

# Chapter 13 Bankruptcy Reorganization/Debt Discharge - A Guide to the Distressed Florida Homeowner Facing Foreclosure

(as of March 13, 2009)

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1. Principal Residence – The following applies generally to principal residences in chapter 13 bankruptcy. The rules as to modification of mortgages on non-principal residences in chapter 13 bankruptcy may actually be more liberal. Changes allowing the more liberal modification of principal residence mortgages in chapter 13 are now before Congress and may soon be enacted. Other more liberal rules for modification may also apply to those qualifying as “family farmers” under chapter 12 bankruptcy.

2. Automatic Stay – With certain exceptions, the filing of a chapter 13 bankruptcy stays or stops most creditor collection actions, including mortgage foreclosure. The automatic stay provides a homeowner a “breathing spell” in order to allow him or her an opportunity to reorganize their debt while under the protection of the U.S. Bankruptcy Court.

3. Timing – Generally, a chapter 13 bankruptcy must be filed before a foreclosure sale if a person desires to attempt to save their home under a chapter 13 bankruptcy plan. A foreclosure sale is normally set by the Florida Circuit Court a number of weeks after the entry of the final judgment of foreclosure.

4. Chapter 13 Bankruptcy Prior to the Present Real Estate Crisis - Chapter 13 bankruptcy plans typically provided to reinstate first and second mortgages on a principal residence over a five year plan while at the same time paying the ongoing regular monthly mortgage payments. Mortgages secured only by a principal residence are generally not “modifiable” under present chapter 13 bankruptcy laws. Second mortgages that are wholly “underwater” are an exception to the rule against modification and may be avoided and deemed as “unsecured” claims and paid a dividend on the same basis as other unsecured claims such as credit cards. Unsecured claims are usually only paid a small percentage on the dollar under a chapter 13 plan.

5. Present Real Estate Crisis – Many homeowners owe more on their home mortgages than their present value (“underwater”) and many are unable to pay their monthly payments.

6. Proposed Changes to Chapter 13 - Changes to chapter 13 bankruptcy laws have not yet been enacted by Congress (as of March 13, 2009). Although a bill was passed by the House of Representatives on March 6, 2009, the bill has not yet been passed by the Senate.

The proposed changes to chapter 13 include a provision allowing in some circumstances the modification of a first mortgage on a principal residence by reducing (“cramming-down”) the principal balance down to the value of the home as well as a possible reduction in interest rate. The proposed changes to chapter 13 bankruptcy may require an attempt by the

homeowner to refinance or modify under the federal government's new "Making Home Affordable Program" prior to attempting to modify the mortgage under chapter 13 bankruptcy.

7. "Making Home Affordable Program" - last week the federal government announced updated information on its "Making Home Affordable Program."  
<http://www.financialstability.gov/makinghomeaffordable/>. This program provides for the refinancing or modification of a mortgage under certain circumstances. More information is available from the federal government's "Homeowner's HOPE Hotline" at (888) 995-HOPE.

8. The Typical Present Distressed Homeowner's Situation - the typical South Florida homeowner is in a situation where the amounts owed on the first and second mortgages substantially exceed the value of his or her home. Many of the comparable sales are sales of foreclosed homes. Many first mortgages may be adjustable rate mortgages. Property taxes may be high for recent purchasers. Condominium and association fees may have risen due to the default of other unit owner's default.

9. What is the Typical Homeowner in Crisis Presently to Do? (March 13, 2009)  
a. Non-bankruptcy Refinancing or Modification – Most distressed homeowners should immediately contact their mortgage servicers or lenders to attempt refinancing or modifications. Patience may be required as the new provisions of the "Making

Home Affordable Program” are now being implemented. Efforts should be made even if you were previously turned down.

b. Participate in Florida Circuit Court Foreclosure Actions- A person who has been served with a mortgage foreclosure action should normally participate in the foreclosure action. There may be opportunities to mediate a modification with the mortgage company. The participation should begin by “answering” the foreclosure complaint within the time period set forth in the summons attached to the foreclosure complaint. The answer may be made by the homeowner himself or through an attorney.

c. Chapter 13 Bankruptcy Protection - If a homeowner is about to lose his or her home in a foreclosure sale, under appropriate circumstances, he or she may consider filing for chapter 13 bankruptcy relief before the foreclosure sale takes place.

i. The Second Mortgage - Most second or junior mortgages are “underwater” and would be avoidable even under the present chapter 13 laws. A wholly underwater second mortgage holder will be avoided and receive a dividend on the same basis as unsecured credit cards.

ii. The First Mortgage - The homeowner will seek to refinance or modify his or her first mortgage under the non-bankruptcy “Making Home Affordable Program” or on such other basis as may be available. As the mortgage company will normally have special bankruptcy counsel, a direct line of communication for modification is available facilitating efforts to modify. The chapter 13 plan will typically provide for the first mortgage in the first phase of the plan (i.e. months 1-30) and a dividend to unsecured creditors during the second phase of the plan (i.e. months 31-36). Until a refinancing or modification is reached, the

first mortgage company will receive its regular payment or such other lesser amount as may be appropriate.

iii. Possible Changes in Chapter 13 Bankruptcy Law - During the coming weeks, the bankruptcy bill may pass Congress and the chapter 13 debtor may have the ability to force a modification of the first mortgage under the chapter 13 laws. The proposed bankruptcy changes to chapter 13 are presently set to be retroactive to all pending cases. The proposed bill allows certain mortgage modification by way of reduction of the principal balance down to the value of the home and a change in interest rate. Adjustable rate mortgages may be modified to be fixed.