

## AUTOMATIC STAY LITIGATION IN A NUTSHELL

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### I. The Real Purpose of the Automatic Stay.

- A. The purpose of the automatic stay depends upon whether the debtor's case is a Chapter 7 liquidation, or a Chapter 13 or 11 reorganization. See generally *Thompson v. General Motors Acceptance Corp, LLC*, 566 F.3d 699, at 705 (7<sup>th</sup> Cir. 2009).
  - i. The purpose of the automatic stay in Chapter 7 is to stop non-bankruptcy collection efforts of the debtor's creditors in favor of a single proceeding in which each creditor's ability to collect its claim from the debtor will be determined.
  - ii. The purpose of the automatic stay in Chapters 13 and 11 is to facilitate the debtor's efforts to reorganize.
- B. The distinction between the purpose of the automatic stay in Chapter 7 vs. Chapters 11 and 13 makes a difference. The same conduct on the part of a creditor may constitute a violation of the automatic stay in a Chapter 13 or 11, but not constitute a violation of the stay in a Chapter 7.
  - i. Ex.) Car finance company holding a lien on debtor's vehicle repossesses it pre-bankruptcy filing of the debtor. Upon receiving notice of the debtor's bankruptcy filing (assuming the car finance company still has possession of the vehicle), car finance company is obligated to turnover the vehicle upon the debtor's request in a Chapter 13 case and is potentially liable to the debtor for sanctions for violating the automatic stay if it does not turn the vehicle over; however, the same car finance company is likely not liable to the debtor for violating the automatic stay for refusing to turnover the same

vehicle upon the request of the debtor in a Chapter 7 case. See *Thompson*, at 705-706.

## II. Changes to the Automatic Stay due to Reform Legislation.

### A. What actions are stayed by the automatic stay?

i. Below is a strike-out version of § 362(a) showing the previous and current versions of the statute:

(a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title . . . operates as a stay, applicable to all entities, of—

(1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;

(2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title;

(3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;

(4) any act to create, perfect, or enforce any lien against property of the estate;

(5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;

(6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title;

(7) the setoff of any debt owing to the debtor that arose before the commencement of the case under this title against any claim against the debtor; and

(8) the commencement or continuation of a proceeding before the United States Tax Court concerning a ~~the debtor~~ *corporate debtor's tax liability for a taxable period the bankruptcy court may determine or concerning the*

*tax liability of a debtor who is an individual for a taxable period ending before the date of the order for relief under this title.*

- ii. As a practical matter, BAPCPA did not add to the types of actions that are stayed by the automatic stay.
- B. What actions are not stayed by the automatic stay? See 11 U.S.C. § 362(b).
- i. BAPCPA added several exceptions to the automatic stay. The following is a list of actions not stayed by the automatic stay. [New exceptions included in BAPCPA are identified as “**New**.”]
    1. Commencement or continuation of criminal actions against the debtor - § 362(b)(1).
    2. Commencement or continuation of any civil action concerning [all contained in § 362(b)(2)(A)]:
      - (a) the establishment of paternity;
      - (b) the establishment or modification of an order for a DSO (Domestic Support Obligation, which includes alimony, maintenance and support, but not property division/debt allocation);
      - (c) concerning child custody or placement (**New**);
      - (d) divorce or legal separation, except that relief from stay is required before proceedings can be held to determine property division (**New**);
      - (e) regarding domestic violence (**New**).
    3. The collection of DSOs from property that is not property of the estate (**New**) - § 362(b)(2)(B).
    4. The withholding of income of the debtor for payment of a DSO under a judicial or administrative order or statute (**New**) – § 362(b)(2)(C).

