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BANKRUPTCY BILL HOLDS LAWYERS ACCOUNTABLE

Expect Passage and New Challenges on Both Sides

BY MARTHA NEIL

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That controversial major rewrite of the nation's bankruptcy code, almost certain to win final approval and a presidential signature soon, is likely to create a lot of change for some lawyers.

"I don't know anybody who practices in the bankruptcy arena, creditor or debtor lawyer, who thinks this is a good law," says Marc S. Stern, a Seattle lawyer who co-chairs the Bankruptcy Committee of the ABA General Practice, Solo and Small Firm Section.

Lawyers representing creditors "thought it was great until they realized they were going to have to deal with pro se debtors," says Stern of the planned legislation, known as the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. At one gathering of creditor lawyers, faces literally paled when this point was made for the first time, Stern recounts.

Although the legislation is intended to make it harder for lawyers representing debtors to help clients walk away from credit card debt and the like, this change "doesn't mean these cases are going to go away," Stern says. "It means they're going to be filed pro se."

The ABA has taken no position on the overall bankruptcy legislation, Senate Bill 256, which the U.S. Senate approved March 10 in a 75-24 vote. The House is expected to pass the bill next month. If the legislation is enacted, a few provisions would take effect immediately, but most would not kick in for 180 days or more.

The ABA has, however, been lobbying to change several aspects of the bill that are viewed as problematic for lawyers. These include requiring attorneys to certify clients' debt schedules and holding attorneys personally liable if the schedules (listings of the clients' debts) are inaccurate, as well as requiring attorneys to certify clients' repayment abilities. The latter requirement, the ABA argues in lobbying material, could require costly financial audits of client finances.

Proponents say the legislation would close longstanding loopholes that

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allow debtors to spend and spend, then declare bankruptcy rather than pay their bills. For example, a tightened means test is intended to steer struggling debtors to Chapter 13 filings that require ongoing payments to creditors rather than allow them simply to wipe their financial slates clean with Chapter 7 filings.

The U.S. Chamber of Commerce describes the legislation as pro-business. The chamber says the bill would help keep prices and interest rates down by riding herd on the abusive debtor who could pay but instead chooses to walk away from financial responsibility and "transfers the debt burden from the individual consumer to businesses."

Opponents, though, complain that the bill seeks to force struggling middle-class and working-class consumers to pay bills with money they don't have, based on what they see as a largely fictitious scenario of abusive debtors gaming the bankruptcy system.

A Feb. 17 letter signed by nearly 100 bankruptcy and commercial law professors throughout the country contends that "bankruptcy abuse" doesn't really exist.

"This bill seeks to shoot a mosquito with a shotgun," it states, arguing true abuse of the bankruptcy system by debtors is relatively rare and bankruptcy judges already have (and exercise) the power to hold such debtors accountable.

The means test to be imposed on all debtors just adds to the difficulties already faced by those drowning in debt, the letter says. "Some people do abuse the bankruptcy system, but the overwhelming majority of those in bankruptcy are in financial distress as a result of job loss, medical expense, divorce or a combination of those causes," it says.

To the extent that consumers are voluntarily taking on more debt than they can afford to pay, blame should be placed on credit issuers who willingly lend to borderline borrowers, the professors write. "Nonetheless, consumer lending remains highly profitable even under current law."

The "deeply flawed" bankruptcy bill should be of concern to practitioners, the law professors write, because "it takes direct aim at attorneys who handle consumer bankruptcy cases by making them liable for errors in the debtors' schedules."

The legal profession should also be concerned, Stern says, because the bill, by mandating that bankruptcy lawyers advertise themselves as "debt relief agencies," restricts attorneys' ability to represent their clients as they think best. "It is an attack on the attorney-client privilege," he says. "It's part of the camel's nose in the tent."

Another organization that opposes the bill is the Commercial Law League of America, which has a 1,200-lawyer bankruptcy section made up of lawyers and judges from throughout the country.

In a Tuesday letter, the league argues that "abusive filings [will] continue unabated under the act because it does not address forum-shopping by

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corporate debtors." Often, the league says, corporate debtors opt to file in a state such as Delaware—where companies routinely elect to incorporate because of its high-quality and business-friendly judiciary—even though their creditors may do no business in the state and hence find it too expensive to travel there to pursue collection efforts.

An earlier amendment to the bankruptcy bill that would have restricted the venue for filing bankruptcy cases has been withdrawn. However, the issue is being pursued as a separate bill, known as the Fairness in Bankruptcy Litigation Act of 2005.

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