THE TRUTH ABOUT BANKRUPTCY

The current debate over reform of the bankruptcy system has been long on rhetoric and short on substance. Unfortunately, isolated anecdotal examples have been used to mischaracterize who seeks bankruptcy relief today and why. This document is intended to lay out the facts about bankruptcy and why the pending reform measures -- H.R. 3150 and S. 1301 -- will adversely impact honest and hard-working Americans families facing financial crisis.

The consumer credit industry claims that bankruptcies are costing each American family $400 per year. Is that true?

In a word, no. We are not sure how the credit industry arrived at these figures, but there is no credible evidence to support them.

Although these claims may have some rhetorical appeal, they have no basis in fact. It is not the bankruptcy system that causes creditors' losses. Indeed, the credit industries' own studies concede that a majority of consumers in financial trouble will not be able to pay their debts, whether or not they file for bankruptcy. On the other hand, some borrowers who file for Chapter 7 relief pay some of their debts notwithstanding the discharge. The industry wants you to believe that it is the bankruptcy system that causes the charge-offs, not their own bad business decisions.

Equally important, there is no evidence that lenders would reduce rates on unsecured consumer lending if they could avoid these losses. Between 1980 and 1992, the rate at which banks borrow money fell from 13.4 percent to 3.5 percent. Nevertheless, credit card interest rates actually increased during the same period. Given this, how likely is it that additional savings realized by lenders will be passed on to consumers?

The simple truth is that bankruptcy laws do not result in an increase in the cost of credit for bill-paying consumers. Credit card interest rates have not risen or fallen due to increases or decreases in bankruptcy filing rates or changes in bankruptcy laws. The average interest rate on credit cards remained relatively constant from the mid-1970s through the early 1990s, while bankruptcy rates fluctuated considerably over the same period. In fact, it may be argued that the high interest rates and the various and substantial penalties paid by marginal borrowers on their outstanding balance each month subsidize the cost of credit for all borrowers who pay their credit card balance in full each month.

Before rushing into bankruptcy, shouldn't debtors be required to undergo credit counseling to see if they can get their financial affairs in order?

There is nothing wrong with encouraging people to seek credit counseling. Given the serious consequences associated with bankruptcy, most people consider it a last resort when all else has failed. Indeed, debtors usually seek out credit counseling and/or attempt to repay their debts before ultimately filing for bankruptcy.

However, there is reason for concern with the specific credit counseling provisions in the pending legislation, which denies access to the bankruptcy system unless and until a debtor has sought the assistance of a credit counseling program. Although the legislation seeks to ensure some measure of creditability with respect to the credit counseling organizations by requiring that they be approved by the local trustee or bankruptcy court, there is no authorization of funds for the investigation of these organizations, their fees or success rates. As a result, there is nothing that will prevent fly-by-night operators from opening credit counseling programs and getting placed on the approved list maintained by the courts and trustees.

In addition, this requirement will place debtors with extremely limited funds in the position of having to use money that otherwise would go to debt repayment to pay for these counseling sessions, which may or may not be successful.

We know that existing credit counseling organizations are swamped with customers. Consumer Credit Counseling Services (CCCS) alone received more than two million requests for assistance last year. Requests for this type of assistance each year have far outstripped the number of bankruptcy filings over the same period of time. As a result, some consumers are placed on waiting lists a month long. It is likely that waiting periods would be further extended if hundreds of thousands of new customers are added to the counseling workload. For debtors facing emergency issues, such as utility shut-off or foreclosure sales, any delay would be disastrous.

Finally, what will happen if one obstinate creditor refuses to go along with the repayment plan worked out with the assistance of the counseling agency? Complicated legal proceedings will flood the bankruptcy system. Credit counselors will find themselves in court constantly, rather than on the job counseling indebted consumers.

Can't a substantial number of people who file for bankruptcy actually repay their debts? Isn't the loss of stigma associated with filing for bankruptcy encouraging more people to walk away from their debts?

Reports advanced by the credit industry ostensibly demonstrating that a substantial number of bankruptcy filers do so for the sake of convenience have been criticized by both the Congressional Budget Office (CBO) and the U.S. General Accounting Office (GAO). There simply is no credible evidence that a significant number of debtors would be able to pay their bills if they were prevented from filing for bankruptcy.

Individuals filing for bankruptcy on average earn under $20,000 a year after taxes. These are not high flyers squirreling way assets in Florida or in unlimited pension plans. These are people struggling to make a go of it who get in financial trouble.

Empirical studies offer assurances that the system has not become overrun with wealthy debtors who use bankruptcy as a mere convenience. Emerging academic research demonstrates that, as a group, the debtors who file for bankruptcy in the mid-1990s are worse off than their counterparts who filed in the early 1980s. Their incomes are lower and their debt loads are higher. Bankruptcy affects the following groups disproportionately: (1) those who have experienced a period of unemployment in the previous two years; (2) those who have experienced a medical crisis (this is leading cause for those in the 50-60 age range); and (3) divorced persons, particularly women.

As is the case with so many other arguments advanced by proponents of the legislation, there is no objective evidence that there is a loss of stigma associated with filing for bankruptcy, thereby increasing the number of "casual filers." A study issued by VISA purporting to show a link to reduced stigma was criticized on its methodology by the CBO.

There is evidence however, that the annual income of bankruptcy filers has steadily decreased over the 16 year period from 1981 to 1997, while at the same time the debt load has increased. If increased bankruptcy filings can be attributed to a loss in the stigma associated with it, wouldn't you expect to see more higher income earners, not more lower income earners, file for bankruptcy?

Attorneys who represent consumer debtors report that the stigma remains very real. Clients are anxious to repay their debts and to keep their financial difficulties quiet. It is reported that consumers frequently ask their attorney whether their employer or family have to be notified and whether there is any kind of notice published in the newspaper for fear that their hardships will be made public. Finally, attorneys report they have few referrals from former clients. Most people find their attorney as the result of advertising because they are too embarrassed to ask family or friends for recommendations.

<u>Why shouldn't people be forced to commit to some kind of repayment plan rather than being able to wipe the slate clean?</u>

This question gets to the difference between Chapter 13 and Chapter 7 filings. Generally, a family that files for Chapter 7 bankruptcy is relieved only of repaying its short-term, high-interest unsecured debt, principally credit card and finance company debt, along with some medical bills. After bankruptcy, however, the family must continue to make all payments on the family home, including interest, late charges and penalties or they will lose their home. Any other debt secured by a home mortgage or home equity loan also must be repaid. These debtors must continue to make car payments, pay back taxes, and satisfy educational loans. Those who have outstanding child support or alimony obligations must also pay those in full. These debts are not eliminated in bankruptcy. Finally, if a debtor signs what is known as a "reaffirmation agreement," agreeing to pay any debts otherwise discharged in the bankruptcy, he or she will be legally obligated to do so. As a result, Chapter 7 is not total debt relief. Debtors often leave bankruptcy court with heavy financial obligations.

For those debtors who can afford to reorganize and pay their creditors, Chapter 13 provides a well-defined and accessible method to adjust those debts. Debtors who file for Chapter 13 voluntarily agree to pay some portion of their debts over a three to five year period. Despite the good faith of those who choose this approach, the reality is that for over 15 years, two out of every three debtors who file for Chapter 13 do not make it through the repayment plan. Many face repeated unemployment and some encounter significant and unexpected expenses. Before forcing people into Chapter 13, we should find out first why so many voluntary reorganizations fail.

<u>Why do lenders continue to extend credit to high-risk borrowers, knowing that they may never be able to repay it? Isn't this costing the industry a lot of money?</u>

The truth is that high-risk lending is high-profit lending. These profits have encouraged many institutions to substantially lower their standards when it comes to consumer credit. More recently, as higher-quality borrowers began relying less on credit card borrowing and more on lower-interest forms of borrowing, credit card issuers were left to pursue more marginally qualified borrowers. Credit card solicitations have jammed mailboxes with more than 2.5 billion such mailings annually. These solicitations targeted those as young as 16 or 17 years old working at their first summer job and senior citizens living on fixed incomes. No one has been immune from the credit card "come on."

Why creditors pursued such a strategy may be found in the profits associated with such practices. In 1993-1994, credit card lending was 135 percent more profitable, as a percentage of assets, than all forms of bank lending combined. Although these net profits have decreased somewhat, they still are substantially more than many other forms of bank lending.

The Office of the Comptroller of the Currency (OCC) cautioned national banks about the risks associated with preapproved solicitations of credit cards in a September 1996, advisory letter. In that advisory, the OCC encouraged bank management to "take appropriate action to limit its exposure to unwarranted risks." Nonetheless, during the first half of 1997, credit card solicitations were at a record level; the second quarter mailing of 881 million such solicitations was the highest on record.

Is lawyer advertising responsible for the increase in the number of bankruptcy filings?

Although proponents of the legislation may have you believe that it is only because of legal advertisements that the number of bankruptcies has increased, the facts are quite different. Bankruptcy attorneys are only responding to the needs of the millions of American families who have debt problems; they are not creating these needs. We allow aspirin manufacturers to advertise their products to solve the problem of headaches. Yet, no one suggests that these advertisements actually cause the headaches.

Consider the experience of the United Auto Workers Legal Services Plan. In 1997, the bankruptcy caseload of the UAW's Legal Services Plan doubled from two to four percent of total cases handled. In the same year, about 10,000 new clients called to inquire about bankruptcy procedures. These increases cannot be explained by advertising. The Plan does not and never has advertised its services. In most places it is not even listed in the Yellow Pages. And, finally, the Plan reports that it never has approached bankruptcy as a first option; it always is considered a last resort when all else has failed.

What are the similarities between the tobacco industry and the consumer credit industry?

The similarities are considerable. Both industries rely on "hooking" consumers on a habit that can be dangerous to their well-being (financial or physical). In the case of tobacco companies, it is smoking cigarettes that is the culprit. In the case of consumer lending, it is easy credit, with initial low interest rates and low minimum payments. Those interest rates later go sky high, after considerable debt has been run up. Both industries have been accused of targeting lower income and young consumers in their marketing campaigns. Smokers who develop health problems get medical treatment. Consumers who get in financial difficulty as a result of getting hooked on easy credit turn to the bankruptcy system for relief. Now, the credit industry wants to choke off access to the "hospital." Like people who smoke, some bankruptcy debtors have made unwise choices. Others are truly blameless, having become disabled or unemployed after accumulating modest debt. We don't close the cancer ward to people who smoke; we shouldn't close the courthouse doors to people facing financial hardship.

FOR MORE INFORMATION, CONTACT:

Mary Rouleau, Consumer Federation of America, 202/387-6121
Maureen Thompson, National Association of Consumer Bankruptcy Attorneys, 703/276-1116

April 1998

THE TRUTH ABOUT BANKRUPTCY REFORM, CHILD SUPPORT, AND SPOUSAL SUPPORT

HR 3150, "The Bankruptcy Reform Act of 1998"
as reported by the House Judiciary Committee May 14, 1998

MYTH #1: **Bankruptcy reform proposals would reverse current protections in bankruptcy law that prioritize the payment of child support and alimony.**

TRUTH: **H.R. 3150 preserves and strengthens the Bankruptcy Code's protections for ex-spouses and children.** In 1994, Congress amended the bankruptcy laws to make child support and alimony obligations priority debts that must be paid before general unsecured debts, such as credit card debts. Nothing in H.R. 3150 changes the priority status of children and ex-spouses.

- According to the Congressional Research Service: **"H.R. 3150 does not repeal or diminish the protections accorded to child support in the U.S. Bankruptcy Code"** (CRS Memorandum by Robin Jeweler, *Impact of consumer bankruptcy reform proposals on child support obligations* at CRS-4 (May 13, 1998) [hereinafter "CRS Memo"]).

- **H.R. 3150 actually *broadens* protections for ex-spouses under the Bankruptcy Code** by making almost all marital obligations nondischargeable debts (for example, agreements by an ex-spouse to pay a mortgage or to provide half of the proceeds from the sale of a house).

MYTH #2: **The bill would place all nondischargeable debts on equal footing with child support and alimony.** Ex-spouses with claims for child support or alimony payments would be "pitted against" credit card companies, "setting up increased competition for the diminished assets of a postbankruptcy debtor."

TRUTH: **Under HR 3150, as reported by the Judiciary Committee, child support and alimony take priority over *all* other postbankruptcy debts. Child support and alimony *get paid first*.** Under the Bankruptcy Code, priority unsecured creditors are paid out in the order in which they are listed under the bankruptcy statute.

- **H.R. 3150 specifically provides that child support obligations (whether current or in arrears) must be paid before any other debt that survives bankruptcy (*i.e.*, other nondischargeable debts).**

MYTH #3: **The legislation disadvantages ex-spouses and children because they lack the kinds of resources that corporate creditors have to collect debts.** Without inexpensive means of collecting child support and marital debts, ex-spouses and children will lose.

to Sara Rosen - 4 pages

TRUTH: **Present law already requires states to provide inexpensive methods for ex-spouses to collect marital debts; H.R. 3150 preserves existing preferences for collecting child support payments.**

- **Child support payments are directly collectable from any federal tax refunds an ex-spouse receives.**
- **Federal law requires states to provide low-cost services for collecting child and spousal support, without the need to hire a lawyer.**

MYTH #4: **If an ex-spouse uses a credit card check to pay part of their child support or other marital obligations, the credit card company will have the same priority as the spouse to whom additional child support or other marital payments are owed when the debtor files for bankruptcy (when the credit card check is written within 90 days of the bankruptcy filing).**

TRUTH: **H.R. 3150, as reported by the Judiciary Committee, ensures that this cannot happen.** H.R. 3150 specifies that child support and alimony have a higher priority than credit card debt.

- **In fact, H.R. 3150 gives credit card debt the lowest priority of any unsecured debt — child support and alimony have much higher priority.**[1]

MYTH #5: **Under the proposed legislation, debtors filing for Chapter 13 bankruptcy could spread debts for child support payments over a five year period.**

TRUTH: **H.R. 3150 preserves the courts' full authority, as under current law, to require child support obligations to be paid *before* any other debts on an accelerated schedule.**

- In fact, according to CRS, **under H.R. 3150: "[I]n order to reorganize successfully, a chapter 13 debtor will have to fulfill priority child support arrearages, and maintain current payments"** (CRS Memo at CRS-4).

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[1] CRS reports that: "The 1994 bankruptcy amendments clarified that child support and alimony payments, in additional to being nondischargeable, are priority payments in bankruptcy. Indeed, seventh priority — with no monetary limits — goes to allowed claims for debts to a spouse, former spouse, or child of the debtor, for alimony or support, in connection with a separation agreement, divorce decree, or property settlement. . . . The first six bankruptcy priorities encompass administrative expenses: involuntary gap creditors; certain employee wages and benefits; certain claims of grain farmers and fishermen; and certain consumer claims for undelivered or unprovided goods or services." CRS Memo at CRS-2 and n.7. Under H.R. 3150, credit card debts would have eleventh priority.

Washington, DC 20515

May 11, 1998

President William J Clinton
1600 Pennsylvania Avenue NW
Washington, D C 20500

Dear Mr President:

During your recent radio address to the nation, you stated that bankruptcy reform legislation currently under consideration by Congress could require mothers "to compete with powerful banks and credit card companies for the money they're owed." We are writing to correct any misinformation and to assure you that this is false.

The existing bankruptcy law gives child support and alimony debt payments priority over credit card debt. H.R. 3150 does nothing to change that priority. Such priority means that any money that is available will first go to pay child support and alimony debts in their entirety before credit card debts are paid. The legislation we have introduced to stop the abusive use of our nation's bankruptcy laws reinforces that child support and alimony payments will continue to have priority over other debts. Since our bill is crafted to curb abuse of the bankruptcy code, it may even improve the current problem with irresponsible individuals failing to make these important payments.

In addition, the needs-based test which is at the heart of our bipartisan bankruptcy reform legislation subtracts all of the debtor's priority debt payments, including child support and alimony, in determining whether there is any income available to repay other debts. The needs-based system will not affect those who are unable to repay their child support and alimony debts and also pay their unsecured, non-priority debts. Only those who make more than 75 percent of the national median family income for a family of equal size and, after subtracting their secured and priority debt payments and their living expenses, are able to pay at least $50 per month to repay 20 percent of their unsecured, non-priority debt over five years will be required to file in Ch. 13 and repay their debt over time. If the debtor does not have sufficient income to repay all his priority debts in their entirety and repay non-priority debts, the needs-based test will weed that debtor out and not require them to enter a bankruptcy debt repayment plan.

Our nation is witnessing an unsustainable epidemic of personal bankruptcies. Bankruptcies have increased over 400 percent since 1980, with 1 million personal bankruptcies filed in 1996 and a 19 percent increase in 1997. Last year, there were more than 1.4 million personal bankruptcies, more than 1 bankruptcy in every 100 American households. This rate of increase is occurring not in the midst of a recession, but during good economic times. From 1986 to 1996, real per capita annual disposable income grew by over 13 percent but personal bankruptcies more than doubled

Our nation's bankruptcy laws play an important and necessary role in our society but we must ensure that our bankruptcy system does not encourage those who can take responsibility for their financial obligations not to do so. Such an abuse of the bankruptcy system is fundamentally unfair to those who play by the rules and take responsibility for their personal obligations. There is no justification for making middle class families bear the burden for irresponsible higher-income borrowers. Bankruptcy will cost our nation $40 billion in 1997 alone. That translates into over $400 per household in higher costs for goods, services and credit.

We are confident that Congress will pass bipartisan bankruptcy legislation that will reform the existing system as well as strengthen the ability of parents to collect child support and alimony payments. We appreciate your interest in this issue and hope that you join this bipartisan effort to pass responsible and fair bankruptcy reform legislation and sign the legislation when it reaches your desk later this year.

Sincerely,

Bill McCollum
Member of Congress

George W. Gekas
Member of Congress

Rick Boucher
Member of Congress

James P. Moran
Member of Congress

Lisa_Fenning @ ce9.uscourts.gov
10/14/98 04:22:45 PM

Record Type: Record

To: Nicole R. Rabner/WHO/EOP

cc:

Subject: Bankruptcy Reform legislation

DETERMINED TO BE AN ADMINISTRATIVE MARKING
INITIALS: @ DATE: 01/04/13

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It is my understanding from the ABI website that the current trend appears to be to tack an extension of Chapter 12 onto the Omnibus Budget Bill, and not press forward with the overall reform package. If so, you will not need to draw upon the emergency fall-back suggestions below. I would urge you, if possible, to try to get the new judgeship portion of the bill (Section 130 of the Conf. bill) included with the Chapter 12 add-on. The current troublesome economic situation truly makes the need for these overdue judgeships extremely urgent. I do not understand that at this point the judgeships are controversial in their proposed temporary format.

Following up on our telephone conversation this morning, I will set forth the changes that I would consider absolutely necessary if a compromise needs to be reached to save the Omnibus Budget Bill. These changes could form the basis for reconsideration next spring, but I would hope that the proposed bill could be improved in many respects if deferred.

CONSUMER PROVISIONS

1. "Means testing" -- Section 102 of Conf. Bill (amending 11 USC Section 707)

The HR3150 formula continues to be based upon an assertion that, "2 + 2 = 7, and (imaginary) dollars 5, 6, and 7 should be paid through the plan." Saying so doesn't make it so.

I understand the House activists continue to insist that judical discretion should be constrained by a formula that establishes a presumption requiring minimum payments through Chapter 13. Any such formula needs to be workable, however.

The concept that I suggested as a possible compromise would be to provide for the creation of a commission charged with responsibility to develop appropriate consumer formulas by a certain date. The effective date of the formula would have to be deferred perhaps a year after the development of the formula so that the necessary forms and procedures could be finalized.

The concept would be to have a four or five member commission appointed by the President, Speaker, Majority Leader, and Chief Justice, etc. They would be responsible for developing an appropriate "means testing" formula that would probably start with the IRS budgets, but also take into account the debtor's actual secured debt obligations, including arrearages to be paid through the plan. The formula could also establish standards for adjustments that take into account the infinite variety of individual circumstances, with the judge given some discretion about upwards or downwards adjustments. The formula should also specify that chapter 7 cases should not be dismissed for failure to meet the formula if either: (1) the debtor was not eligible for chapter 13 relief (due to debt in excess of statutory limits, for example), or (2) the debtor would be unable to propose a confirmable plan for some reason.

The formula should be subject to annual review and adjustment by the Commission. The Commission should also be required to report annually on the number of cases affected by the formula, their disposition, and the amount of additional payout to creditors that was achieved in those cases converted to chapter 13s, so that the effect of "means testing" requirements can be evaluated and quantified.

2. Cram down of personal property secured debt in Chapter 13 cases -- Section 124 of Conf. Bill (amending 11 USC Section 506).

The conference's "compromise" on this issue calls for prohibition of lien-stripping with respect to any secured debt incurred re personal property within 5 years before the bankruptcy filing. The issue here is whether the secured portion of the car debt can be reduced to the collateral value of the car as of the petition. The ability to reduce payout of the unsecured portion of the car debt is a critical feasibility question in many Chapter 13 cases. For all practical purposes, the 5-year limitation is the same as the unlimited Senate prohibition -- almost all personal property secured debt involved in Chapter 13 cases was incurred within 5 years.

This provision should be eliminated as unduly harsh. It provides a windfall for secured creditors whose debts carry particularly high interest rates, resulting in outstanding debts much greater that the value of the car.

3. Adequate protection pending Chapter 13 confirmation -- Section 137 of Conf. bill (adding 11 USC Section 1307A)

This provision will require debtors to make double payments to secured creditors while awaiting confirmation of their Chapter 13 case. The plan payments required to be made to the trustee pending confirmation already include the regular monthly payments due on cars and houses.

If debtors are also required to pay regular monthly payments directly to the secured creditors, literally no one will be able to survive economically to confirm a plan. This provision should be amended to require that either the regular monthly payment shall be paid to the trustee as part of the plan payment, or paid directly to the secured creditor, but NOT both.

BUSINESS PROVISIONS

1. Deadline for assumption of leases -- Section 205 of Conf. bill (amending 11 USC Section 365)

This provision sets an absolute time limit of 180 days to assume or reject leases, subject only to extension on motion "of the lessor." Lessors will never want to pay for the filing of such a motion. This prohibition on extensions will kill retail bankruptcy cases, which often involve hundreds of leases. This provision would force debtors to assume leases prematurely, before it can be determined whether the case is reorganizable and whether the particular lease will be advantageous in the reorganization. The problem with premature assumption is that any arrearages have to be cured, and any liability for a subsequent breach or termination becomes an administrative priority claim for all consequential damages and amounts due under the lease, avoiding the statutory cap on the amount of pre-petition lease claims, and elevating these prepetition claims to a priority above all other unsecured claims.

This provision would be acceptable only if amended to provide that the period could be extended upon the consent of the lessor, or because necessary for a reorganization reasonably in prospect or other good cause shown. A limit to an additional 180-days period not be unreasonable, or imposing a requirement that a confirmable plan be on file.

We can reasonably anticipate some major retail chain filings within the year. This provision would destroy many of them.

