to Debtor.

Trustee's Avoidance Power

In re Persley, 07-00407, 2008 WL 249855 (Bankr. D.D.C. Jan. 25, 2008). Wife obtained a relief from stay to proceed in a state court divorce division of property including Husband's interests in retirement and stock option plans. Trustee managed to condition the stay to allow him the ability to recover any interests the debtor might have in an employee stock ownership plan.

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