

# Bankruptcy

# And

# Title Insurance



Joe Reinhardt

Regional Counsel

Chicago Title Insurance Company

# Bankruptcy From Our Perspective

- Pending bankruptcy of Seller/Borrower
- Past bankruptcies in the chain
- Post-closing bankruptcy



# Pending Bankruptcy

## Notice to Third Parties

- Prior Law – Filing of bankruptcy was notice to third parties
  - Title search included Bankruptcy Court records
- Effective October 1984 –
  - Now must file separate Notice in County where property is located
  - What about actual knowledge?



# Pending Bankruptcy

- Creation of bankruptcy estate (541)
  - Estate created at time of filing
  - All interests in property transferred to Trustee
- Automatic stay (362a)
  - No enforcement of any obligation or action against Debtor
  - Must lift stay to proceed



## Getting the Property Out

- Exempt property
- Sale by trustee or DIP
- Abandonment
- Chapter 11 revesting



## Exempt Property

- Exempt property determined by State Law
- Most common is homestead and entireties
- Claim it on schedules with petition
- Objections filed within 30 days of creditor mtg
- Title reverts back to Debtor – Still subject to liens



## **Sales By Trustee or DIP**

- After notice and hearing
- Sale in the “ordinary course of business”
- Sale or mortgage under Ch. 11 Plan
- Sale “free and clear”



# Pending Bankruptcy

## **By Trustee upon “Notice and Hearing”**

- Court Order not required
- Many exceptions to the rule
- Generally require Court Order to insure larger transactions





# Pending Bankruptcy

## **Sales in the “ordinary course of business”**

- When business of Debtor is selling property
- Trustee has authority to operate the business of the Debtor
- Court Order not required for sale or lease
- What property is part of the inventory to be sold in the “ordinary course”??
- Get Underwriter approval



# Pending Bankruptcy

## Sale as part of Chapter 11 plan

- The approved plan of reorganization may provide for or require the sale or encumbrance of property
- Review the plan and the order confirming the plan to make certain the conveyance is not inconsistent with what was approved



# Pending Bankruptcy

## Sales “free and clear” §363(f)

- Trustee can sell free and clear of liens
- By notice and hearing
- By court order (generally required)
- Review order carefully – All or specific liens?
- Make certain notice provided to creditor whose lien is divested
- 10 day appeal period



## **Abandoned Property**

- Property of no value or burdensome may be returned to the Debtor
- By notice or order
- Parties have 15 days to object
- Liens are still attached



## Chapter 11 Revesting

- Property reverts to Debtor after plan finalized.
- Approval of plan by Creditors does not act to release their liens.



# Pending Bankruptcy

## Appeals

- Must file within 10 days following order
- Mootness Doctrine (363m) – Any reversal on appeal will not affect a sale by a Trustee to a “good faith” purchaser, unless a stay of order is granted. (Does not apply to approval of plans)
- Rule 6004(g) – 10 day automatic stay unless Court orders otherwise.



# Past Bankruptcies



## How Bankruptcy Cases Are Concluded

- Dismissal
  - When action does not go through to final fruition
  - Order required to dismiss in Chapter 7 & 11
  - Debtor may dismiss at anytime in Chapter 12 & 13
  - Dismissal revokes stay and all limitations against Debtor and Creditors removed





## How Bankruptcy Cases Are Concluded

- Plan of Reorganization
  - Successful rehabilitation of debtor in Chapter 11
  - Plan needs to be confirmed by Court
  - Plan stands alone once confirmed and appeal period expires
  - Exemption from state documentary taxes (1146c)



# Past Bankruptcies

## How Bankruptcy Cases Are Concluded

### ■ Discharge

- Upon liquidation and distribution of assets in Chapter 7 and 13
- Discharges debts, NOT liens against property
- Non-dischargeable debts unaffected
  - Fraud
  - Child support



# Past Bankruptcies

## Review Standards

- Can not set arbitrary period to disregard a past bankruptcy
- If you find the necessary orders in land records and case no longer open, should not need to review bankruptcy file
- Review file if orders not in land records



# Post Closing Bankruptcies



# Post Closing Bankruptcy

## Trustee Avoidance Powers (Creditors Rights)

- Preference (547)
- Fraudulent Transfers (548 and NC §39-23.1)



## Preferences

- Transfer within 90 days of filing that gives one Creditor preference over another
- Pre-existing debt
- Debtor insolvent or becomes insolvent due to transfer
- Examples
  - Deed-in-lieu of foreclosure
  - Certain mortgage modifications



## Fraudulent Transfers

- Made within 1 year of filing (4 year state statute)

**AND**

- Made with intent to “hinder, delay or defraud”  
Creditor, **OR**
- Less than “reasonably equivalent value” **AND** Debtor was or became insolvent



## Fraudulent Transfers Actual Fraud

- Deed recorded just prior to a judgment
- Transfers to related parties
- Gifts





# Post Closing Bankruptcy

## **Fraudulent Transfers Less than Equivalent Value**

**Can't give away property for less than it's worth when you're broke, or if giving it away will break you**



# Post Closing Bankruptcy

## **Fraudulent Transfers Less than Equivalent Value**

- **Sales**
  - **Transactions among relatives or related entities.**
  - **Sales price substantially below market**
- **Financing**
  - **Debt Guaranties**
  - **Leveraged Buyouts**
  - **Upstream/Downstream/Sidestream Financing**
  - **Refinance with Cash Out**



# Post Closing Bankruptcy

## Reasonably Equivalent Value

**OK**

**ABC, LLC**

<b>ASSETS</b>	<b>LIABILITIES</b>
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100,000

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100,000

**NOT**

**ABC, LLC**

<b>ASSETS</b>	<b>LIABILITIES</b>
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50,000

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100,000

**Joe Member**

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50,000

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# Post Closing Bankruptcy Concerns

## Creditor's Rights

- Title insurance considerations
  - 1992 policies contain exclusion for creditor's rights
  - 1970 policy
  - Endorsements to modify coverage



**QUESTIONS?**

**COMMENTS?**

**CONFUSION?**

