

LAW CURRENTS An informational newsletter from Richard A. Klass, Esq.

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\$73K Buys \$200,000 House Thanks to Debtor's "Hat Trick" Screw-up.

THE foreclosure auction of the defendant's Staten Island house came up on a Wednesday at 9:30AM. The courtroom was packed with people ready to bid on the house. The Referee announced the sale of the house, took bids, and struck down the sale at \$73,000 to the successful bidder.

Moments later, the Referee informed the successful bidder that one of the two owners of the house had filed bankruptcy at 9:26AM; therefore, the foreclosure sale was invalid and the bidder should take back his bid deposit. At that moment, the successful bidder called *Richard A. Klass, Your Court Street Lawyer* about whether the sale was indeed invalid.

Automatic Stay Operates as a "Stop" Sign:

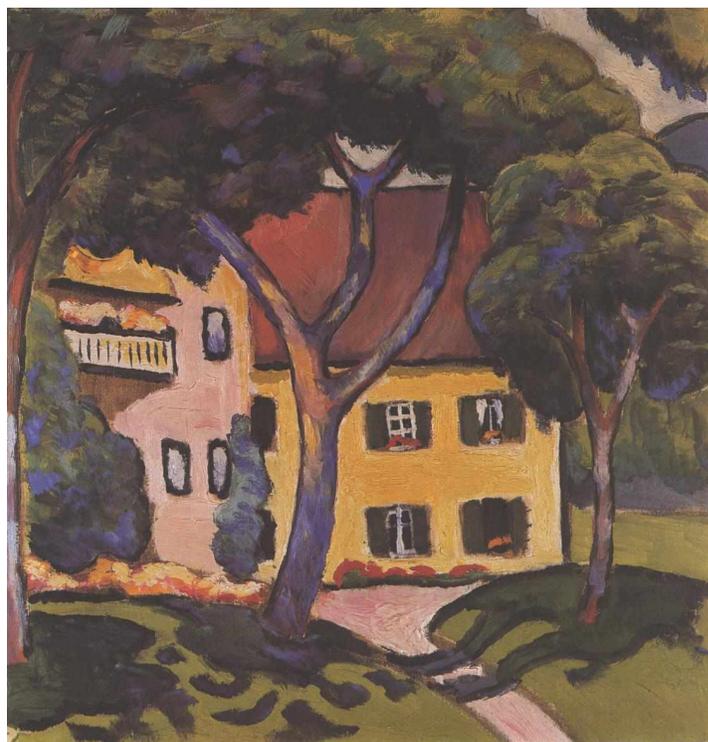
People normally file for bankruptcy protection for one or both of two reasons: (1) to discharge debt; and (2) to "stay" (or stop) proceedings against the debtor, such as foreclosures, lawsuits, repossessions, evictions, etc.

Under Bankruptcy Code §362(a), the filing of a bankruptcy petition with the United States Bankruptcy Court imposes an automatic stay upon creditors from taking certain actions, including specifically auctioning off the debtor's house (Note: there are exceptions which may apply). Generally, actions taken *after* the filing of the bankruptcy petition are null and void, as if they never occurred. In this particular situation, the foreclosure auction happened *4 minutes after* the bankruptcy filing. Under normal circumstances, the automatic stay would have voided this sale and the successful bidder would have merely gotten back his bid deposit, without getting the house.

Before the drastic changes to the Bankruptcy Code in 2005 (under the Bankruptcy Abuse Prevention and Consumer Protection Act [BAPCPA]), debtors would go in and out of bankruptcy to prevent their houses from being sold. Since BAPCPA, it has gotten more difficult for debtors to get the benefit of the "Stop" sign – the first filing will trigger a stay, the second filing a briefer stay, and the third filing no stay unless requested. These "Stop" signs begin to feel like a "Hat Trick," where one player scores three times.

Searching for Details:

The first step in trying to salvage the foreclosure sale for the successful bidder was reviewing every document filed in the bankruptcy case. This included the "bare bones" petition and the



"Credit Counseling Certificate." This Certificate states that the debtor completed a credit counseling course within six months before the bankruptcy filing, which must be done in order to be eligible to file bankruptcy. Upon very close review, it appeared that the debtor simply took the old, expired Certificate from her prior bankruptcy case the year before (more than 6 months old) and filed the same one again – a big but little-noticed "no-no."

Upon further digging, it appeared that the co-owner of the house had previously filed bankruptcy and there was an order terminating the stay a year earlier. Also, the debtor had both unsuccessfully filed a bankruptcy before and had filed the current one without complying with the rules, including paying the court's filing fee.

Validation of Post-Petition Foreclosure Sale:

The Court found that grounds existed to warrant the annulment or termination of the automatic stay and validation of the foreclosure sale. Citing to several cases, the court identified various factors

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that should be considered in determining whether to validate a post-petition foreclosure sale, including whether:

(1) the creditor had actual or constructive knowledge of the bankruptcy filing and, therefore, of the stay; (2) the debtor has acted in bad faith; (3) there is equity in the property of the estate; (4) the property is necessary for an effective reorganization; (5) grounds for relief from stay exist and a motion, if filed, would have been granted prior to the violation; (6) failure to grant retroactive relief would cause unnecessary expense to the creditor; (7) the creditor has detrimentally changed its position on the basis of the action taken; (8) the creditor took some affirmative action post-petition to bring about the violation of the stay; and (9) the creditor promptly seeks a retroactive lifting of the stay and approval of the action taken. *In re Campbell*, 356 BR 722 (WD Mo.2006); *In re Williams*, 257 BR 297 (Bankr.WD Mo. 2001).

Reviewing the facts of the particular situation, the Court found “ample support” for annulling the stay retroactively and validating the post-petition foreclosure sale. These facts included the bare bones petition filed by the debtor with the expired Certificate, her case being filed on the same date as the auction sale, her significant prior experience in bankruptcy, and the negative effect to the successful bidder’s (an independent third party) rights.

In granting the successful bidder’s motion, the Bankruptcy Judge determined that the “debtor’s failure to act in good faith in this case warrants the annulment of the automatic stay and the validation of the petition day foreclosure sale.” *In re Annie Williams*, US Bankruptcy Court, Eastern District of New York, Case No. 1-09-44856-dem [Decision dated January 27, 2010]. Since the Bankruptcy Court validated the foreclosure sale, the successful bidder achieved his desired result – the purchase of the Staten Island house, valued at more than \$200,000, for \$73,000.

— Richard A. Klass, Esq.

Richard A. Klass, Esq., maintains a law firm engaged in civil litigation at 16 Court Street, 29th Floor, Brooklyn Heights, New York. He may be reached by phone at (718) COURT-ST or e-mail at RichKlass@CourtStreetLaw.com with any questions. Prior results do not guarantee a similar outcome.



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