

CHAPTER 13 BANKRUPTCY, WHERE MONEY AND ETHICS MEET



Bankruptcy

- “The efficacy of the bankruptcy system depends in important aspects on accurate self-reporting by debtors. Debtors and bankruptcy professionals who do not fulfill their obligations deserve to be chastised severely.”
In re An-Tze Cheng, 308 B.R. 448, 458 (9th Cir. BAP 2004) aff’d 160 Fed. Appx. 644 (9th Cir. 2005).

Why Chapter 13?

- **Delay foreclosure and catch up on mortgage over time.**
- **Debts are non-dischargeable in Chapter 7.**
- **Protection of co-debtors.**
- **Strip junior liens.**

Limitations on Chapter 13

- **Individuals**
- **Regular income**
- **Debt Ceilings**

Chapter 13 Plans

- **Projected Disposable Monthly Income**
- **36-60 months**
- **Discharge after completion of plan**
- **Debtor's attorney's fees**

Rights and Responsibilities of Chapter 13 Debtors and Attorneys (per Hawaii local rules)

- **Debtor -- Disclose, disclose, disclose.**
- **Debtor's Attorney – Must provide personal service, not delegable to staff.**

WHAT COULD GO WRONG?

Incompetent

- **Examples:**
 - Means Test form
 - Exemptions
 - Best interests of creditors test

Inadequate

- **Failure to meet with and counsel client prior to filing**
- **Failure to appear at meeting of creditors with client**

Intentional

- **Having clients sign blank documents.**
- **Bad Faith**
 - **Filing for sole purpose of delaying foreclosure and without ability to pay**
 - **Serial filings to avoid foreclosure**
 - **Debtor plainly ineligible because debts exceed statutory limits**

Types of Sanctions
in Bankruptcy



Fed. Rule Bankr. Proc. 9011

- **Rule 9011 authorizes sanctions when a filing**
 - **Is brought for an improper purpose**
 - **Is without legal support**
 - **Is without evidentiary support**

Fed. Rule Bankr. Proc. 9011

- **Rule 9011 applies to writings presented to the court**
 - Presentation of “a petition, pleading, written motion, or other paper”
 - “Presenting” include signing, filing, submitting, or later advocating
 - E-filing is “presenting.”

Fed. Rule Bankr. Proc. 9011

- **Presentation to the court is a certification by the attorney**
 - To the best of his or her knowledge, information and belief
 - Formed after an inquiry reasonable under the circumstances
 - The paper is not being presented for any improper purpose, *and* is supported by law and facts.

Fed. Rule Bankr. Proc. 9011

- **Improper purposes include**
 - To harass
 - To cause unnecessary delay
 - To cause needless increase in the cost of litigation
 - Any other improper purpose

Fed. Rule Bankr. Proc. 9011

- **Petitions may be filed for an improper purpose**
 - Such as solely to delay foreclosure
 - Causing unnecessary delay and needless costs
 - Creating unnecessary burdens on the court
- **Proofs of claim and motions for relief from the automatic stay may be filed for an improper purpose**
 - An inaccurate proof of claim or motion for relief may enable a creditor to obtain an advantage over other creditors or over the debtor, while perpetrating a fraud on the court.

Fed. Rule Bankr. Proc. 9011

- **Support for legal contentions**
 - Legal contentions must be warranted by:
 - Existing law, or
 - A non-frivolous argument for the extension, modification, or reversal of the law or establishment of a new law
- **Support for factual contentions**
 - Must have evidentiary support, or
 - If so identified, are likely to have evidentiary support after a reasonable opportunity for further investigation or discovery

Fed. Rule Bankr. Proc. 9011

- **Objective standard of reasonableness**
 - Whether a reasonable, competent attorney would have taken such an action.
 - Attorney's assertions of good faith are not enough.
- **Example**
 - Sanctions upheld against party that filed proof of claim without inquiry as to whether claim had legal or factual basis. Cash Advance v. Dansereau, 64 Fed. Appx. 417, 2003 WL 1528932 (5th Cir. 2003)

Fed. Rule Bankr. Proc. 9011

- **Safe harbor provision**
 - Before it is filed, a 9011 motion must be served on the responding party
 - The respondent has 21 days to withdraw or correct
- **Exceptions to Safe harbor**
 - Filing of the bankruptcy petition
 - Court OSC

Fed. Rule Bankr. Proc. 9011

- **Possible Sanctions**
 - Limited to what is sufficient to deter repetition of conduct or comparable conduct by others similarly situated.
 - Directives of non-monetary nature
 - Penalty to court
 - Reasonable attorney's fees and expenses to movant.

28 USC § 1927

- Any attorney who so multiplies the proceedings in any case unreasonably and vexatiously may be required by the court to satisfy personally the excess costs, expenses, and attorneys' fees reasonably incurred because of such conduct.
- Section 1927 imposes an obligation on attorneys throughout the entire litigation to avoid dilatory tactics. United States v. Int'l Brotherhood of Teamsters, 948 F.2d 1338, 1345 (2nd Cir. 1991)

11 USC § 329

- **Section 329**
 - Applies to any attorney representing a debtor
 - Requires disclosure of compensation paid or agreed to be paid for bankruptcy services within one year before filing
 - Covered services include “services rendered or to be rendered in contemplation of or in connection with the case”
 - Requires disclosure of the source of compensation

11 USC section 329

- **Related rules**
 - FRBP Rule 2016(b)
 - FRBP Rule 2017

11 USC § 329

- “One of the surest means for the bankruptcy system to come under public disrepute is for the perception to take hold that it allows attorneys to milk the last cent out of debtors while leaving creditors nothing” In re Levin, 1998 WL 732878 at *2 (Bankr. E.D. Pa. 1998).

