

CONSUMER BANKRUPTCY

HOA Dues in Bankruptcy Cases — Debts Not Treated Like Ordinary Deb

By Craig D. Robins

Consumers who own co-ops and condos have monthly obligations to a homeowner's or community association. What happens when a consumer seeks bankruptcy relief? Can the consumer discharge HOA dues?

Although consumers can easily discharge many types of debts, discharging HOA dues is somewhat more complicated. In general, HOA dues that exist at the time of the bankruptcy filing can be discharged, but dues that arise after the date of filing cannot.

Let's look at some history. Prior to the 2005 Bankruptcy Amendment Act (BAPCPA), there was a great deal of confusion regarding dischargeability of HOA dues. A Bankruptcy code section that was added in 1994 in an effort to simplify things, actually made HOA dischargeability issues more unclear.

As a practical matter, prior to 2005, most homeowners were able to walk away from their units and not worry about HOA fees because the lender or new owner would ultimately have to pay the HOA arrears when the unit was eventually resold. This approach no longer works.

When Congress overhauled the laws with BAPCPA, it decided that, based on public policy, HOA associations deserved a certain amount of protection. Since HOAs are comprised of fellow homeowners, as opposed to being a for-profit corporation, Congress determined that it would be an unfair burden for one bankrupt homeowner to severely hurt the other homeowners. The fact that HOAs had a strong lobbying effort at the time certainly helped. Accordingly, Congress decided to promulgate a new statute making some HOA dues dischargeable, and others non-

dischargeable.

HOA dues that a consumer owes pre-petition are dischargeable. That means a consumer can discharge HOA arrears in a Chapter 7 case. However, HOA dues that arise post-petition are not dischargeable. See Bankruptcy Code section 523(a)(16).

This becomes a very delicate issue with many of my clients.

A great number of homeowners are "underwater" and have no equity in their homes. A common strategy for these folks who find it difficult to make the monthly mortgage payments or have an unmanageable amount of arrears is to discharge their mortgage obligation in a Chapter 7 case and eventually walk away from the home. However, this approach does not work so smoothly for those with co-ops and condos.

In a bankruptcy proceeding, the homeowner can discharge the HOA arrears and any condo mortgage or co-op loan obligations. However, as long as the consumer remains the owner of the property, any post-petition HOA charges continue to accrue and they are non-dischargeable. This creates a dilemma for the homeowner. They can't easily walk away because they will remain on the hook for the HOA fees. In addition, the consumer can't just surrender the property.

To add to potential misery, banks are usually in no hurry to foreclose co-op and condo units because they know that once they obtain title, they will be on the hook for future HOA dues. Some consumers and HOAs in other jurisdictions have even brought suit against slow-moving lenders, alleging that they deliberately delayed the foreclosure proceedings.

This gridlock in moving forward can



result in a large buildup of nondischargeable debt for the beleaguered consumer. Unfortunately, there are no magic answers. The best approach in helping your Chapter 7 clients who have HOA dues is to explain how the law works. Sometimes a short sale will solve the problem, but this requires a cooperative lender.

Another approach is to negotiate some kind of surrender to the HOA combined with a deed-in-lieu of foreclosure, although some HOAs may not be interested in cooperating.

Of course, the obvious but undesirable option is for the homeowner to continue to pay the post-petition HOA dues until the property is no longer in the homeowner's name — either as the result of foreclosure or other means.

Homeowners who intend to keep their property after a Chapter 7 proceeding should be aware that HOA dues may or may not be secured debts. Whether they are would be governed by the contract entered into with the HOA when the unit was purchased. If the HOA has a lien, then the dues must be paid as a condition to remain in the property. If there is no lien, the debtor can discharge the pre-petition dues and remain in the property.

In Chapter 13 proceedings, if the homeowner is surrendering the property, the pre-petition HOA dues are treated as unsecured debt. However, the post-petition dues continue to be an obligation until ownership changes.

Some attorneys used to indicate in the Chapter 13 plan that the debtor is surrendering and/or abandoning the property in

the hope of escaping post-petition liability. However, this no longer works. Generally, when a debtor surrenders a property, it gives the lender increased ability to take certain action but it does not result in a transfer of legal title.

For homeowners in Chapter 13 intent on keeping the property, the arrears may be an unsecured debt if they are subordinated by the mortgage or property is underwater. In that case, the HOA lien can be stripped off by a motion pursuant to code section 541(c)(2). Of course, this only benefits the debtor if the plan pays significantly less than the amount of the debt. In any event, any HOA arrears would be through the plan either as secured or cured debt.

Unfortunately, like Chapter 7 cases, homeowners cannot discharge post-petition HOA dues in Chapter 13 filings.

The most important aspect in representing homeowners with HOA dues is to explain how post-petition obligations are not dischargeable and to assist with a reasonable strategy that take into consideration. It would be wise to prepare a letter to the client explaining the nondischargeability of post-petition dues and have the client sign it.

Note: Craig D. Robins, Esq., a real estate lawyer, is a Long Island bank lawyer who has represented thousands of consumers and business clients during the past twenty years. He has offices in West Babylon, Patchogue, Woodbury Valley Stream. (516) 496-0800. He can be reached at CraigR@CraigRobinsLaw.com. Please visit his Bankruptcy Web site at www.BankruptcyCanHelp.com and his Bankruptcy Blog: www.LongIslandBankruptcyBlog.com.