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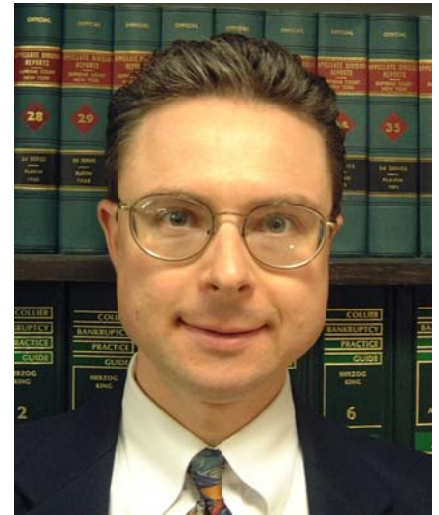
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CONSUMER BANKRUPTCY

Five Bankruptcy Practice Pointers to Deal with the Effects of the Real Estate Boom

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Most Long Island homes have doubled in value over the past six years. This increase in real estate values has produced a windfall of increased equity to those who own homes, which in turn has affected the bankruptcy options of those homeowners who have serious debt problems.

Despite this boom, foreclosures are at record numbers. This may be attributable in large part to easy financing that enables people to refinance and obtain home equity loans without having to satisfy their existing credit card debts. Although most bankruptcies are attributable to financial crises such as large medical bills, divorce, loss of job, etc., many homeowners get into a bind because they tap their home equity ostensibly to satisfy

existing consumer credit debt, yet continue to accumulate more debt.

The tremendous increase in real estate values also means that bankruptcy practitioners must be more careful in advising clients. In many instances, what was often done several years ago in the course of representing a consumer debtor homeowner should not be done today. Here are some tips and practice pointers that address how you should change your approach to such cases:

1. Be Cautious About Recommending Chapter 7 to Homeowners. Chapter 7 filings may not be feasible. Remember that the permitted homestead exemption in New York is only \$10,000 worth of equity per person.

In the early to mid 1990's, many homes had declined in value and had very little equity. It was common practice during that time for homeowners to take advantage of utilizing Chapter 7 to eliminate their credit card debts, yet keep and protect their homes. However, the recent increase in real estate values means that there are extremely few homes that would be fully exempt and protected. What would have worked smoothly several years ago will not necessarily work well today.

2. Be Cautious About Submitting Chapter 13 Plans That Pay Less Than 100%. Before the real estate boom, when many homeowners had relatively little equity in their homes, it was commonplace to see many Chapter 13 plans offering only a 10%

distribution to unsecured creditors, which is generally accepted as the smallest permitted distribution to that class of creditors. However, 10% plans in Chapter 13 cases for homeowners are becoming sparse as the amount of equity has substantially increased. If you offer a plan that pays less than 100%, the Chapter 13 trustee will very closely scrutinize that plan. If it appears that the amount of non-exempt equity is greater than the amount of unsecured debt, then you should consider a 100% plan.

Such 100% Chapter 13 plans offer many benefits over conventional refinancing. Generally, there is no interest on any mortgage arrears or unsecured debt. In most cases, only older mortgages which originated prior to October 1994 are entitled to interest. I explain to my Chapter 13 clients that a 100% plan is like a forced refinance that creditors must accept. It is as if the client borrowed all of the necessary funds to satisfy all existing debts, but was given the opportunity to pay that back with no interest over a five-year period.

3. Be Aware That Some Chapter 7 Trustees Are Becoming Very Aggressive. With the potential to administer a valuable asset (which in turn will pay the trustee a sizable commission), trustees are becoming very aggressive in trying to administer and sell houses as an asset of the bankruptcy estate. For this reason, even after you and your debtor client have engaged in due diligence before filing to ascertain the current fair market value of the property, it is quite possible to encounter a trustee who thinks the property is worth even more. The issues to consider in addressing such situations can easily take up an entire column and more, and I will try to devote a future column to this topic.

In any event, if you encounter a very aggressive trustee,

some possibilities include: negotiating a settlement that can be paid from exempt, borrowed or gifted funds; converting to Chapter 13 (which overly-aggressive Chapter 7 trustees will try to oppose); litigating against the trustee; or letting the trustee try to sell the house, in which event the debtor would have to leave upon a sale, but this would nevertheless require the trustee to pay the debtor the \$10,000 per person homestead exemption from the proceeds of sale.

4. Be Very Cautious About Real Estate Valuations. Several years ago, when real estate was not increasing at an incredible rate, many attorneys would simply tell their bankruptcy clients to obtain broker price opinion letters in order to determine the value of their property. However, in today's very volatile real estate market in which values can change overnight, it is essential to utilize the services of an unbiased and highly qualified real estate appraiser. Be aware that in Nassau County, where there is a property value assessment system, the assessed value is not an accurate indication of the current value of the property.

Also be cautious that the appraisal can become obsolete within a matter of weeks or months. Many a client will retain a bankruptcy attorney, obtain an appraisal, and then put off filing for many months. If this happens, you should consider obtaining an update on the appraisal if the disposition of the existing case is very dependent on the real estate valuation.

Another difference in today's practice is that trustees generally no longer rely on appraisals submitted by debtors or their counsel. Several years ago, trustees would often accept submitted appraisals as conclusive proof of the value of real estate. Today however, many trustees will

obtain their own independent real estate valuation, often well before the meeting of creditors. Accordingly, the real estate appraisal is becoming more of a tool to assist counsel in determining how to best represent the client, than a means for persuading a trustee that there is little equity.

5. Consider Non-Bankruptcy Options Such as Refinancing or Sale. Bankruptcy is not the answer for everyone. Some debtors cannot file chapter 7 because of extensive non-exempt real estate equity, yet they are not eligible to file Chapter 13 because they do not have sufficient income to fund a plan. Keep in mind that there are a number of lenders who specialize in the sub-prime market. However, many individuals who are over-extended, or who have already cashed out most of their home's equity, may not qualify for any type of financing. If bankruptcy and refinancing are both out of the question, then the only remaining option may be for the debtor to sell the home. It is important to help your clients be realistic about their options.

Editor's Note (revised 2008): Craig D. Robins, Esq., a regular columnist, is a bankruptcy attorney who has represented thousands of consumer and business clients during the past twenty years. He is located in Nassau County and Suffolk County with offices in Medford, Commack, Woodbury and Valley Stream. (516) 496-0800. He can be reached at CraigR@CraigRobinsLaw.com. Please visit his Bankruptcy Website: CraigRobinsLaw.com.