

LESSON 3

AUTOMATIC STAY (Chapter 3, Bankruptcy Code)

CONTENTS

- I. Introduction
- II. The Automatic Stay – 11 U.S.C. § 362(a)
- III. Exceptions to the Automatic Stay – 11 U.S.C. § 362(b)
- IV. Duration of the Automatic Stay
- V. Relief from the Automatic Stay – 11 U.S.C. § 362(d)
- VI. Damages for Willful Automatic Stay Violations

I. INTRODUCTION

The filing of a bankruptcy petition, whether voluntary or involuntary, triggers the automatic stay under section 362. The automatic stay, which arises by operation of law and requires no judicial action, halts certain actions that were or could have been taken before the bankruptcy case was filed (i.e., prepetition) and protects the debtor from harassment by creditors. The automatic stay has the force of an order signed by the judge, and contempt sanctions, damages, and administrative and litigation costs exist for its violation. See 11 U.S.C. § 362(k); I.R.C. § 7433(e).

The automatic stay protects property that may be required for a debtor's fresh start and gives a debtor in a reorganization case time to rehabilitate. It also protects all creditors by preventing individual creditors from seizing assets, and enables the trustee (or the debtor-in-possession) to preserve the estate and to carry out his administrative duties.

II. THE AUTOMATIC STAY – 11 U.S.C. § 362(a)

Section 362(a) stays an "entity" (as defined by section 101(15)) from the actions listed below.

- A. The commencement or continuation of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced prepetition to recover a claim against the debtor that arose prepetition. Accordingly, civil actions to collect taxes (e.g., foreclosure or judgment actions) are stayed.

Note: There is a split as to whether a taxpayer's/debtor's appeal of a Tax Court case is stayed under section 362(a)(1). In the Ninth Circuit, such an appeal is stayed. See Delpit v. Commissioner, 18 F.3d 768 (9th Cir. 1994);

contra Roberts v. Commissioner, 175 F.3d 889 (11th Cir. 1999); Schoppe v. Commissioner, 711 F.3d 1190 (10th Cir. 2013); Freeman v. Commissioner, 799 F.2d 1091 (5th Cir. 1986); Rhone-Poulenc Surfactants and Specialties, L.P. v. Commissioner, 249 F.3d 175 (3^d Cir. 2001); Haag v. U.S., 485 F.3d 1 (1st Cir. 2007).

- B. The enforcement of a prepetition judgment against the debtor or against property of the estate.
 - C. Any act to obtain possession of property of or from the estate or to exercise control over property of the estate.
 - D. Any act to create, perfect, or enforce any lien against property of the estate.
 - E. Any act to create, perfect, or enforce any lien against the debtor's property to the extent that the lien secures a prepetition claim. An act to maintain the status quo of a perfected lien, e.g., the filing of a periodic financial statement, is not a violation of the automatic stay. See 11 U.S.C. § 362(b)(3).
 - F. Any act to collect, assess, or recover a prepetition claim against the debtor.
 - 1. Section 362(b)(9), effective for cases filed on or after October 22, 1994, modifies the prohibition against making tax assessments See Section III.B., below.
 - 2. Collection of a prepetition tax claim, including the serving of a notice of levy or seizure of property by levy, is stayed.
 - G. The setoff of any prepetition debt owing to the debtor against any claim against the debtor.
- Note:** For cases filed on or after October 17, 2005, the automatic stay does not bar the setoff of an income tax refund for a prepetition period against a prepetition income tax liability. If the setoff is not permitted because of a pending action to determine the amount or legality of a tax liability, the governmental unit may hold the refund pending the resolution of the action unless the taxing authority is granted adequate protection for its setoff interest. See 11 U.S.C. § 362(b)(26).
- H. The commencement or continuation of a proceeding before the Tax Court concerning a corporate debtor's tax liability for a period the bankruptcy court may determine or the tax liability of an individual debtor for a prepetition tax.

Note: Section 362(a)(8) was amended in 2005 by the BAPCPA to clarify that the automatic stay applies to Tax Court proceedings concerning tax years that ended prepetition.

III. EXCEPTIONS TO THE AUTOMATIC STAY – 11 U.S.C. § 362(b)

- A. Sections 362(b)(1) through (28) list exceptions to the automatic stay. Several exceptions that may be applicable to the Service are listed below.
1. An individual owed a domestic support obligation may intercept the debtor's tax refund. 11 U.S.C. § 362(b)(2)(F).
 2. Setoffs of prepetition income tax refunds against prepetition tax liabilities. 11 U.S.C. § 362(b)(26).
 3. Criminal actions against the debtor. 11 U.S.C. § 362(b)(1).
 4. Actions taken under police or regulatory powers. 11 U.S.C. § 362(b)(4).
- B. Particularly applicable to the Service is section 362(b)(9), which permits a governmental unit to audit to determine tax liability, issue to the debtor a notice of tax deficiency, demand tax returns, or make an assessment for any tax and issuance of a notice and demand for payment of such an assessment. Such assessment and issuance of notice and demand does not create the statutory tax lien described in I.R.C. § 6321 unless such tax is a debt that will not be discharged in the case and until the property, or its proceeds, to which the lien would attach, are transferred out of the estate to, or otherwise revested in, the debtor.

Note: The assessment exception applies to the assessment of taxes listed on a filed return, a signed Form 870, an executed Tax Court decision document, or any other agreement that will lift the suspension of the statute of limitations created by a notice of deficiency.

IV. DURATION OF THE AUTOMATIC STAY

Section 362(c) provides when the automatic stay terminates.

- A. The stay of acts against property of the estate continues until the property is no longer property of the estate.

