

In this scenario, your client is considered an unsecured creditor. Does this mean she is out of court and will never get what she bargained for in the settlement?

In fact, under the new bankruptcy law, she is protected, because some debts are not dischargeable, including domestic support obligations and equitable distribution awards and agreements.

The Reform Act 11 USC §101(14) defines the term "domestic support obligation."

A domestic support obligation, which is not subject to discharge if certain criteria are met, 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."

A bankruptcy court, not state court, determines whether an obligation is support or equitable distribution, not state court.

The bankruptcy court is not bound by the labels the parties use in their agreement. But the court has said significant weight will be given if parties have labeled an obligation as support. In the past, bankruptcy courts have considered such factors as whether payments are made in monthly installments over time or in a lump sum and the purpose of the payments.

If your client's ex-husband filed a Chapter 7, she should receive all of her alimony, equitable distribution award, counsel fees and credit card debt repayment.

In fact, 11 USC §523(a)(15) completely eliminates the distinction between orders providing for division of property and orders providing for support of a spouse or child.

Previously, orders dividing property were dischargeable and support was not. Now, all obligations owed to a spouse, former spouse or child of a debtor incurred in connection with a divorce or separation agreement to other family-law related order are nondischargeable in a Chapter 7.

Chapter 13

But what if your client's ex-husband filed a Chapter 13?

In this scenario, the ex-husband can claim very few exemptions, but enters into a three-to-five year payment plan to pay back the secured creditors. Most of the unsecured debt owed to your client will still be discharged.

In a Chapter 13, there is a distinction between domestic support obligations, or DSOs, and equitable distribution awards.

DSOs cannot be discharged but equitable distribution awards and agreements can be discharged in some cases.

You may be thinking, "Am I really out of court for the equitable distribution? What about counsel fees and all of that credit card debt my client's ex-husband was supposed to pay?"

Well, there still may be some hope.

Your client may still get paid her equitable distribution award even if her ex-husband filed a Chapter 13, because the Chapter 13 plan may fail for the following reasons:

- Your client may timely object to the plan before it is confirmed to protect her equitable distribution claim.
- A discharge of equitable distribution only occurs if a debtor completes an entire Chapter 13 plan. Discharge does not apply if the debtor applies for an early discharge or if the case is dismissed. Nationwide, less than 50 percent of Chapter 13 debtors complete all of their plan payments, thereby resulting in the case being dismissed.
- The debtor must pay all support obligations that come due after the date of the bankruptcy filing or the court will not confirm the plan. The debtor must also remain current on his or her support obligation, or risk having his or her house sold to satisfy the DSO.

Therefore, if your client makes her claim as a creditor, all she has to do is sit back and wait.

It is very likely her ex-husband will not make all of the plan payments and, therefore, the bankruptcy will be dismissed and your client will get paid.

The ex-husband also has to certify that all of his support is current and all arrears are paid! What a gift from the bankruptcy court.

Probably more than half of the family law attorneys reading this article can identify at least three cases where clients are behind on their support and owe arrears.

Other 'Gifts'

A few other gifts the reform act gave to a debtor include making DSOs first priority.

The bankruptcy code established an order by which claims are paid from the bankruptcy estate. All creditors with higher priority must be paid in full before creditors with lower priority receive payment. Two creditors with equal priority get paid equally and receive prorated shares of their debt. DSOs assigned to a governmental unit, such as the Department of Public Welfare, are second priority. Therefore, your client gets paid before most creditors.

Prior to the new code it was unclear whether a spouse could proceed with a support action without seeking relief from the automatic stay.

Under the amendments, however, the statute clearly states the automatic stay does not stay support actions, actions for divorce (with no ancillary property claims), custody, abuse or the establishment, modification or collection of "a domestic support obligation from property that is not property of the estate."

Since income or assets received by a debtor after the filing of a Chapter 7 is not property of the estate, a creditor may file an action to establish, modify or collect back support from a Chapter 7 debtor, to the extent the creditor seeks to attach current income or assets acquired after the filing of a Chapter 7.

Bankruptcy isn't that scary after all.

Impact on Practice

How does the new act affect the family law practitioner?

If you are owed attorney's fees and another client, a husband in similar case, successfully receives a discharge in a Chapter 7, you most likely will not get paid unless there are assets that are not exempt.

If a debtor was court-ordered to pay your fees as part of the equitable distribution award, support order or other penalty, such as discovery or contempt, then it may depend on the type of bankruptcy filed as to whether you get paid. If the fees were granted as part of an equitable distribution award, they are probably not dischargeable in a Chapter 7. They probably are dischargeable in a Chapter 13, however. If the fees are "support," they are nondischargeable in both a Chapter 7 or 13.

If a client pays a retainer you deposit into your escrow account and the client later files bankruptcy, you may have to return the unused retainer to the client or the bankruptcy trustee. In a Chapter 7 or 13, the unapplied funds are part of the bankruptcy estate.

Finally, here are some hot tips to consider when drafting a property settlement agreement:

- A spouse's obligation to pay sums due for equitable distribution or to assume a marital debt could be discharged.
- A bankruptcy court judge might not consider a debtor spouse took over an obligation owed a non-debtor spouse for a more relaxed support obligation.
- Counsel fees owed to the non-debtor spouse may be dischargeable by the debtor spouse.

Consider the dilemma if an ex-wife is living in the marital home with the children and the ex-husband's name is still on the marital residence when the ex-husband files a Chapter 13.

The ex-husband must certify all support has been paid to his ex-wife so the Chapter 13 plan can be confirmed. If the support has not been certified as having been paid, the ex-husband's residence may be sold to settle his obligation.

May the ex-wife waive her right to have her ex-husband certify support is current or even waive her right to the support? May she waive the child's right to support? May she waive her right to certify all money has been paid or the right of the child in order to save the house?

What if she is to receive the marital residence in equitable distribution? What if the Chapter 13 plan gets dismissed subsequent to her waiver?

OK, maybe bankruptcy is a little scary after all. Hopefully, after reading this article you have the tools necessary to ask the right questions and get your client what she bargained for in the divorce. •

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