

Testimony of

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TESTIMONY OF
NATIONAL MULTI HOUSING COUNCIL/
NATIONAL APARTMENT ASSOCIATION
BEFORE
THE COMMITTEE ON THE JUDICIARY
U.S. SENATE
HEARING ON S. 256,
THE BANKRUPTCY ABUSE PREVENTION AND
CONSUMER PROTECTION ACT OF 2005
FEBRUARY 10, 2005

Chairman Specter, Ranking Member Leahy, and distinguished members of the Committee, I thank you for this opportunity to share the views of rental housing providers as you consider the issue of bankruptcy reform and the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (S. 256).

My name is Malcolm Bennett and I am from Los Angeles, California where I am President and Founder of International Realty and Investments. I am proud to say that my company is one of the largest minority-owned property management and investment property firms in the city. In 1987, I also founded the Minority Apartment Owners Association which is a network rental property owners with rental property throughout Southern California. Today I am representing the National Multi Housing Council and the National Apartment Association (NMHC/NAA), whose combined memberships represent the nation's leading firms participating in the multifamily rental housing industry. Our memberships are engaged in all aspects of the apartment industry, including ownership, development, management, and finance. The National Multi Housing Council represents the principal officers of the apartment industry's largest and most prominent firms. The National Apartment Association is the largest national federation of state and local apartment associations. NAA is comprised of 164 affiliates and represents more than 31,505 professionals who own and manage more than 5 million apartments. NMHC and NAA jointly operate a federal legislative program and provide a unified voice for the private apartment industry.

As the chief representatives of the nation's rental housing providers, NMHC/NAA are uniquely qualified to speak about how the current bankruptcy law impacts our industry and the compelling need for reform. I would like to share with you some of the experiences of the apartment community in this area and how they have been negatively impacted by the abuses in the current system.

The Automatic Stay Provision

We agree that reform of the Bankruptcy Code should be comprehensive and meaningful. Today, I will limit my statement to the provision that is of most interest and concern to the rental housing industry and that is the automatic stay provision. As you are well aware, Section 362 of the Code essentially commands that all collection efforts by creditors should cease upon the filing of a bankruptcy petition. For the rental housing community, this prevents the continuation of an eviction proceeding. While the purpose of the automatic stay provision, "to give the debtor a breathing spell from his creditors", is laudable, the rental housing industry and renters in general are disproportionately disadvantaged by this provision, especially when it is manipulated by those who "game the system" simply for personal gain. For over ten years, hundreds of apartment operators, mostly small businesses, have written to the National Bankruptcy Review Commission and Congress, and provided persuasive evidence of the need for reform. I am attaching for your review some of these examples. (Attachment A). According to a recently released report by the Administrative Office of the U.S. Courts, non-business or personal

bankruptcy filings remain at "historic highs." The latest data show that well over 1.5 million personal bankruptcy petitions were filed in the twelve-month period ending September 30, 2004.

When a person files for bankruptcy protection, most of his or her creditors, while not being able to pursue past debts, have no obligation to continue extending credit. However, if the person is renting an apartment, the owner not only forfeits the ability to pursue past rent, the apartment owner must involuntarily continue to extend credit to someone who has no intention of or apparent ability to make payments. At the same time, the apartment owner must continue to pay his or her monthly costs associated with maintaining the unit. In addition, the owner is prevented from renting the occupied apartment to a new resident, further increasing the financial burden. A rental unit is much like a perishable product. Unless an owner can regain possession in a timely manner and place the unit back into service, its value is diminished. For small apartment owners in particular, such situations cause serious financial hardship. Consumers are harmed as well, because for every unit that is taken off the market due to these abusive situations, the availability of rental housing is reduced, not a small problem in a state like California.

The Eviction Process

I am proud of my work in the housing industry and feel a deep satisfaction that I have made it my life's goal to put people into housing. Most of the time this is a tremendously rewarding experience. Unfortunately, there are times when it becomes necessary to remove a resident from his or her rental unit through the eviction process. This is not an easy decision and in most cases, it is one that is reached only after exhausting all other options. When it becomes necessary to take such action, we do so by following state eviction laws and procedures, which we believe to be fair and fully protective of the resident.

Today, residents are well served by state and local eviction procedures that already provide numerous due process protections. Many states make housing providers go through very onerous and costly procedures before an eviction can occur. The owner cannot simply change the locks or take possession of the premises. A court order or a voluntary surrender of the premises by the resident is required before a resident can lawfully be evicted. As a result, there are numerous legal matters that can and do occur as a result of the filing of an eviction case against a resident. Customarily the court gives the resident time to move out, usually one to four weeks. If the resident remains after that period, the owner has to hire the sheriff or marshal to carry out a forcible eviction. That will take several weeks more. Further delays are possible if the resident files a motion for more time or objects to the court determination.

On average, this process can take approximately three months. During these three months, rent is not being paid, the potential for property damage increases, and I am unable to rent the unit to another party. I am also incurring legal bills associated with the eviction process as well as paying the ongoing utilities associated with that unit. Once I have been granted judgment in state court forfeiting a resident's right to possession, if the resident invokes a bankruptcy filing, the "automatic stay" provision of the bankruptcy code stops this process in its tracks. As a result, the resident is permitted to remain in the apartment rent-free for what could be several additional months. It is most absurd in situations where the owner is aware of illegal drug use and property destruction but nonetheless is prevented from regaining possession of his or her property.

"Eviction Mills" Exacerbate the Problem

What we have found is that in many of these situations, filings are made just so a debtor resident can avoid paying rent. What is even more distressful are the business practices of some unscrupulous opportunists who exploit the automatic stay provision by actively soliciting business from residents facing evictions. These entities research pending eviction cases and then market their services directly to these residents. For a nominal fee, they offer to file various frivolous motions with the court to temporarily halt the eviction proceeding. Once those efforts are exhausted, a bankruptcy petition is then filed, thus stalling eviction for several additional months.

