

Important Changes to Federal Bankruptcy Rules Effective December 1, 2011

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Mortgage holders and servicers should prepare for important changes to Federal Bankruptcy Rules of Procedure ("FRBP"), effective December 1, 2011, including requirements for new forms. The changes to FRBP 3001, the procedural rule for filing proofs of claim, and the introduction of new FRBP 3002.1 requiring notices relating to claims secured by a mortgage on a debtor's principal residence, impose new obligations on mortgage holders, servicers and their attorneys for borrowers who are individual debtors in current and new bankruptcy cases. Failure to abide by these new requirements can result in serious consequences, including sanctions.

This article will describe the changes to the proof of claim forms; the escrow statement requirement; a new requirement for the filing of a payment change notice 21 days prior to any change in the debtor's postpetition payments in Chapter 13 cases (this requirement may wreak havoc for home equity line of credit ("HELOC") servicers); and a required notice of any postpetition fees, expenses and charges (some examples are legal fees, appraisal fees and inspection fees) that must be filed within 180 days after the charge is incurred. Even more onerous is the new notice of final cure which the creditor must respond to within 21 days after it is filed.

The amendments become effective December 1, 2011, and "shall govern all proceedings in bankruptcy cases thereafter commenced and, as it relates to all bankruptcy cases thereafter commenced and, insofar as just and practical, all proceedings then pending." We suggest that mortgage creditors treat it as if the amended Bankruptcy Rules are effective in all pending cases, as well as in all cases filed on or after December 1, 2011.

New Proof of Claim Forms (Official Form B10 and Attachment A; FRBP 3001(c)(1) and 3001(c)(2))

FRBP 3001(c)(1) contains the requirement that claims be made in writing. Official Form B10 has changed, and the instructions for completing it have been amended. Creditors must now include information about the interest rate; they must sign off on a statement that the creditor has attached documentation that is evidence of the creditor's perfected security interest, and the signature block on Official Form B10 has changed.

The changes to the signature block result in another issue for creditors: “who will prepare and sign the proof of claim and required forms?” The signature block includes boxes for the creditor, the creditor’s authorized agent, the trustee, the debtor, or a guarantor. The choice for “the creditor’s authorized agent” includes the instruction “(Attach a copy of the power of attorney, if any)”. Employees of the mortgage holder and employees of mortgage servicers who sign POC Forms are not required to include power of attorney documents.

FRBP 3001(c)(2) is amended and entitled “Additional Requirements in an Individual Debtor Case; Sanctions for Failure to Comply”. Changes require a claimant to include an itemized statement of the prepetition interest, fees, expenses, or charges with a proof of claim, as well as a statement of the amount necessary to cure a default as of the petition date. If the mortgage payments include an escrow payment, an escrow statement must also be attached to the proof of claim. These requirements can be partially fulfilled by the completion and filing of new Official Form B10, Attachment A.

To complete Official Form B10, Attachment A, in Part 1 the mortgage creditor must itemize the amount of principal and interest due as of the date of the filing of the bankruptcy petition, and the total interest due as of the petition date must be broken down by interest rate and the corresponding time periods. Part 2 requires a description of the fees, expenses and charges incurred in connection with the claim, as of the petition date, the dates these charges were incurred, and the amounts of these charges.

Part 3 requires a statement of the amount necessary to cure the default as of the petition date. It is in this section that a mortgage creditor will check off the box indicating whether or not the mortgage payments that are in arrears include an escrow component. If so, the mortgage creditor must include a copy of an escrow statement. Also required in Part 3 is the date the last payment was received by the creditor, the number of payments due, and the amount of the payments due which the mortgage creditor must further analyze by adding the total of prepetition fees and expenses to the overdue payments and subtracting the total of any unapplied funds, resulting in an amount which is the total amount necessary to cure the default as of the petition date.

Several issues arise when one attempts to complete Official Form B10, Attachment A. For example, how will mortgage creditors comply with the escrow statement requirement? Should an escrow analysis be prepared as of the time of the filing of the bankruptcy, instead of every six to twelve months? FRBP 3001 and Form B10 do not provide instructions on how the prepetition escrow arrearage should be calculated, although there is some limited guidance in the Bankruptcy Rules Committee Notes which are published with the FRPBs. The

Notes provide that claimants may submit escrow statements in the same form they use outside of bankruptcy for this purpose.