2. Elimination of the automatic stay for Chapter 11 cases -- Section 412 of Conf. bill (amending 11 USC Section 362)

The problem with this section has to be the result of a potentially disasterous drafting error, rather than intentional. The new subsection "(j)" would provide that "the filing of a petition under chapter 11 of this title operates as a stay of the acts described in subsection (a) only in an involuntary case involving no collusion by the debtor with creditors and in which the debtor [is a small business that hasn't recently filed]". As written, no automatic stay would apply in any voluntary Chapter 11 case.

I assume, given the apparent intent of the section, that the problem is a misplaced modifier. It would be okay if revised as follows:

"(j)" would provide that "the filing of a INVOLUNTARY petition under chapter 11 of this title operates as a stay of the acts described in subsection (a) only IN A CASE involving no collusion by the debtor with creditors and in which the debtor [is a small business that hasn't recently filed, etc]".

Many other provisions of the Conf. bill are problematic as a matter of policy, drafting, etc., but the foregoing are the crucial problems that should not be allowed to become law.

I hope that these comments provide you with some ideas if truly hard choices must be made.

Lisa_Fenning @ ce9.uscourts.gov
10/13/98 12:21:33 PM

Record Type: Record

To: Nicole R. Rabner/WHO/EOP, Sarah Rosen/OPD/EOP

cc:
Subject: Bankruptcy Reform legislation

Over the weekend, I reviewed the Conference Report in greater detail. In many important respects, it is worse than HR 3150. It threatens to destroy Chapter 13 as an effective method of rehabilitation, and to swamp the bankruptcy courts in litigation about budgetary issues that are likely to require evidentiary hearings.

I realize that the Administration is facing many political tradeoffs with respect to budget issues. But this last-ditch effort to derail the bipartisan Senate compromise should not be rewarded. I urge the Administration to stand firm on its veto threats of last week.

Please call or e-mail me if you have any questions or if I can be of any assistance.

UNITED STATES BANKRUPTCY COURT

CENTRAL DISTRICT OF CALIFORNIA

Chambers of the Honorable Lisa Hill Fenning
United States Bankruptcy Judge
255 East Temple Street, Suite 1682
Los Angeles, CA 90012
Telephone: (213) 894-2553 Facsimile: (213) 894-3731

June 5, 1998

DICTATED BUT NOT READ

Via Facsimile

(202)456-2878
Ms. Nicole Rabner
Associate Director for Domestic Policy
c/o The White House
Washington, D.C.

Re: Follow-Up Materials

Dear Ms. Rabner:

It was a pleasure meeting you at the White House on May 19th with Ms. Sarah Rosen. Enclosed are follow-up comments on H.R. 3150 and S. 1301 that I indicated I would send to you.

Please do not hesitate to call me if you should you have any questions regarding the attachments. I can be reached at my office (213)894-3557 which is my direct line. I am also providing you with my home telephone number, (949)496-2915, should you need to reach me after office hours.

Very truly yours,

Lisa Hill Fenning by K.B. Pierce

Lisa Hill Fenning
United States Bankruptcy Judge

Attachments (15 pages)

TEN KEY ELEMENTS FOR A WORKABLE S. 1301
Submitted by Bankruptcy Judge Lisa Hill Fenning

Ten elements are required to assure that S. 1301 results in effective consumer bankruptcy reform:

1. No "gateway" eligibility requirement for pre-bankruptcy work-outs should be imposed. Stress post-filing education and budget management programs instead. Consider adding a post-filing requirement for good faith work-outs under court-annexed mediation as well as education for Chapter 7 debtors as well as Chapter 13 debtors.

   Proposed change in S. 1301:
   - Delete proposed Sections 322 (a), (d), and (e) of S. 1301.
   - Modify proposed Section 322 (c) to apply to all individual debtors.

2. Require proof of identity and social security or tax number as prerequisite for filing all petitions to reduce fraud and identity theft problems.

   Proposed change in S. 1301: Add new subsection (h) to 11 U.S.C. § 109:
   (h) The petition must be accompanied by proof of identity (including all names used by the debtor within the past six years), address, social security number, and employer's tax identification number (if any), in a form acceptable to the clerk. The clerk may refuse to accept a petition for filing if such proof is not provided, unless otherwise ordered by the court.

3. Use 11 U.S.C. § 707(b) as the model for testing whether debtors could substantially repay unsecured debt through a Chapter 13 plan, using a flexible standard based upon debtor's ability to confirm a Chapter 13 plan that would provide for at least 20% repayment of general unsecured creditors.

   Proposed change in S. 1301: Clarify appropriate standards for debtor's attorney sanctions in Section 102 as follows:
   - Delete proposed new subsection 707(b)(3)(B).
   - Add at the end of § 707(b)(3): *", if the attorney's filings were not substantially justified,"* like the standard set forth in proposed new § 707(b)(4)(A) to be applied to the award of sanctions against creditors for making frivolous motions under this section.

4. Allow creditors to bring 11 U.S.C. § 707(b) motions in cases involving debtors above a certain income, but counterbalance that authority with a prohibition on reaffirmations for all unsecured consumer debt, and secured consumer debt below a specified purchase amount.

   Proposed change in S. 1301: Limit reaffirmation agreements to secured claims of $500 or more to deter creditors from bringing motions under modified 11 U.S.C. § 707(b) to pressure reaffirmations of unsecured debts. Proposed modification of 11 U.S.C. § 524(c) by adding a new subsection (7) follows:

"(7) the claim is a allowed secured claim that is secured by property having a fair market value of at least $500.00.
"Agreements between an individual debtor and a holder of a claim that is wholly unsecured, or between a debtor and a holder of a claim that is secured by a lien on property having a fair market value of less than $500.00, are prohibited, and shall be deemed void and unenforceable.

5. Retain the "superdischarge" to encourage debtors to complete Chapter 13 plans and to avoid competing nondischargeable debt that adversely impacts the ability of child and spousal support creditors to get paid.

   Proposed change to S. 1301: Delete Sections 314 and 316.

6. Do not use the H.R. 3150 formulas for Chapter 7 eligibility or Chapter 13 plan confirmations because they are administratively unworkable; they will effectively bar many financially distressed debtors from any type of discharge; and they will impede the ability of child support and other nondischargeable priority creditors to collect on their claims.

   Proposed change to S. 1301: None.

7. Change proposed amendment to 11 U.S.C. § 523(a)(2)(A) to address confused state of case law regarding dischargeability of credit card debt, using a standard that recognizes the reasonable repayment expectations of the parties at the time the debt was incurred as the touchstone for determining whether the debtor intended to obtain credit by false pretenses or fraud.

   Proposed alternative language: Modify 11 U.S.C. § 523(a)(2)(A) as follows:

   "actual fraud, or use of a credit or charge card or other device to access a credit line without a reasonable expectation of having income sufficient to make the regular payments on such debt as they come due during the next six months."

8. Eliminate debt refinancing from the proposed presumption of nondischargeability provision of 11 U.S.C. § 523(a)(2)(C).

   Proposed change to S. 1301: Modify Section 317's proposed amendment to 11 U.S.C. § 523(a)(2)(C) to add the following immediately before the close parens:
   ", except debt incurred in the course of refinancing a pre-existing dischargeable debt)"

9. Provide more effective defenses against abuse of the automatic stay by strengthening proposed *in rem* relief and related provisions. See attached memorandum for substitute language for Section 303 of S. 1301.

10. Keep the streamlined appeals provisions to enhance uniformity of rulings by bankruptcy judges, who will have more controlling precedents upon which to base their decisions.

    Proposed change to S. 1301: None.

UPDATED COMMENTS ON H.R. 3150 AND S. 1301
AS OF 6/2/98
Submitted individually by Bankruptcy Judge Lisa Hill Fenning

The proposed bankruptcy reform legislation offers a mix of beneficial and harmful provisions from the standpoint of the administration of the bankruptcy system. As a veteran nearly 13 years on the bankruptcy bench of the highest volume bankruptcy court in the country, I have examined the proposed legislation from the perspective of one who would be expected to apply the new statutory provisions in the real world of the cases that come before me. I am deeply concerned that the current version of the legislation appears likely to impose significant burdens and costs on both the debtors and the courts that outweigh any monetary benefit for creditors.

The comments here focus on what is likely to happen if the current proposals are enacted. Of particular concern are provisions that will probably not work properly in the courts, or that will probably produce unintended consequences for the bankruptcy system. Some of the problems lie in drafting, and could perhaps be remedied with changes to text. Other problems are more fundamental: as drafted, the "means-testing" formulas and approach appear to create a burdensome procedure that is likely to cause substantial numbers of debtors to be disqualified from either Chapter 7 or 13 relief, as well as discourage attorneys from representing consumers and cause trustees to resign *en masse* due to the increased duties and costs of administering Chapter 7 cases. Two of the other most controversial proposals – the proposed amendments regarding dischargeability standards for credit card debts under 11 U.S.C. § 523(a)(2), and the proposed elimination of the "superdischarge" in Chapter 13 cases -- are highly likely to generate substantial litigation cost and delay.

Some of the detailed formulas and requirements are apparently intended to restrain perceived leniency or inconsistency of some judges. For that kind of problem, however, the single, most effective remedy will probably prove to be the more effective appellate review resulting from the streamlined appellate process embodied in **Section 411 of H.R. 3150**, and the parallel **Section 603 of S. 1914.** Expedited appellate review should result in quicker development of controlling precedents in case law that will guide statutory construction and provide defined limits for the bankruptcy judges wrestling with difficult statutory applications. Indeed, the change in appellate structure, plus the provisions giving judges more tools to deal with abusive filings -- like *in rem* relief from stay powers -- may rein in abusive filings to a significant degree without the immediate need for some of the controversial provisions in the current bills.

All participants in the legislative debate appear to agree that debtors who can repay a substantial portion of their unsecured debt through a Chapter 13 plan should be required to do so. However, for the reasons set forth below, ability to repay should be determined *as a condition of discharge*, not as a condition of eligibility to file.

I. H.R. 3150, Section 104 -- "Gateway" prepetition credit counseling requirement.

Proposed "gateway" eligibility restrictions imposed by **Section 104 of H.R. 3150** and **Section 322 of S. 1301** will delay -- and potentially bar -- access to the courts, without offering any proven benefit to either debtors or creditors. From the standpoint of bankruptcy administration, proof problems about "gateway" eligibility requirements will result in costly litigation about issues that have nothing to do with whether the debtor can afford to repay creditors. Motions to dismiss for failure to attempt a pre-petition workout will result in litigation in many cases, resulting in additional cost and delay for both debtors and the court. Any requirement that Chapter 7 panel trustees be required to bring such motions will impose significant costs in trustee time and attorney fees that will be impossible to recoup from typical "no-asset" Chapter 7 cases, particularly if the debtor is unrepresented by counsel. Eligibility criteria set forth in the proposed amendment will require collateral litigation about a variety of factors that may be difficult to establish, such as how hard the debtor tried to work out the debt problems, whether the negotiations were carried out in good faith by the debtors and creditors, and whether the available debt counseling programs met the quality, availability, and effectiveness requirements contemplated by the proposed amendments.

Alternatives: If the goal is to maximize repayment from those debtors who *can* repay, then the focus of any litigation about eligibility should be upon the debtor's actual ability to repay. The bills should be modified to:

- Eliminate the linkage between pre-bankruptcy counseling and eligibility, in favor of stressing – and funding – effective post-filing debt-management education as a condition of discharge in any chapter. Requiring completion of a debtor education program during a bankruptcy case *would be* a reasonable condition of receiving a discharge under any chapter. If the court or the U.S. Trustee are to provide or certify providers of education, sufficient funding should be appropriated for that purpose.
- Require court-annexed mediation within 30 days *after filing (instead of before)* via credit counselors or others to attempt consensual work-out. Such a program could reward debtors who enter into work-outs that result in stipulated dismissals, by providing a form of dismissal order that purges their record of the bankruptcy filings, while rendering them ineligible for any repeat filing for 180 days.

NOTE re drafting problems: Certain language in proposed **new 11 U.S.C. § 109 (i)(1)**-- conditioning eligibility upon proof that a debt-workout was attempted pre-petition "notwithstanding any other provision of this section" -- is inconsistent with subsection (5) that permits a court to waive the requirement under certain circumstances.

II. The "means-testing" formula is too complex, and is likely to cause more problems than it solves.

A. Pro se filings are likely to increase because of the additional work required of counsel, as well as the mandatory penalties if they make a mistake.

Debtors will have more difficulty finding affordable legal representation if H.R. 3150 is adopted, because consumer attorneys are unlikely to be willing to undertake the time-consuming reporting and analysis required by the "means-testing" provisions for a price that debtors can afford. In the Central District of California, already nearly 40% of all cases are filed *pro se*, without a lawyer. Unrepresented parties often find compliance with the rules and requirements of bankruptcy to be extremely difficult, and tend to demand excessive amounts of court and trustee time and assistance. Attorneys' reluctance to take individual cases is likely to be exacerbated by the potentially expensive sanctions mandated under proposed **Section 103 of H.R. 3150** if the judge disagrees with the attorney's analysis of eligibility for Chapter 7 relief.

B. **H.R. 3150's formulas will deny discharge in Chapter 7 to debtors who cannot confirm a Chapter 13 plan.**

1. **Definition of "projected monthly net income" in proposed section 11 U.S.C. § 109(h), fails to include many expenses and required payments in determining eligibility for Chapter 7 relief:**

The definition of "projected monthly net income" to be incorporated in **new 11 U.S.C. § 109 (h)** [per **section 101 of H.R. 3150**] omits from its calculation the accumulated prepetition arrearages owed on both secured debt and priority debt that would have to be repaid through a Chapter 13 plan, as well as Chapter 13 administrative priority claims.

Secured debt arrearages, interest and fees are omitted. The amount of secured debt to be factored into "monthly net income" under **new § 109(h)(3)(B)** does NOT include either the arrearage that would have to be repaid under a Chapter 13 plan, or any interest or fees (such as attorney fees, foreclosure fees, or other charges) that would be included in the secured claim in Chapter 13. As currently drafted, subsection (3)(B) only factors in the "amounts scheduled as contractually payable to secured creditors in each month of the 60 months following the date of the petition." The amounts "contractually payable . . . in each month" would ordinarily be the regular monthly payment according to the contract, not the claim for arrearages to be repaid through the Chapter 13 plan.

Current family support orders are omitted. The determination of the amount of priority debt under proposed **new § 109(h)(3)(C)**, by contrast, only includes the amounts due and payable "as of the date of the petition", NOT the monthly amounts that come due post-petition on regular child and spousal support obligations. Moreover, the language of (3)(A) does not indicate whether recipients of current child and spousal support qualify as dependents for purposes of determining the total dependents under the applicable expense allowance formulas, nor does the applicable formula provide for the full amounts set by the family court order.

Chapter 13 administrative expenses and trustee fees are omitted. Proposed § 109 (h) does not include the cost of Chapter 13 -- administrative priority expenses and trustee percentage fees -- in the formula to test whether Chapter 13 would generate returns for general unsecured creditors. It also omits any provision for tithing as allowed by the pending bill now before Congress.

2. **The definition of "monthly net income" in proposed 11 U.S.C. § 101 (39A) for confirming Chapter 13 plans omits regular monthly secured and priority payments due outside the plan.**

This new formula is to be used to determine the amounts to be paid in Chapter 13 plans per new Section 111. This definition differs materially from the "projected monthly net income" formula used to determine eligibility for Chapter 7. Like that formula, however, the "monthly net income" definition omits various regular expenses from its calculations.

Secured debt determination omits regular monthly payments due outside the plan. The average monthly payment amount is determined for purposes of proposed **Subsection § 101 (39A)(B)** on the basis of the "total of all amounts to be paid on account of secured claims pursuant to the plan." This means the arrearage amounts, including interest and fees portions of the secured claim, to be paid through the plan. It would NOT, however, ordinarily include the regular monthly payment to be paid outside the plan. In other words, it is the obverse of the definition under 109 (h): it excludes the very amounts that are included in the calculation under that section. Because regular debt service is also excluded from the regular living expenses set forth in § **101 (39A)(A),** the amounts required to be paid to general unsecured creditors will not permit debtors to make all of the required payments to their secured creditors.

Current family support orders also appear to be omitted from this formula. The determination of the amount of priority debt under proposed **new § 101(39A)(C),** like that for proposed **new § 109 (h)(3)(C),** only includes the amounts due and payable "as of the date of the petition", NOT the monthly amounts that come due post-petition on regular child and spousal support obligations. Moreover, it is not at all clear from the language of **§ 101(39A)(A),** whether recipients of current child and spousal support would qualify as dependents for purposes of determining the total dependents under the applicable expense allowance formulas, nor is it clear that the applicable formula would provide for the full court-ordered amounts.

Conclusion: Despite the formula's failure to provide for the actual secured and priority payments owed by debtors, the proposed amendment to **§1325(b)(1)(B)** would require that "the total amount of monthly net income received by the debtor shall be paid to unsecured nonpriority creditors under the plan." The amounts required to be paid to unsecured creditors under this provision will be impossible for many debtors to pay -- they just will not have sufficient income. This formula will also effectively eliminate the right to tithe set forth in S. 1244. The effort to craft such a detailed formula should either be abandoned, or a full-scale revision should be undertaken that carefully works out the details of these proposals in real-life scenarios.

3. **The proposed "means test" formulas completely ignore the fact that at least 3% of the individual Chapter 13 cases, and an unknown number of the individual Chapter 7 cases involve the operation of small businesses.**

The "means test" formulas are impossible to apply in cases involving individual debtors operating small businesses, as they only relate to personal income and expenses, not business income and expenses. Determining "disposable income" in business Chapter 13s under current law is often complicated and uncertain. The proposed new standards are totally inapplicable to business cases.

III. As provided by S. 1301, 11 U.S.C. § 707 (b) should be used as the mechanism to prevent Chapter 7 discharges if debtors can in fact repay a substantial portion of their general unsecured debts. However, any "means test" should only be used to bar a Chapter 7 discharge if the debtors would be able to confirm a Chapter 13 plan resulting in meaningful repayment to general unsecured creditors.

Using a broader, flexible formula tied to the amounts that the individual debtors could repay to general unsecured creditors in a Chapter 13 plan is a more appropriate basis to deny Chapter 7 relief. The trustees and the U.S. Trustee are in a better position to perform any required calculations than an unrepresented debtor, and can be required to do so, once the case is in the bankruptcy system.

Thus, a more effective approach is likely to be to strengthen 11 U.S.C. § 707 (b) by establishing a benchmark like the 20% repayment standard set forth in **Section 102 of S. 1301,** which incorporates by reference the standards of 11 U.S.C. § 1325(b), thus avoiding any inconsistencies. A specific obligation could be imposed upon the Chapter 7 panel trustees or the United States Trustee to conduct a computerized analysis of either all Chapter 7 cases or a sample to verify whether such a Chapter 13 plan could be proposed in individual cases.

Like those of the comparable section of H.R. 3150, the sanctions provisions of **Section 102 of S. 1301** also appear to require attorneys to guarantee results: that is, if the judge disagrees with their analysis of whether Chapter 7 is an appropriate remedy, then the court is required to assess a civil penalty against the attorney. Yet many cases fall in factual gray areas, about which reasonable people may disagree. Just because the evidence presented at the hearing is sufficient to justify a determination that the debtor can repay sufficient debts to justify dismissal or conversion, it does not necessarily follow that the attorney should have been able to predict that result with certainty. Fed. R. Bankr. Proc. Rule 9011 already authorizes the court to sanction parties and counsel for frivolous filings. This proposal would be a significant deterrent to any attorney accepting representation of any individual debtors, with the result that debtors will be deprived of representation.

Alternatives:

- Delete proposed new subsection 707(b)(3)(B).
- Add at the end of § 707(b)(3): ", if the attorney's filings were not substantially justified," like the standard set forth in proposed new § 707(b)(4)(A) to be applied to the award of sanctions against creditors for making frivolous motions under this section.

IV. The proposed amendments to § 523(a)(2)(A) and (C) relating to credit card debt are overly broad.

These provisions represent a major change in the traditional philosophy that financially distressed debtors can generally obtain a discharge of all but two types of unsecured debts: obligations that should be paid as a matter of public policy (like taxes, federally-insured student loans, family support), and debts arising from intentionally wrongful conduct (like damages from the debtor's fraud or willfully malicious injuries). By contrast, the proposed changes will make credit card debts nondischargeable without any intentional wrongful conduct by the debtor. All the creditor would have to prove about the debtor's conduct under the proposed change, is that the credit card debt was incurred by a debtor who could not afford to repay it, applying an objective, hindsight standard for affordability. It would not matter whether debtors understood that their debt was already too high, and that objectively they should not have taken on more debt. It would not matter whether the debtors genuinely thought they could meet the required, minimum monthly payments as they came due. It would not matter if the debtors reasonably believed that their financial condition would improve shortly, thus providing the ability to repay. None of these factors would support a defense of a nondischargeability complaint under the proposed change, although they are defenses under current prevailing standards.

Proponents of the current legislation are correct, however, that § 523 needs to be amended to specify more clearly when credit card debt should be nondischargeable due to debtor's fraud or false pretenses. Proving wrongful intent is hard: debtors rarely admit it on the stand. Intent is inferred from various factors, not an easy or predictable process in many cases. The proposed amendment does not, however, provide assistance in refining the circumstances supporting a finding of wrongful intent; rather it eliminates the need for any proof of specific intent by substituting an objective standard of actual ability to repay. As drafted, **Section 145 of H.R. 3150** effectively makes all credit card debt nondischargeable if debtors have negligently used credit cards to live beyond their means -- in effect, imposing an effectively "no-fault" standard for nondischargeability of this category of voluntary debt alone. No other debts under the Code become nondischargeable merely because the debtor was negligent or reckless. No justification has been offered for this departure from the existing standards and principles.

Moreover, the amended version of **§ 523(a)(2)(A)** set forth in **Section 145 of H.R. 3150** is ambiguous and will foster litigation. The amendment requires that the credit must have been extended "without an application therefor and reasonable evaluation of the debtor's ability to repay." But who has the burden of proof on this issue? It is not clear whether this requirement is in the nature of an affirmative defense that must be proven by the debtor, or an element of the proof that must be provided by the creditor pursing a § 523 complaint. An "application" for a credit card could be simply a signature on a form requesting the card, or it could be the equivalent of a financial statement, listing other cards held, the outstanding balances on them, as well as other income and expense information. Perhaps the application should require the same information as required to file a bankruptcy, so that both the prospective borrower and the credit card issuer can see the full profile of the applicant's financial condition. Similarly, the proposed reasonable reliance language does not provide sufficient direction to the courts: is a credit check required when the card is issued? If so, then the language should so specify. Perhaps the issuer should also be required to show that the information upon which it relies has been updated at reasonable intervals, for example, by requiring annual updates of the original financial information before the card is renewed.

Conclusion: If credit card issuers do not take reasonable steps to reduce their lending risk, debtors who find themselves overextended should not be penalized by imposing "no-fault" nondischargeability determinations. If it is uneconomic for issuers to take such simple precautions to prevent overextension risk, it is even harder to justify the litigation cost of § 523 actions after a bankruptcy filing.. Of course, if the debtors lie on their applications, traditional nondischargeability rules would apply.