These abusive scenarios are played out all across the country and in all types of properties, large multifamily communities as well as the small property owner renting out a duplex or a garage apartment. It should be noted that the latest data show that nearly 47 percent of all rental housing properties are owned by individuals. Thirty-five percent of all rental apartments are located in properties with fewer than ten units. The added expense and liability of these abuses negatively

impacts the availability of rental housing, especially low- and moderate-income housing. Clearly this was not the intent of the automatic stay provision and the negative consequences of such abuse require immediate attention.

Section 311 provides a balanced solution for business and consumers

Section 311 of S. 256 represents a much-needed yet balanced step toward improving the automatic stay for the benefit of rental housing providers and residents alike. While it does not exempt rental housing from the automatic stay provisions, it goes a long way toward offering much-needed protection against abusive practices.

Specifically, section 311 denies an automatic stay of a real property eviction in the following scenarios:

1) When an owner or manager obtains a judgment for possession prior to the date the resident filed a petition for bankruptcy. This is a significant improvement over current law, which rewards those who simply file a petition with the court clerk without regard for the rigorous process already followed by the property owner to rightfully regain possession of his or her property.

2) When the property is endangered or illegal use of controlled substances is taking place on the property. The owner will be required to file a certification statement with the court.

This is another improvement over current law which offers little or no protection to an owner facing potential destruction of the property and unlawful activity.

Section 311 also provides additional protection to the resident who wishes to cure the entire monetary default thus enabling the resident to stay the eviction, provided specific requirements are met. As mentioned earlier, housing providers typically attempt to work out situations with their residents before they become larger problems. If an eviction can be avoided, all parties benefit.

While there will always exist opportunities for abuse by those seeking ways to exploit the system, it is important that we take the necessary steps to reduce those opportunities while still protecting the resident. Section 311 will go a long way toward curbing some of the more egregious abuses faced by rental apartment providers.

On behalf of NMHC/NAA, I thank you for the opportunity to present our position on these important issues. I urge the members of this Committee and the entire U.S. Senate to pass S. 256 this year and close the automatic stay loophole. This will not only ensure the viability of small business rental housing providers but also help to preserve the affordable and market-rate housing they provide. I thank you for your time and look forward to answering any questions.

ATTACHMENT A

I. An Army Colonel leased his home to a couple with three small children while he was stationed overseas. Before leasing the property, the firm that managed the Colonel's property ran a credit check and found that the couple had a joint income well in excess of the monthly rent. There was nothing in the credit report to indicate what the Colonel and his family would face over the next two years. Over the course of the lease term, the residents occasionally made late payments, but their rent was always paid. Eventually, however, the residents failed to pay their rent despite several notices. After the management firm sent them a three-day notice to vacate for non-payment of rent, the firm decided to give the residents yet another chance to work out a repayment schedule.

What the management firm representatives found when they approached the house was shocking: It was in shambles. The oven door had been ripped off its hinges; there were large and numerous holes in the sheet rock, some with silk flowers stuck in them; you could not tell what color the carpet was due to the trash and food strewn on it; the toilet in the upstairs bathroom had been ripped out of the floor; the air conditioning compressor was in pieces; several windows were broken; and the downstairs bathroom door had been kicked in and was hanging by one hinge. The management firm gave the residents a final three-day notice to vacate for non-payment of rent. The residents never responded to that notice, and after the required three-day notice period, the managers filed for eviction.

Even after the eviction filing, the residents failed to pay their rent. Finally, a judge granted the eviction and ruled that the residents would have to pay all overdue rent. The residents then claimed that they were financially unable to post the required bond to appeal. At a hearing on that claim, the judge confirmed that the residents had both the income and the assets to post the appeal bond and granted the management firm a writ of possession. The next day, however, the managers were notified that the residents had filed for bankruptcy, effectively stopping the eviction process because of the Code's automatic stay provision.

Following multiple failed attempts to negotiate a settlement, the management firm filed for relief from the automatic stay. The residents then demanded a hearing on that motion. During the three-month period before the hearing, the residents lived in the house rent-free. Seven months after the ordeal began, and four months after the bankruptcy court assumed jurisdiction, the judge agreed to a settlement that directed the residents to move out and repair all damages. When the residents had not moved out in accordance with the settlement, the court issued another writ of possession for the next day. Finally, the resident's possessions were removed from the house and their bankruptcy petition was dismissed. The overall cost to the Colonel (the owner of the property) was approximately \$21,000. By the time the residents were finally evicted, the Colonel had to borrow on his life insurance, sell assets, and run up the balance on his credit cards. When the house was sold shortly thereafter, the Colonel received nothing.

II. Sheri Perez, an owner of eight rental units in Costa Mesa, CA, had renters in two of the units declare bankruptcy in the same month. "I know for a fact that these two tenants used the automatic stay and filing bankruptcy just to get out of paying any rent," she wrote to the National Bankruptcy Review Commission. Each of the renters owed two months' rent when they moved out - 25 percent of Ms. Perez's entire rental income for those months.

III. Dan Snell, a property owner in Temple City, CA who manages 50 rental properties, recounted the loss sustained on a 10-unit property he manages in his letter to the National Bankruptcy Review Commission. A resident who was being evicted for selling drugs on the property declared bankruptcy. Before the bankruptcy court ordered relief from the automatic stay to permit Mr. Snell to remove this drug-seller, Mr. Snell had to wait two months for the court to permit the eviction to proceed. "During that period," wrote Mr. Snell, "the tenant continued his illegal activities and three of the other tenants moved out because of that activity. This episode cost the owner several thousand dollars in legal fees and lost rent."