11 USC § 329

- **Disgorgement –**
 - (per section 329(b)) - If the compensation exceeds the reasonable value of the attorney’s services; OR
 - (per Rule 2017) - Is “excessive”

11 USC § 329

- It is well-settled that disgorgement of fees is an appropriate sanction for failure to comply with the disclosure requirements of section 329 and Rule 2017. In re Redding, 263 B.R. 874, 880 (8th Cir. BAP 2001).

11 USC § 105

- Authorizes the court to issue any order or judgment “that is necessary or appropriate to carry out the provisions of this title.”

11 USC § 105

- **May be invoked to prevent abuse even if no specific violation of another section of the Bankruptcy Code.**
- **U.S. Supreme Court recognized the “broad authority” of the bankruptcy judge to prevent abuse under section 105(a).**
- **Marrama v. Citizens Bank of Mass., 549 U.S. 365, 375 (2007)**

Inherent Powers

- **Provide a mechanism for courts to**
 - **Punish misconduct**
 - **Regulate the practice of bankruptcy law before them**
- **Chambers v. NASCO, Inc., 501 U.S. 32, 34 (1991) (discussing “inherent powers” as independent basis for sanctioning power of federal court.)**

Inherent Powers

- **A clear expression of congressional intent is required to displace a court’s inherent power to sanction bad faith conduct**
- **The inherent power of a court can be invoked even if procedural rules or statutes exist which sanction the same conduct (e.g., FRBP Rule 9011 and 28 USC 1927)**

Examples

- **Intake information**
 - In re Nguyen, ___ B.R. ___, 2011 WL 1043898 (9th Cir. BAP 2011)
- **Preparing Schedules**
 - In re Kayne, ___ B.R. ___, 2011 WL 3244066 (9th Cir. BAP 2011).
 - In re Thomas, 337 B.R. 879 (Bankr. S.D. Tex. 2006).
 - In re Tran, 427 B.R. 805 (Bankr. N.D. Cal. 2010).

Examples

- **Obtaining Credit Counseling Certificate**
 - In re Pagaduan, ___ B.R. ___, 2011 WL 1113281 (D. Nev. 2011)
- **Dangers in electronic filing**
 - In re Doe (D. Hawaii 2010)
 - In re Daw, 2011 WL 231362 (Bankr. D. Idaho 2011)
 - In re Retz, 606 F.3d 1189 (9th Cir. 2010)

CREDITOR ABUSE

Proofs of Claim: Examples of Procedural Issues

- **Failure to attach evidence of claim based on a writing (e.g., promissory notes, lines of credit, etc.).**
- **Failure to attach evidence of perfection for secured claims (e.g., deeds of trust, mortgages). Fed. R. Bankr. P. 3001(d).**
- **Failure to itemize statement of accounts. Official Form B-10, ¶ 7.**

Proofs of Claim: Examples of Substantive Issues

- (1) **Estimated Fees**
- (2) **Pay Off Statement Fee (e.g., \$60)**
- (3) **Overnight Mail Fees (e.g., \$137)**
- (4) **Fax Fee (e.g., \$79)**
- (5) **Unnecessary Forced Place Insurance**
- (6) **Unreasonable Inspection/BPO Fees**
- (7) **Vague Descriptions for Fees (“bankruptcy fee”, “delinquency expense”)**

Proofs of Claim: Examples of Substantive Issues (continued)

- (8) **Multiple Charges under Single Line Item**
- (9) **Fees for Unwarranted Motions or Motions Denied as Improper**
- (10) **Arrearage Overstatements or Lack of Evidentiary Support**
- (11) **Excessive/Unusually High Escrow Arrearage**

Motions for Relief From Stay—Procedural Issues

- Failure to comply with local requirements
- Failure to attach affidavits
- No evidence movant is mortgage holder

Motions for Relief From Stay—Substantive Issues

- Post-petition payments applied to pre-petition arrearage
- Failure of dual accounting system
 - Example – Regular post-petition payments are applied to pre-petition arrearage causing creditor to erroneously report post-petition default

Motions for Relief From Stay—Substantive Issues (Cont.)

- Possible payment misapplication fallout –
 - Erroneous late charges
 - Erroneous interest calculations
 - Erroneous escrow calculations
- Payments may also be erroneously deposited into “suspense” accounts

Possible Informal UST Actions

- **Personal communication with creditor’s counsel – telephone call, conversation at Court or Section 341 meeting or in-person conference**
- **Written contact with creditor’s counsel – letter or email requesting information or setting forth an informal demand for action**
- **Informal request for amended POC or to withdraw relief from stay motion**

Possible Formal UST Actions

- **Motion or Notice for 2004 Exam**
- **Objection to Proof of Claim**
- **Objection to Relief From Stay Motion**
- **Motion for Order to Show Cause**
- **Complaint**

UST Settlements

- **Capital One (2008)**
- **Countrywide (2010)**