5. The withholding or other restriction imposed on the debtor's driver's or professional license if the restriction was imposed for non-payment of child support (**New**) - § 362(b)(2)(D).
6. The reporting of debtor's overdue child support obligations to the credit reporting bureaus (**New**) - § 362(b)(2)(E).
7. The interception of a tax refund for payment of past due child support (**New**) - § 362(b)(2)(F).
8. Acts to perfect a lien or security interest within the 30-day time limit set forth in 11 U.S.C. § 457(e)(2)(A) - § 362(b)(3).
  - (a) Ex) debtor buys a house financed through a loan given by ABC Mortgage Co., then debtor files a bankruptcy case the next day. ABC Mortgage Co., can record its mortgage without violating the automatic stay for up to 30 days from the date of the closing under this exception.
9. Audits of the debtor by governmental entities - § 362(b)(9)(A).
10. A taxing authority's notices to the debtor of tax deficiencies - § 362(b)(9)(B).
11. A taxing authority's demand for tax returns - § 362(b)(9)(C).
12. Taxing authority assessments, notices, and demand for payment of such assessments - § 362(b)(9)(D).
13. Any act by a landlord under a commercial lease of real property to take possession of such property, if the underlying lease terminated by its terms prior to or during the bankruptcy case - § 362(d)(10).
14. Presentment of a check tendered pre-petition, the giving of notice of dishonor of such check, and protesting dishonor of such check - § 362(d)(11).
15. Creation or perfection of a statutory lien for a real or personal property tax, *or a special assessment on real property*, if such tax *or*

*assessment* becomes due after the date of the filing of the petition (**sort of New**, new component in italics) - §362(d)(18).

16. Withholding from debtor's income to repay 401(k) and other retirement and thrift savings plan loans. (**New**) - § 362(d)(19).

17. Any act to enforce a lien on real property for the period of two years following the entry of an order in a prior bankruptcy case finding that the filing of the debtor's prior petition was part of a scheme to delay, hinder, and defraud creditors, which scheme involved either the debtor's transfer of ownership of such property without the secured creditor's approval or multiple bankruptcy filings affecting such real property (**New**) - § 362(d)(20).

18. Any act to enforce a lien on real property if the debtor was ineligible under section 109(g) to be a debtor in that case or if the debtor's filing of the current case violated an order entered in a prior case prohibiting the subsequent case (**New**) - § 362(d)(21). [Mostly applies in Chapter 13 filings in which the debtor is over the debt limit contained in 109(g) or in which the debtor was ineligible under 109(g) to re-file under Chapter 13 due to the debtor having voluntarily dismissed his previous case after a motion for relief had been filed in that case, which bars the debtor from filing Chapter 13 for 180 days from the date of voluntary dismissal of the prior case.]

19. A landlord's continuation and enforcement of a residential eviction action in which the landlord had obtained a judgment for possession prior to the bankruptcy filing, except that this exception does not allow the landlord to pursue the debtor for unpaid rent or other financial damages from the debtor (**New**) - § 362(d)(22).

20. A governmental unit's right to set off a pre-petition tax from a pre-petition refund (**New**) - § 362(d)(26).

C. When does the stay terminate, or never even arise?

i. One of the most sweeping changes to the automatic stay incorporated in BAPCPA is the conditions it imposes on the automatic stay based on prior bankruptcy filings.

1. Pre-BAPCPA, the automatic stay arose upon the filing of a bankruptcy petition and did not terminate with respect to any particular creditor until the court granted that creditor relief from the stay or until a creditor's collateral ceased to be property of the estate.

2. Under BAPCPA, whether the automatic stay arises at all upon the filing of a bankruptcy petition depends upon whether the debtor has had more than one bankruptcy case dismissed (not counting dismissals under 707(b)) within one year prior to the filing of the current bankruptcy case, and if so, whether the debtor can obtain an order imposing the stay within 30 days of the date the current case was filed.

In order for the debtor to obtain an order imposing the stay in such circumstances, the debtor has to prove a "substantial change in the financial or personal affairs of the debtor" since the dismissal of the most recent case. § 362(c)(4)(A),(B),(C),&(D). [More on that below.]

3. Under BAPCA, whether the automatic stay automatically terminates 30 days after the filing of the petition depends upon whether the debtor had a case dismissed (other than under 707(b)) within one year prior to the filing of the current case, and if so, whether the debtor can obtain an order extending the stay within that 30-day time period.

