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Closing When Property is Affected by Bankruptcy and Receivership

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Bankruptcy vs Receivership

- Bankruptcy is entirely Federal law
- The goal of a bankruptcy is to relieve the Debtor of unsecured debts, administer the rights of the secured creditors and distribute the non-exempt property among unsecured creditors.
- Receivership is usually State law
- The goal of a receivership is to enforce the rights of the particular creditor that initiated the petition and administer the rights of the owner and other creditors.



Bankruptcy vs Receivership

- Automatic Stay of all Actions affecting the person who filed bankruptcy or property owned by that person.
- Automatic Stay of all Actions affecting the person or property that is the subject of the Receivership.
- Bankruptcy can extinguish a Debtor's liability for debt payment [Discharge.]
- Receiverships do not affect the Debtor's later liability for debt payment.



When is Property Affected by Bankruptcy?

- Bankruptcy filed by the owner. Can be filed in *any* bankruptcy court in *any* state. No notice is required to be recorded.
- Bankruptcy filed by another owner:
 - Spouse, or former spouse
 - Life Estate Owner, or Remainder Estate Owner
 - Fee Owner, or Leasehold Owner
 - Contract Seller, or Purchaser



When is Property Affected by Bankruptcy?

- “True owners” of entity owner:
 - Sole LLC Member; not corp shareholders
 - General Partners; not Limited Partners.
 - Grantors of Living Trusts, Revocable Trusts, or a “Land Trust”
 - Beneficiaries of True Trusts or Irrevocable Trusts



When is Property Affected by Bankruptcy?

- Bankruptcy filed by a party that holds a lien on the land.
- Bankruptcy filed by a person that is the plaintiff or defendant in a lawsuit that affects the land.



When is Property Affected by Bankruptcy?

- Sometimes AFTER the conveyance!
- If a Grantor later files bankruptcy, in certain circumstances other than a full value sale, the Trustee can unwind the prior transaction:
 - If a creditor receives value more than would be entitled in the bankruptcy within 90 days it is called a “Preference”
 - If the Grantor received less than reasonably equivalent value while insolvent within 2 years, or within ten years if a transfer to a living trust.



When is Property Affected by Receivership?

- Receivership affects property when a state court Orders that all property owned by the designated person is within the authority of the designated General Receiver.
- An alternative Order will specifically affect a specified property designating a Custodial Receiver to have authority as the owner.
- If the Superior Court is in a different county, a Lis Pendens or a copy of the Order Appointing must be recorded.



Bankruptcy continues to affect the property, even after:

- Discharge of the Debtor
- Trustee Report of No Assets / No Distribution
- Order Lifting Stay
- Order Confirming Plan
- After a confirmed Plan, the property is affected by that Plan even though the bankruptcy is closed, for the life of that Plan.



Sales While Pending Bankruptcy or Receivership

- Any sale that affects the Bankruptcy Estate Property must be permitted. The proceedings differ a lot.
- Ordinary Course of Business does not require a new Order Permitting the Sale.
- An Order of Abandonment allows a sale because the rights of the Trustee to administer the property are given up.
 - A Report of No Assets is not Abandonment



Sales While Pending Bankruptcy or Receivership

- Often a new bankruptcy Order Permitting Sale is not required:
 - Notice of Intent to Sell, with no objections
 - Prior Confirmed Plan either specifically allows the sale, or does not restrict sales.
- Property in a Receivership will always require a Court Order to allow a sale, whether by the owner or by the Receiver. The Order Appointing the Receiver may include that authority.



Orders Allowing Sale

- An Order Authorizing Sale merely authorizes the sale to close as a normal sale. No liens are removed.
- Orders Authorizing Sale do not authorize or require a short payoff to a secured creditor.
- All Orders of Sale can be appealed. 14 days for bankruptcy. 30 days for receivership.
- No sale before the appeal period is safe from attack. The title company underwriter may, *or may not*, approve.



Orders Allowing Sale Free and Clear of Liens

- The requisites are complicated and different in bankruptcy and receivership. Involve the title underwriter – early.
- WA state receivership law is considered easier to obtain free and clear authority.
- WA state receivership law is also considered safer to insure before the appeal time has expired.



After Bankruptcy is Closed:

- A prior Plan may continue to restrict the Debtor's right to sell the property.
- Unless a specific Order is found:
 - Liens that attached prior to the bankruptcy are not changed by the bankruptcy. Discharge does not remove a lien.
 - After bankruptcy, creditors are free to foreclose based on the full debt.
- Sometimes a specific Order will remove a lien that interferes with the debtor's homestead exemption.



After Bankruptcy is Closed:

- Orders entered during the bankruptcy may have “Avoided” liens
- The Trustee may have “Rejected” leases or contracts
- Involve your title company underwriter to confirm before removing an exception.
- If a debtor fails to complete a Plan, or if a debtor dismisses the bankruptcy, prior Orders are usually no longer effective.



Questions?