Alternative: Establish clearer, but flexible statutory criteria that would provide statutory standards to determine when credit card debt should be found to have been wrongfully incurred without intent to repay. Possible language to implement this concept would modify 11 U.S.C. § 523(a)(2)(A) as follows:

> "actual fraud, or use of a credit or charge card or other device to access a credit line without a reasonable expectation of having income sufficient to make the regular payments on such debt as they come due during the next six months."

Such a standard would recognize and honor the expectations of the borrower and the credit card issuer at the inception of the debt. The issuer does not usually expect or intend that the debt be repaid in full in the near term. Rather, the nature of the bargain is the implied promise of the debtor to make regular monthly payments of at least the minimum specified in the regular monthly invoices, essentially in perpetuity, since the monthly minimums for many of these debts would amortize over as much as 20 to 30 years. Thus, if the debtor reasonably believed that the minimum monthly payments could be paid out of future income in the relatively short term, then no fraud has been committed.

It should be noted that, even if the H.R. 3150 version is adopted, it should be clarified to define "repay" to refer to ability to make required installment payments over the contemplated period for the debt. Neither a balance sheet insolvency standard nor an arbitrary short-term amortized repayment schedule should be used to test whether the debtor's belief is reasonable, because neither the borrower nor the issuer entered into the transaction upon the assumption that immediate repayment would be required. The issuer looks to future income for repayment, not to assets. If, on the other hand, the issuer really expects repayment within a specific period of time, then the billing statements should so specify and the borrower should be informed before the borrowing occurs.

B. H.R. 3150's Section 142 proposed 90-day conclusive presumption of nondischargeability is overbroad.

This new provision should not apply to refinancing of existing debt, where the new credit is used solely to pay existing dischargeable debt. This commonly occurs when the debtor responds to a solicitation to refinance existing debt by transferring balances to a lower-interest credit card. In these transactions, the debt repayment is direct to the other creditor. Assuming that the debtor did not misrepresent his or her financial condition in connection with the new credit, the credit card issuer should not be immunized from risky lending practices by the fortuity that the repayment of debt occurred within 90 days. The new credit issuer can protect itself by evaluating its risk; the debtor does not pocket any money – it is merely being used to repay other debt.

Alternative: Invited balance transfers from one credit card to another should not be treated as fraudulent so long as they do not increase the overall amount of debt, and the debtor reasonably believes that the new minimum monthly payments can be made out of expected future income.

Proposed change to S. 1301: Modify Section 317's proposed amendment to 11 U.S.C. § 523(a)(2)(C) to add the following immediately before the close parens:

", except debt incurred in the course of refinancing a pre-existing dischargeable debt)"

V. The Chapter 13 "superdischarge" should be preserved as an incentive for completing a Chapter 13 plan.

Elimination of the "superdischarge" will require litigation of § 523 nondischargeability cases in Chapter 13, with attendant cost and delay. Attorney fees incurred for defense of such complaints may sink otherwise feasible plans, and will certainly delay confirmation in many cases. Currently, only about one-third of all Chapter 13 plans are consummated; most debtors find themselves unable to maintain payments because of interruption of income, or underestimating of expenses. Adding expensive litigation to the Chapter 13 process will undoubtedly cause more plans to fail. Moreover, attorney fees and other administrative expenses are not included in the formula for testing eligibility for Chapter 7 under proposed § 109(h), thus increasing the risk that neither a Chapter 7 or 13 discharge will be available under H.R. 3150 if it is enacted.

VI. Benefits from bankruptcy-- including both the automatic stay and discharge -- should be dependent upon full disclosure by debtors. Disclosure requirements, however, should not expose the debtors or the system to new kinds of fraud.

A. Tax returns and account numbers should not be part of the public record on file with the court. Otherwise, debtors may be victimized by identity theft.

Requiring tax information and other documentation to be provided to the trustee as a condition for discharge is essential to the integrity of the overall bankruptcy process. However, **Section 301 of S. 1301** requires the tax returns to be filed with the court, and **H.R. 3150** requires them to be filed with the U.S. Trustee, where they will be part of the public record, downloadable, and subject to copying. However, making tax returns part of the public record -- and thus available to "data miners" and con artists -- is dangerous. Court records are already available electronically on-line in some jurisdictions, and will soon be in most, if not all, courts. If tax returns can be downloaded or photocopied, then they can be misused. If debtors' credit account numbers also become part of the public record as also proposed by **Section 405 of H.R. 3150**, and payroll stubs are attached to the petition as required by **Section 407 of H.R. 3150**, then anyone would have access to sufficient information about debtors to assume their credit identities. This kind of detailed information should be furnished by debtors to the trustees, but should not be in the public records of the court.

B. The "automatic dismissal" required by Section 407 of H.R. 3150 and Section 301 of S. 1301, if the debtor fails to provide tax returns or other documents, penalizes inexperienced *pro se* debtors, and cannot readily be implemented given the present terms of the bill.

The court will not be able to tell from its own records whether all required documentation has been supplied to the correct party, because some documents are required to be provided to the standing or panel trustee, or the United States Trustee, instead of being filed with the court. However, if all of the documentation were to be required to be provided to the panel or standing trustee, then the trustee could include a statement as to compliance as part of the report to the court upon completion of the § 341(a) meeting. The Bankruptcy Court for the Central District of California already has in place an automated dismissal process that dismisses cases for failure to appear at the § 341(a) meetings, upon report of the trustee. Failure to provide specified documents could be added as another ground for automated dismissal based upon a trustee's report.

Additional documentation of income is especially important to a ready determination as to ability to repay debt. At a minimum, current Schedule I must be revised to require disclosure of all household income that is available to meet the household expenses that are itemized in Schedule J. The omission of such income often gives a seriously misleading impression of an individual's actual disposable income.

Alternative: Clarify by statute the debtor's duty to provide more information and documentation to the panel and standing trustees, with greater assurance of availability to creditors. Changes that might accomplish this goal should:

1. Mandate more comprehensive disclosures on revised schedules to be formulated by the Administrative Office.

2. Require copies of paystubs, tax returns, and similar documentation of income and expenses to be provided to the case trustees, where it will not be available to the public.
3. Permit scheduled creditors to copies of such documentation to scheduled creditors upon request of the trustees. Privacy concerns justify limiting such administrative requests to those of scheduled creditors to avoid blanket requests being made by "data miners" or other third parties without a stake in the case in question. Unscheduled parties should have to obtain a court order for an examination of the debtor, in accordance with current rules.
4. Require trustees to respond to requests for copies of such documentation within reasonable times and subject to a reasonable per-page charge to be determined by a schedule of fees to be promulgated by the U.S. Trustee's Office. Failure of trustees to respond to requests for such copies in accordance with the rules or guidelines should be grounds for sanctions, including monetary sanctions or possible removal from the trustee panel.
5. Consider increasing the statutory fee for Chapter 7 panel trustees and Chapter 13 standing trustees if these documentation requirements prove unduly burdensome.

C. Proof of identity, social security or tax identification number, and address should be required as a condition for filing a bankruptcy petition.

Currently, more ID is required to cash a $10 check than file bankruptcy and obtain the most powerful federal injunction under the law. The only effective way to stop serial filings is to be able to verify whether a particular debtor has filed before. Section 109 should be amended to require such proof be presented to debtor's counsel, who should be required to certify that the identification information has been verified, with copies of the documentation maintained in the attorney's records, or by the clerk for filings by unrepresented debtors, though not inserted into the publicly available files for the reasons set forth above.

A national registry of bankruptcy cases is currently being developed by the Administrative Office of the United States Courts for on-line access to listings of all filings in the country. Such a national registry, however, will be useful only if it is reliable. It will be reliable only if the identity of the debtors is verified. The identification information currently being provided to the bankruptcy courts, however, is not reliable, and has not been verified. For example, in a recent study, the United States Attorneys Office in the Central District of California reported that it receives hundreds of complaints each year about bankruptcy petitions containing forged signatures, phony social security numbers, and other false identifying information. Similarly, efforts to bar refiling of cases by ineligible debtors will only be effective if the ineligilibity is determinable at the petition window.

The answer is to require debtors to present identification sufficient to verify the essential information on the face of their petition, and permit the bankruptcy courts to have access to the Social Security database to verify the social security numbers of filers. Such identification requirements are used in an increasing number of commercial transactions, so debtors should not find them unduly intrusive, but rather typical and commonplace.

Proposed amendment to 11 U.S.C. § 109: [add new text at end]

> *(h) The petition must be accompanied by proof of identity (including all names used by the debtor within the past six years), address, social security number, and employer's tax identification number (if any), in a form acceptable to the clerk. The clerk may refuse to accept a petition for filing if such proof is not provided, unless otherwise ordered by the court.*

A corollary amendment to the Social Security Act should authorize the bankruptcy clerks to have online access to the social security database to verify the information provided by the debtor.

D. The benefit of the automatic stay should be limited to scheduled property, particularly real property.

For a variety of fraudulent reasons, real property is being omitted from schedules. Sometimes the debtor is hiding the property to prevent it from being sold for the benefit of creditors. Sometimes, the entire bankruptcy case is a front for a foreclosure scam, in which multiple properties are transferred into a bankruptcy case to delay foreclosure. If the debtor has a reasonable explanation for inadvertent omission, then a motion to amend the schedules to add property and obtain protection of the automatic stay could cure the problem. Section 362 should be amended accordingly, as set forth in the attached proposals from the Bankruptcy Foreclosure Scam Task Force of the Central District of California Bankruptcy Court.

E. Preventing serial filings by ineligible debtors: Proposed amendment to 11 U.S.C. § 109(g)

Ineligible debtors should not be rewarded for filing another bankruptcy case. A parallel amendment to § 109(g) would clarify that the stay does not arise for an ineligible filing. The proposed new language is italicized:

> **Proposed addition to S. 1301:**
> [add at end of 11 U.S.C. § 109(g) subsection, following subparagraph (2)]
>
> *During the 180-day period, the automatic stay shall not arise in any new case filed by or against a debtor who is ineligible to be a debtor under this subsection.*

VII. S. 1301's proposal to strengthen 11 U.S.C. § 707(b) by permitting creditors to move to dismiss Chapter 7 cases on the grounds of abuse might be workable, with certain changes.

Section 707(b) has not allowed for creditors to bring motions to dismiss because of concerns that such motions might be used solely for the purpose of extracting unwarranted reaffirmation agreements, or for other improper advantage. That concern was well-founded, as the Sears reaffirmation debacle of the spring of 1997 demonstrated.

Yet no one has more information or more incentive to ask the court to make the debtors pay what they can afford to pay than the creditors of the estate. So, the proposed broadening of movants under

Section 707(b) to include creditors makes sense. However, such misuse could be substantially avoided if this broadening of Section 707(b) were counterbalanced by adding to S. 1301 a provision to prohibit reaffirmation of unsecured debts and of consumer purchase money security interests below a specified value. Such an amendment would also substantially prevent the abusive reaffirmation tactics used by Sears and others.

Proposed amendment to prevent abusive creditor motions under 11 U.S.C. § 707(b):

Modify 11 U.S.C. § 524(c) by adding a new subsection (7) as follows:

> *"(7) the claim is a allowed secured claim that is secured by property having a fair market value of at least $500.00.*
> *"Agreements between an individual debtor and a holder of a claim that is wholly unsecured, or between a debtor and a holder of a claim that is secured by a lien on property having a fair market value of less than $500.00, are prohibited, and shall be deemed void and unenforceable.*

VIII. Proposed amendments to 11 U.S.C. § 362 to address serial filing problems should be revised.

The Central District of California has been plagued in recent years by thousands of bankruptcy petitions filed solely to delay residential evictions or foreclosures for a few weeks or months, without any intention to complete the bankruptcy case. The problems with abusive filings have been sufficiently severe that the Bankruptcy Court created a Bankruptcy Foreclosure Scam Task Force to investigate the problems, examine the issues, and recommend solutions. Local remedies have to some extent ameliorated the adverse impact of these kinds of abusive filings in recent years. However, the Task Force concluded that the ultimate answer is to change 11 U.S.C. § 362 to stop the automatic stay from going into effect in subsequent cases affecting the particular property filed after a bankruptcy judge has made a finding of abuse, and has issued an "*in rem*"order or an order dismissing the case with a prohibition on the refiling of another case for the 180-day period specified in 11 U.S.C. § 109(g). This change would prevent relitigation of issues *already determined* by court order.

The purpose of this proposal is essentially similar to that of the repeat filing provisions of H.R. 3150 (section 121) and S. 1301 (section 303), but would improve upon those provisions in several ways. First, it would withhold automatic stay protections in a *second* filing, if the bankruptcy court has determined that abusive conduct occurred in the prior case. By relying upon an actual determination by the court, it avoids unduly burdensome or complicated presumptions while providing direction to the court as to the kinds of conduct that would justify the "*in rem*" bar. Second, it would assure access to the court for an initial determination of the propriety of the prior filing, as well as an opportunity to show that the new filing should not be tainted by the misconduct in the prior case. Third, it is consistent with the limitations for eligibility for relief set forth in 11 U.S.C. § 109(g).

Under proposed § 362(b)(19), the filing of a bankruptcy petition would not operate as a stay of any foreclosure proceeding affecting property governed by the entry of an *in rem* order under § 362(d)(4) in a prior bankruptcy case for a period of two years, which should be ample time to complete any foreclosure proceedings. Proposed new text is italicized.

<u>Proposed substitute amendment to 11 U.S.C. § 362(d)</u>: [to replace Section 303 of S. 1301]

(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay –

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(4) with respect to a stay of an act against real property under subsection (a) of this section, by a creditor whose claim is secured by an interest in such real estate, if the court finds that the filing of the bankruptcy petition was part of a scheme to delay, hinder and defraud creditors that involved either

(A) transfer of all or part ownership of, or other interest in, the real property without the consent of the secured creditor or court approval; or

(B) multiple bankruptcy filings affecting the real property; or

(C) omission of the real property from the schedules filed with the court.

If recorded in compliance with applicable state laws governing notices of interests or liens in real property, an order entered pursuant to this subsection shall be binding in any other bankruptcy case purporting to affect the real property filed within two years, except that a debtor in a subsequent case may move for relief from such order based upon changed circumstances or for good cause shown, after notice and a hearing.

<u>Proposed amendment to 11 U.S.C. § 362(b)</u>

(b) The filing of the petition under section 301, 302, or 303 of this title or of an application under section 5(a)(3) of the Securities Investor Protection Act of 1970, does not operate as a stay –

(19) under subsection (a) of this section, of any act to enforce any lien against or security interest in real property following the entry of an order under section 362(d)(4) as to that property in any prior bankruptcy case for a period of two years after entry of such an order. The debtor in a subsequent case, however, may move the court for relief from such order based upon changed circumstances or for other good cause shown, after notice and a hearing.

(20) under subsection (a) of this section, of any act to enforce any lien against or security interest in real property

(A) if the debtor is ineligible under section 109(g) to be a debtor in a bankruptcy case, or
(B) if the bankruptcy case was filed in violation of a bankruptcy court order in a prior bankruptcy case prohibiting the debtor from being a debtor in another bankruptcy case, or
(C) if the real property was not listed on the debtor's schedules as filed with the

Chambers of Honorable Lisa Hill Fenning
U.S. Bankruptcy Judge
255 East Temple Street, Suite 1682.
Los Angeles, CA 9012
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FAX COVER SHEET

FAX NUMBER TRANSMITTED TO:(202) 456-1605

To: Sally Katzen, Deputy Assistant to the President
and Deputy Director of NEC
Attn: Shannon Mason, Assistant

From: I.B. Pierce, Judicial Assistant to Judge Lisa Hill Fenning

Date: May 19, 1998

DOCUMENTS	NUMBER OF PAGES*
Comments on Proposed HR 3150 & S.1301	4
Proposed Corrective Amendments to the Bkcy Code	5

COMMENTS: Judge Fenning would like 15-20 minutes of Ms. Katzen's time on May 20th after 10:30am to discuss the impact on the court and consumer debtor that the pending bankruptcy legislation will have. Attached is a short position paper and suggested corrective amendments to the Bankruptcy Code for your review.
Please confirm whether Judge Fenning will be able to see Ms. Katzen so that I may advise her as quickly as possible.

****

* NOT COUNTING COVER SHEET. IF YOU DO NOT RECEIVE <u>ALL</u> PAGES, PLEASE TELEPHONE US IMMEDIATELY AT (213) 894-2553.

COMMENTS ON PROPOSED HR 3150 AND S. 1301 (as of 5/15/98)

Submitted Individually by Bankruptcy Judge Lisa Hill Fenning

The current rush to enact bankruptcy reform legislation appears likely to produce a bill with far-reaching, unintended consequences, as well as numerous technical glitches. While I agree that reform is necessary and support many of the specific provisions of S. 1301, some of the key provisions of the current are likely to cause problems for the courts, impair the ability of family support creditors among others to collect on their claims, as well as imposing serious hardship on many debtors who will be denied effective bankruptcy relief. The current drafts are based upon some flawed assumptions about how the bankruptcy system currently operates, and about how the proposed changes would work.

The text of the bills changes almost daily, as the legislative process accelerates, so it is difficult to provide detailed commentary on the wording of the various provisions. In this letter, I address only some of the conceptual and systemic problems likely to cause difficulty if the bills are enacted in their present general form. The problems fall into four general categories:

1. SECURED AND PRIORITY CREDITORS – ESPECIALLY FAMILY SUPPORT CLAIMANTS – WILL EFFECTIVELY LOSE THEIR PRIORITY STATUS.

- **Nondischargeability of credit card debt will compete for the same post-petition dollars available for payment.**
- **Debtors will be far less likely to obtain any discharge.**

On the surface, HR 3150 and S. 1301 do not expressly alter the statutory priority requirements set forth in 11 U.S.C. § 507 which give payment priority to family support, tax, and student loan debts, by contrast to general unsecured creditors. These statutory priorities have long been embodied in bankruptcy and state collection laws as a matter of public policy. The proposed bills, however, will significantly interfere *de facto* with the ability of such creditors to obtain payment from the debtor's available post-petition income. This results from two major aspects of the proposed bills; together they will make it *much* harder for debtors to discharge general unsecured debt by either completing Chapter 13 plans or qualifying for a Chapter 7 discharge.

- First, both bills will make nondischargeable significant portions of commonly occurring credit card debt – that incurred over time by debtors living consistently somewhat beyond their means – as opposed to limiting nondischargeability to intentionally wrongful conduct.

- Second, the specifics of the "means-testing" provisions, coupled with minimum unsecured payment amounts and a lengthening of Chapter 13 plans from three years to five, will simultaneously make it harder to confirm a feasible plan, and to complete the repayments over such a long time.

By making it more difficult for many debtors to obtain any discharge at all, these bills will mean that less of the debtor's post-petition income will be available to pay family support and other secured and priority creditors. If such a transfer from one type of creditor to another is intended by the drafters, then the priorities should be expressly reordered to avoid difficult statutory interpretation problems for the courts.

Currently, Chapter 13 plans may use all of the debtor's disposable income to repay mortgage and support arrearages, and can confirm a three-year plan even if no funds are available to pay unsecured creditors. These so-called "zero percent" plans are common, and genuinely appear to represent the debtor's best efforts in many cases. Indeed, the question is often whether the budgets are too *lean* in a desperate effort to save the house, not whether the debtors are padding their expenses for an extravagant lifestyle. In California, the housing costs are so high that many debtors are paying an unusually high percentage of their income for housing, especially if their income has dropped due to downsizing efforts over the past few years (as has happened for aerospace or financial industry workers who have been unable to find new employment at the same income level). Selling their homes to reduce living expenses has not been an option for most of our debtors during the past six years, because most of them have owed more on their homes than the current value, due to the precipitous drop in regional real estate values. Under HR 3150's formula, these debtors would be required to pay at least $50 monthly to general unsecured creditors, litigate the dischargeability of credit card debt accumulated during a period of unemployment, and stretch out their mortgage arrearage for whatever period is required to pay it, in light of the mandatory unsecured creditor payments. They will still face the balance of nondischargeable debt at the end of their plan.

Moreover, under the caselaw in some circuits, including the Ninth, holders of nondischargeable debts have the right to pursue a Chapter 13 debtor's current income, thereby disrupting any payment plan. *See In re Pacana,* 125 B. R. 19 (9th Cir. BAP 1991) (child support creditor holding nondischargeable debt is not barred by the automatic stay from enforcing state law wage garnishments against Chapter 13 debtor's post-petition income). Currently, as a practical matter, if the nondischargeable support debt is provided for in full for payment through the Chapter 13 plan, the child support creditors do not object to Chapter 13 plans over a three-year maximum period. By contrast, support creditors are unlikely to be willing to wait for five years under the proposed legislation while part of the debtor's income is diverted to payment of unsecured debts or nondischargeable credit card debt rather than being devoted to child support payments. Moreover, under this caselaw, nondischargeable credit card debt could also be collected by state law remedies, unprotected by the automatic stay. If Chapter 13 thereby becomes ineffective for support debtors, then they are likely to lose their houses and cars due to inability to cure arrearage amounts through Chapter 13 plans.

Other likely consequences of the proposed changes relating to stricter "means-testing" under the proposed, complex formulas are the following:

- Secured creditors will have to wait five to seven years for full repayment of their arrearages, instead of the standard three years under current law.
- The expansion of nondischargeable debt categories in Chapter 13 cases effectively eliminates the "superdischarge" that was intended to encourage filings under

Chapter 13, and means that more claimants will be seeking payment out of the debtor's post-petition income, in competition with support and tax priority creditors.

- Significantly increased dischargeability litigation in Chapter 13 will increase attorney fees and administrative priority claims, and delay confirmation of plans, thereby delaying payment to secured and priority creditors.
- The requirement of mandatory minimum payments to general unsecured creditors in Chapter 13 will force longer plans, stretching out payments of arrearages on home mortgages and cars, and diluting and delaying payments to priority tax and family support creditors.
- Most debtors do not have sufficient job stability and longevity to sustain a five-year plan, based upon their job histories coming into Chapter 13, thus substantially increasing the probability that the plan will fail. Since the bill precludes any other bankruptcy relief, debtors are likely to lose their houses and, because of the lack of a discharge of their general unsecured debt, be unable to make support payments.

Strongly preferable alternatives to the HR 3150 approach:

- Preserve Chapter 13 "superdischarge," subject to a stricter "good faith" standard to restrict confirmation of Chapter 13 plans where minimal or no payments are proposed for debts that would be nondischargeable in a Chapter 7 case.

- Amend 11 U.S.C. § 707(b) simply by allowing creditors to bring motions under the current, or slightly clarified standards, and allow courts to decide such motions on an individualized, "totality of the circumstances" basis.

Crucial modifications if the HR 3150 approach is used:

- Modify HR 3150 to clarify that the "means test" properly accounts for payment of all secured debt arrearages and Chapter 13 administrative expenses in evaluating whether unsecured creditors would benefit from forcing the debtor into Chapter 13.

- Modify HR 3150 to eliminate the $50 minimum payment to unsecured creditors, if secured or priority debt require all disposable income for repayment to be achieved in a three-year period.

