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March/April 2010

Features

Supreme Court Clarifies Bankruptcy Rules
Aided by the CLLA's amicus brief, the court issued an opinion in March. What changes can the industry expect?

On March 8, 2010, the Supreme Court issued an opinion on Milavetz, Gallop & Milavetz v. U.S., finally offering some clarification on the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005's amendments to the Bankruptcy Code.When the initial changes were made in 2005, many members of the legal industry were concerned.

"There was extreme disappointment in the industry," says Nancy Rapoport, the Gordon Silver Professor at the William S. Boyd School of Law, University of Nevada, Las Vegas, who co-presented a program on Milavetz in early April for continuing legal education provider ALI-ABA. "We had seen it coming, but every year, the amendments would fail — and one year, they didn't."

The BAPCPA declared that attorneys were considered debt relief agencies and prohibited them from advising clients to incur debt when contemplating bankruptcy.

The act also required them to disclose that some services may involve bankruptcy relief in their advertisements.

Many attorneys found themselves in an uncomfortable position due to the amendments' ambiguity — until recently. Last year, a case filed in federal district court by the Minnesota-based law firm Milavetz, Gallop & Milavetz — claiming that the act severely limited their ability to advise clients — was accepted for review by the U.S. Supreme Court.

The court's opinion, offered in early March, didn't completely eliminate the Bankruptcy Code provisions in question – but it did more clearly define them.

Are Attorneys Still Considered Debt Relief Agencies?
Under the BAPCPA, attorneys were considered debt relief agencies – which, according to Rapoport, was a concern.

"We weren't sure if Congress meant we had to restrict the advice we were able to give clients competently and diligently, which every state's ethics rules requires," Rapoport says.

In its Milavetz decision, the Supreme Court held that attorneys who represent debtors are considered debt relief agencies.

The opinion said that "some forms of bankruptcy assistance, including the 'provision of legal representation with respect to a case or proceeding,' may be provided only by attorneys" and suggested that Congress did not identify attorneys as being exempt from being considered debt relief agencies.

Do Attorneys Need To Include Special Ad Disclaimers?
Section 528 of the Bankruptcy Code requires attorneys who are debt relief agencies to include the statement, "We are a debt relief agency. We help people file for bankruptcy relief under the Bankruptcy Code."

The industry had expressed concern because the statute implied that attorneys had to include the statement in any advertising about debt relief and mortgage services.

"It covered a broad range of advertising," says Bill Schorling, a member of the CLLA's Bankruptcy Section executive council and an attorney at Buchanan Ingersoll & Rooney, a 450-attorney firm with offices in more than five states. "And if you were aiming the advertising at creditors as opposed to debtors, the way the statute was written, you had to include [the statement] in your advertising."

The court maintained that the disclosure requirements were still required and said that they "entail only an accurate statement identifying the advertiser's legal status and the character of the assistance provided."

However, there was some good news for attorneys who represent creditors. The Supreme Court also held that, as argued by the CLLA, attorneys who represent assisted persons who are creditors are not considered debt relief agencies.

As a result, attorneys representing consumer creditors do not need to include the disclaimer in ads because they aren't required to follow the debt relief agency requirements.

How Did The Decision Affect Attorney-Client Consultations?
The 2005 Bankruptcy Code amendments also set regulations about attorneys encouraging their clients to take on more debt before filing for bankruptcy.

Lobbyists had been telling Congress that too many debtors were "wildly discharging debts and skating out on creditors" – when, in reality, the Bankruptcy Code "had always had the tools to deal with debtors who were abusing the system," Rapoport says.

"The percentage of people who would go on wild spending sprees and then file for bankruptcy was way smaller than Congress was told," she says.

The Supreme Court's opinion helped formalize the expectations for attorney-client bankruptcy advice.

The court maintained that section 526(a)(4) was constitutional – and limited the prohibition to advise clients to incur debt solely to incur more debt and cheat the bankruptcy system.

However, the court also said that an attorney has the ability to openly discuss options with clients – including incurring debt in contemplation of filing for bankruptcy.

Justice Sonia Sotomayor, who wrote the majority opinion, significantly narrowed the scope of the provisions that impact the advice a lawyer can give to clients and the advertising restrictions, Schorling says.

"Justice Sotomayor narrowed the statute [by saying] that it is only advice to incur debt that was impelled by the potential filing of bankruptcy that was prohibited," he says. "Attorneys can have full and frank conversations about incurring and not incurring debt and what it means. You just can't give advice to incur debt."

Does Milavetz Allow For Pre-Bankruptcy Planning?
In short: Yes.

"We have to be more stylized in how we do it," Rapoport says. "There are certain things that we could have never, ever advised a client. You can't advise a client to go on a shopping spree and buy fancy things you don't need and not pay for it – Milavetz doesn't change that."

Although the Supreme Court opinion didn't declare the Bankruptcy Code amendments unconstitutional, as many attorneys and legal groups had hoped it would, the opinion has helped define some of the vaguest aspects of the amendments.

"Milavetz is a step in the right direction," Rapoport says. "The narrowed reading answered a lot of questions – but we still have to spend time and see how cases fold out with debt incurred in contemplation of bankruptcy. Justice Sotomayor at least eliminated some of the worst interpretations."

The CLLA And Milavetz
When the initial Bankruptcy Code changes were announced in 2005, some legal groups and individual attorneys expressed apprehension about what the implications could be.

Continuing with its commitment to quickly address policy concerns and file amicus briefs in cases that raise policy issues that are relevant to its members, the CLLA filed an amicus brief on Milavetz, Gallop & Milavetz's behalf when the firm filed its lawsuit.

According to Schorling, the CLLA chose to get involved for three main reasons.

“One, debt relief agencies appeared to include creditors’ lawyers, which would impose restrictions on creditors’ lawyers that made no sense,” Schorling says. “Two, provisions prohibiting debtors from incurring additional debt meant that debtors weren’t getting full and complete advice from their lawyers; and three, advertising is compelled speech, and if a debt relief agency included creditors’ lawyers, they would have to include [the statement in] advertising — which made no sense.”

The CLLA brief advocated that the Bankruptcy Code section limiting attorneys’ ability to advise assisted persons to incur debt before filing was unconstitutional.

The brief also said that lawyers who represent creditors shouldn’t be considered debt relief agencies — or, if creditors’ lawyers are included in the term debt relief agencies, then the stipulation that debt relief agencies must include the required bankruptcy relief statement in their advertising is unconstitutional.