In order for the debtor to obtain an order continuing the stay in such circumstances, the debtor has to prove a "substantial change in the financial or personal affairs of the debtor" since the dismissal of the most recent case. § 362(c)(3)(A),(B),&(C). [More on that below.]

4. Under BAPCPA the stay also terminates as to any creditor holding a claim secured by personal property of the debtor if the debtor does

not perform his statement of intention within 30 days of the first date set for the meeting of creditors. § 362(h).

- D. What penalties does a creditor face if the debtor can prove a willful violation of the stay?
- i. Prior to BAPCPA, if a debtor could prove that a creditor willfully violated the stay, the debtor was entitled to actual damages, including costs and attorney fees, and within the discretion of the court, punitive damages.
  - ii. BAPCPA limits a debtor's remedy to actual damages, not punitive damages, if the creditor can prove that the action complained of was taken in a good faith belief that the stay terminated by virtue of the debtor's failure within 30 days of the first date set for the meeting of creditors to perform his statement of intention regarding a debt secured by personal property. § 362(k).

### III. Terminating the Stay.

- A. When does the automatic stay arise (and when does it not arise)?
- i. The automatic stay arises immediately upon the filing of the petition (unless it doesn't – see below). § 362(a).
  - ii. The automatic stay does not arise upon the filing of the petition if the debtor has had 2 or more prior cases (doesn't matter under what chapter) dismissed (other than a dismissal under 707(b)) within the one year prior to the filing of the current case - § 362(c)(4).
    1. If the debtor wants the automatic stay imposed in such a case, the debtor must;
      - (a) Within 30 days of the filing of the case, file a motion with the court requesting the stay be imposed on all or certain creditors (practice pointer: file the motion to impose the stay along with the petition) - § 362(c)(4)(B); [If the motion is not filed within 30 days of the filing of the petition, the court cannot impose the stay.]

(b) Demonstrate to the court that the filing of the current case is in good faith as to the creditors to be stayed - § 362(c)(4).

(1) BAPCPA contains no guidance as to how a debtor is to prove the filing of the current case was in good faith, and case law has been slow to develop on that standard. Primarily, the issue of imposing the stay will arise in Chapter 13s, due to the fact that Chapter 7s rarely present a proposal for retaining property that is collateral for an obligation that is in default. “Good faith under § 362(c)(3)(B) is determined by a consideration of the totality of the circumstances. The most significant considerations in evaluating good faith are: (1) why the previous plan failed, and (2) what has changed so that the present plan is likely to succeed.” *In re Sharpe*, 2008 Bankr. LEXIS 451, at 4 (C. Dist. IL 2008) (internal citations omitted);

1. *In re Sharpe* involved back to back Chapter 13 filings, but the reasoning in that decision would apply to proving good faith in a Chapter 13 filed on the heels of a Chapter 7 (often referred to as a “Chapter 20”).

iii. When does the automatic stay automatically terminate?

1. If the debtor has had a prior case (doesn't matter under what chapter) dismissed (other than a dismissal under 707(b)) within the one year prior to the filing of the current case then the automatic stay automatically terminates on the 30<sup>th</sup> day following the filing of the petition - § 362(c)(3).

2. If the debtor in such case wants to extend the automatic stay beyond the first 30 days of the case, then the debtor must:



**(a)** Within 30 days of the filing of the case, file a motion to extend the stay AND attend a hearing on that motion within such 30 days (practice pointer: file the motion to impose the stay along with the petition or the court may not have time to conduct a hearing on the motion within 30 days of the date the case was filed) - § 362(c)(3)(A)&(B); [If the court does not conduct a hearing in the debtor's motion to extend the stay within 30 days of the filing of the petition, the court cannot extend the stay.]

