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HANDLING AND PROTECTING THE ASSOCIATION, WITH RESPECT TO AN OWNER'S BANKRUPTCY

Almost every day we go online, read the newspaper or watch the news without hearing about our recession, declining real estate values, lending institutions in trouble and the rise in residential foreclosures. During times like these, it is essential that every community create and maintain an effective, efficient and aggressive collection policy. Any such collection policy must account for an owner's bankruptcy.

For a bankruptcy filed after October 17, 2005, an owner must pay post-petition fees and assessments due to condominium associations, homeowners associations and cooperative corporations (collectively "Associations") after that bankruptcy is filed. If the debtor's bankruptcy was filed before October 17, 2005, the post-petition assessments must be paid by that debtor only if he either occupies the unit or rents it. In October of 2005, Congress extensively amended the Bankruptcy Code via a law that was known as the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (the "2005 Amendments").

Prior to the 2005 Amendments, assessments due to the Associations were non-dischargeable, so long as the debtor physically occupied a dwelling unit in the condominium or cooperative project; or the debtor rented the dwelling unit to a tenant and received payments from the tenant for such period. The 2005 Amendments eliminated these two provisions entirely and added language that clearly provides that mere ownership of a unit creates the non-dischargeability of the assessments. In the end, so long as the debtor has a mere ownership interest in the property, he must pay post-petition assessments with respect to any bankruptcy filed after October 17, 2005.

An individual owner can file either a chapter 13 or chapter 7 bankruptcy. Associations generally face the chapter 13, as it is this type of bankruptcy that allows an owner to preserve home ownership. Via a chapter 13, an owner has a "time out" so to speak, during which his creditors, including the mortgage company and association, cannot act to collect unpaid amounts. So long as the debtor adheres to the requirements of United States Bankruptcy law, he can maintain his home and pay the, presumably, delinquent mortgage over time.

While this discussion is certainly overly simplistic given the numerous issues related to bankruptcy, and the specific facts of each particular case, a "secured" debt is likely to be paid via a chapter 13 bankruptcy, and an "unsecured" debt is not. A mortgage is a "secured" debt. An association lien makes unpaid assessments into "secured" debt, and thus likely to be paid. In fact, the bankruptcy, by allowing the owner to free himself from certain debts, makes it more likely that there will be funds available to pay the association's secured claim. In turn, and in relation to the obligation to pay post-petition assessments, it is imperative that associations file the appropriate papers in connection with a bankruptcy. Otherwise, the association may lose the ability to recover, in bankruptcy, an otherwise recoverable debt. An owner's bankruptcy is not a death sentence with respect to an association's debt, but is instead an opportunity, to be seized upon by associations that are prepared and represented by skilled and creative legal counsel.

If you would like to discuss this client alert in more detail or how it may affect your community association, please contact David J. Byrne at 609-895-7365 or by email at dbyrne@stark-stark.com.