2. **THE REQUIREMENTS FOR FINANCIAL AND TAX RETURN INFORMATION REQUIRE SIGNIFICANT REVISION. IN THEIR PRESENT FORM, THEY WILL LIKELY CAUSE:**

- **UNWARRANTED DISMISSALS OF CASES**
- **UNDUE INVASION DEBTORS' PRIVACY**
- **EXPOSURE OF DEBTORS TO IDENTITY THEFT FRAUD**
- **ADMINISTRATIVE PROBLEMS DUE TO DOCUMENTS BEING FILED WITH INAPPROPRIATE ENTITIES**

Debtors should be required to provide case trustees and their creditors, with all necessary information about their financial condition for the processing of their cases. For example, the it is already the practice in the Central District of California to required filing of all tax returns as a condition of confirmation of Chapter 13 plans. The specific provisions of Sections 406 and 407 of HR 3150, however, need to be revised for the following reasons:

- Debtors frequently are disorganized in their record-keeping, and may not have three years' worth of tax returns readily available. The 45-day deadline before "automatic dismissal" is unreasonably short: in fact, it usually takes more than 45 days to receive copies of missing tax returns from the IRS

- Filing the detailed financial information required by these sections with either the US Trustee or the court raises concerns of invasion of privacy concerns especially in light of expanded electronic access to court files. Of particular concern is the requirement for filing of a pay stub and tax returns. Under current tax law, parties cannot routinely obtain tax returns in civil litigation in discovery, absent a showing of good cause, and even if obtained in discovery, returns would not be routinely filed with the court in civil litigation.

- Public availability of copies of pay stubs, tax returns, exact account numbers and similar information will give rise to serious identity theft fraud. While the trustees should (and currently *do*) receive and review this information, it should NOT be part of the public record.

- Requiring all of these documents to be filed will cause record-keeping and record-storing problems for both the U.S. Trustee and the clerk's offices.

- The proposed "automatic" dismissal requirement cannot be implemented: the documentation is required to be filed with the U.S. Trustee and is therefore not part of the court record from which compliance could be routinely determined.

If, despite these serious concerns, these public filing requirements are to be implemented, an alternative to "automatic" dismissal would be:

A noticed motion or declaration of noncompliance from the case trustee, based upon a review of the debtor's file, would appear to be a more appropriate mechanism to implement this provision, which would work best if the documents were required to be furnished to the case trustee, and not to the U.S. Trustee.

PROPOSED CORRECTIVE AMENDMENTS TO THE BANKRUPTCY CODE

Submitted individually by Bankruptcy Judge Lisa Hill Fenning

INTRODUCTION: *PREVENTING BANKRUPTCY ABUSE AND SERIAL FILINGS*

The Central District of California has been plagued in recent years by thousands of bankruptcy petitions filed solely to delay residential evictions or foreclosures for a few weeks or months, without any intention to complete the bankruptcy case.

For purposes of this analysis, a bankruptcy case is considered to be "abusive" if it was filed to delay or defraud creditors, without any intention of complying with the requirements to obtain a discharge or complete a plan.

This definition of "abuse" thus differs sharply from another usage that has recently become relatively commonplace: lenders and others debating consumer bankruptcy policy sometimes use the term "abusive bankruptcies" to refer to cases in which debtors seek to discharge substantial credit card and other unsecured debt that possibly could be partially repaid via Chapter 13. By contrast to those arguments over the appropriate *scope* of consumer discharges, the cases of concern here do not seek *any* discharge, because they are never intended to be completed. All they seek is the automatic stay for purposes of delay.

Local remedies have to some extent ameliorated the adverse impact of these kinds of abusive filings in recent years. However, the ultimate answer is to change 11 U.S.C. § 362 in two ways:

- to stop the automatic stay from going into effect in subsequent cases affecting the particular property filed after a bankruptcy judge has issued an "*in rem*" order based upon evidence of abuse
- to except from the automatic stay the enforcement of state court judgments for eviction from residential tenancies, to permit landlords to recover possession of the premises without having to obtain bankruptcy orders for relief from the automatic stay

Both of these changes would prevent relitigation of issues *already determined* by court order. Neither would impair a debtor's ability to obtain a discharge of debt. Both would reinforce the principle that the availability of bankruptcy relief should not constitute an open invitation to undermine the finality of prior orders of bankruptcy courts or state courts.

I. Preventing serial filings to prevent foreclosures: "*In Rem*" Amendments to 11 U.S.C. §362

Under proposed § 362(d)(4), the bankruptcy court would be authorized to issue "*in rem*" relief based upon a showing of intentional fraud. The resulting *in rem* order would bind all parties with notice and opportunity to be heard. If recorded, it would also constitute binding notice to third parties. Moreover, the filing of future bankruptcies involving the property would not give rise to an automatic stay if an *in rem* order has been entered. The debtor in the subsequent case or any other party to that case, however, would have the right to seek the imposition of a stay for cause shown.

The purpose of this proposal is essentially similar to that of the repeat filing provisions of H.R. 3150 (section 121) and S. 1301 (section 303), but would improve upon those provisions in several ways.

First, it would withhold automatic stay protections in a *second* filing, if the bankruptcy court has determined that abusive conduct occurred in the prior case. By relying upon an actual determination by the court, it avoids unduly burdensome or complicated presumptions while providing direction to the court as to the kinds of conduct that would justify the "*in rem*" bar. Second, it would assure access to the court for an initial determination of the propriety of the prior filing, as well as an opportunity to show that the new filing should not be tainted by the misconduct in the prior case. Third, it is consistent with the limitations for eligibility for relief set forth in 11 U.S.C. § 109(g).

Other recurring fact patterns involved in abusive bankruptcies are the omission of the real property from the schedules, or the post-petition transfer of the interest into the estate after the schedules were filed. Full and accurate disclosure of the debtor's assets is required by 11 U.S.C. § 521 as part of the basic duties owed by the debtors for the privilege of the automatic stay and potential discharge of debts. Debtors filing in good faith would have no reason to omit real property from their schedules. The automatic stay should only protect real property disclosed to the court as an asset of the estate; it should not protect concealed property or property transferred into the estate post-petition without court authorization. Section 362 should be amended to except unscheduled real property from the scope of the automatic stay.

Under proposed § 362(b)(19), the filing of a bankruptcy petition would not operate as a stay of any foreclosure proceeding affecting property governed by the entry of an *in rem* order under § 362(d)(4) in a prior bankruptcy case for a period of two years, which should be ample time to complete any foreclosure proceedings. Proposed new text is italicized.

<u>Proposed amendment to 11 U.S.C. § 362(d)</u>

(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay --

***

(4) with respect to a stay of an act against real property under subsection (a) of this section, by a creditor whose claim is secured by an interest in such real estate, if the court finds that the filing of the bankruptcy petition was part of a scheme to delay, hinder and defraud creditors that involved either

(A) transfer of all or part ownership of, or other interest in, the real property without the consent of the secured creditor or court approval; or

(B) multiple bankruptcy filings affecting the real property; or

(C) omission of the real property from the schedules filed with the court.

If recorded in compliance with applicable state laws governing notices of interests or liens in real property, an order entered pursuant to this subsection shall be binding in any other bankruptcy case purporting to affect the real property filed within two years, except that a debtor in a subsequent case may move for relief from such order based upon changed circumstances or for good cause shown, after notice and a hearing.

<u>Proposed amendment to 11 U.S.C. § 362(b)</u>

(b) The filing of the petition under section 301, 302, or 303 of this title or of an application under section 5(a)(3) of the Securities Investor Protection Act of 1970, does not operate as a stay -

(19) under subsection (a) of this section, of any act to enforce any lien against or security interest in real property following the entry of an order under section 362(d)(4) as to that property in any prior bankruptcy case for a period of two years after entry of such an order. The debtor in a subsequent case, however, may move the court for relief from such order based upon changed circumstances or for other good cause shown, after notice and a hearing.

(20) under subsection (a) of this section, of any act to enforce any lien against or security interest in real property

(A) if the debtor is ineligible under section 109(g) to be a debtor in a bankruptcy case, or
(B) if the bankruptcy case was filed in violation of a bankruptcy court order in a prior bankruptcy case prohibiting the debtor from being a debtor in another bankruptcy case, or
(C) if the real property was not listed on the debtor's schedules as filed with the court, provided that the debtor may move the court for protection of real property that is proposed to be added to the schedules, based upon a showing of good cause as to why the property was not originally included in the schedules.

II. Preventing serial filings by ineligible debtors: Proposed amendment to 11 U.S.C. § 109(g)

Ineligible debtors should not be rewarded for filing another bankruptcy case. A parallel amendment to § 109(g) would clarify that the stay does not arise for an ineligible filing. The proposed new language is italicized:

[add at end of subsection, following subparagraph (2)]

During the 180-day period, the automatic stay shall not arise in any new case filed by or against a debtor who is ineligible to be a debtor under this subsection.

III. Reducing the number of consumer bankruptcy cases filed solely to delay residential evictions: Proposed amendment to 11 U.S.C. § 362(b)

The most recent study in the Central District of California shows that approximately 20% of the motions for relief from stay involve requests to complete residential evictions following an unlawful detainer judgment in state court. The court hears thousands of such motions each year. In effect, the bankruptcy courts are being asked to second-guess the state courts that have already heard and decided the matter, and have entered judgment awarding possession of the residential unit to the landlord.

Conservative estimates indicate that cases filed solely to stop eviction constitute about 2% of the 117,000 cases filed in the Central District last year based upon the court's most recent figures. If the incentive to delay eviction were eliminated, then presumably at least 2,500 fewer cases would be filed in the district, thereby eliminating 20% of the relief from stay motions. It is important to note that these cases are usually not completed after the relief from stay motion is decided. In most bankruptcy cases filed to stop an eviction, the debtors fail to file their schedules or fail to appear at the first meeting of creditors, causing their bankruptcy cases to be dismissed for lack of prosecution.

No bankruptcy purpose is served by requiring landlords to seek relief from the automatic stay to complete the eviction process. If the tenants have a defense to eviction, or if entitlement to subsidized public housing is at issue, the debtor/tenants' remedy should be to make their case in the state court proceeding, or obtain a stay of that proceeding *before* judgment by filing a bankruptcy petition before the state court trial. Once the state court judgment has been entered, principles of state/federal comity preclude the bankruptcy courts from acting as appellate courts reviewing the judgment. The only purpose in filing a bankruptcy case after an unlawful detainer judgment has already been entered is to delay eviction without just cause. The solution is simple: the stay should not bar eviction pursuant to a prepetition judgment.

The provisions of H.R. 3150 and S. 1301 address this issue as well.

Proposed amendment to 11 U.S.C. § 362(b):

[add new text]

(19) under subsection (a)(2) of this section, of the enforcement of a judgment, other than a money judgment, obtained in an unlawful detainer action or proceeding to conduct an eviction or otherwise obtain possession of residential property;

IV. Preventing bankruptcy fraud by requiring identification: Proposed amendment to 11 U.S.C. § 109

Several of the pending proposals include recommendations for creation of a national bankruptcy registry to maintain unified records of the individuals and entities who have filed bankruptcy cases. Such a registry serves many informational purposes, but it also is a key tool in the effort to prevent bankruptcy abuse and serial filings. Such a registry would include the debtor's name, social security number or other taxpayer identification number, as well as address and other identifying information. The court system is currently implementing a prototype of such a registry.

A national registry, however, will be useful only if it is reliable. It will be reliable only if the identity of the debtors is verified. The identification information currently being provided to the bankruptcy courts, however, is not reliable, and has not been verified. For example, in a recent study, the United States Attorneys Office in the Central District of California reported that it receives hundreds of complaints each year about bankruptcy petitions containing forged signatures, phony social security numbers, and other false identifying information. Similarly, efforts to bar refiling of cases by ineligible debtors will only be effective if the ineligilibity is determinable at the petition window.

The answer is to require debtors to present identification sufficient to verify the essential information on the face of their petition, and permit the bankruptcy courts to have access to the Social Security database to verify the social security numbers of filers. Such identification requirements are used in an increasing number of commercial transactions, so debtors should not find them unduly intrusive, but rather typical and commonplace.

Proposed amendment to 11 U.S.C. § 109:

[add new text at end]

(h) The petition must be accompanied by proof of identity (including all names used by the debtor within the past six years), address, social security number, and employer's tax identification number (if any), in a form acceptable to the clerk. The clerk may refuse to accept a petition for filing if such proof is not provided, unless otherwise ordered by the court.

A corollary amendment to the Social Security Act should authorize the bankruptcy clerks to have online access to the social security database to verify the information provided by the debtor.

COMMENTS ON PROPOSED HR 3150 AND S. 1301 (as of 5/19/98)
Submitted Individually by Bankruptcy Judge Lisa Hill Fenning

Unless significant revisions are made, the current rush to enact bankruptcy reform legislation may produce a bill with far-reaching, unintended consequences, as well as numerous technical glitches. I agree that reform is necessary and do not object to most of the provisions of S. 1301, but H.R. 3150 is seriously flawed, particularly with respect to the complex "means-testing" formula to be applied in determining eligibility for Chapter 7 relief, and confirmability for Chapter 13 plans. In particular, H.R. 3150's inconsistent and incomplete formulas may mean that debtors are found ineligible for Chapter 7, but lack sufficient income, in light of their secured debt, to confirm a Chapter 13 plan. Such debtors would be entirely denied access to a bankruptcy discharge. Other key provisions of the current bills are likely to invade debtors' privacy, impose arduous administrative burdens on the courts and trustees without much benefit to any creditors, and impair the ability of family support creditors among others to collect on their claims. The current drafts are based upon some flawed assumptions about how the bankruptcy system currently operates, and about how the proposed changes would work.

The text of the bills changes almost daily, as the legislative process accelerates, so it is difficult to provide detailed commentary on the wording of the various provisions. In this letter, I address only some of the conceptual and systemic problems likely to cause difficulty if the bills are enacted in their present general form. The problems fall into four general categories:

1. H.R. 3150's formulas for eligibility will result in some debtors barred from a discharge under either Chapter 7 or Chapter 13.

It is difficult to assess exactly how the formulas set forth in Sections 101 and 102 of H.R. 3150 will work in the real world. Neither formula takes into account Chapter 13 trustee fees or attorney fees and administrative expenses in a Chapter 13. Moreover, it appears that the formula in Section 101 governing eligibility for Chapter 7 relief omits accrued arrearages, foreclosure fees, attorney fees and similar additional elements of the secured amount due, and does not provide for interest during the repayment period. Conversely, Section 102 bases the monthly expense calculation of proposed section 101 (39A)(A) on a national formula without reference to the actual monthly obligations of a particular debtor for secured debt, while omitting from (B) any amounts attributable for current monthly mortgage and car payments that are not going through the plan. These poorly drafted and overly detailed provisions will undoubtedly produce costly and unnecessary litigation, and will deny any bankruptcy discharge to those unfortunate debtors falling between the two standards. These provisions would be a nightmare to implement.

By contrast, S. 1301 addresses this issue by an appropriate method: modifying Section 707(b), which already embodies a "means test." The proposed standard is workable, requiring debtors who can do so, to repay 20% of their unsecured debt via a Chapter 13 plan under the relevant legal and cost of living standards. Judges can evaluate each case in light of the strengthened standard, on an appropriate case-by-case analysis. No debtors should end up without a remedy under this approach.

Finally, under both bills, the debtors' attorneys bear a significant risk if they misanalyze a case and it is found to be ineligible for Chapter 7 relief: they will have to reimburse all attorney fees for the successful movant. Asking debtors' attorneys to guarantee the outcome of any case is unfair and unreasonable. Already nearly 40% of the debtors in the Central District of California are unrepresented. The additional costs and risks under these draconian mandatory sanction provisions will discourage attorneys from representing consumer debtors – a result that is not in the best interests of the bankruptcy system. The sanctions should be discretionary; judges will impose them if true abuse is found.

2. Secured and priority creditors – especially family support claimants – will effectively lose their priority status.

- **Nondischargeability of credit card debt will compete for the same post-petition dollars available for payment.**
- **Debtors will be far less likely to obtain any discharge.**

On the surface, HR 3150 and S. 1301 do not expressly alter the statutory priority requirements set forth in 11 U.S.C. § 507 which give payment priority to family support, tax, and student loan debts, by contrast to general unsecured creditors. These statutory priorities have long been embodied in bankruptcy and state collection laws as a matter of public policy. The proposed bills, however, will significantly interfere *de facto* with the ability of such creditors to obtain payment from the debtor's available post-petition income. This results from two major aspects of the proposed bills; together they will make it *much* harder for debtors to discharge general unsecured debt by either completing Chapter 13 plans or qualifying for a Chapter 7 discharge.

- First, many debts will become nondischargeable in Chapter 13 cases as well as Chapter 7 cases. These creditors would have the same right to compete for payment out of debtors' post-petition income as support creditors, thereby diluting the effectiveness of the priority.

- Second, imposing a minimum unsecured payment amount as H.R. 3150 does, means that a Chapter 13 plan cannot commit all of the available income to prompt payment of secured and priority creditors. The limited amount of post-petition net monthly income will have to be shared with nonpriority unsecured creditors.

- Lengthening of Chapter 13 plans from three years to five will make it harder to complete a Chapter 13 plan, as many debtors lack a sufficiently stable job and income to maintain repayment plans for such a long period. More such cases will be dismissed. If the unsecured debt is thus not discharged, the support creditors will have to compete post-bankruptcy with such creditors for repayment.

- Finally, significantly increased dischargeability litigation in Chapter 13 will increase attorney fees and administrative priority claims, and delay confirmation of plans, thereby delaying payment to secured and priority creditors.

This inability to complete a case and obtain a discharge is exacerbated by the formula problems created by H.R.3150, which make it more difficult for many debtors to obtain any discharge at all. Thus, both of these bills, but especially H.R. 3150, will mean that less of the debtor's post-petition income will be available to pay family support obligations. If such a transfer from one type of creditor to another is intended by the drafters, then the priorities should be expressly reordered to avoid difficult statutory interpretation problems for the courts.

Examples: Currently, Chapter 13 plans may use all of the debtor's disposable income to repay mortgage and support arrearages, and can confirm a three-year plan even if no funds are available to pay unsecured creditors. These so-called "zero percent" plans are common, and genuinely appear to represent the debtor's best efforts in many cases. Indeed, the question is often whether the budgets are too *lean* in a desperate effort to save the house, not whether the debtors are padding their expenses for an extravagant lifestyle. In California, the housing costs are so high that many debtors are paying an unusually high percentage of their income for housing, especially if their income has dropped due to downsizing efforts over the past few years (as has happened for aerospace or financial industry workers who have been unable to find new employment at the same income level). Selling their homes to reduce living expenses has not been an option for most of our debtors during the past six years, because most of them have owed more on their homes than the current value, due to the precipitous drop in regional real estate values. Under HR 3150's formula, these debtors would be required to pay at least $50 monthly to general unsecured creditors, litigate the dischargeability of credit card debt accumulated during a period of unemployment, and stretch out their mortgage arrearage for whatever period is required to pay it, in light of the mandatory unsecured creditor payments. They will still face the balance of nondischargeable debt at the end of their plan.

Moreover, under the case law in some circuits, holders of nondischargeable debts may have the right to pursue a Chapter 13 debtor's current income, thereby disrupting any payment plan. *See In re Pacana,* 125 B. R. 19 (9th Cir. BAP 1991) (child support creditor holding nondischargeable debt is not barred by the automatic stay from enforcing state law wage garnishments against Chapter 13 debtor's post-petition income). Currently, as a practical matter, if the nondischargeable support debt is provided for in full for payment through the Chapter 13 plan, the child support creditors do not object to Chapter 13 plans over a three-year maximum period. By contrast, support creditors are unlikely to be willing to wait for five years under the proposed legislation while part of the debtor's income is diverted to payment of unsecured debts or nondischargeable credit card debt rather than being devoted to child support payments. Moreover, under this caselaw, nondischargeable credit card debt could also be collected by state law remedies, unprotected by the automatic stay. If Chapter 13 thereby becomes ineffective for support debtors, then they are likely to lose their houses and cars due to inability to cure arrearage amounts through Chapter 13 plans.

Strongly preferable alternatives to the HR 3150 approach:

- Preserve Chapter 13 "superdischarge," subject to a stricter "good faith" standard to restrict confirmation of Chapter 13 plans where minimal or no payments are proposed for debts that would be nondischargeable in a Chapter 7 case.

- Adopt the S. 1301 approach to amend 11 U.S.C. § 707(b) simply by allowing creditors to bring motions under the current, or slightly clarified standards, and allow courts to decide such motions on an individualized, "totality of the circumstances" basis.

Crucial modifications if the HR 3150 approach is used:

- Modify HR 3150 to clarify that the "means test" properly accounts for payment of all secured debt arrearages and Chapter 13 administrative expenses in evaluating whether unsecured creditors would benefit from forcing the debtor into Chapter 13.

- Modify HR 3150 to eliminate the $50 minimum payment to unsecured creditors, if secured or priority debt require all disposable income for repayment to be achieved in a three-year period.

3. **The requirements in both bills for filing financial and tax return information require significant revision. In their present form, they will likely cause:**
   - **unwarranted dismissals of cases**
   - **undue invasion debtors' privacy**
   - **exposure of debtors to identity theft fraud**
   - **administrative problems due to documents being filed with inappropriate entities**

Debtors should be required to provide case trustees and their creditors, with all necessary information about their financial condition for the processing of their cases. For example, the it is already the practice in the Central District of California to required filing of all tax returns as a condition of confirmation of Chapter 13 plans. The specific provisions of Sections 406 and 407 of **HR 3150**, however, need to be revised for the following reasons:

- Debtors frequently are disorganized in their record-keeping, and may not have three years' worth of tax returns readily available. The 45-day deadline before "automatic dismissal" is unreasonably short: in fact, it usually takes more than 45 days to receive copies of missing tax returns from the IRS

- Filing the detailed financial information required by these sections with either the US Trustee or the court raises concerns of invasion of privacy concerns especially in light of expanded electronic access to court files. Of particular concern is the requirement for filing of a pay stub and tax returns. Under current tax law, parties cannot routinely obtain tax returns in civil litigation in discovery, absent a showing of good cause, and even if obtained in discovery, returns would not be routinely filed with the court in civil litigation.

- Public availability of copies of pay stubs, tax returns, exact account numbers and similar information will give rise to serious identity theft fraud. While the trustees should (and currently *do*) receive and review this information, it should NOT be part of the public record.

- Requiring all of these documents to be filed will cause record-keeping and record-storing problems for both the U.S. Trustee and the clerk's offices.

- The proposed "automatic" dismissal requirement cannot be implemented: the documentation is required to be filed with the U.S. Trustee and is therefore not part of the court record from which compliance could be routinely determined.

By requiring the tax returns to be filed as part of the public court record, **S.1301** in some ways creates more risks of identity theft and administrative problems than H.R. 3150. The court files are by definition public records. Moreover, they will be available in electronic form in the near future, searchable and subject to being copied via the Internet.

Alternative to public filing:

Require the pay stubs and tax returns to be filed with the case trustee, available upon request by any party in interest in the case.