Sanctions for Failure to Comply with FRBP 3001(c)

The bankruptcy court can impose sanctions against a creditor who files a proof of claim, but fails to provide the documentation and information required by FRBP 3001(c). Those sanctions can be evidentiary, monetary or punitive. An example of evidentiary sanctions is this: if there is an objection to the creditor's claim, the creditor's failure to provide the required information can result in the court refusing to allow the creditor to introduce that information later in court to prove its claim, unless the creditor can show its failure was substantially justified or harmless. Note that the Rules Committee Notes state that the creditor's failure to provide the required documentation will not result, by itself, in a disallowance of the creditor's claim.

Proofs of claim must be signed under pains and penalties of perjury that the statements in the claim are "true and correct and to the best of my knowledge, information and reasonable belief." The penalty for presenting a fraudulent claim is a fine of up to \$500,000 or imprisonment for up to 5 years, or both. There is recent case law imposing sanctions upon attorneys who have run afoul of these provisions.

The changes in FRBP 3001 and the addition of FRBP 3002.1 come from cases with circumstances that the courts found to be unacceptable. The liability for attorneys and proof of claim preparers who sign the forms is substantial, and as a result of the very specific information required for filing claims and change notices, mortgage holders and servicers should expect their attorneys to be reluctant to sign the required forms on their clients' behalf.

Notice of Payment Change To Be Filed No Later Than 21 Days Before the New Payment Is Due (Official Form B10, Supplement 1; FRBP 3002.1(A) and (B))

Creditors in Chapter 13 cases whose claims are secured by a security interest in a debtor's principal residence and whose claims are for arrearages being cured through a Chapter 13 plan, are required to file a Notice of Payment Change (Official Form B10, Supplement 1) no later than 21 days before the new amount is due. This consists of a change in the mortgage payment amount, including those changes which arise from escrow adjustments or from interest rate changes. The Notice of Payment Change must be served upon the debtor, the debtor's counsel and the Chapter 13 trustee. The Notice of Payment Change must be filed as a proof of claim supplement in the proof of claims registry.

At the National Conference of Bankruptcy Judges held on October 2011 ("NCBJ"), panelists Bankruptcy Judge Eugene R. Wedoff of Chicago, and John Rao of the National Consumer Law Center spoke about the amendments to the FRBP's. Both are members of the Rules Committee. They pointed out that the requirement for filing of a Notice of Payment Change applies to HELOC's that are being cured through the Chapter 13 plan, and they acknowledged that the requirement that creditors file and serve Notice of Payment Change for HELOC's is going to be difficult, if not impossible, within the required deadline of 21 days prior to the payment change. A suggestion was made that HELOC creditors whose claims include payment amounts which will change every month may want to request a modification or enlargement of the 21-day deadline by utilizing FRBP 9006(b) "Computing and Extending Time".

Sanctions for Failing to File a Notice Payment Change

The consequences for the mortgage creditor who fails to file a timely Notice of Payment Change will render the payment change ineffective. Mortgage creditors who fail to comply can expect evidentiary sanctions, where the court can prohibit a creditor from presenting evidence in a dispute about the claim. The court also has discretion to "award appropriate relief, including reasonable expenses and attorneys' fees".

Notice of Postpetition Fees, Expenses and Charges To Be Filed Within 180 Days (Official Form B10, Supplement 2; FRBP 3002.1(A) and (B))

Mortgage creditors in Chapter 13 cases whose claims are secured by a security interest in a debtor's principal residence and whose claims are being paid through a Chapter 13 plan, are required to file a Notice of Fees, Expenses and Charges (Official Form B10, Supplement 2) every 180 days (the "Notice of Fees") while the Chapter 13 case is ongoing. The Notice of Fees must be filed as a supplement to the mortgage creditor's proof of claim in the bankruptcy court's claims registry, and it must be served on the debtor, the debtor's attorney and the trustee within 180 days of when the charges were incurred. Failure to timely file the Notice of Fees will result in the inability for the creditor to collect the fees and expenses which should have been disclosed in the Notice of Fees.

Fees, expenses and charges include late fees, attorneys' fees, inspection fees, taxes advanced, property preservation fees and forced place insurance. FRBP 3002.1 is not clear on when the first of these Notices of Fees must be filed. For example, are mortgage creditors required to file the Notices on December 1, 2011 and disclose the fees and expense incurred and paid in the prior 180 days before December 1, 2011, or can mortgage creditors wait for 180 days after

December 1, 2011 and disclose only those fees and expenses incurred after December 1, 2011? The most conservative approach would be for the mortgage creditor to file a Notice of Fees in all pending Chapter 13 cases disclosing all of the fees and costs that have been incurred by the mortgage creditor (and that are going to be charged to the borrower's account) in the prior 180 days.