3. A presumption that the current case was not filed in good faith arises if any of the following are true:

**(a)** the debtor has had more than one prior case (doesn't matter under what chapter) dismissed (other than a dismissal under 707(b)) within the one year prior to the filing of the current case, or

**(b)** the debtor had even one case dismissed within the year prior to the filing of the current case and the previous case was dismissed after the debtor failed to (i) file or amend a petition or other documents without substantial excuse other than the debtor's inadvertence or negligence but including debtor's attorney's negligence, (ii) provide adequate protection as ordered by the court, or (iii) perform the terms of a confirmed plan; or

**(c)** there has not been a substantial change in the financial or personal affairs of the debtor since the dismissal of the next most previous case, or any other reason to conclude that the current case will be concluded without a discharge, even if the debtor has had only one previous case pending that was

dismissed within the one year prior to the filing of the current case (most common issue in extension of stay cases);

4. If the presumption arises that the current case was not filed in good faith, then the debtor must prove at the hearing, by clear and convincing evidence, that his current case was filed in good faith.

(a) “Good faith under § 362(c)(3)(B) is determined by a consideration of the totality of the circumstances. The most significant considerations in evaluating good faith are: (1) why the previous plan failed, and (2) what has changed so that the present plan is likely to succeed.” *In re Sharpe*, 2008 Bankr. LEXIS 451, at 4 (C. Dist. IL 2008) (internal citations omitted);

5. Note: The 30-day stay termination does not apply to the case of a debtor who receives a discharge in a Chapter 7 case, then immediately files a Chapter 13 (often referred to as the “Chapter 20”), because the 30-day stay termination only applies to debtors who have had a previous case “dismissed” within a year of the filing of the current case. A Chapter 7 is not “dismissed” if it is completed with a discharge, it is simply “closed.”

(a) For the same reason, it would not apply to a debtor who receives a discharge in a Chapter 13 within a year of the filing of the current case, but that scenario is much less common.

(b) The 30-day stay termination also does not apply to a debtor who had a case dismissed under 707(b) (for abuse – usually for failing to “pass” the means test [707(b)(2)] or under the “totality of the circumstances” analysis [707(b)(3)]) within one year of the filing of the current case.

(1) Ex.) debtor receives an inheritance within the 6 months prior to the filing of his 1<sup>st</sup> Chapter 7, which income grossly inflates the debtor’s Current Monthly

Income under the means test and results in the debtor being “over median.” The United States Trustee brings a motion to dismiss for abuse under 707(b) for the debtor’s failure to pass the means test and, after a hearing, court orders case dismissed for abuse. Debtor can re-file Chapter 7 within one year of the dismissal of the prior case without invoking the 30-day stay termination, preferably at a point at which the inheritance is outside the CMI period (the 6 months prior to the month in which the debtor files his case.)

- B. The stay also terminates:
- i. As to actions affecting particular property of the estate, when that property is abandoned by the estate - §§ 362(c)(1) & 554, or if not previously abandoned by the estate, when the case is closed - § 554(c).
  - ii. As to all other actions, including actions against the debtor, the earlier of the date
    1. the case is closed;
    2. the case is dismissed; or
    3. the discharge is entered.
  - iii. Cautionary note: the automatic stay with respect to an act to repossess a vehicle that is property of the estate continues until the case is closed if the secured creditor has not previously obtained relief from stay and abandonment. If the case is held open for a year after the discharge is entered (because of a pending adversary case, for example), the automatic stay enjoins that creditor from taking possession of the vehicle until the case is closed, which will not happen until the adversary proceeding is concluded.

#### IV. Obtaining Relief from the Automatic Stay.

- A. Upon the filing of a bankruptcy case, assuming the stay arises, a secured creditor, including a car finance company or mortgage holder, cannot assert its rights in its collateral if that collateral is property of the estate (Ex. repo the car or foreclose the house) without first obtaining an order from the bankruptcy court granting it relief from the automatic stay.
- B. Relief from stay issues arise in both Chapter 7 and Chapter 13 cases, but are far more commonly contested by the debtor in Chapter 13.
  - i. A creditor will not move for relief from stay unless the obligation that is secured by property of the estate is in default.
  - ii. In Chapter 7, if the debtor is in default of a secured debt at the time he files his case, he most often intends to surrender the collateral to the creditor and does not contest the creditor's motion for relief from the automatic stay. The debtor is not required to contest a motion for relief from stay and a default order will be granted to the creditor in the absence of a contest to it.
  - iii. If the debtor is current with the secured debt when he files his Chapter 7, the secured creditor will be interested in reaffirmation, but absent a default of the underlying obligation, that creditor does not have grounds to move for relief from stay.
  - iv. Contested motions for relief from stay are far more common in Chapter 13, in which the debtor is often attempting to keep the collateral that is the subject of a motion for relief from stay.
- C. A creditor's entitlement to request relief from the automatic stay is contained in § 362(d).