Alternative to automatic dismissal:

The case trustee could follow current procedures and submit a report of the 341(a) meeting or confirmation hearing indicating that the debtor has failed to comply with the reporting requirements. In most districts, a report of nonappearance or noncompliance results in the issuance of a dismissal order. It should be the action of the trustee that triggers the dismissal. Alternatively, a noticed motion or declaration of noncompliance from the case trustee could be the vehicle to prompt dismissal. Either way, this proposal can only be readily implemented if the documents were required to be furnished to the case trustee, and not to the court or the U.S. Trustee.

4. Serial filings can only be effectively prevented if debtors are required to provide adequate identification and proof of social security or tax numbers as a condition of filing.

Both bills seek to prevent bankruptcy abuse in the form of serial filings. The measures proposed will give the courts many of the tools needed to address these issues effectively. However, all of these effort will fail if debtors are not required to provide identification as a condition for filing a petition.

The court system is currently implementing a national bankruptcy registry or index to maintain unified records of the individuals and entities who have filed bankruptcy cases. Such a registry serves many informational purposes, but it also is a key tool in the effort to prevent bankruptcy abuse and serial filings. Such a registry would include the debtor's name, social security number or other taxpayer identification number, as well as address and other identifying information.

A national registry, however, will be useful only if it is reliable. It will be reliable only if the identity of the debtors is verified. The identification information currently being provided to the bankruptcy courts, however, is not reliable, and has not been verified. For example, in a recent study, the United States Attorneys Office in the Central District of California reported that it receives hundreds of complaints each year about bankruptcy petitions containing forged signatures, phony social security numbers, and other false identifying information. Similarly, efforts to bar refiling of cases by ineligible debtors will only be effective if the ineligilibity is determinable at the petition window.

The answer is to require debtors to present identification sufficient to verify the essential information on the face of their petition, and permit the bankruptcy courts to have access to the Social Security database to verify the social security numbers of filers. Such identification requirements are used in an increasing number of commercial transactions, so debtors should not find them unduly intrusive, but rather typical and commonplace.

Proposed amendment to 11 U.S.C. § 109:

[add new text at end]

(h) The petition must be accompanied by proof of identity (including

all names used by the debtor within the past six years), address, social security number, and employer's tax identification number (if any), in a form acceptable to the clerk. The clerk may refuse to accept a petition for filing if such proof is not provided, unless otherwise ordered by the court.

Only with such verification will a system intended to limit the number of bankruptcy filings by individuals or entities be truly effective.

PROPOSED CORRECTIVE AMENDMENTS TO THE BANKRUPTCY CODE

Submitted individually by Bankruptcy Judge Lisa Hill Fenning

INTRODUCTION: *PREVENTING BANKRUPTCY ABUSE AND SERIAL FILINGS*

The Central District of California has been plagued in recent years by thousands of bankruptcy petitions filed solely to delay residential evictions or foreclosures for a few weeks or months, without any intention to complete the bankruptcy case.

> *For purposes of this analysis, a bankruptcy case is considered to be "abusive" if it was filed to delay or defraud creditors, without any intention of complying with the requirements to obtain a discharge or complete a plan.*

This definition of "abuse" thus differs sharply from another usage that has recently become relatively commonplace: lenders and others debating consumer bankruptcy policy sometimes use the term "abusive bankruptcies" to refer to cases in which debtors seek to discharge substantial credit card and other unsecured debt that possibly could be partially repaid via Chapter 13. By contrast to those arguments over the appropriate *scope* of consumer discharges, the cases of concern here do not seek *any* discharge, because they are never intended to be completed. All they seek is the automatic stay for purposes of delay.

Local remedies have to some extent ameliorated the adverse impact of these kinds of abusive filings in recent years. However, the ultimate answer is to change 11 U.S.C. § 362 in two ways:

- to stop the automatic stay from going into effect in subsequent cases affecting the particular property filed after a bankruptcy judge has issued an "*in rem*" order based upon evidence of abuse

- to except from the automatic stay the enforcement of state court judgments for eviction from residential tenancies, to permit landlords to recover possession of the premises without having to obtain bankruptcy orders for relief from the automatic stay

Both of these changes would prevent relitigation of issues *already determined* by court order. Neither would impair a debtor's ability to obtain a discharge of debt. Both would reinforce the principle that the availability of bankruptcy relief should not constitute an open invitation to undermine the finality of prior orders of bankruptcy courts or state courts.

I. Preventing serial filings to prevent foreclosures: "*In Rem*" Amendments to 11 U.S.C. §362

Under proposed § 362(d)(4), the bankruptcy court would be authorized to issue "*in rem*" relief based upon a showing of intentional fraud. The resulting *in rem* order would bind all parties with notice and opportunity to be heard. If recorded, it would also constitute binding notice to third parties. Moreover, the filing of future bankruptcies involving the property would not give rise to an automatic stay if an *in rem* order has been entered. The debtor in the subsequent case or any other party to that case, however, would have the right to seek the imposition of a stay for cause shown.

The purpose of this proposal is essentially similar to that of the repeat filing provisions of H.R. 3150 (section 121) and S. 1301 (section 303), but would improve upon those provisions in several ways. First, it would withhold automatic stay protections in a *second* filing, if the bankruptcy court has determined that abusive conduct occurred in the prior case. By relying upon an actual determination by the court, it avoids unduly burdensome or complicated presumptions while providing direction to the court as to the kinds of conduct that would justify the "*in rem*" bar. Second, it would assure access to the court for an initial determination of the propriety of the prior filing, as well as an opportunity to show that the new filing should not be tainted by the misconduct in the prior case. Third, it is consistent with the limitations for eligibility for relief set forth in 11 U.S.C. § 109(g).

Other recurring fact patterns involved in abusive bankruptcies are the omission of the real property from the schedules, or the post-petition transfer of the interest into the estate after the schedules were filed. Full and accurate disclosure of the debtor's assets is required by 11 U.S.C. § 521 as part of the basic duties owed by the debtors for the privilege of the automatic stay and potential discharge of debts. Debtors filing in good faith would have no reason to omit real property from their schedules. The automatic stay should only protect real property disclosed to the court as an asset of the estate; it should not protect concealed property or property transferred into the estate post-petition without court authorization. Section 362 should be amended to except unscheduled real property from the scope of the automatic stay.

Under proposed § 362(b)(19), the filing of a bankruptcy petition would not operate as a stay of any foreclosure proceeding affecting property governed by the entry of an *in rem* order under § 362(d)(4) in a prior bankruptcy case for a period of two years, which should be ample time to complete any foreclosure proceedings. Proposed new text is italicized.

Proposed amendment to 11 U.S.C. § 362(d)

(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay –

***

(4) with respect to a stay of an act against real property under subsection (a) of this section, by a creditor whose claim is secured by an interest in such real estate, if the court finds that the filing of the bankruptcy petition was part of a scheme to delay, hinder and defraud creditors that involved either

(A) transfer of all or part ownership of, or other interest in, the real property without the consent of the secured creditor or court approval; or

(B) multiple bankruptcy filings affecting the real property; or

(C) omission of the real property from the schedules filed with the court.

If recorded in compliance with applicable state laws governing notices of interests or liens in real property, an order entered pursuant to this subsection shall be binding in any other bankruptcy case purporting to affect the real property filed within two years, except that a debtor in a subsequent case may move for relief from such order based upon changed circumstances or for good cause shown, after notice and a hearing.

Proposed amendment to 11 U.S.C. § 362(b)

(b) The filing of the petition under section 301, 302, or 303 of this title or of an application under section 5(a)(3) of the Securities Investor Protection Act of 1970, does not operate as a stay –

(19) under subsection (a) of this section, of any act to enforce any lien against or security interest in real property following the entry of an order under section 362(d)(4) as to that property in any prior bankruptcy case for a period of two years after entry of such an order. The debtor in a subsequent case, however, may move the court for relief from such order based upon changed circumstances or for other good cause shown, after notice and a hearing.

(20) under subsection (a) of this section, of any act to enforce any lien against or security interest in real property

(A) if the debtor is ineligible under section 109(g) to be a debtor in a bankruptcy case, or
(B) if the bankruptcy case was filed in violation of a bankruptcy court order in a prior bankruptcy case prohibiting the debtor from being a debtor in another bankruptcy case, or
(C) if the real property was not listed on the debtor's schedules as filed with the court, provided that the debtor may move the court for protection of real property that is proposed to be added to the schedules, based upon a showing of good cause as to why the property was not originally included in the schedules.

II. Preventing serial filings by ineligible debtors: Proposed amendment to 11 U.S.C. § 109(g)

Ineligible debtors should not be rewarded for filing another bankruptcy case. A parallel amendment to § 109(g) would clarify that the stay does not arise for an ineligible filing. The proposed new language is italicized:

[add at end of subsection, following subparagraph (2)]

During the 180-day period, the automatic stay shall not arise in any new case filed by or against a debtor who is ineligible to be a debtor under this subsection.

III. Reducing the number of consumer bankruptcy cases filed solely to delay residential evictions: Proposed amendment to 11 U.S.C. § 362(b)

The most recent study in the Central District of California shows that approximately 20% of the motions for relief from stay involve requests to complete residential evictions following an unlawful detainer judgment in state court. The court hears thousands of such motions each year. In effect, the bankruptcy courts are being asked to second-guess the state courts that have already heard and decided the matter, and have entered judgment awarding possession of the residential unit to the landlord.

Conservative estimates indicate that cases filed solely to stop eviction constitute about 2% of the 117,000 cases filed in the Central District last year based upon the court's most recent figures. If the incentive to delay eviction were eliminated, then presumably at least 2,500 fewer cases would be filed in the district, thereby eliminating 20% of the relief from stay motions. It is important to note that these cases are usually not completed after the relief from stay motion is decided. In most bankruptcy cases filed to stop an eviction, the debtors fail to file their schedules or fail to appear at the first meeting of creditors, causing their bankruptcy cases to be dismissed for lack of prosecution.

No bankruptcy purpose is served by requiring landlords to seek relief from the automatic stay to complete the eviction process. If the tenants have a defense to eviction, or if entitlement to subsidized public housing is at issue, the debtor/tenants' remedy should be to make their case in the state court proceeding, or obtain a stay of that proceeding *before* judgment by filing a bankruptcy petition before the state court trial. Once the state court judgment has been entered, principles of state/federal comity preclude the bankruptcy courts from acting as appellate courts reviewing the judgment. The only purpose in filing a bankruptcy case after an unlawful detainer judgment has already been entered is to delay eviction without just cause. The solution is simple: the stay should not bar eviction pursuant to a prepetition judgment.

The provisions of H.R. 3150 and S. 1301 address this issue as well.

Proposed amendment to 11 U.S.C. § 362(b):

[add new text]

(19) under subsection (a)(2) of this section, of the enforcement of a judgment, other than a money judgment, obtained in an unlawful detainer action or proceeding to conduct an eviction or otherwise obtain possession of residential property;

IV. Preventing bankruptcy fraud by requiring identification: Proposed amendment to 11 U.S.C. § 109

Several of the pending proposals include recommendations for creation of a national bankruptcy registry to maintain unified records of the individuals and entities who have filed bankruptcy cases. Such a registry serves many informational purposes, but it also is a key tool in the effort to prevent bankruptcy abuse and serial filings. Such a registry would include the debtor's name, social security number or other taxpayer identification number, as well as address and other identifying information. The court system is currently implementing a prototype of such a registry.

A national registry, however, will be useful only if it is reliable. It will be reliable only if the identity of the debtors is verified. The identification information currently being provided to the bankruptcy courts, however, is not reliable, and has not been verified. For example, in a recent study, the United States Attorneys Office in the Central District of California reported that it receives hundreds of complaints each year about bankruptcy petitions containing forged signatures, phony social security numbers, and other false identifying information. Similarly, efforts to bar refiling of cases by ineligible debtors will only be effective if the ineligilibity is determinable at the petition window.

The answer is to require debtors to present identification sufficient to verify the essential information on the face of their petition, and permit the bankruptcy courts to have access to the Social Security database to verify the social security numbers of filers. Such identification requirements are used in an increasing number of commercial transactions, so debtors should not find them unduly intrusive, but rather typical and commonplace.

Proposed amendment to 11 U.S.C. § 109:

[add new text at end]

(h) The petition must be accompanied by proof of identity (including

> *all names used by the debtor within the past six years), address, social security number, and employer's tax identification number (if any), in a form acceptable to the clerk. The clerk may refuse to accept a petition for filing if such proof is not provided, unless otherwise ordered by the court.*

A corollary amendment to the Social Security Act should authorize the bankruptcy clerks to have online access to the social security database to verify the information provided by the debtor.

A Credit Card is Not a Toy, and Bankruptcy is Not Cool.
But With Toys Like "Cool Shoppin' Barbie," How Are Kids To Know?

By U.S. Sen. Dick Durbin

At a time when more Americans than ever before are going into serious credit card debt and facing financial crisis, one of the world's most recognized toy doll icons, Barbie, is priming children to go on unlimited shopping sprees with credit cards. Believe it or not, Barbie now has her very own MasterCard.

Introduced by Mattel and MasterCard International in 1997, "Cool Shoppin' Barbie" doesn't rollerblade, swim, or hold plastic hands with boyfriend Ken doll. She shops. And shops. And shops. All on credit. And, with no apparent credit limit, and no specified A.P.R., there's nothing she can't buy. Want a sporty pink convertible? Furnishings for that dream house? More beauty and fashion accessories? In Cool Shoppin' Barbie's world, she can visit the boutique (included as part of the Cool Shoppin' Barbie set) and charge all the neat stuff she wants. Because in this Barbie financial dream world, it's always — "Credit Approved!"

Designed for children ages three and older, Cool Shoppin' Barbie is equipped with batteries, a purse, an oversized shopping bag, and, of course, her MasterCard. After the completion of a sale, the doll's talking cash register thanks Barbie for shopping and says "credit approved" when her MasterCard is swiped. Barbie's credit never expires, and she can never go over her credit limit. More importantly, she doesn't have to worry about the monthly bills to pay off her debts.

I think any American who has ever used a credit card or experienced the financial hardships of consumer debt would agree that Cool Shoppin' Barbie's world doesn't come close to resembling the real world. Mattel officials have claimed that Cool Shoppin' Barbie is designed to give young Barbie fans a greater sense of realism as they play shop. However, if Barbie's financial picture matched that of many Americans she'd more likely be called "Goin' Bankrupt Barbie."

What's more, Mattel and MasterCard fail to provide Barbie with some of the important supporting cast associated with real-life credit card financing. If they had, she'd probably be having a few conversations with "Collection Ken" and be living in fear of a visit from "Repo G.I. Joe."

The credit card company wouldn't charge Barbie late fees if her payments arrived just one day late. Or charge her interest on interest, or extract interest on her late fees. Or raise her stated interest rates. Her credit issuer would not tease her to spend beyond her income with low introductory rates or "instant cash" checks. No, that sounds too much like the real world, not Barbie's dream world.

I am concerned that Cool Shoppin' Barbie may leave children with the impression that credit cards are toys. Barbie is a role model for many children and shouldn't be a symbol for irresponsible consumerism and an undesirable introduction for them into the consumer culture.

What the kids who play with Cool Shoppin' Barbie are not made aware of is that credit card debt is a major crisis for many American families today. This year, about 1.4 million families will file for consumer bankruptcy. In addition, credit card debt has doubled in just four years. At the end of 1997, the amount of credit card loans outstanding was $422 billion, twice as much as the amount in 1993. Women, especially those who are divorced and raising families, often are hit the hardest. Divorced women file for bankruptcy in greater proportions than divorced men, and frequently use the bankruptcy courts to eliminate credit card and other debts to concentrate their incomes on paying for current expenses. Should Barbie and Ken ever decide to "tie the knot," Mattel and MasterCard might want to remember this sad reality.

While MasterCard has targeted young Barbie fans as the future generation of MasterCard users, credit issuers also have set their sights on another young, vulnerable and under-informed group to get hooked on credit — college students.

Credit card issuers have been especially aggressive in luring college students to join the masses of plastic users. Cards are available on almost any campus to almost any student — no income, no credit history, and no parental consent required. I'm not surprised to hear reports that the typical college freshman receives more than 50 solicitations in his or her first few months in school. Vendors have staked out campuses all over the country, wooing students to sign up for new cards by hawking free gifts with their applications.

Go to any "Big Ten" football game this autumn and walk into the stadium. What you will probably find, in addition to the concession and souvenir stands, is a booth giving away t-shirts or frisbees to people who sign up for a credit card. Kids fresh out of high school are signing up for credit cards when they are 18 to get a free t-shirt. A recent report released by the Public Interest Research Group (PIRG) confirmed that most students responsible for their own bills (about 61 percent) obtained their cards at campus tables.

While credit cards have become a resource for extra income during college years, credit companies' predatory and misleading marketing activities on campuses has contributed significantly to the growing financial nightmares of many students. One Indiana University administrator recently remarked that the school "loses more students to credit card debt than academic failure." (*Chicago Tribune*, August 16, 1998) According to Elizabeth Warren, a bankruptcy expert at Harvard University, the number of bankruptcies among those under 25, particularly students, has doubled in the last six years, from 250,000 to 500,000.

But as consumer bankruptcy levels have risen to frightening levels, the credit card issuers have gotten even richer. Credit card lending is now twice as profitable as all other lending activities.

Bankruptcy is not cool, and credit cards are not toys. Cool Shoppin' Barbie's financial world may be make-believe, but in the real world, it's credit card companies that are toying with American families. Just ask college students.

A reaffirmation is a private agreement between a debtor and a creditor to continue paying a debt – even though that debt could be discharged through bankruptcy. It sounds like a good idea, but just listen to Francis Latanowich's story about reaffirmations.

Mr. Lantanowich declared bankruptcy in 1995. But when Sears came to him and told him that his television and car battery would be repossessed unless he reaffirmed his debt, he signed the papers they gave him. Mr. Latanowich wanted to keep the television for his children. Less than a year later after he filed for bankruptcy, this father of ___ wrote a Boston federal bankruptcy judge a desperate, hand scrawled note: "I receive 518 dollars a month on social security for a disability I have. I have tried to meet the payment every month but it is keeping food off the table for my kids. I would like to know if you could reopen my case so I could get rid of all my debt forever."

When the judge looked at the note and Mr. Latanowich's case, she was appalled. Sears ignored almost every law on the books about how to obtain a reaffirmation. Moreover, although Mr. Latanowich was making regular payments that should have reduced his debt, because of interest he actually owed Sears more than when he initially filed for bankruptcy.

Sadly Mr. Latanowich's story is not unique. Since his case came to light, bankruptcy judges throughout the country have started looking at creditor practices more carefully. And 40 state attorneys general launched investigations. So far the practices of Sears, Bloomingdale's, Macy's, Sterns, Montgomery Wards, Mays Department Stores, the Discover Card, and AT&T credit have ~~come under scrutiny~~ been shown to be suspicious, and the reaffirmation agreements of more than 300,000 people have been affected.

Unlike the House bill, the Senate bill actually attempts to address this problem by requiring that a judge review these reaffirmations and determine if they ~~are~~ were obtained unfairly or would affect the debtor's ability to feed his family.

from John Yurowsky

Bankruptcy Talking Points

I) Balance

- Since the first Bankruptcy Act was passed 100 years ago, "balance" has been the hallmark of every attempt by Congress to strike the right policy that would be fair to creditors and debtors alike.

- There is obviously no magic "bright" line that suddenly appears before Congressional policymakers, but common sense and understanding the real-life consequences of bankruptcy on individuals and families have always gone a long way in helping Congress to shape a wise policy that does not reward the few "bad actors" but also does not unduly punish hard-working citizens who have tried everything to avoid bankruptcy and still want to pay their bills as best they can.

- The key then is to make sure that both consumers and credit card companies act responsibly in the extension and use of credit before problems with debt become overwhelming.

II) Disclosure

- The Senate-passed bill is notable because for the first time, it requires the credit card industry to act responsibly in soliciting and extending credit.

- During the Senate debate last week, an amendment offered by Senators Dodd, Durbin and Sarbanes was adopted that required all credit card statements to show, among other things, how long it would take to pay off one's outstanding balance using only the minimum payment requested.

- Because increasing numbers of consumers do not look past enticing "introductory rates" or unbelievably low "minimum" payments each month to see when they will actually be paying in 6 months or 6 years, it is essential that this provision stay in the bill.

- It is not a coincidence that the rise in consumer bankruptcy filings has occurred during a period of unprecedented marketing efforts by credit card companies.

  - Today there are **well over a billion credit cards in circulation** -- a dozen credit cards for every American household. (Estimates from *1996 Statistical Abstract*, Table 793 and Table 66)

  - In 1997, credit card issuers **mailed more than three billion card solicitations to consumers.** The solicitation rate so far in 1998 is even higher. Based on industry estimates, such mail offers add up to about $243,000 of credit per household per year. At this rate, in a little over four years, the **credit card companies have offered about a million dollars of credit to each household** in the United States. Salem & Clark, GMK Banking Industry Report, Jun 11, 1996, p. 5)

- With this barrage of easy credit opportunities, Americans often do not consider the long-term implications of simply paying the minimum payment each month.

  - Industry analysts estimate that, using a typical minimum monthly payment rate on a credit card, **it would take 34 years** to pay off a $2,500 loan, and total payments would exceed 300% of the loan principal. (Salem & Clark, GMK Banking Industry Report, Jun 11, 1996, p. 5)

  - Nonetheless, credit card statements -- unlike mortgage loans and car loans -- **do not disclose the amortization rates** or the total interest that will be paid if the cardholder makes only the minimum monthly payment.

III) Solicitation of Minors

- Another amendment offered by Senator Dodd would have placed some restrictions on the currently unfettered solicitation of minors by the credit card industry. The Dodd amendment would have required a parental signature before a credit card account could be opened for a minor without an independent source of income. This amendment did not carry, but the subject is one that deserves more attention from Congress in the future. We cannot afford to have young Americans so deeply into debt before they even graduate high school or college, before they can secure their first full-time job, before they can start a family.

  - Direct solicitation of both college and high school students has intensified in the past two years. Credit cards are available at many colleges to almost any student -- no income, no credit history and no parental signature required. (Report of the National Bankruptcy Review Commission 93, October 20, 1997)

  - Last year an estimated 250,000 Americans filed for bankruptcy before they reached their 25th birthdays. (Sullivan, Warren and Westbrook, "From Golden Years to Bankrupt Years," 7 Norton Bankruptcy Law Adviser, 1 , July 1998)

  - The proportion of bankrupt debtors aged 18-24 doubled between 1991 and 1997. (Sullivan, Warren and Westbrook, "From Golden Years to Bankrupt Years," 7 Norton Bankruptcy Law Adviser, 1 , July 1998.

VII) THE LEGISLATION WRITTEN BY THE CREDIT CARD COMPANIES IS UNFAIR TO SINGLE MOTHERS AND THEIR CHILDREN

- The legislation written by the credit card companies would **give many credit card bills the same legal status as child support and alimony payments**. If the credit card lobbyists succeed, credit card debts could survive bankruptcy proceedings. As a result, single mothers seeking child support payments from bankrupt ex-husbands will be competing with well-funded lawyers from the credit card companies.

- If the credit card companies persuade Congress to promote credit card debt to the same status as child support and alimony payments, millions of children would be threatened.

