
Stop or Go? –Bankruptcy and Debt Collection

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Legal Disclaimer

- This presentation **does not** constitute legal advice. Prior to any legal or compliance changes within your organization, please consult your legal counsel.
- This presentation may be recorded for future dissemination.
- Finally, although we believe the information in this presentation is accurate as of this date, the statutes, regulatory guidance and case law in this area is constantly changing. Please continue to monitor, with your legal counsel, for changes.



Two General Types of Bankruptcy

Chapter 7 of Title 11 of the United States Code, bankruptcy laws:

- Trustee is appointed to administer the case, review debtor's bankruptcy papers and supporting documents. Chapter 7 trustee's job is also to sell the debtor's nonexempt property to pay back the debtor's creditors to the extent possible.
- Generally referred to as a "Liquidation bankruptcy": nonexempt assets are liquidated in order to pay back the debtor's unsecured creditors.
- Designed for low income debtors with little or no assets.

Chapter 13 of Title 11 of the United States Code, bankruptcy laws:

- Designed for debtors with steady income who will be able to make regular payments, to get caught up on payments on, or to pay off non-dischargeable debts, such as: federal student loans, alimony or child support arrears.
- In Chapter 13 bankruptcy, the debtor gets to keep all of his property (including nonexempt assets). In exchange, the debtor must pay back all or a portion of his debts through a repayment plan (the amount you must pay back depends on your income, expenses, and types of debt).
- Essentially, a Chapter 13 filing operates as a "Reorganization bankruptcy": the debtor keeps property and sets up a repayment plan.



The Automatic Stay

- The Automatic Stay applies to all creditors, not just ones listed by the debtor.
- Begins the day the debtor files the bankruptcy petition.
- As long as the stay is in effect (with very limited exception), it lasts the duration of the Bankruptcy case, and creditors (including debt collectors, servicers and those acting on the creditors' behalf) may not initiate or continue lawsuits, wage garnishments, or even send letters or place telephone calls demanding payments. Any one of these actions may subject them to monetary damages.
- Generally, our procedure at GRC is to keep the A/R & Perkins accounts open, anticipating that collection activity may resume once the bankruptcy is closed (if the debt is not discharged because the debt is a federal loan).
- Although the bankruptcy clerk gives notice of the bankruptcy case to all creditors whose names and addresses are provided by the debtor, the stay applies to every creditors, whether listed by the debtor or not. A best practice is to continuously scrub for bankruptcy filings/status (and instruct your debt collectors and other agents to do so as well).



Debts that Survive Bankruptcy

- Most unsecured debt is discharged in a bankruptcy. That includes most tuition and A/R receivables owed directly to an educational institution.
- Examples of debt that is NOT discharged in a bankruptcy:
 - Home mortgage
 - Alimony or child support
 - Certain taxes
 - Some debts that arise from criminal acts
 - Most government funded or guaranteed educational loans or benefit overpayments, including Perkins programs loans.
 - May include student loans funded in part by a nonprofit entity
- If a debt is not discharged, the debtor will continue to be liable (to the extent the debt is not paid in the Chapter 7 case).



What Type of Debt IS Discharged by Bankruptcy?

- A bankruptcy discharge releases the debtor from personal liability for almost all other types of debts, such as credit card loans non-federal student loans, and most unsecured debts.
- The Order of Discharge is a **permanent order** prohibiting the creditors, and their agents and debt collectors, from taking any form of collection action on discharged debts, including legal action and sending dunning communications to the debtor (also phone calls, letters, and personal contacts).
- The discharge will likely apply even if the debtor fails to properly schedule debt. Note: this can operate as a defense for creditors or their agents, which may be asserted in a subsequent contempt proceeding or FDCPA action.
- The availability of bankruptcy scrubbing technology and the collections industry standards will require creditors, and their debt collectors and servicers, to have systems in place in order to detect bankruptcy filings related to their consumer accounts.
- What happens after discharge? Any violation of the bankruptcy discharge may give rise to an FDCPA action against both the creditor and its collection agency.



Adversary Proceeding

Most federal student loan liabilities, like Perkins Loans and other Federally guaranteed loans are **not** dischargeable in a bankruptcy proceeding.