- B. The stay against any other act continues until the case is closed or dismissed, or the time a discharge is granted or denied, whichever is earlier.
- C. Under section 362(c)(3)(A), in Chapter 7, 11, or 13 cases filed by or against individual debtors who had had a prior bankruptcy case dismissed within the year, certain aspects of the automatic stay expire on the 30th day after the filing of a second case. This limitation applies unless the court orders otherwise or if the current bankruptcy case was refilled under another Chapter following dismissal under section 707(b) (the means test).
 - 1. Most courts interpreting section 362(c)(3)(A) hold that the automatic stay is terminated only with respect to property of the debtor and not to property of the estate. See In re Williford, 2013 Bankr. LEXIS 2871 (Bankr. N.D. Tex.); In re Rinard, 451 B.R. 12 (Bankr. C.D.Ca. 2011); In re Holcomb, 380 B.R. 813 (10th Cir. BAP 2008); In re Tubman, 364 B.R. 574 (Bankr. D.Md. 2007); In re Jump, 356 B.R. 789 (1st Cir. BAP 2006); In re Pope, 351 B.R. 14 (Bankr. D.R.I. 2006); In re Murray, 350 B.R. 408 (Bankr. S.D. Ohio 2006); In re Brandon, 349 B.R. 130 (Bankr. M.D.N.C. 2006); In re Gillcrese, 346 B.R. 373 (Bankr. W.D. Pa. 2006); In re Williams, 346 B.R. 361 (Bankr. E.D. Pa. 2006); In re Harris, 342 B.R. 274 (Bankr. N.D. Ohio 2006); In re Jones, 339 B.R. 360 (Bankr. E.D.N.C. 2006); In re Moon, 339 B.R. 668 (Bankr. N.D. Ohio 2006); In re Johnson, 335 B.R. 805 (Bankr. W.D. Tenn. 2006). But see, St. Anne's Credit Union v. Ackell, 490 B.R. 141 (D.Mass. 2013); In re Reswick, 446 B.R. 362 (B.A.P. 9th Cir. 2011); In re Furlong, 426 B.R. 303 (Bankr. C.D.Ill. 2010); In re Daniel, 404 B.R. 318 (Bankr. N.D.Ill. 2009); In re Curry, 362 B.R. 394 (Bankr. N.D. Ill. 2007); In re Jupiter, 344 B.R. 754 (Bankr. D. S.C.2006).
 - 2. It is the position of Chief Counsel's Office, in line with the majority of courts, that the stay termination under section 362(c)(3)(A) is specifically limited to actions against the debtor personally and to "in rem" actions taken against the debtor's property, but that the stay does not terminate with respect to actions taken against property of the bankruptcy estate. Chief Counsel Notice 2008-007. Issues arising under this section should be coordinated with Procedure & Administration, Branch 5.
 - 3. Courts have construed section 362(c)(3)'s "with respect to any action taken" language as applying only in situations

where the creditor has taken an action against the debtor prior to the filing of the second bankruptcy case. See In re Paschal, 337 B.R. 274 (Bankr. E.D.N.C. 2006); In re Baldassaro, 338 B.R. 178 (Bankr. D.N.H. 2006).

- D. Section 362(c)(4) provides that the automatic stay does not take effect in a case filed by an individual who has had two or more prior cases dismissed within one year (except for cases that were dismissed under section 707(b) (means test)).

Note: Section 362(j) allows a party in interest to seek an order confirming that the automatic stay has been terminated under section 362(c).

- E. Section 362(n) creates an exception from the automatic stay in certain cases arising from a prior small business case filed under chapter 11.

V. RELIEF FROM THE AUTOMATIC STAY – 11 U.S.C. § 362(d)

- A. Section 362(d) allows the court, upon request of a party in interest and after notice and a hearing, to terminate, modify, condition, or annul the automatic stay. The court shall grant relief from the automatic stay as set forth below.
 - 1. For cause, including the lack of adequate protection of an interest in the property.
 - 2. With respect to a stay of an act against property, if the debtor has no equity in the property, and the property is not necessary to an effective reorganization.
 - 3. With respect to a stay of an act against single asset real estate by a creditor whose claim is secured by such interest in certain situations.
 - 4. With respect to a stay of an act against real property by a creditor whose claim is secured by such interest in certain abusive situations.
- B. Under section 362(g), the party requesting relief has the burden of proof on the debtor's equity in property and the opposing party has the burden on all other issues. Bankruptcy Rule 4001(a) sets forth the procedures to be followed in filing a motion for relief from the automatic stay.

VI. DAMAGES FOR WILLFUL AUTOMATIC STAY VIOLATIONS

- A. Section 362(k)(1) (previously section 362(h)) allows for recovery of actual damages, including costs and attorneys' fees, and, in appropriate circumstances, punitive damages, by an individual who is injured by any willful violation of the automatic stay. Section 362(k) does not apply to debtors who are corporations, or any entity other than individuals. Putative damages may not be awarded against the Government. 11 U.S.C. § 106(a)(3).
- B. I.R.C. § 7433(e) specifically allows for the recovery of damages when the IRS willfully violates the automatic stay or discharge injunction. Section 7433(e) provides that the bankruptcy court cannot use 11 U.S.C. § 105 to award damages, so section 7433(e) is the exclusive remedy for debtors who are not individuals. Section 7433(e) does allow debtors (who are individuals) to seek damages under section 362(k), with the exception that administrative and litigation costs (including attorney fees) may only be awarded under I.R.C. § 7430, which contains a requirement that the debtor must exhaust administrative remedies. Section 7433(e) does not require the exhaustion of administrative remedies for other types of damages awarded under section 362(k). However, no damage award may be made under section 7433, including 7433(e), unless the debtor exhausted administrative remedies. See I.R.C. § 7433(b) and (d), and Treas. Reg. § 301.7433-2.