The trustee and/or the debtor have up to one year after the filing of the Notice of Fees to file a motion requesting a hearing on whether or not the payment of the fees and charges in the Notice of Fees are lawful.

The Notice of Fees may remedy the problem of what to do with attorneys' fees that are incurred by the mortgage creditor postpetition but before the Chapter 13 plan is confirmed. Many bankruptcy courts allow mortgage creditors to include those fees in the proof of claim, while other bankruptcy courts require the filing of a fee application. The resolution of that issue may be that creditors will include those postpetition and preconfirmation legal fees in the first Notices of Fees they file in Chapter 13 cases, which they could file with their Proofs of Claim.

Sanctions for Failing to File a Notice of Fees, Expenses and Charges

In addition to the potential disallowance of the fees, expenses and charges that should have been disclosed, the consequences for the creditor who fails to file a timely Notice of Fees can be evidentiary, where the court can prohibit a creditor from presenting evidence in a dispute about the claim, or the court has discretion to "award appropriate relief, including reasonable expenses and attorneys' fees".

Notice of Final Cure (FRBP 3002.1(f)-(h))

Within 30 days after a debtor completes all Chapter 13 plan payments, the trustee must file and serve a notice stating the debtor has paid in full the amount required to cure the default on the creditor's claim (the "Final Cure Notice"). The Final Cure Notice must include a statement that advises mortgage creditors of their obligation to file a response within 21 days after the Final Cure Notice is served. The concern for mortgage creditors is that compliance with the 21-day response period is going to be difficult or next to impossible. Creditors are urged to pay attention to the 21-day response period as failure to file the written response within this time period may be fatal to the creditor's position.

The mortgage creditor's response must state (1) whether it agrees with the assertion that the debtor has paid the amount needed to cure the default on the creditor's claim; (2) whether the debtor is otherwise current; or (3) if the creditor

asserts the debtor has not cured the default, the creditor must provide an itemization of the cure amount. Note that the mortgage creditor's required response must be filed as a supplement to the mortgage creditor's proof of claim in the claims registry, in addition to being served on the debtor, debtor's attorney and the Chapter 13 trustee.

Sanctions for Failing to File a Response to Notice of Final Cure

The consequences for the mortgage creditor who fails to file a response to the Final Cure Notice can be evidentiary, where the court can prohibit a creditor from presenting evidence in a dispute about the claim, or the court has discretion to "award appropriate relief, including reasonable expenses and attorneys' fees". In addition, if the mortgage creditor's records are not identical to the trustee's records, such that the trustee asserts the mortgage creditor's claim is paid in full, but the mortgage creditor's records show there are still funds owed to the mortgage creditor, the mortgage creditor who fails to file a response will be prohibited from collecting those additional funds.

In judicial foreclosure states where a servicer fails to respond to a trustee's Notice of Final Cure, servicers may be faced with debtors asserting judicial estoppel in the judicial foreclosure action if the foreclosure action is brought because of unpaid fees, costs or charges. On the other hand, the judicial estoppel argument may not be as successful if the default in the post-bankruptcy judicial foreclosure action is for mortgage payments that were not made, even though the servicer should expect some level of sanctions for failure to comply with FRBP 3002.1.

Summary

The amendments to FRBP 3001 and new FRBP 3002.1 will require dramatic changes to procedures for filing claims and the creation of an entirely new set of procedures to comply with requirements that mortgage creditors disclose postpetition payment changes as well as postpetition fees and costs being added to the mortgage accounts of debtors in Chapter 13 cases. The penalties for failure to comply are ominous.

The Rules Committee panelists at NCBJ noted that surprisingly the Rules Committee received very few comments on the changes to the FRBP's during the official comment period. While the official comment period is now closed, comments can still be sent to the Rules Committee, and the panelists urged the audience to get the word out that comments would be welcome. Technical corrections to the Official Forms and FRBP's can be accomplished in one year, while formal rule changes require a three-year process.

[Click here for copies of the new Proof of Claim form \(Official Form B10\), Attachment A for the Proof of Claim \(Official Form B10, Attachment A\), the Notice of Payment Changes form \(Official Form B10, Supplement 1\) and the Notice of Fees, Expenses and Charges \(Official Form B10, Supplement 2\).](#)

[Click here for copies of amended FRBP 3001 and new FRBP 3001.2](#)