However, a debtor may file an “adversary proceeding” to attempt to have student debt discharged:

- Debtor must successfully argue for the student loan’s eligibility for nondischargeable status, and/or arguing that the court’s failure to discharge the student loan debt will constitute an “undue hardship” upon the debtor.
- Undue Hardship
 - Requires proof that the debtor will remain financially unable to pay the loan
 - Might involve a trial
 - Often involves a debtor with a physical disability who is unable to work
 - Most importantly, debtor must show that he/she made a “good faith” effort to repay the loan.



Aftermath of Bankruptcy for Creditors

- Depends on the Type of Bankruptcy Filing
- Chapter 7 Filing - a creditor holding an unsecured claim will get a distribution from the bankruptcy estate only if the case is an asset case and the creditor files a proof of claim with the bankruptcy court. If the trustee later recovers assets for distribution to unsecured creditors, the Bankruptcy Court will provide notice to creditors and will allow additional time to file proofs of claim. But if the case appears to be an “asset” case at the outset, unsecured creditors must file their claims with the court within 90 days after first date for meeting of creditors.
- Chapter 13 Filing – Since Chapter 13 is designed for an individual debtor who has a regular source of income, it allows the debtor to propose a “plan” to repay creditors over time—usually three to five years. Unlike Chapter 7, the debtor does not receive an immediate discharge of debts. The debtor must complete the payments required under the plan before the discharge is received. The debtor is protected from lawsuits, garnishments, and other creditor actions while the plan is in effect. The discharge is also somewhat broader.



How Do You Preserve Your Rights as a Creditor?

- First of all, GRC STRONGLY recommends that creditors and their agents, including collection agencies, continuously scrub accounts so that they can be immediately aware when a debtor files a bankruptcy.
- To avoid violating the stay, upon notice of the bankruptcy filing, creditors should do the following (and also instruct agents working on their behalf):
 1. Notify any and all debt collection agencies working on the debtor's accounts of the bankruptcy filing and of the automatic stay.
 2. Immediately cease all communications and collection efforts on the account.
 3. Halt or delete all furnishing of account information (i.e. tradelines) to the major credit reporting agencies (e.g. Experian, Equifax, Transunion), or, at a minimum, annotate within the tradeline that the account is subject to the consumer's bankruptcy, and thereafter cease to actively furnish the tradeline on an ongoing basis (See Metro 2® Format for Credit Reporting, published by the Consumer Data Industry Association). As a best practice, GRC does not report bankrupt accounts and deletes the tradeline immediately.
 4. Track the bankruptcy proceeding to ensure it is completed and that the debtor indeed receives the Order of Discharge. At that point in time, the creditor can make a determination as to whether the debt it is owed has been discharged.



How Do You Preserve Your Rights as a Creditor? (Continued)

- Other practical considerations that creditors and their agents should plan for:
- **Filing a Proof of Claim**: unsecured creditors should file a Proof of Claim within 90 days of the first date set for the Meeting of Creditors
 - Generally not necessary if Chapter 7 and the debtor has no assets
 - A proof of claim is **not** collection activity and does not violate the automatic stay: reversing the 11th Circuit Court of Appeals, the United States Supreme Court recently held that filing a proof of claim on a debt that is time-barred does not violate the Fair Debt Collections Practices Act. *Midland Funding, LLC v. Johnson*, No. 16-348, 2017 WL 2039159 (U.S. May 15, 2017).



How Do You Preserve Your Rights as a Creditor? (Continued)

Student Loan Eligibility for Discharge Under Chapter 13 Repayment Plans

- If a Chapter 13 repayment plan includes provisions regarding repayment of student loans, an objection to the confirmation of the plan must be filed. This is because a Chapter 13 debtor is entitled to a discharge upon completion of all unsecured debts covered under the Chapter 13 plan. Said another way, **if the Chapter 13 plan seeks to eliminate, discharge, or otherwise impair the student loan creditor's claim, the student loan creditor must file an objection to confirmation of the plan.**
- Generally, collection activity may resume following the Order of Discharge, if the debts have not been discharged in the bankruptcy.
 - Note: With Chapter 13 bankruptcy filers, the discharge occurs after all payments have been made (generally a 3-5 year period)



QUESTIONS?



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