

## Are unpaid dues protected in bankruptcy?

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*Q. Is the debt of an uncollected homeowners association annual dues assessment considered a "secured debt" when filing a Proof of Claim if the owner files for bankruptcy, since it involves real estate (vacant land or land with a home)? Or is it just an unsecured debt?*

COLUMNISTS »

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Creditors of a bankrupt person who has filed for protection are generally lumped into one of two categories by the federal Bankruptcy Code: secured creditors and unsecured creditors. To understand the difference, it is important to understand the difference between a debt and a lien. A debt is a legal obligation to pay money to a creditor. A lien, on the other hand, is a property interest held by the creditor that secures the underlying debt. Thus, secured creditors hold a lien on certain property owned by the debtor (real estate, motor vehicle, equipment, etc.), while unsecured creditors do not have a lien on property owned by the debtor.

A Chapter 7 or completed Chapter 13 plan will discharge most or all of a person's debts, but many liens will survive the bankruptcy discharge, meaning that the creditor may still repossess or foreclose on the collateral even though the debt has been discharged. While this may seem counterintuitive, it makes sense if you think of a mortgage loan. If the lender's mortgage lien on a home were wiped out by a bankruptcy filing along with the underlying debt, then that would mean any homeowner who filed bankruptcy could keep his house free and clear of the lender's debt. Certainly that is not the result that Congress intended with the Bankruptcy Code.

A homeowners association (HOA) will be a secured creditor in a bankruptcy case only if it has filed a claim of lien against the owner's property before the bankruptcy filing. Being a secured creditor means that the owner will have to pay the amount of the claim, up to the amount of equity available in the property to secure the claim, over the life of a Chapter 13 plan. Chapter 13 plans (the debtor pays back some or all of his/her debt over time) typically run from three to five years. In a Chapter 7 case, the owner will have to pay the secured claim in order to obtain a release of property from the HOA's lien.

If the HOA has not filed a lien on the property prior to the bankruptcy filing, it will be classified as an unsecured creditor, meaning it will get paid as little as 5 percent of its claim over the life of a Chapter 13 plan, and little or nothing in a Chapter 7 case (a straight liquidation of assets).



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Thus, in this time of dramatically increasing bankruptcy filings, it is imperative that HOAs adopt a written policy for dealing with delinquent assessments and adhere to it. HOAs do not do themselves or the homeowners any favors by letting delinquent accounts rise to unmanageable levels. An HOA will lose its right to file a lien if the homeowner files bankruptcy. Also, it's much easier for the homeowner to negotiate a payment plan on a \$300 debt than a \$3,000 debt.

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