    - In the past five years alone, **more than one million men owing alimony and child support filed for bankruptcy**. (Department of Health and Human Services support data and Sullivan, Warren and Westbrook, "Bankruptcy and the Family," 21 *Marriage and Family Review* 193, 1995)

    - Over the past five years, more than one million women have collected alimony and child support after their ex-husbands filed for bankruptcy. Under the current law, the women's debts survived the bankruptcy filing, often leaving them as the only creditor collecting from the ex-husbands. (Department of Health and Human Services support data and Sullivan, Warren and Westbrook, "Bankruptcy and the Family," 21 *Marriage and Family Review* 193, 1995)

    - During 1997, an estimated 300,000 bankruptcy cases involved child support and alimony orders.

In about half of these cases, women were creditors trying to collect alimony and child support from their bankrupt ex-husbands. In about half, women who rely on support payments filed for bankruptcy themselves as they tried to stabilize their post-divorce economic condition. (Department of Health and Human Services support data and Sullivan, Warren and Westbrook, "Bankruptcy and the Family," 21 *Marriage and Family Review* 193, 1995)

- About 650,000 homeowners filed for bankruptcy during 1997. Many of them were trying to save their homes from foreclosure. (Calculated from data in Sullivan, Warren and Westbrook, *As We Forgive Our Debtors*, 1989)

- The credit card industry's claim that the child support problem has been fixed is **false**.

  - The House bill would require that credit card debt be paid in **preference** to family support and taxes in Chapter 13 bankruptcies.

  - Both House and Senate bills would still allow much credit card debt to survive bankruptcy. This surviving credit card debt would **compete with family support obligations** for repayment by the debtor after bankruptcy.

  - "[U]nsecured credit card debt would be reclassified as a non-dischargeable debt, in the same category as child support, alimony and taxes. **Women could have a harder time collecting child support** if their ex-husbands had to decide between meeting family obligations or fending off aggressive collection agents." (*Los Angeles Times*, Jun 8, 1998) (emphasis added)

  - National Conference of Bankruptcy Judges: "It is very likely that some of the changes being considered by Congress would cause consumers, both within and outside the bankruptcy system, to be **unable to pay such basic obligations as mortgages, alimony, child support**, and student loans." (April 2, 1998 letter to Speaker Newt Gingrich) (emphasis added)

- "In a bow to the banks, the House bill elevates a significant portion of credit card debt to equal status with unpaid taxes, student loans and child support – debt that cannot be canceled. Kids and MasterCard would end up fighting for the same slice of the pie, attaching the same wages. Last year, the independent, congressionally-appointed National Bankruptcy Review Commission overwhelmingly rejected such a radical reshuffling of priorities." (*San Jose Mercury News*, June 18, 1998)

IV) We must Reinforce -- not Discourage -- the Responsible Use of Credit.

- If responsibility and accountability are to be reinforced for consumers and credit card companies alike, it makes no sense whatsoever for credit card companies to penalize consumers who responsibly use their cards. But that is precisely what has started to happen. The Senate bill would prohibit the emerging practice of some credit card companies that actually terminate customers who pay their bills on time!

  - Credit card companies often **cancel the credit cards of consumers who pay their bills on time.** Credit card companies terminate people who pay their balances in full because they are not profitable. The most profitable customers are the ones who make only the minimum payments; these are also the customers who are most likely to have financial problems.

    - "In October, Beneficial National Bank cut off 12,000 MasterCard holders because they paid their credit card bills in full every month, running up no interest. Too good a credit risk, no credit." (*Fort Worth Star-Telegram*, June 21, 1998)

V) The Senate Means-Test Provides Needed Flexibility

- The rigid House means-test would prevent many financially-distressed debtors from obtaining needed bankruptcy relief by failing to account for differing needs of families and regional variations in living expenses.

  - By using such a rigid test, the House bill would likely prevent many debtors from getting any bankruptcy relief and, in many cases, lose the ability to keep their homes, to pay child support and to keep their very jobs.

- The Senate means-test is preferable because it provides the bankruptcy judge more flexibility in reviewing the needs and expenses of the debtor, and because it requires less administrative cost to implement for all parties -- the courts, trustees, debtors, and creditors.

VI) Reaffirmations Should be Limited in Chapter 7

- In the last few years, certain major creditors have been found to have coerced lower income debtors into agreeing to repay debts which were actually discharged in bankruptcy. The courts should supervise reaffirmations to make sure that debtors are aware of their rights and that creditors are not overreaching.

VIII) THE CREDIT CARD INDUSTRY'S PROPOSED LEGISLATION IS UNFAIR TO OLDER AMERICANS TRYING TO PROTECT THEIR HOMES

- More than **a quarter million** Americans over the age of 50 filed for bankruptcy last year.

- More than one-half of all older Americans who file for **bankruptcy have lost their jobs**.

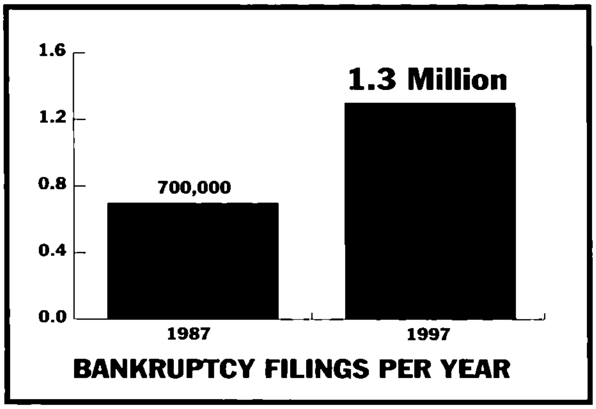
- Nearly a third of all older Americans who filed for bankruptcy **have medical debts they cannot pay**.

- Older Americans are disproportionately the **victims of credit scams and abuses**. More than one in ten of those who file for bankruptcy say they did so to deal with a creditor scams or aggressive creditor collection efforts.

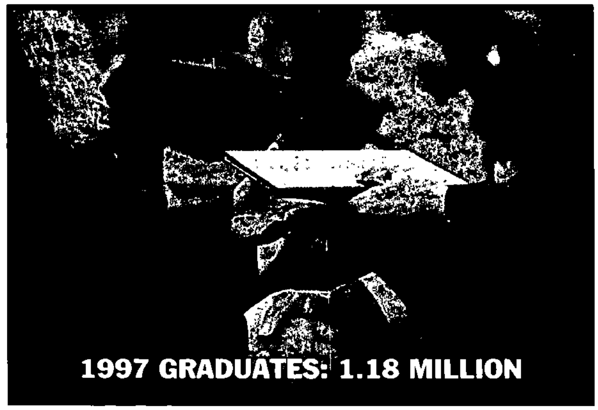
- One in ten older Americans who file for bankruptcy have **been thrown into financial crisis by a family problem** – a son on drugs, a divorced daughter and her family they are attempting to house and feed.

- The safety net provided by Social Security and Medicare is fraying: More than a third of the debtors over age 65 explained that they filed for bankruptcy because they lost the part-time jobs they had to supplement their Social Security payments. Another one-third said they had medical expenses not covered by Medicare.

- The legislation proposed by the credit card companies would make it much easier to creditors to foreclose on the homes of older Americans. About 650,000 homeowners filed for bankruptcy during 1997. Many of them were trying to save their homes from foreclosure. (Calculated from data in Sullivan, Warren and Westbrook, *As We Forgive Our Debtors*, 1989)



Source- *U.S. Administrative Office of the Courts*



Source- *National Center for Education Statistics.* Based on projected number of 1997 college graduates with Bachelor's degrees.

More people declared BANKRUPTCY than graduated from college last year.

IN TODAY'S CULTURE, it's easier to declare bankruptcy than to graduate from college. Skyrocketing personal bankruptcies have doubled in the past decade, at a time when economic growth and disposable personal income have risen steadily.

Our Federal bankruptcy laws discourage personal responsibility. More and more people who can pay down their debt are using bankruptcy as a financial planning tool, sheltering substantial wealth while sticking other consumers with the cost of their "bankruptcies of convenience."

Personal bankruptcies now cost consumers over $400 per household, and it takes 33 Americans to pay for one bankruptcy of convenience.* Maybe that's why 76% in a recent nationwide poll said "individuals should not be allowed to erase all their debt in bankruptcy if they are able to repay a portion of what they owe."

It's time to reform our flawed bankruptcy laws.

Support the **Bankruptcy Reform Act of 1998,** the Gekas-Moran Bill

Don't let people who can afford to pay down their debt stick others with the tab.

Paid for by the American Financial Services Association

*Analysis by SMR Research Corporation

Political Roundup

In Conn., A Boost For Koskoff ...

■ FORESHADOWING A THIRD matchup between **Rep. Nancy Johnson**, R-Conn., and Democrat Charlotte Koskoff, state Rep. Demetrios Giannaros Monday abandoned his bid for the House and endorsed Koskoff, the *Hartford Courant* reported.

"... It's good news for the Democrats and me, because now we can concentrate our energies on the election and beating Nancy Johnson," said Koskoff, a retired education professor and attorney — who came within 1,600 votes of toppling Johnson in 1996 after losing to the incumbent by nearly 2-1 two years earlier.

Koskoff still faces a battle for the Democratic nomination against James Griffin, a defense consultant whom she handily defeated in intraparty competition two years ago. The 6th District takes in the northwestern portion of the state.

This year, Griffin has tossed about $400,000 of his own money into the effort. But he was embarrassed last week when the *Courant* reported that, in FEC reports filed in January, he had signed the name of his campaign treasurer —who, it turned out, had been dead for about three months at the time.

Giannaros, who plans to seek reelection to the state legislature, said he had quit the congressional race because "it was pretty clear that for us to continue, we would have a divisive primary in September."

However, Griffin charged Giannaros had been "bludgeoned" out of the race, declaring, "Apparently the party leaders are looking to be simple rather than correct." Giannaros acknowledged having discussions with party leaders and Koskoff's campaign, but said there had been no "bludgeoning."

... As Kennelly Gets More Bad News

■ SEVEN MONTHS BEFORE voters go to the polls, Democratic **Rep. Barbara Kennelly** continues to trail GOP Gov. John Rowland by a wide margin in the race for Connecticut governor, according to a new public opinion survey.

The latest *Hartford Courant* poll gives Rowland a 50-28 point lead over Kennelly. The survey of 500 state residents, conducted April 14-22, has a 5 point error margin, and was conducted after Kennelly began her first round of TV advertising April 3.

Notwithstanding that exposure, Kennelly's numbers were virtually unchanged from March, when the previous *Courant* poll showed Rowland up by 52-31.

Nearly two-thirds of those polled approved of the way Rowland is handling his job. Perhaps the one silver lining for Kennelly is that 44 percent of those surveyed said they did not know enough about her to form an opinion, indicating she may have an opportunity to pick up support among those voters.

Challengers Fire $25,000 Question At Fox

■ TWO-TERM **REP. JON FOX**, R-Pa., came under fire Monday from two GOP primary foes over a $25,000 loan that is the subject of a complaint filed with the FEC by a conservative organization.

During a debate in the Philadelphia suburban district, attorney Jonathan Newman and anti-abortion activist Michael McMonagle repeatedly questioned Fox over the 1992 loan from a developer — which Fox says was for personal rather than campaign expenses, and thus exempt from campaign finance rules.

"If we don't get to the bottom of this problem with this illegal loan scenario with Jon Fox, this election is going to be handed to Joe Hoeffel," Newman declared in referring to the likely Democratic nominee — who lost to Fox by 84 votes in 1996.

Fox accused Newman of engaging in "character assassination," but also declared, "I'll give the money back," the *Philadelphia Inquirer* reported.

The other major contender in the May 19 GOP primary, ophthalmologist Melissa Brown, steered clear of the back-and-forth over the loan and sought to focus voters on her call to reform the nation's managed care system.

In Ohio, Dueling Senate Polls

■ IN THE LATEST ENTRY in the dueling polls department, the *Toledo Blade* Tuesday published a Senate race survey that is significantly at odds with a poll published just a day earlier by another major Ohio newspaper, the *Akron Beacon Journal*.

Both polls show GOP Gov. George Voinovich leading in the race for the seat of retiring Democratic **Sen. John Glenn**. And both show the likely Democratic candidate, former Cuyahoga County Commissioner Mary Boyle, running closer to Voinovich than had been widely expected.

So what is the discrepancy? The *Blade* poll of 685 likely voters, conducted April 17-24, shows only 5 percent of the electorate to be undecided. But the *Beacon Journal* survey of 800 registered voters, taken April 6-23, shows a whopping 40 percent in the undecided column.

The horserace numbers: The *Blade* has Voinovich up by 53-42 percent, while the *Beacon Journal* puts Voinovich in the lead by 36-23. The *Blade* survey, conducted by Louis Harris & Associates, has a 4 point error margin, while the *Beacon Journal* poll — by the University of Akron — has a 3.5 point error margin.

April 30, 1998

MEMORANDUM FOR HILLARY RODHAM CLINTON

FROM: NICOLE RABNER

SUBJECT: Meeting with Harvard Professor Elizabeth Warren

Tomorrow, you are scheduled to meet with Harvard Law Professor Elizabeth Warren, who has been a leading opponent of proposed bankruptcy reform legislation.

Recently, Warren has been effective in highlighting the adverse impact of this proposed legislation on child support and alimony collection for single parents. Today, alimony and child support, past taxes and educational loans survive a Chapter 7 bankruptcy. Recipients of child support and alimony benefit when their financially troubled ex-spouses can discharge their other debts and get their finances in order so that they can make the payments on their non-dischargeable debts, including their alimony and child support. The proposed legislation would increase the amount of potentially non-dischargeable debt (including some credit card debt), thereby putting child support collection in direct competition with credit card and other commercial lenders for the limited resources of the ex-husband.

The Administration plans to send a letter to the Congress next week outlining our position on this proposed legislation. As currently drafted, the letter concludes that we cannot support the pending legislation in its present form, but expresses our openness to responsible bankruptcy reform consistent with a range of principles -- including careful protections for child support and alimony payments.

While the Administration agrees with Warren on the important point of protecting alimony and child support payments, there are many within the Administration who, unlike Warren, believe that bankruptcy reform that meets our principles is good policy. Warren believes that the rise in Chapter 7 bankruptcies over the past year reflects in large measure the predatory activities of credit card companies, providing untempered and irresponsible access to credit; Warren therefore opposes even narrow changes to our bankruptcy laws that would provide credit card companies with any protections. There are many in the Administration, however, who believe that this is only in part true -- that there is also abuse in the system, *i.e.* those who are able to pay their debts (after they have met their child support and alimony obligations), and that these debts can be too easily discharged through bankruptcy. They believe that we can and should achieve responsible bankruptcy reform legislation that protects single parents.

Some in the Administration have advised that Warren is effective and persuasive, but has a broader agenda of opposition to any bankruptcy reform legislation.

To see the press release related to this letter, click here.
This letter is constantly being updated to reflect additional signatures.
This document last modified on 04/03/98

March 31, 1998

Bruce A. Markell
Professor of Law
211 South Indiana Avenue
Bloomington, IN 47405
bmarkell@indiana.edu

To all members of the House and Senate Judiciary Committees:

We are fifty-eight (58) academics who are deeply concerned about proposed legislation seeking to reform the federal bankruptcy law affecting consumers. We teach and study bankruptcy, and together have over 889 years of experience with bankruptcy matters. We come from different political, academic and economic perspectives, and from every region of this country.

We do not write to support or oppose any particular piece of legislation. Rather, we write to urge Congress to consider more carefully the pending reform proposals. If enacted, any of the current drafts of legislation would bring about dramatic and far-reaching changes. Yet the pace related to the examination of this legislation has been fast, and the study of its consequences superficial. In less than a year, at least three bills proposing radical changes to the consumer provisions of the bankruptcy code are on the verge of floor consideration by both houses of Congress. Combined, there have been fewer than five hearings on all bills. In contrast, the 1978 revision of the federal bankruptcy laws consumed more than five years, and over 60 days of hearings in both houses.

We are also concerned about the quality of information presented at the few hearings which have been held. The studies that have been the driving force behind many proposed reforms appear to have been inadequate, and to have emphasized the interests of institutional creditors. To date, virtually no one has spoken for those Americans who have declared bankruptcy or who may one day be forced into that position.

Aside from the tax code and the Social Security laws, no other federal law affects more Americans. Most individuals who file bankruptcy are average, middle class Americans. Focusing on one interest -- that of creditors (and in particular creditors who hold credit card debt) -- tends to mute the voices of the millions of other Americans affected by bankruptcy law. This imbalance affects more than debtors; when debt institutions hold the stage and suggest the changes, non-institutional creditors -- such as former spouses with support claims -- stand to lose.

In conclusion, we believe that the current debate is ill-considered, rushed and unbalanced. Before undertaking changes affecting all Americans whose lives are touched by bankruptcy, we urge you to pause, to hold full hearings on the issues, and to seek out a balanced, reasoned approach.

Very truly yours,

April 9, 1998

To All Members of the United States Congress:

Dear Senator or Representative:

We are a group of 110 United States bankruptcy judges. Most of us have been bankruptcy judges for more than ten years, and we have applied the complex provisions of the Bankruptcy Code to thousands of bankruptcy cases filed by individual debtors. Although we come from different political, intellectual and economic perspectives, and represent districts from every federal judicial circuit, we share a single, deep concern that legislation presently before Congress would make fundamental changes in bankruptcy for individual debtors that have not been sufficiently considered.

The proposed bills H.R. 2500, H.R. 3146, H.R. 3150, and S.1301 all impose new limits on the availability of bankruptcy relief. Since 1898, an individual s debts have been discharged upon surrender of the individual s nonexempt property, and the property has been liquidated to pay the individual s creditors. The proposed legislation would deny this basis for discharge in many cases, requiring instead that individuals make payment out of their future earnings, for as much as seven years. The bills also propose major changes in what debt may be discharged, in the relative amounts paid to secured and unsecured creditors, and in the extent to which documentation must be filed and processed in connection with a bankruptcy case.

We do not take any position on the merits of these bills. However, we strongly believe that these bills are too important and their proposed changes too sweeping to be acted upon without thorough consideration. We are alarmed by how little study appears to have been given to the pending bills. Although we understand that these bills are on the verge of floor consideration, fewer than a dozen hearings have been held on all of the bills combined. The oldest of the bills, H.R. 2500, was introduced little more than six months ago. The haste with which these bills are being processed can be seen by a comparison with the changes made by the Bankruptcy Code of 1978. That legislation was enacted only after sixty days of hearings during a five-year period of consideration.

Without sufficient study and consideration, it is likely that the proposed bills will (1) fail to fully accomplish their intended purpose, (2) generate unnecessary litigation over unclear terms, and (3) impose excessive costs on all of the participants in the bankruptcy system. As those charged with responsibility for applying the bankruptcy laws, we urge that the pending bills be given the full attention that they require, including additional hearings, held after sufficient time has been accorded for thorough study by all interested organizations, legal scholars, and participants in the bankruptcy process.

Respectfully,

The Honorable Louise D. Adler
Southern District of CaliforniaThe Honorable Frank R. Alley
District of OregonThe Honorable J. Vincent Aug
Southern District of OhioThe Honorable Ronald S. Barliant
Northern District of IllinoisThe Honorable Redfield T. Baum
District of ArizonaThe Honorable Joyce Bihary
Northern District of GeorgiaThe Honorable William T. Bodoh
Northern District of OhioThe Honorable Richard L. Bohanon
Western District of OklahomaThe Honorable Henry J. Boroff
District of MassachusettsThe Honorable Peter W. Bowie
Southern District of CaliforniaThe Honorable Philip H. Brandt
Western District of WashingtonThe Honorable Jerry A. Brown
Eastern District of LouisianaThe Honorable Samuel L. Bufford
Central District of CaliforniaThe Honorable Charles M. Caldwell
Southern District of OhioThe Honorable Donald E. Calhoun
Southern District of OhioThe Honorable Ellen Carroll
Central District of CaliforniaThe Honorable Catherine Carruthers
Middle District of North CarolinaThe Honorable Charles G. Case
District of ArizonaThe Honorable Leif M. Clark
Western District of TexasThe Honorable Tom R. Cornish
Eastern District of OklahomaThe Honorable A. Jay Cristol
Southern District of FloridaThe Honorable Sarah Sharer Curley
District of ArizonaThe Honorable Sara E. deJesus
District of Puerto RicoThe Honorable Henry H. Dickinson
Western District of KentuckyThe Honorable Russell A. Eisenberg
Eastern District of WisconsinThe Honorable Joan N. Feeney
District of MassachusettsThe Honorable Jerome Feller
Eastern District of New YorkThe Honorable Lisa Hill Fenning
Central District of CaliforniaThe Honorable Gerald D. Fines
Central District of IllinoisThe Honorable Judith K. Fitzgerald
Western District of PennsylvaniaThe Honorable John T. Flannagan
District of KansasThe Honorable Steven H. Friedman
Southern District of FloridaThe Honorable Robert F. Fussell
Eastern and Western District of ArkansasThe Honorable Stephen D. Gerling
Northern District of New YorkThe Honorable William H. Gindin
District of New JerseyThe Honorable James A. Goodman

Lisa_Fenning @ ce9.uscourts.gov
04/13/99 03:23:55 PM

Record Type: Record

To: Nicole R. Rabner/WHO/EOP

cc:
Subject: Re[2]:meeting in April

Nicole --

I have been swamped here, and have not written up the business issues. Let me just give you a brief notes on a couple of points.

1. Patent and copyright problems:

The Ninth Circuit recently held that a nonexclusive patent license agreement cannot be assumed by a debtor in possession. In re Catapult, 165 F.3d 747 (9th Cir. 1999). The logic of its reasoning probably applies to copyrights also, though that is not yet the subject of any case law. Inability to assume such contracts, even where the license was fully paid for by the debtor before the bankruptcy, may effectively prevent reorganization in Chapter 11. The issue is the scope of the exception to assumability that has traditionally be interpreted to apply to personal services agreements. Catapult builds on several recent cases in extending this principle to restrict the ability of a debtor to assume executory contracts relating to intellectual property, especially license agreements. This issue has extremely broad ramifications for computer software licenses, patent licenses, etc. I will bring you some materials related to these issues.

2. Partnership bankruptcies.

Partnership issues are not fully addressed in Chapter 11. This defect has been obvious for a long time. A consortium of ABA and National Bankruptcy Conference representatives have developed a set of thoroughly analyzed proposals to address the current deficiencies in the Code. The partnership package was endorsed by the National Bankruptcy Review Commission, and has been included in some of the bills introduced in Congress. Increasingly, partnerships and joint ventures are major vehicles for business enterprises. The next wave of bankruptcies will undoubtedly include many such entities. The Administration should insist that this relatively noncontroversial package be included in any reform bill.

3. International bankruptcies.

International bankruptcies have also been inadequately addressed in the Code. Again, a thoroughly vetted set of proposed amendments have already been developed, and were included in some of the bills last session. These provisions are crucial. I have handled many Chapter 11 cases with parallel proceedings pending in other countries. It will be increasingly common in the future. The US should lead on this issue, not trail other developed countries. THe Administration should insist that this noncontroversial package be included in any reform bill.

