



# THE ENFORCER

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## **BANKRUPTCY AND DIVORCE: A LIKELY PAIR**

Divorce and bankruptcy are often intertwined, more so today due to the depressed economy. This column has raised some pretty sophisticated insolvency issues for family practitioners to consider. After five years, it seemed like an appropriate time to take a step back and offer a primer of some basic bankruptcy concepts.

Much of divorce revolves around the division of assets and liabilities, both of which are significantly affected by bankruptcy. Therefore, it can make sense for people who are in financial distress and divorcing to meet with bankruptcy counsel as part of their divorce plan. Following is a brief overview to familiarize you with a few bankruptcy concepts that frequently impact the family law universe.

### **Property of the Estate in a Chapter 7<sup>1</sup>**

Upon the commencement of a bankruptcy case, an estate is created. It is comprised of all legal or equitable interests of the debtor in property as of the commencement of the case, subject to certain exceptions. This includes a Debtor/spouse's interest in marital property. See 11 U.S.C. §541 for the full definition. For family law attorneys, it is important to understand the concept of "property of the estate". This is because in the event of a party's pre-judgment bankruptcy filing, you might have to negotiate your client's property settlement with the bankruptcy trustee.

### **The Automatic Stay**

Do you understand when you can, and cannot, proceed in a family law case when one or both parties are in bankruptcy?<sup>2</sup> The infamous "Automatic Stay" found at 11 U.S.C. § 362 provides generally that the filing of a bankruptcy petition

stays the start or continuation of certain proceedings to collect a debt, or against property, of the debtor. However, there are many specific exceptions which are particular to family law matters:

- § 362(b) The filing of a petition....does not operate as a stay –
  - (1) under subsection (a) of this section, of the commencement or continuation of a criminal action or proceeding against the debtor;
  - (2) under subsection (a) –
    - (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 not 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 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;

\* \* \*

### **Exceptions to Discharge and Domestic Support Obligations**

People typically file for bankruptcy seeking discharge from their debts. However, not every debt is dischargeable in bankruptcy. Many attorneys fail to recognize that in family practice there are two debts: one is the obligation to the creditor and the second is the one set forth in the Judgment of Divorce for indemnification. The exceptions to discharge are set forth in 11 U.S.C. §523, and are worth review. They include two that directly relate to support and indemnification obligations created by a divorce decree:

§523(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt –

\* \* \*

(5) for a domestic support obligation;

\* \* \*

(15) to a spouse, former spouse, or child of the debtor and not of the kind described in paragraph (5) that is incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court of record, or a determination made in accordance with State or territorial law by a governmental unit;<sup>3</sup>

\* \* \*

The bankruptcy code defines domestic support obligation or "DSO" at 11 U.S.C. §101(14A). It includes those obligations that are "in the nature" of alimony, maintenance or support, and doesn't require those obligations to be labeled as such.<sup>4</sup> To appreciate the implications of the exceptions listed in

§523(a), it is necessary to understand how the bankruptcy code defines a DSO.

§101(14A) 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;

(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 the debt.

A knowledge of these basic bankruptcy concepts will enable you to more effectively communicate with your client's bankruptcy counsel and better understand your client's options.

## Endnotes

1. The Chapter 13 “property of the estate” definition is more expansive than for a Chapter 7. Section 1306 includes the assets set forth in Section 541 together with the Debtor’s post-petition income.
2. While I hope you find my columns helpful, it is recommended that you consult a bankruptcy attorney when the automatic stay is involved.
3. Note that the exception set forth in § 523(a) (15) is dischargeable upon the successful completion of a Chapter 13 Plan.
4. Whether an obligation is in the “nature of support” is based on bankruptcy law, not traditional state law concepts of support.

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