

The New State of Bankruptcy: An Overview, Comparison and Tips For Moving Forward

Preamble: The bankruptcy bar is predicting that the credit industry and some pretend "clients" will call attorney offices, soliciting bankruptcy advice. Such calls could be the basis of a lawsuit against the attorney or firm for not disclosing that they are "Debt Relief Agencies" as required under federal law. It is foreseeable that an attorney handling a divorce might have to discuss the possibility of bankruptcy filing, whether by the client, the prospective client or of the other spouse. If not a "debt relief agency," there could be ethics charges made against that divorce lawyer for failure to comply with federal notices.

1 Bankruptcy Abuse Prevention and Consumer Protection Act of 2005

The "BARF" Act

A This new law has so many contradictory and confusing provisions that it is hard for even experienced bankruptcy attorneys to comprehend. It will tie up the court in litigation for years.

B **REGULATION OF SPEECH**. If you are a bankruptcy "dabbler", think twice about continuing to practice bankruptcy or giving ANY bankruptcy advice

1 If you choose to stay in the field, be prepared:

A At midnight October 16, 2005, YOU ARE NO LONGER AN ATTORNEY. **YOU ARE A DEBT RELIEF AGENCY**

1 Your letterhead, business cards, and all advertisement must state plainly that you are a DEBT RELIEF AGENCY. This applies to anyone who gives bankruptcy advice. In other words, even if you represent creditors or banks, or if you give simple bankruptcy advice to a divorce client, you are a **DEBT RELIEF AGENCY**.

2 Effective October 17, 2005, you are required to advise your client "Bankruptcy is a simple and uncomplicated matter. You do not need an attorney".

3 The new law also imposes a "gag order" on you as a DEBT RELIEF AGENCY. You cannot advise your client to pay your fees. You also

cannot advise your client to incur new debt. (For example, you cannot suggest to your client that he replace his 20-year-old Yugo before he begins a 5 year Chapter 13 plan.)

- 4 Within 5 days of giving any bankruptcy advice, you must provide the prospective client, whether s/he hired you or not, with a detailed, written contract describing your services and fees, and disclosing that “I help people file for relief under the Bankruptcy Code.”

Your “client” can sue you if you fail to send a contract. It is also a Rule 11 violation now. So, NO MORE phone consultations. DO NOT give casual bankruptcy advice. Litigants will get wise to this “get rich quick” scheme soon.

C **REPEAT FILINGS**

Some clients simply will not qualify for Chapter 7 bankruptcy, and they will not qualify for Chapter 13, either.

- 1 The previous rules allowed a Chapter 7 every 6 years. Now, it is every 8 years. Previously, you could file a Chapter 13 as needed. Now, you can only file a Chapter 13 after 4 years have passed since your last Chapter 7, or two years since your last Chapter 13.

A Stop and think about that: 85% of all Chapter 13 bankruptcies failed when they were 36 months plans. Now they must all 60 months. Failure rates will be huge. Do you dare put your client in a Chapter 13, in which he will very likely fail, and then leave him without a remedy?

A way around it (but a lousy one)

Your client can file a repeat Chapter 13, but they are not entitled to the automatic stay. Creditors who are wise to the new law and who choose to use it can continue to collect even though your

client is in bankruptcy. (Maybe GMAC won't repossess the car, just to be nice...)

2 No more "Chapter 20"

A Previously, a client with huge debt could file a Chapter 7, discharge all of the unsecured debt, and then go into a Chapter 13 to pay his taxes and child support. Not any more. If your client owes too much to go into a Chapter 13 (and the ceilings have NOT been changed- right around \$300,000.00 in unsecured debt), then your client has no remedy.

Think about it: Doesn't this just guarantee an underground economy?

D The new law imposes a **MEANS TEST**.

1 The debtor's attorney now must calculate if the debtor's household income is greater than the "median income". If your client is below the median income, then you don't need to calculate further.

A **MEDIAN INCOME**. That's \$72,379.00 for Minnesota for a family of 4, based on the last census.