"...(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay--

(1) for cause, including the lack of adequate protection of an interest in

property of such party in interest;

(2) with respect to a stay of an act against property under subsection (a) of this section, if--

(A) the debtor does not have an equity in such property; and

(B) such property is not necessary to an effective reorganization;

...

(4) with respect to a stay of an act against real property under subsection (a), by a creditor whose claim is secured by an interest in such real property, if the court finds that the filing of the petition was part of a scheme to delay, hinder, and defraud creditors that involved either--

(A) transfer of all or part ownership of, or other interest in, such real property without the consent of the secured creditor or court approval; or

(B) multiple bankruptcy filings affecting such real property.

If recorded in compliance with applicable State laws governing notices of interests or liens in real property, an order entered under paragraph (4) shall be binding in any other case under this title purporting to affect such real property filed not later than 2 years after the date of the entry of such order by the court, except that a debtor in a subsequent case under this title may move for relief from such order based upon changed circumstances or for good cause shown, after notice and a hearing. Any Federal, State, or local governmental unit that accepts notices of interests or liens in real property shall accept any certified copy of an order described in this subsection for indexing and recording. § 362(d) (underlining added for emphasis) (sub 3 pertaining to relief from stay in single asset real estate cases omitted due to the uncommon nature of such grounds)

i. Burdens of proof on most motions for relief from stay:

1. In a hearing under § 362(d):

(a) the party requesting relief (typically a creditor) bears the burden of proof on the issue of the debtor's equity in the property; and

(b) the party opposing the relief (typically the debtor) has the burden of proof on all other issues, including whether the property is necessary for an effective reorganization.

D. The most commonly cited grounds in motions for relief from stay are:

i. Lack of adequate protection;

1. Ex) debtor does not have insurance covering the property [practice pointer: make sure your debtors have insurance coverage for property they intend to keep before you file their case.]

(a) Like it or not, bankruptcy court is the court of second chances. If a secured creditor of your debtor files a motion for relief citing lack of insurance as grounds, make sure debtor obtains insurance before the hearing and bring a copy of the insurance binder to the hearing. Under those circumstances, court will sustain the debtor's objection to the motion for relief from stay the majority of the time.

ii. No equity in the property in the property and the property is not necessary for an effective reorganization (court has to find both for creditor to win).

1. Ex) 2009 tax bill states that the assessed value of the debtor's house is \$175,000 and the balance owed on the mortgage is \$200,000.00. Chapter 13 debtor defaults on his mortgage payments post-petition and lender responds with motion for relief and abandonment.

(a) Debtor can file an objection, citing a recent appraisal done for refinancing purposes that values the property at \$220,000.00, proving there is equity in the property and

defeating the motion for relief (if the court finds that creditor failed to prove there is no equity in the house).

**(b)** Debtor can file an objection stating that the debtor's house is necessary for an effective reorganization because debtor has a family of 6 and could not find cheaper housing than the \$1,400.00/mo debtor is paying in mortgage payments.