4. Tax issues.

The Administration should consider supporting the set of tax proposals adopted by the special tax "blue ribbon" committee organized by the National Bankruptcy Review Commission. While I recognize that DOJ does not like some of the proposals (I disagree with some also), the set as a whole improves that balance and functioning of the Code significantly. Representatives from DOJ participated in the tax group, and although they obviously were not there in their official capacities and could not bind the department, they supported the resulting set.

Please let me know today if possible, or tomorrow morning, if a meeting can be arranged. I will be leaving my office tomorrow (Wed.) around 2:30 p.m., and will arrive in DC around midnight.

I look forward to seeing you -- and hopefully the First Lady.

__________________Reply Separator__________________
Subject: Re:meeting in April
Author: Nicole_R._Rabner@who.eop.gov
Date: 3/25/99 7:41 PM

I look forward to meeting with you, and will get back in touch with a
proposed date and time once I have a better sense of the First Lady's
schedule (for your convenience, I'd rather schedule the meetings around
her, so you don't have to come here more than once).

Would you mind sending some material to me about the business bankruptcy
issues that you noted in your last e-mail? This way, I can

make sure that
we have done our homework and that the appropriate
Admininstration
officials are with us. You can feel free to send by e-mail,
fax
(202-456-2878) or mail (2nd floor, West Wing, The White House,
Washington,
D.C. 20502). Thanks.

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image moved Lisa_Fenning @ ce9.uscourts.gov
to file: 03/25/99 12:25:38 PM
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Record Type: Record

To: Nicole R. Rabner/WHO/EOP

cc:
Subject: Re:meeting in April

Thanks for your message. I am scheduled to arrive late at
night on
Wednesday, April 14, and will be staying at the JW
Marriott Hotel. I
have meetings scheduled for Thursday mid-afternoon, but am
otherwise
available to meet with you at your convenience on Thursday
morning or
Friday.
As you know, I think that the bankruptcy laws would
benefit from
reform in a number of areas, including anti-fraud measures
endorsed by
my court. Since last year, however, I have become
increasingly
concerned about recent trends in case law at the appellate
level that
are likely to severely impact businesses in the next wave
of

bankruptcy filings, particularly those involving
technology companies.
I would hope to discuss those issues as well.
I look forward to seeing you again, and would be delighted
to see the
First Lady too, if her schedule permits.
__________________Reply Separator__________________
Subject: meeting in April
Author: Nicole_R._Rabner@who.eop.gov
Date: 3/24/99 8:02 PM

Mrs. Clinton forwarded to me your recent letter, in
which you
note that you
are planning a trip to Washington in mid April. She
suggested
that you and
I meet to discuss the rapid activity on bankruptcy
reform and
hopes to see
you herself, as well. Please let me know as your plans
unfold,
and I'll
continue to monitor her *hectic* schedule, as well.
I look forward to seeing you again.
Nicole

(See attached file: PIC18881.PCX)

- PIC18881.PCX

What Do Bankruptcies

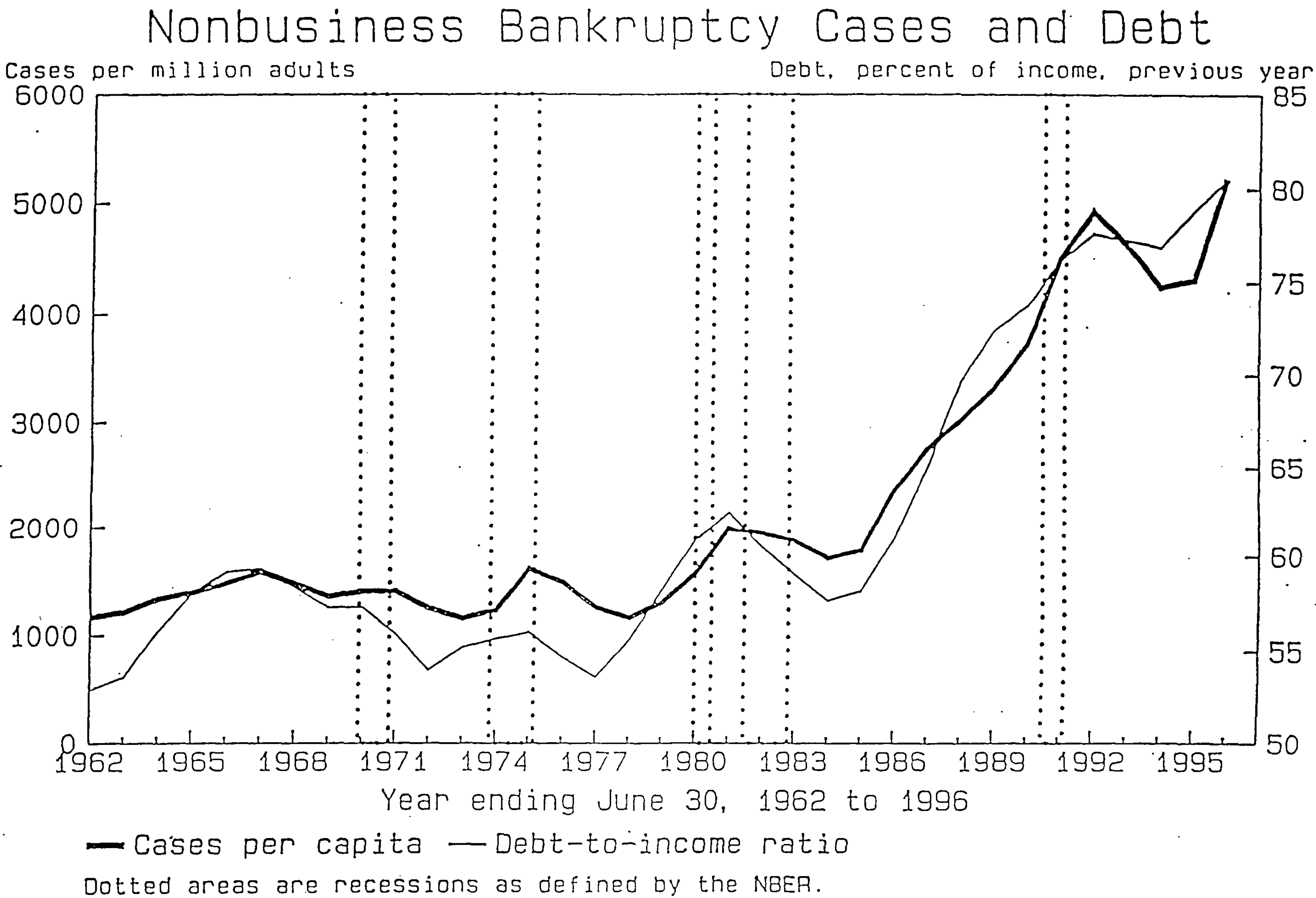
ost American Families?

$400! That's what every American household will pay in higher prices and higher interest rates this year because of personal bankruptcies.

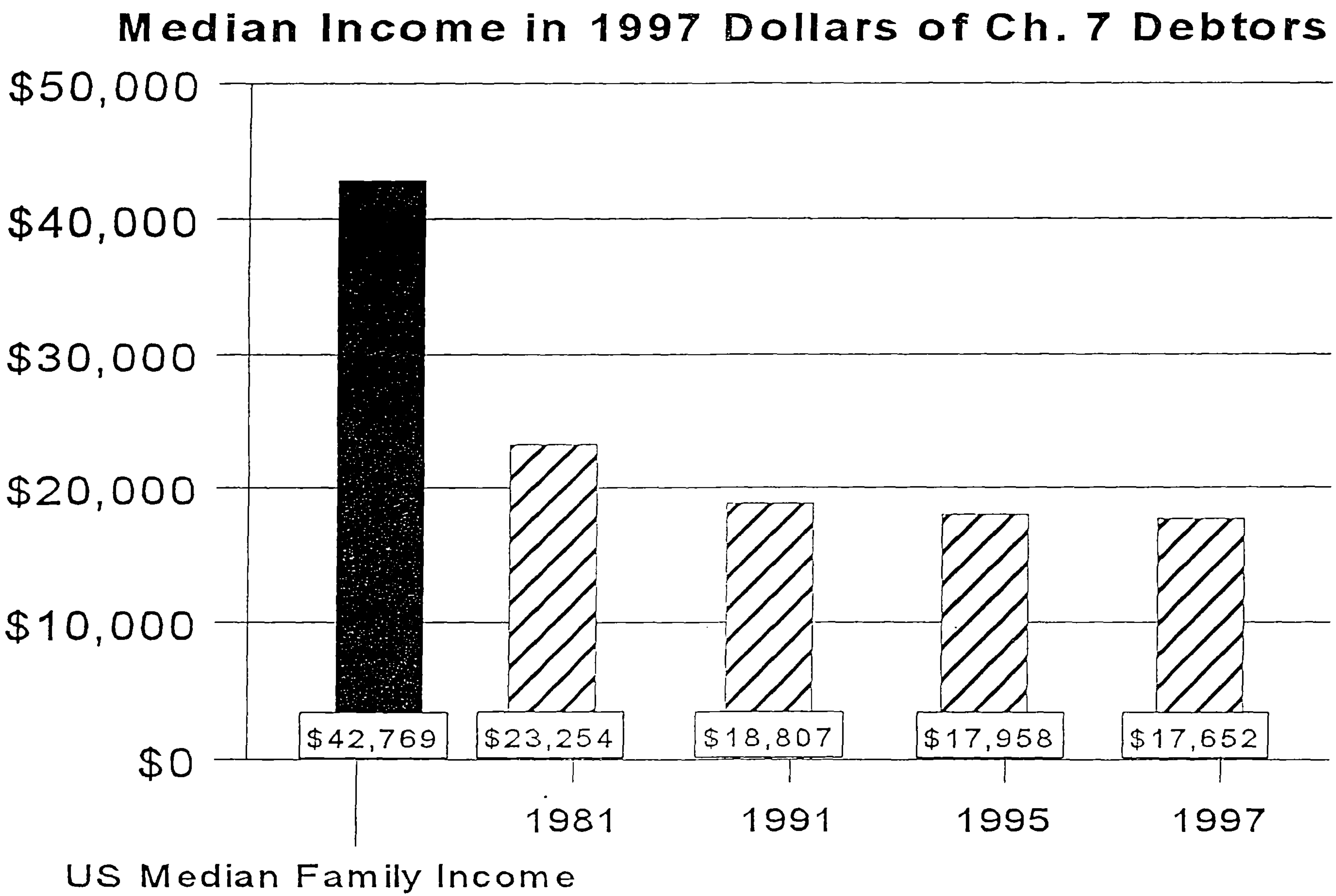
Last year, a record 1.3 million Americans declared personal bankruptcy, erasing more than $40 billion in debt. But not everyone who obtained bankruptcy relief actually needed it. Thirty-three percent had the ability to repay a significant portion of what they owed. Ten percent could pay back everything. Yet our bankruptcy laws make it possible for them to avoid paying their bills. Bankruptcy laws should protect those who legitimately need financial relief, but require those who can pay back their debts to do so. It's time to end the financial burden that bankruptcies place on America's families. Call your member of Congress and voice your support for H.R. 3150.

To learn more, visit www.digitalrelease.com and enter "bankruptcy" in the search engine.

American Bankers Association • American Financial Services Association
America's Community Bankers • Bankruptcy Issues Council • Consumer Bankers Association
Credit Union National Association • Independent Bankers Association of America
National Retail Federation • U.S. Chamber of Commerce

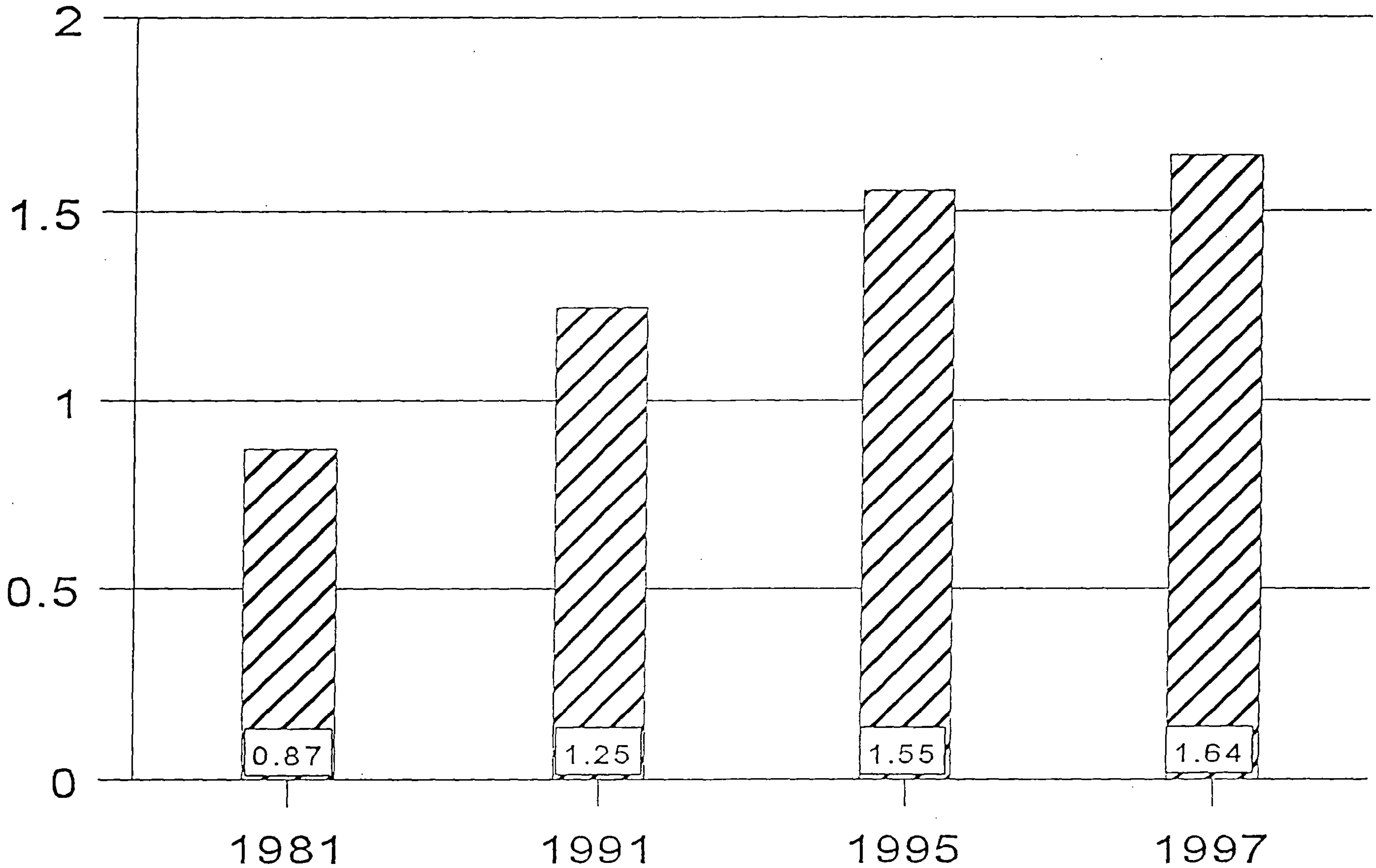


Source: Kim Kowalewski, Congressional Budget Office



Source: Data to be published in Elizabeth Warren, "The Bankruptcy Crisis", Indiana Law Journal (forthcoming Spring 1998)

Median Nonmortgage Debt-to-Income Ratios for Ch. 7 Debtors



Source: Data to be published in Elizabeth Warren, "The Bankruptcy Crisis", Indiana Law Journal, (forthcoming Spring 1998)

Consumer Federation of America

"NEEDS-BASED BANKRUPTCY" IS A CAMPAIGN MANUFACTURED AND PAID FOR BY THE CREDIT CARD INDUSTRY IN AN ATTEMPT TO MAKE THE BANKRUPTCY SYSTEM THE SCAPEGOAT FOR THE INDUSTRY'S RISKY AND PREDATORY LENDING PRACTICES-- AT THE SAME TIME, CREDIT CARDS HAVE BEEN A VERY PROFITABLE LINE OF BUSINESS.

CREDIT CARD DEBT PRESENTS SERIOUS RISK FOR MANY HOUSEHOLDS
As of late 1997:
*$1.6T in credit lines approved--about $20K for each household with at least one credit card
*$450B in revolving debt--double what it was in 1990--is carried by 55-60M households that revolve debt
*the average debt per "revolving" household is $7000, and those households paid more than $1000 in interest and fees during the past year

*lower middle income households are especially burdened by credit card debt--their consumer debt-to-income ratios are far higher than those of other income groups
*based on research numbers generated by Georgetown's Credit Research Center, Chapter 7 bankrupts studied in 1996 had after-tax incomes averaging $19,800 and credit card debts averaging $17,544

*In June 1997, the Opinion Research Corp. asked, on behalf of CFA, a sample of 1006 persons:"How concerned are you about meeting your credit card monthly payments?" 36% of all households said "very concerned" and among lower income households [$15-25,000] that number was 42%

[See "Expanding Credit Card Debt: The Role of Creditors and the Impact on Consumers, CFA, December 16, 1997]

*Under the facade of "democratization of credit"; credit card companies have preyed upon low income persons. "What the poor do not understand, and what helps keep them poor, is that credit cards and other forms of consumer credit do not provide additional income but rather place a mortgage-an expensive one- on future income". [Easy Credit: A Wall Around the Poor", The New York Times, February, 1998]

*This behavior was also noted in the Wall Street Journal in an article describing new marketing plans aimed at wealthy consumers. "After years of earning fat profits from the least creditworthy customers-those who rack up big debts and pay them off over long periods at steep interest rates-MasterCard International and Visa U.S.A. are going after the nation's affluent". [Burned by the Masses, Cards Court the Elite, WSJ 11/5/97]

CREDIT CARD COMPANIES CONTINUED TO AGGRESSIVELY MARKET, DESPITE WARNINGS OF RISK AND RISING CHARGE-OFF RATES

*In September 1996, the Office of the Comptroller of the Currency issued an Advisory Letter to alert national banks to risks associated with preapproved solicitations of credit cards". The OCC encouraged management to "take appropriate action to limit its exposure to unwarranted risks". [OCC Advisory Letter 9/25/96]

*During the first half of 1997, credit card solicitations were at a record level; the second quarter mailing of 881M was the highest on record [CFA, 12/16/97]
*From 1995 to 1996, credit card telemarketing expenses rose 30% [CFA 12/16/97]
*From 1995 to 1996, credit card ad expense rose 14% [CFA 12/16/97]

*Credit card lenders "shot themselves in the foot by using some of the weakest and most pitiful loan underwriting techniques [he had] ever witnessed," according to a securities analyst in testimony to the House Banking and Financial Services Committee in the fall of 1996 [Over the Edge, National Journal, 5/3/97]

*"'The Principal factor in the increase in bankruptcies has been the dramatic lowering of loan standards throughout the recent five years,' said Mark Zandi, chief economist for the Pennsylvania-based Regional Financial Associates, a consulting firm with credit-card companies as clients...Zandi sees the Gekas bill as adding fuel to the crisis. 'What it will do is induce the lenders to lower their standards even further,' he said." [Congress might make debt harder to escape, The Boston Globe, March 10, 1998]

THE PROFITABILITY OF CREDIT CARDS HAS BEEN HIGH & NOW THAT LENDERS ARE EXPERIENCING SOME DECLINE, THEY ARE BECOMING MORE AGGRESSIVE IN COLLECTIONS AND IMPOSING PENALTIES

*Credit card banks [defined as those which engage primarily in consumer lending; more than 90% of their loans involve credit cards] attain a return on assets that is double the return on assets of commercial banks [Credit Card Charge-Offs, Subprime Lending and High-LTV Loans, Beverly Burden, 1998]

*The difference between the roughly 14-16% yield on credit cards and the 3-5% cost of funds is much larger than that on other kinds of consumer credit [The Consumer Impacts of Expanding Credit Card Debt, CFA, February 1997]

*Banks are also able to securitize and sell credit card debt and may now receive more favorable tax treatment [Burden]

*But, the present rate of charge-offs, about 5%, is the highest rate recorded [CFA 2/97, Burden]
And profit levels on credit cards have fallen [CFA, Burden, WSJ 11/5/97]

*According to an industry researcher, the cost of credit has been rising in 1997. Average interest rates and charges have risen and issuers have become less tolerant when it comes to late payments and exceeding credit limits. Some banks are also for the first time imposing punitive interest rates on top of the penalty charges, rates that can last for a year or more before returning to standard level [Now, Time to Dig Out From 1997 Debt, Wall Street Journal ½/98]

*Credit card companies are also imposing fees, or reserving the right to, on customers who don't use their account for a while, pay off the monthly balance or close the account [Are New Fees for Canceling an Account in the Cards? WSJ, 6/11/97]

*There are about 6,000 collection agencies nationally. Bad debt placed with agencies rose 39% to $117B in 1995 from $84B in 1994. During that period debt collected by agencies rose 40% to $31B [As Many People Sink Into Debt, One Group Prospers, WSJ 11/20/97]

National Consumer Law Center Inc.

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Boston, MA 02108
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(202) 986-6060

April 23, 1998

SUMMARY CRITIQUE OF S. 1301: A BILL WHICH WOULD DEVASTATE AMERICA'S CONSUMER BANKRUPTCY SYSTEM

In 1997, more than 1.3 million American families turned to the consumer bankruptcy system for help in managing overwhelming financial problems including foreclosure, repossession, utility termination, wage garnishment and debt collection harassment. The vast majority of these debtors were low-income working class American families earning less than $50,000 per year.

American families file bankruptcy out of necessity. The typical bankruptcy debtor is facing income reductions due to transition to a lower paying job, illness, death of a breadwinner, loss of overtime, divorce, or retirement. As credit card debt has doubled in five years, more families carry more debt, without a corresponding increase in income. Uninsured medical expenses, doubling of the average student loan debt burden, and a tripling of home equity credit compound the problem.

Carefully crafted legislation to reform the bankruptcy laws is necessary to avoid penalizing the many American families who legitimately need help. Most debtors in the bankruptcy system are struggling with massive credit card debts which carry interest rates ranging from 16 to 20%. It is irresponsible for the banks that have earned record profits by encouraging families to borrow at high rates to place full blame on consumers for the rise in bankruptcies.

S. 1301 is unbalanced Senate legislation which was voted out of subcommittee in haste on April 2, 1998. It contains numerous pitfalls for American consumers without a corresponding effort to reign in irresponsible practices of lenders. The bill would:

- Create new eligibility barriers, filing requirements and procedural hurdles which would be expensive for debtors to meet. These new impediments would preclude effective debt relief for those at the bottom of the economic spectrum. If S. 1301 is passed, many working class families will be too poor to afford bankruptcy.

• Increase the cost of the bankruptcy system to taxpayers by generating hundreds of thousands of new litigated disputes in bankruptcy each year. These would require new Judges trustees and courtroom personnel.

• Institutionalize unresolvable conflicts of interest between lawyers and their clients by creating automatic personal liability for lawyers who represent debtors in cases which fail.

• Encourage fraudulent debt counseling operations by giving government imprimatur to any counseling organization without oversight and review.