1 If your husband and wife client both earn \$17.50 an hour, and they have 2 kids, your client fails the "median income" test and is PRESUMED to be abusing the bankruptcy system. The clerk will send out a notice to all creditors, encouraging them to object to your client's bankruptcy

2 IT GETS WORSE. The median income is your average income over the last six months. If you were earning \$50,000.00 a month 6 months ago, and you have earned nothing in the last five months, you are deemed to still be earning \$8333.33 a month. Unemployed, with no income, you earn too much for Chapter 7 bankruptcy and YOU

EARN NOTHING for calculating a Chapter 13 bankruptcy.

You have no remedy.

- a. A way around it: Note that the law refers to “household income”. It might be a good time to move in unemployed Uncle Fred, your deadbeat mother-in-law and the Nanny. For each additional person in the house, you get another \$6600.00 in annual income allowance added before you fail the median income test

2 Once you have calculated the median income, you then deduct all secured payments over the next 60 months (For example, client owes \$20,000 on his car, divided by 60) and all priority (tax and child support) debts (divided by 60).

3 After you deduct secured and priority debts, then you deduct the expenses the IRS would allow you in a levy.

- a. It’s not much. For example, using general numbers, a household with 4 persons and a net monthly income of \$4000.00 can have the following expenses:

Food	\$640
Housekeeping supplies:	\$ 61
Apparel and Services	\$189
Personal Care	\$ 53
<u>Miscellaneous</u>	<u>\$188</u>
Total	\$1131

4 If you have \$100.00 left over, you are forced into a Chapter 13

- a. A way around it:

A last minute amendment allows a debtor to deduct reasonable health and

disability insurance policies. It may be time for your uninsured client to get a Cadillac of a policy.

CAUTION: Does the Gag Provision keep you from telling your client about this?

5 If you flunk the means test and still try a Chapter 7, you can try to rebut the presumption of abuse by showing “special circumstances”

CAUTION: If you lose, the attorney (YOU) must pay everyone’s fees.

E. **CREDIT COUNSELING**

1 Your client must go to credit counseling. No way out. The counselor has to be approved by the United States Trustee. It can’t be done by an attorney, or any member of an attorney’s family.

A We don’t know who the counselor will be, where it will be, or what it will cost. The Federal Regs are not out yet.

Think about it: What does this do to emergency filing? When your client comes in at 4:00 PM to avoid an 8:30AM foreclosure, how do you do it?

F **STRIPPING AND STRETCHING**

1 Under our previous law, you could file a chapter 13 plan, and only pay for a car what it was worth, and you could stretch the payments over 5 years.

a. Not any more. You can’t strip or stretch a car unless the car has been in repayment for 2 ½ years.

1 IT GETS WORSE.

A The law is so poorly written, that it says NO DEBT, other than unsecured debt, can be paid in the first 3 years of a plan.

SO, CAN YOU EVEN PAY FOR A CAR THROUGH A

PLAN? CAN YOU CURE AN ARREARAGE ON A HOUSE?

Not as it is written. If your client is behind on a house or a car, then he may have no remedy but foreclosure and repossession. We hope the Chapter 13 trustees won't enforce this provisions, since it will end Chapter 13. We also hope the court will call it a "typo", and refuse to enforce it.

G No more SUPER DISCHARGE

1 One of the joys of Chapter 13 was that you can get rid of debts you couldn't discharge in Chapter 7.

A Now, 523(a)(2) debt (credit card charge ups, tax fraud, etc) cannot be avoided in Chapter 13. You also never get rid of debt that wasn't properly scheduled. Most divorce related debt, or violation of a fiduciary duty, or malicious action resulting in personal injury or death is ever dischargeable in any type of bankruptcy.

H The HOMESTEAD EXEMPTION

1 The law on homesteads changed immediately upon signing. It is effective now.

A No more carpetbaggers:

1 You can't use the homestead exemptions of a state you live in unless you have been there for 730 days. You must use the homestead exemption of the state you lived in before.