- E. Notice required on motions for relief from stay.
  - i. Eastern District Bankruptcy Court Local Rule 9014 states that a motion for relief from stay must state that objections to the motion must be filed within 15 days of the service of the motion.
- F. Service of motions for relief from stay.
  - i. Service of motions for relief from stay is accomplished by 1<sup>st</sup> class mail pursuant to Fed. Rule Bankruptcy Procedure 9014.
  - ii. Motion must be served on debtor, Standing Chapter 7 Trustee, the United States Trustee, and on all creditors in the case.
- G. If no one objects to the motion for relief from stay, the moving creditor files an affidavit of no objection when the response period has passed, along with a proposed order granting the creditor relief from stay.
- H. The debtor can also enter into a voluntary stipulation to relief from stay with a particular creditor to save the creditor the time and effort (and filing fee) of filing a motion for relief from stay.
  - i. Often, the debtor stands nothing to gain from entering into such stipulations and probably for that reason, they are uncommon.
- I. The order granting relief from stay.
  - i. If the court grants a creditor's motion for relief from stay, the order does not become effective until 10 days from entry of the order, unless the order specifically states that the order shall be effective immediately. Unsavvy creditors will unwittingly extend the automatic stay 10 days by not specifying in the order that relief from stay is effective immediately. See

Fed. Rule Bankruptcy Procedure 4001(3). The bankruptcy courts in the Eastern District of Wisconsin routinely grant creditors' requests to make the order granting relief effective immediately upon entry.

- V. Determining violations of the automatic stay.
- A. If the debtor believes a creditor has violated the automatic stay, the debtor may file a motion for sanctions against the creditor, but must file an adversary proceeding (no fee required when filed by debtor) if the debtor's claim for relief includes a request for injunctive or other equitable relief, or requests relief that would affect a lien on property of the estate. § 362(k) and Fed. Rule Bankruptcy Procedure 7001.
  - B. BAPCPA added a little known provision (§ 342(g)(2)) which provides that no monetary penalty can be imposed on a creditor for a violation of the stay unless the conduct complained of occurred after such creditor receives notice of the filing of the case.
  - C. Actions taken in violation of the stay, regardless of whether they were taken before or after receiving notice of the case, are void – not voidable. *Middle Tennessee News Co., Inc., v. Charnel of Cincinnati, Inc.*, 250 F.3d 1077, 1082 (7<sup>th</sup> Cir. 2001). Voidable implies action must be taken to undo the act done in violation of the stay. Void means the act has no validity or legal existence.
  - D. Hot topics in automatic stay litigation:
    - i. 7<sup>th</sup> Cir. recently held that upon the filing of a Chapter 13, the holder of a security interest in the debtor's car who has repossessed the vehicle pre-petition and remains in possession of the vehicle at the time of filing, is under an unconditional obligation to return the vehicle to the debtor and the creditor's refusal to do so is a violation of the stay. Previously, the law in Illinois (the state in which this case arose) was that until the debtor tendered adequate protection to the creditor, the lender did not have to turn the car over post-petition. *Thompson v. GMAC*, 566 F.3d 699 (7<sup>th</sup> Cir. 2009).



- ii. 7<sup>th</sup> Cir. recently held that an educational institution that withholds a transcript post-petition as a means of inducing payment on the discharged claim of the educational institution, is a violation of the stay. ***Kuehn v. Cardinal Stritch University, Inc.***, 566 F.3d 289 (7<sup>th</sup> Cir. 2009).

VI. How the Stay affects Statutes of Limitation - Affect of limitations periods while debtor is in bankruptcy: § 108

- A. If non-bankruptcy law sets a limitations period on a claim against a debtor, and such limitation period has not expired before the debtor filed his bankruptcy case, then such period does not expire until the later of:
  - i. the end of such period; or
  - ii. 30 days after notice of the termination or expiration of the stay.
- B. If applicable non-bankruptcy law fixes a limitations period within which the debtor may commence an action, and such period has not expired before the date the debtor filed his bankruptcy case, the trustee may commence such action by the later of:
  - i. the end of such period; or
  - ii. two years after the filing of the bankruptcy petition.
- C. If applicable non-bankruptcy law fixes a limitations period within which the debtor may file a pleading, file a claim, cure a default, or perform some other similar act, and such period has not expired before the date the debtor filed his bankruptcy case, the trustee may file the pleading, claim, etc... by the later of:
  - i. the end of such period; or
  - ii. 60 days after the order for relief.

VII. See sample forms in the accompanying Appendix.