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Client Alert

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New Bankruptcy Rules Effective December 1, 2017, Will Impact Financial Institutions

Major changes to bankruptcy rules that govern the administration of consumer bankruptcy cases, and Chapter 13 cases in particular, were recently approved by the Supreme Court and transmitted to Congress.[1] After several years of drafting and debate by the rules committee, these rule amendments will become effective December 1, 2017. The most noteworthy changes include: (1) the adoption of a model Chapter 13 plan that is subject to an opt-out in favor of local forms if certain conditions are met; (2) a new requirement that secured creditors must file proofs of claim with a qualification that failure to do so will not void the creditor's lien; (3) a new bar date for filing proofs of claim; (4) new rules for service and noticing of claim objections; and (5) an express mechanism for determining the amount of secured claims.

The following provides a more detailed summary of the new amendments and explains why they are important for financial institutions:

Introduction of Model Chapter 13 Plan

A new Official Form 113 must be filed in a Chapter 13 case unless a local form is adopted in compliance with Rule 3015.1. *See* Amended Rule 3015. Local forms not in compliance with Rule 3015.1 cannot be used. Nonstandard plan provisions are effective only if included in a designated section of the national or local form.

Why this matters*:* The Judicial Conference has been considering a national Chapter 13 plan since 2011, but did not originally propose an opt-out mechanism like the one in the final rule. We understand that, to date, more jurisdictions have opted to use a local form instead of the model form. Nevertheless, new Rule 3015.1 sets forth a number of requirements that a local form must satisfy. On balance, we believe that the new rule will facilitate review of Chapter 13 plans by creditors, but financial institutions should not rely solely on the model plan for employee training purposes due to the likely continued prevalence of local forms.

Changes to Rules Governing Claims Filing

A secured creditor now must file a proof of claim for its claim to be allowed, but failure to file a proof of claim will not void the creditor's lien. *See* Amended Rule 3002(a).

A proof of claim in a voluntary Chapter 7, 12 or 13 case must be filed no later than 70 days after the order for relief. *See* Amended Rule 3002(c) (changing the date from 90 days after the § 341 meeting). A proof of claim in an *involuntary* Chapter 7 case must be filed not later than 90 days after the order for relief. *Id.*

The following exceptions to complying with the new proof of claim bar date apply: (1) on a motion filed by a creditor before or after the filing deadline, the court may extend the deadline by not more than 60 days if the court finds insufficient notice because (i) the debtor failed to timely file the list of creditors' names and

[1] These rules will become effective unless Congress passes a contrary law, which is unlikely.

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addresses required by Rule 1007(a), or (ii) notice was mailed to the creditor at a foreign address. *See* Amended Rule 3002(c)(6).

Creditors with a security interest in the debtor's principal residence have additional time to file attachments to proofs of claim in compliance with Rule 3001(c)(1) (a copy of the writing on which the claim is based) and Rule 3001(d) (evidence of perfection), each of which must be filed no later than 120 days after the order for relief. *See* Amended Rule 3002(c)(7).

Why this matters: The shift forward of the claims-filing deadline is a significant change. Under the current rule, creditors generally have at least four months (or 135 days if the § 341 meeting occurs 45 days after filing) to file a proof of claim. Under the new rule, the time period shrinks to just over two months (70 days). For financial institutions that may run searches for borrower bankruptcies on a monthly basis, that could mean that the institution would have slightly more than 30 days to prepare and file a proof of claim. For claims buyers who purchase debt post-petition, the new rule potentially leaves an even smaller window. Financial institutions should consider re-examining their claims filing process to ensure they can meet the new deadlines.

Changes to Rules Governing Claim Objections

The claim objection and notice must be served by first-class mail to the person designated on the creditor's proof of claim. *See* Amended Rule 3007(a)(2) (new provision). Objections to claims of an insured depository institution must also be served as provided by Rule 7004(h) (certified mail addressed to a designated officer of the institution).

Hearings on claims objections are no longer mandatory. *See* Amended Rule 3007(a)(1).

Why this matters: This rule change is important because creditors now have better control over where a debtor mails a claim objection. However, the removal of the requirement of a hearing means that local rules will control whether a creditor must file a response and request a hearing if a debtor files a claim objection.

Changes to Rules Governing Determination of Amount of Secured Claims

A request to determine the amount of a secured claim may now be made by motion, in a claim objection, or in a Chapter 12 or 13 plan. *See* Amended Rule 3012(b). When such a request is made through a Chapter 12 or 13 plan, the plan must be served on the holder of the claim in the manner provided for service of a summons and complaint by Rule 7004. *Id.*

A request to determine the amount of a secured claim of a governmental unit may not be made through a Chapter 13 plan. *Id.*

Why this matters: Secured creditors, such as mortgage lenders, must remain extra vigilant in reviewing Chapter 13 plans for any request within the plan to reduce the amount of their secured claim. While some jurisdictions previously allowed a debtor to "strip down" a secured claim such as a mortgage lien (but not on a debtor's primary residence), the new rule clarifies this issue and adds the heightened service requirement. The new rule does not appear to address a debtor's ability to "strip off" a mortgage lien through a Chapter 13 plan, which likely will continue to vary from jurisdiction to jurisdiction.

Changes to Rules Governing Avoidance of Liens in Exempt Property

A request under § 522(f) (avoidance of a lien impairing an exemption) may now be made by a Chapter 12 or 13 plan. *See* Amended Rule 4003.

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Why this matters: Similar to new Rule 3012(b), this rule allows debtors to utilize a Chapter 13 plan to avoid a judicial lien or nonpossessory, nonpurchase-money security interest in certain goods to the extent the lien impairs an exemption. This would not apply to mortgages.

Addition of Rule Providing for Order Declaring Lien Satisfied

In a Chapter 12 or 13 case, the debtor may request an order declaring that a secured claim has been satisfied and that the lien has been released under the terms of the confirmed plan. *See* Amended Rule 5009(d).

Why this matters: The Judicial Conference noted that a debtor may need documentation for title purposes of the elimination of a second mortgage or other lien that was secured by property of the estate. Secured creditors should monitor these additional filings for accuracy.

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