2 If you bought your home within the last 1215 days of moving to your new state, you are limited to \$125,000 in equity no matter what your state allows.

1 Example: You sold your home in Wisconsin for \$200,000

profit and moved to Minnesota 2 ½ years ago. You were debt free at the time, and bought a \$200,000 home for cash. Now, you lost your job and you were hit by a truck. You must file bankruptcy. You can use the Wisconsin exemption, which is \$40,000, because it has been 730 days. You may also use the \$125,000 exemption, because the new law allows it. Either way, you lose a large piece of your home. You can't use Minnesota's \$200,000 exemption.

B No more pre-estate planning

1 There is now a **10 YEAR** look back period for “fraudulent transfers”

a You can't tell your client anymore to cash in his bank account and pay down his mortgage before filing. The trustee, or a creditor, can force you to surrender the asset “fraudulently converted”.

Think about it: Grandpa died 9 years ago, and left a life insurance policy to Grandma. She finally used it to pay off her mortgage last year, but then had a medical emergency. Grandma will have to fend off the nasty creditors, and will have to prove that she wasn't defrauding them, when she paid down her mortgage.

I **REAFFIRMATION AGREEMENTS**

1 Minnesota has never required “Reaffirmation agreements”, or new contracts, signed by the debtor, that allow a creditor to continue to collect from him personally after a bankruptcy. We have always been a “ride through” state.

NO MORE.

2 Now, a secured debt must be reaffirmed, redeemed, or surrendered.

A You as a DEBT RELIEF AGENCY have to sign, under oath, that the reaffirmation is in your client's best interest- but it never is. Your client is allowed to sue you for giving bad advice. If your client can't repay the debt at a later date, then the creditor can sue you for a Rule 11 violation. DO NOT sign a reaffirmation agreement. Ever. This is a "no win" situation. If you refuse to reaffirm, the creditor can take your client's car- and your client will hate you. If you sign a reaffirmation so he can keep his car, and he screws up later and has a repossession - he will hate you because you reaffirmed the debt and set him up to get sued.

B Be aware: credit unions, who helped write this bill, get special privileges. They can file a reaffirmation at any time, provided your client signed it before the discharge. WARN YOUR CLIENT. Be wary of backdated documents.

BEST ADVICE: Give all cars back. The car industry will eat 1,000,000 cars in the first year, according to predictions. Then, it will be back to "ride through" as usual.

J **GRUESOME FILING REQUIREMENTS**

1 Your case will be dismissed automatically if you don't provide within 45 days of filing your bankruptcy, the following:

A Certificate of credit counseling

B 60 days of pay stubs, or evidence of income

C Statement of monthly income and any anticipated increase in income

Remember: This is income averaged over last 6 months

- D Last year's tax returns
- E Any outstanding tax returns
- F A photo ID

K **YOU PERSONALLY GUARANTEE ALL INFORMATION ON THE SCHEDULES**

1 The new law makes you, the DEBT RELIEF AGENCY, personally liable for all information on the schedules. What if your client forgot his IRA? You get fined. Under valued his car? You get fined. Claimed an exemption that was later overruled? You get fined.

Think about it How can we ever guarantee what our clients tell us? Do we have to tour every house with a video camera and an appraiser?

A We hope the court applies regular Rule 11 standards. But, the credit card industry is pushing for these penalties, and the US Trustee has no funding to pay for this new law. So, watch out. Your fines will fund all of the new initiatives.

L **NEW FILING FEES**

The new filing fee for a Chapter 7 was supposed to be \$264.00, and increase from the current \$209.00. But Congress, in their zeal, wrote the law so poorly that the fee provision can never take effect. It will probably be corrected before October. Chapter 13 fees remain \$194.00. Rumor has it that the actual fee will be \$284.00, or \$304.00, before October 17, 2005.

This is just the tip of the iceberg, guys. The law will now undergo a "technical correction" bill, where the advocates of the bill will try to make it worse. Stay tuned!

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