• Allow creditors to take children's toys, VCR's and heirlooms of minimal value by changing the longstanding definition of household goods. These items have no economic value to creditors because they cannot be cost-effectively resold. However, they have high replacement cost or sentimental value to debtors.

• Encourage continued reckless lending practices and abusive lawsuits by allowing creditors to claim fraud against borrowers without having to prove it.

• Undermine debtors' attempts to save their homes from foreclosure by redirecting money to legal fees and credit card debts which could otherwise be used to get caught get up on mortgage payments.

• Eliminate the right of many debtors to use the bankruptcy system to pay back rent and prevent eviction. The bill will increase homelessness with corresponding social costs.

• Invade the privacy of American families and facilitate theft of identity fraud by making debtor's tax returns publicly available.

• Punish debtors who make mistakes in filing their voluminous bankruptcy papers by eliminating existing mechanisms to correct errors and by denying debtors a fair opportunity to refile.

• Undermine collection of child support and alimony by redirecting income to a debtor's less urgent debts.

S. 1301 is radical anti-consumer legislation. Both the UAW and the AFL-CIO have expressed concern about the impact of this bill on American consumers and have urged the Senate to come up with more balanced proposals. Bankruptcy Judges and law professors have encouraged Congress to slow down, because the existing proposals are not well thought out. Passage of the bill in it current form would be disastrous to American families who are mired in the quicksand of overwhelming debt.

A more complete critique of S.1301 is available from the National Consumer Law Center, the Consumer Federation of America, or the National Association of Consumer Bankruptcy Attorneys.

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CRITIQUE OF S.1301
"CONSUMER BANKRUPTCY REFORM ACT OF 1998"

A BILL THAT WOULD DEVASTATE AMERICA'S CONSUMER BANKRUPTCY SYSTEM

S. 1301 would undermine the effective and efficient operation of the existing consumer bankruptcy system. The bill would raise the cost of bankruptcy for all debtors and require that taxpayers fund an expanded bureaucracy to collect small amounts of money from families facing overwhelming financial problems.[1] If it is passed, a significant American judicial system would be undermined in order to provide a marginal enhancement to the already record-breaking profit margins of banks and other lenders.

Raising the costs and burdens of bankruptcy ultimately hurts the poorest debtors -- those that can't afford to pay a lawyer to navigate complicated new legal hurdles -- rather than the high-income debtors who some believe commit abuses. More narrowly targeted provisions can be drafted to get at the perceived abuses without hurting the financially strapped American families who urgently need debt relief to avoid financial catastrophe.

S. 1301 was voted out of subcommittee on April 2, 1998 in great haste. The subcommittee added numerous amendments which had never been addressed at a hearing. Several of these amendments would cause the bankruptcy system to grind to a virtual halt and cause great additional hardship to families already suffering under the burdens of

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[1] There are numerous provisions of the bill which would be impracticable or which would create creditor bankruptcy abuses. Because the bill is extensive, only the most important problems are discussed here. Another critique of this bill is available on the American Bankruptcy Institute website: www.abiworld.org. That critique is particularly thorough in its discussion of how these amendments would undermine effective administration of our nation's bankruptcy laws.

overwhelming financial problems. Further study is needed before such radical new provisions are adopted in a large-scale judicial system affecting millions of American families.

I. NEEDS BASED BANKRUPTCY (TITLE I)

These provisions would establish new hurdles for consumers seeking bankruptcy relief by forcing them to meet an arbitrary test concerning ability to repay. Any consumer's filing under chapter 7 could be challenged by any creditor who believed that consumer could pay more than 20% of his or her debts in five years without interest. The provision would also create personal liability for bankruptcy lawyers who zealously represent their clients, if a client's case is dismissed after court review.

PROBLEMS WITH THESE PROVISIONS:

- **The bill does not protect consumers who have no ability to pay their creditors.** The bill would allow creditors to file litigation concerning a debtor's eligibility for bankruptcy against debtors of extremely limited financial means. Even unfounded motions would serve as leverage for creditors, because low-income debtors are least able to pay an attorney to represent them in this potentially complex litigation.

- **A bright line 20% repayment capacity test to establish ability to pay will reward debtors who run up more debt or who reduce their income.**

- **The bill would create irremediable conflicts of interest between attorneys and their clients.** Attorneys' exposure to potential liability will prevent them from taking on meritorious cases. Attorneys should never have personal liability simply because their client's cases are politically unpopular.

- **The bill would create a substantial federal bureaucracy to collect money for creditors even though there is no evidence that the new expenditures would capture significant new funds for creditors.** Evidence shows that better off debtors are already choosing to enter repayment plans in chapter 13 or chapter 11 voluntarily. Creditors' evidence purporting to show substantial ability to repay in chapter 7 has been discredited by the General Accounting Office and the Congressional Budget Office. It makes little sense to force people into repayment plans which are likely to raise less than four cents per dollar per year for creditors at an estimated cost of ten cents per dollar per year for taxpayers.

• Two thirds of repayment plan cases already fail. Involuntary plans based on unrealistic expectations concerning future income would fail at an even higher rate.

HOW TO FIX THE PROBLEMS:

• Include an effective "safe harbor" which would preclude unwarranted attacks on debtor's eligibility if the debtor has less than average income. These debtors are highly unlikely to have income available to make significant payments to creditors and they should be protected from the leverage created by an attack which forces them to spend money on a legal defense. The "safe harbor" provision currently in the bill is insufficient to do the job.

• Provide an effective fee shifting provision for all other creditor motions. Creditors with small claims cannot be excepted from fee shifting since most chapter 7 creditors do not file proofs of claim at all. Moreover, raising a motion based on a small claim can create inappropriate leverage against a debtor who would have to pay more to an attorney to defend than the total amount of the creditor's claim.

• Provide some discretion to Judges to determine when a debtor is abusing the system. Any bright line test is subject to abuse by those who would manipulate the system by incurring more prebankruptcy debt or by reducing their ability to pay.

• Delete the provision for attorney's personal liability for handling cases.

II. ENHANCED PROCEDURAL PROTECTION FOR CONSUMERS (TITLE II)

Consumers need effective remedies against creditors that violate their obligations in the bankruptcy system. The hundreds of thousands of debtors who were hurt by the recent bankruptcy related misconduct of Sears and other retailers were inadequately protected until the Federal Trade Commission, the Attorneys General and others stepped in. In the original version of S. 1301, enhanced protections for consumers were effective and enforceable. These provisions were watered down in the subcommittee mark-up at the insistence of creditors who would prefer not to be held accountable when they violate the Bankruptcy Code. The original version of these provisions should be restored.

III. NOTICE OF ALTERNATIVES AND NEW FILING REQUIREMENTS (Section 301)

This section would give government imprimatur to credit counseling agencies that register with the court. It would also substantially expand filing requirements for debtors, beyond the existing twenty pages of certified official forms. Of particular concern, debtors would be required to make many years of tax returns available as part of the public record.

PROBLEMS WITH THESE PROVISIONS:

• **Although not all credit counseling agencies are fraudulent, there are numerous fly by night operations which charge debtors substantial sums of money for very little service.** For example, a court found in Fleet vs. United States Consumer Council[2] that the fee charged to hundreds of consumers by a credit counseling organization was "an unconscionable price and a fraud". The bill does not provide oversight funding or a mechanism to prevent unqualified organizations from registering with the court. Nevertheless, the court will have no choice other than to recommend all registering agencies to consumer in financial trouble. (N.B. Another provision of the bill, added by a split vote of the subcommittee, would actually require that consumers use credit counseling programs prior to filing bankruptcy. This provision would dissipate a debtor's scarce resources, further encourage fraud, and prevent many debtors from filing when they need emergency relief. It is discussed in more detail below.)

• **Additional filing requirements are traps for the unwary.** If bankruptcy needs to be filed on an emergency basis, necessary information is unlikely to be quickly available. The IRS takes approximately six months, for example, to provide copies of tax returns. If a debtor is missing even one document, the bill provides that the case must be dismissed (sec. 312). That debtor would then have to litigate their right to get bankruptcy relief when the missing document is secured. (sec. 303).

• **Bankruptcy courts have no room to store the millions of new documents which would have to be filed if this provision becomes law.**

• **Tax returns filed by the debtor would become part of the public record -- available for inspection by any member of the public. This would invade the privacy of the many American families who legitimately need bankruptcy and would facilitate theft of identity fraud.** Theft of identity is a common crime which is conducted, often by organized rings, to obtain fraudulent credit or public benefits, and as a cover for illegal immigration.

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[2] 95 B.R. 334 (E.D.Pa 1989).

HOW TO FIX THE PROBLEMS:

- The bankruptcy system can develop a form which describes alternatives to bankruptcy without providing specific names of service providers. The court should no more be in the business of recommending particular credit counselors than it would be willing to recommend particular attorneys.

- Allow trustees to obtain additional documentation when further investigation of a debtor's circumstances in warranted. Continue to allow creditors to initiate a process to investigate the debtor by holding an examination pursuant to Bankruptcy Rule 2004.

- Allow trustees to request tax returns in any case upon a reasonable suspicion of fraud without making the returns a part of the public record. This would serve as a necessary filter to prevent unwarranted documentation requirements affecting all debtors, but nevertheless allow fraudulent filers to be caught.

IV. DISCOURAGING REPEAT FILINGS (Section 303)

The section eliminates the automatic stay after 30 days whenever a debtor has had a case dismissed and refiles within the following one-year period. The debtor would have to bring an immediate motion to obtain an additional stay, at considerable additional expense.

PROBLEMS WITH THESE PROVISIONS:

- **Many bankruptcy debtors file a second bankruptcy case after their first case fails for entirely legitimate reasons.** The most common reason for refiling is that a debtor, generally unrepresented, inadvertently fails to meet one of the complicated filing requirements of the Bankruptcy Code. The second case becomes necessary to fix the problem. The next most common reason is a legitimate change in circumstances which would allow debtors to complete a chapter 13 plan and pay their creditors. If S. 1301 is passed, these debtors would be required to incur substantial litigation costs in the second case even if they did not do anything wrong in the first case. These litigation expenses would take money away from what is available to pay creditors.

- **The bill would create a common new type of emergency motion to be resolved within 30 days by already overburdened courts.**

- **This provision would work in concert with new provisions requiring dismissals of cases for technical reasons.** If a case is dismissed for technical reasons under section 312, debtors without resources to pay for litigation, i.e. the poorest debtors, could not get back into court.

HOW TO FIX THE PROBLEMS:

The American Bankruptcy Institute and National Bankruptcy Review Commission have recommended limits on refilings which prevent abusive refilings without precluding legitimate cases. These provisions would make it hard for debtors to refile when their goal is to hinder creditors, but allow refiling when the goal is to pay creditors.

V. LIMITATIONS ON THE CODEBTOR STAY (SECTION 305)

The codebtor stay applies only in chapter 13 (11 U.S.C. § 1301). If a consumer files bankruptcy and proposes to pay a creditor, this stay prohibits the creditor from pursuing a codebtor who is not in bankruptcy -- to the extent the debt will be paid in the bankruptcy process. S.1301 would allow creditors to ignore the stay if they believe that the debtor did not receive consideration upon incurring the debt or if the property securing the debt is not in the possession of the debtor.

Thus, for example if a husband-debtor is separated from his non-debtor wife, **a creditor could simply repossess a car from the wife even though the husband was making payments on the car in chapter 13**. The current statute properly places such decisions in the hands of the court, not creditors, and should not be changed.

VI. AUDIT PROCEDURES (SECTION 307)

This provision gives power to the Attorney General to establish audit procedures to verify information given by bankruptcy debtors. One audit in every 50 cases will be required.

PROBLEMS WITH THESE PROVISIONS:

- **This provision is unnecessary. The United States trustee already has the power and responsibility to audit cases.** By adding the costs of paying accountants to perform these audits, the creditors are again seeking to drive up the costs of bankruptcy paid by debtors and taxpayers.

- **One audit in 50 cases will require more than 25,000 audits in the bankruptcy system.** Even the IRS, which has responsibility to the public fisc, audits less than one case in one thousand.

• **Large numbers of audits would drive up the costs of bankruptcy for all debtors.** Since audits would require significant attorney time, bankruptcy attorneys would need to raise fees to cover the cost of a potential audit. Since debtors to be audited are unlikely to be able to afford additional attorney fees at the time of the audit, attorneys are likely to raise their fees generally and spread the risk of new costs. This would drive up the cost of bankruptcy and make it unaffordable for additional low and moderate income debtors.

HOW TO FIX THE PROBLEMS:

Rewrite the provision for audits to make them available as an additional tool for trustees and the United States trustee. Create a provision which would require audits in a limited number of cases based on reasonable suspicion that the debtor is engaged in fraud upon creditors.

VII. NOTICE TO CREDITORS (Section 309).

This provision would strike the language in the Bankruptcy Code (11 U.S.C. § 342(c)) which currently protects a debtor for minor deficiencies in notices to creditors which do not effect the ability of a creditor to understand its rights. Creditors would be allowed to ignore notices they receive which are not sent to a preferred address. (Most often the only address information in the possession of a debtor is the address on the billing statement.)

This amendment thus provides opportunities to creditors to claim that their debts were not discharged, and to violate the automatic stay with impunity, based upon minor irregularities in giving notice of the bankruptcy, even if the creditor received actual notice.

A better solution would be to require creditors that want notice sent to a particular address to provide that information to a central registry which would be available, perhaps on the internet, to all debtors and their lawyers. However, creditors like any other participant in an American legal system, should not be allowed to avoid responsibility for transmitting information through internal processes. Creditors must take responsibility so that notice which is actually delivered is redirected intraoffice to the appropriate personnel.

VIII. DISMISSALS FOR FAILING TO MEET TECHNICAL FILING REQUIREMENTS (Section 312)

This section would provide for automatic dismissal for failure to file required documents, including many which the debtor would not be able to obtain quickly as described above (Sec. 301). This provision would work in tandem with section 303 of the bill which would eliminate the automatic stay if the debtor then attempted to refile because of the presumption that such a dismissal is always in bad faith.

Judicial discretion on this issue, as under current law, is necessary to prevent hardship. The amendment, other than giving debtors the right to request an additional 20 days to file documents, eliminates all judicial discretion.

IX. DEBTS INCURRED TO PAY NONDISCHARGEABLE DEBTS (Section 316)

This section would give a creditor the right to claim that its debt is a priority debt or a nondischargeable debt if its debt was incurred to pay a priority or nondischargeable debt.

Many credit card lenders will use this provision to argue that because the debtor incurred debt from that lender, the debtor had other funds available to pay child support, taxes, or other types of non-dischargeable debts. Extensive litigation will undoubtedly be necessary to trace borrowed funds. This litigation would give enormous leverage to creditors since bankruptcy debtors are typically poor and cannot fund litigation costs in the bankruptcy process. Many default judgements would result.

This provision should be deleted from the bill.

X. RESTRICTIVE DEFINITION OF HOUSEHOLD GOODS (Section 318)

This proposed amendment revives the creditors' attempts to import the restrictive Federal Trade Commission definition of household goods into the Bankruptcy Code. Current law already protects creditors by limiting a debtors exemption in any particular household good to $400 (11 U.S.C. § 523(d)(3)). Valuable household goods are thus already available to creditors.

This provision would allow creditors to threaten repossession of items that have *minimal resale value*, but high sentimental or replacement value to the debtor. **Based on the FTC definition, creditors in the past have claimed the right to repossess children's swing sets, lawn mowers, children's toys, sleeping bags, family heirlooms worth less than $400, and other similar items.** Because there is no market for profitable resale of these items, the right to threaten repossession is the only value which these items have to the creditor -- the value of this threat should not be institutionalized as federal policy. These claims have been repeatedly rejected by Congress and the courts in the past.

The context of the FTC rule is important. The FTC rule applies whether or not a debtor is having financial problems. Bankruptcy debtors, almost by definition, are in default and unlikely to be able to afford substitute property. The leverage associated with a threat of repossession thus goes up substantially.

Because the FTC definition of household good is so restrictive, there has been substantial litigation over many years concerning what property qualifies for exemption under the rules. There are many open issues. All of this litigation would be imported into the bankruptcy process in place of the present plain language definition adopted by the Courts.

This provision should be deleted from the bill.

ADDITIONAL AMENDMENTS MADE IN THE SUBCOMMITTEE

A. CAP ON HOMESTEADS

This provision would limit homestead exemption in all states to $100,000. This provision restricts states right to protect their citizens as they see fit with safeguards for their homes.

A provision in the bill to provide additional protections for family farms would not work as intended. The residence of the farmer would be protected, but not the farmland.

A better and more expansive provision would preclude transfers of property into any exemptible form if the transfer exceeds $100,000. See H.R. 3146, section 7 (1997). This provision would preclude debtors from moving to a state solely to claim an unlimited homestead. It would also protect against debtors transferring substantial property into exemption pension funds. In addition, any ceiling on state exemptions should be balanced by a modest state floor.

B. PROVISION REQURING PRE-BANKRUPTCY DEBT REPAYMENT PLANS

This provision overlaps and conflicts with section 301. It requires all debtors to make a good faith pre-bankruptcy attempt to create a debt repayment plan through approved credit counseling program.

PROBLEMS WITH THESE PROVISIONS:

- **The bill provides no funds or procedures for courts or trustees to investigate credit counseling organizations, their fees, or the success rate of the plans they set up.** As discussed above (section 301), the availability of fees for credit counseling business will induce fraudulent operations to claim to provide these services.

- **Debtors will be forced to use funds which might be available to pay creditors on unsuccessful credit counseling plans.**

- **Existing credit counseling organizations are swamped with customers.** CCCS alone received more than two million requests for assistance in 1997. Requests for this assistance has increased far faster than bankruptcy filings. Consumers may have to wait more than a month for an appointment.

• **Some debtors have emergency problems, such as utility shut-off, which prevent them from taking advantage of credit counseling.**

• **One obstinate creditor can prevent a credit counseling plan from going forward.** If a family has six creditors, five may agree to the plan but the sixth one will not. If bankruptcy is necessary to deal with the sixth creditor, the other five can use this provision to litigate the consumer's eligibility for bankruptcy even if the consumer was not at fault.

• **Hundreds of thousands of disputes about the debtor's good faith will flood the courts. Complicated trials will be necessary.** Credit counselor testimony concerning the extent of the debtor's efforts to arrange a repayment agreement will be necessary at these hearings. This testimony will take away from counselors' ability to do their jobs.

HOW TO FIX THE PROBLEMS:

This provision should be deleted from the bill. As discussed above under section 301, the bankruptcy system can provide better educational materials and programs for debtors including information on alternatives to bankruptcy.

C. EVISCERATION OF THE AUTOMATIC STAY FOR TENANTS

This provision would allow landlords to continue eviction proceedings against their tenants when they file bankruptcy without regard to the automatic stay.

PROBLEMS WITH THIS PROVISION:

• **Debtors cannot make their best efforts to participate in the bankruptcy process, if immediately after they file, they lose their homes.** Landlords can already proceed against tenants after a brief breathing spell, if the tenant fails to make payments.

• **A significant number of tenants wish to use the bankruptcy process to cure their back rent obligations by full payment.** This provision will contribute to homelessness by preventing debtors from using the bankruptcy system to get caught up on their obligations to their landlords.

• **Upon eviction, those tenants who are not homeless most often have their housing costs go up.** This reduces the money which can be committed to creditors in the bankruptcy system.

HOW TO FIX THE PROBLEMS:

Rewrite the provision so that landlords can obtain expedited relief from stay, if the debtor fails to resume making monthly payments within 30 days.

D. PRESUMING FRAUD FOR CREDIT EXTENSIONS ON THE EVE OF BANKRUPTCY

This provision creates a presumption that any use of credit no matter how necessary or minor, if incurred within 90 days of bankruptcy is fraudulent. The Bankruptcy Code already contains a provision creating a presumption that purchases of luxury items or cash advances or cash advances within 60 days before bankruptcy were fraudulent. 11 U.S.C. § 523(a)(2)(C). This prevents debtors from loading up on luxury goods on the eve of bankruptcy.

PROBLEMS WITH THIS PROVISION:

• **Creditors want to be able to assert fraud against honest debtors who have done nothing wrong.** Fraud is a serious offense. If words are to have any relation to their true meanings, Congress should not so casually classify millions of American consumers as dishonest and fraudulent. Honest people ought not to have their good name and reputation besmirched by having fraud established based on a set of circumstances which have nothing to do with fraud.

• **The credit industry is constantly claiming that consumers commit fraud, but in real life rarely can convince a court that this is true -- generally because the American consumer is, by and large, honest.** The industry has apparently decided to dispense with the nuisance of having to show any fraud by creating a presumption based on the temporal relationship between use of credit and bankruptcy. In the vast majority of cases, the presumption would be false, but debtors would nevertheless have to expend litigation costs to overcome it.

• **The only debtors that would be hurt by such a presumption would be those who were innocent of fraud.** Any debtor who actually did seek to run up debts and then avoid them in bankruptcy would simply wait out the 90 days, or whatever period was necessary. Only those debtors who were compelled to file due to an emergency, or were too unsophisticated to even know about the 90 day rule would be ensnared.

• **The provision would enhance the leverage of creditors who retain a nondischargeable claim.** The poorest debtors would be threatened with draconian collection action on the nondischargeable portion of their claim. Debtors would have little choice other than to agree to pay a larger amount than is legitimately nondischargeable in order to obtain manageable payment terms.

HOW TO FIX THE PROBLEMS:

Delete this provision from the bill. Current law and the presumption of fraud for use of credit for luxury goods are sufficient to prevent dishonesty and protect creditors.

F. DEBTS INCURRED BY FRAUD IN CHAPTER 13

This provision makes debts incurred by fraud nondischargeable in chapter 13.

PROBLEMS WITH THE REVISION:

• **While this proposal has some facial appeal, it is unworkable due to the structure of chapter 13.** As the proliferation of creditor claims of fraud in chapter 7 has shown, fraud litigation is time-intensive and expensive. In chapter 13, all of a debtors income is devoted to payments for necessities or payments to creditors. 11 U.S.C. § 1325(b). A chapter 13 debtor thus has no ability to pay for the litigation necessary to oppose a creditor claim of fraud.

• **Because debtors would have no allowable funds to pay for the litigation, they would typically lose by default. Creditor leverage would go up accordingly, including leverage for unfounded claims.**

• **If the law is changed to create a mechanism to allow debtors to pay attorneys for this work those payments come from available income and would reduce the money available to pay all other creditors.** One creditor could effectively prevent other creditors from being paid.

HOW TO FIX THE PROBLEMS:

Define a very narrow class of fraud claims which would be nondischargeable in chapter 13 in order to prevent the truly dishonest debtor from gaming the system. Marginal claims of fraud based on use of credit within the creditor's extended limits should not be actionable. Provide heavy sanctions for creditors who raise fraud in chapter 13, but cannot prove it. This would help to prevent unfounded claims.

CONCLUSION

The bankruptcy laws are complex. Radical change has the potential to undermine the economy by making the risk of borrowing too great for many American consumers. Banks are continuing to report record profits. There is no reason to take action that jeopardizes the safety net for working class American families.