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An Agricultural Law Research Article

**Are You a Debt Relief Agency? You Might Be Surprised and You Should Be Concerned**

by

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## **Are You a Debt Relief Agency? You Might Be Surprised and You Should Be Concerned**

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The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 was signed into law on April 20, 2005 as Public Law No.109-8.<sup>1</sup> Most provisions of the bill were not immediately effective but rather took effect with respect to cases filed on or after October 17, 2005.<sup>2</sup>

This massive new act makes profound changes in bankruptcy law, some of which are controversial. The requirements regarding “debt relief agencies” provide an example of a particularly controversial change that has generated concern among the bar. The definition of this term by the new act is expansive, and if a person or entity falls within the term, violating the act’s requirements can result in serious consequences.

This article provides an overview of the definition of a debt relief agency and the requirements now in place for such entities. It also discusses challenges to the requirements that have been brought in the courts.

### **Defining the Term**

The Bankruptcy Code, as amended by the new act provides that the term “debt relief agency” means “any person who provides any bankruptcy assistance to an assisted person in return for the payment of money or other valuable consideration, or who is a bankruptcy petition preparer under section 110.”<sup>3</sup>

Specifically excluded from this definition are the following categories of persons and entities:

- (A) any person who is an officer, director, employee, or agent of a person who provides such assistance or of the bankruptcy petition preparer;
- (B) a nonprofit organization that is exempt from taxation under section 501(c)(3) of the Internal Revenue Code of 1986;
- (C) a creditor of such assisted person, to the extent that the creditor is assisting such assisted person to restructure any debt owed by such assisted person to the creditor;
- (D) a depository institution (as defined in section 3 of the Federal Deposit Insurance Act) or any Federal credit union or State credit union (as those terms are defined in section 101 of the

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<sup>1</sup> The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 (codified in scattered sections of 11 U.S.C.).

<sup>2</sup> *Id.* at § 1501, 119 Stat. at 216.

<sup>3</sup> 11 U.S.C. § 101(12A).

Federal Credit Union Act), or any affiliate or subsidiary of such depository institution or credit union; or  
(E) an author, publisher, distributor, or seller of works subject to copyright protection under title 17, when acting in such capacity.

There are three key elements to the definition of a debt relief agency. First, the person must provide “bankruptcy assistance.” Second, this assistance must be provided to an “assisted person.” Third, the assistance must be provided in return for money or other valuable compensation.

The term “bankruptcy assistance” is defined as “any goods or services sold or otherwise provided to an assisted person with the express or implied purpose of providing information, advice, counsel, document preparation, or filing, or attendance at a creditors’ meeting or appearing in a case or proceeding on behalf of another or providing legal representation with respect to a case or proceeding under this title.”<sup>4</sup> Thus, it appears that attorneys could be included in the definition.<sup>5</sup> Moreover, “bankruptcy assistance” is not limited to those who file a bankruptcy case for their client. Providing any information or advice about bankruptcy to an “assisted person” can fall within the scope of this definition.

The term “assisted person” means “any person whose debts consist primarily of consumer debts and the value of whose nonexempt property is less than \$150,000.”<sup>6</sup> “Consumer debt” is “debt incurred by an individual primarily for a personal, family, or household purpose.”<sup>7</sup> It appears that most farm clients will not qualify as assisted persons because of the extent of their business debt. Similarly, a farmer is likely to have more than \$150,000 in nonexempt farm assets, unless the value of nonexempt property is construed to mean equity.

The third requirement limits the definition to those who receive compensation for the information or advice provided. This distinction could be critical for volunteer organizations that work with financially distressed individuals. However, it describes the typical attorney-client relationship.

### **Restrictions on Debt Relief Agencies**

Section 526 of the Bankruptcy Code lists the restrictions imposed on debt relief agencies.<sup>8</sup> These relate to the agency’s duty to the assisted person, and each also applies to any “prospective assisted person.”<sup>9</sup> The restrictions are drafted with detailed and expansive language, e.g., “directly or

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<sup>4</sup> 11 U.S.C. § 101(4A).

<sup>5</sup> See, Erwin Chemerinsky, *Constitutional Issues Posed in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 79 AM. BANKR. L.J. 571, 576 (2005); Keith M. Lundin, *Ten Principles of BAPCPA: Not What was Advertised*, 24 AM. BANKR. INST. J. 1, 69 (Sept.2005); Henry J. Sommer, *Trying to Make Sense Out of Nonsense: Representing Consumers Under the "Bankruptcy Abuse Prevention and Consumer Protection Act of 2005"*, 79 AM. BANKR. L.J. 191, 206-07 (Spring 2005).

<sup>6</sup> 11 U.S.C. § 101(3).

<sup>7</sup> 11 U.S.C. § 101(8).

<sup>8</sup> 11 U.S.C. § 526.

<sup>9</sup> 11 U.S.C. § 526(a).

indirectly, affirmatively or by material omission,”<sup>10</sup> but each can be generally summarized. A debt relief agency must not:

- “fail to perform” any service promised to the assisted person in connection with a bankruptcy proceeding;
- advise the assisted person to make an “untrue and misleading” statement in a document filed in a bankruptcy proceeding;
- make any misrepresentation to an assisted person regarding the services that will be provided or the benefits and risks of filing bankruptcy;
- advise an assisted person to incur more debt in contemplation of filing bankruptcy.<sup>11</sup>

The last of these restrictions raises concern. It is poorly drafted, but as written, it appears that the debt relief agency cannot advise the assisted person to incur more debt nor can the agency advise the debtor to pay for bankruptcy related services. Although not completely consistent with the language used, it is this author’s assumption that Congress intended to prohibit debt relief agencies from advising assisted persons to borrow money for any purpose prior to filing bankruptcy, including the purpose of paying an attorney retainer fee. The actual language of this subsection provides that a debt relief agency shall not “advise an assisted person or prospective assisted person to incur more debt in contemplation of such person filing a case under this title or to pay an attorney or bankruptcy petition preparer fee or charge for services performed as part of preparing for or representing a debtor in a case under this title.”<sup>12</sup>

Section 526 provides that “[a]ny waiver by any assisted person of any protection or right provided under this section shall not be enforceable against the debtor [sic - assisted person?]. . . , but may be enforced against a debt relief agency.”<sup>13</sup>

### **Requirements Placed on Debt Relief Agencies**

Sections 527 and 528 set forth explicit requirements for debt relief agencies. Section 527 contains the disclosure requirements that are imposed on debt relief agencies<sup>14</sup> and § 528 contains requirements regarding the services advertised and provided by debt relief agencies.<sup>15</sup>

Under § 527, a debt relief agency must provide the assisted person with a copy of the written notice that is required under § 342(b)(1).<sup>16</sup> This is the notice that the bankruptcy clerk is required to

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<sup>10</sup> 11 U.S.C. § 526(a)(3).

<sup>11</sup> 11 U.S.C. § 526(a).

<sup>12</sup> 11 U.S.C. § 526(a)(4).

<sup>13</sup> 11 U.S.C. § 526(b).

<sup>14</sup> 11 U.S.C. § 527.

<sup>15</sup> 11 U.S.C. § 528.

<sup>16</sup> 11 U.S.C. § 342(b)(1).

give the consumer debtor before the commencement of their case.<sup>17</sup> This notice must include a brief description of the types of bankruptcies and the types of services available from credit counseling services.<sup>18</sup>

Section 527 also requires that “not later than 3 business days after the first date that the debt relief agency first offers to provide bankruptcy assistance to an assisted person,” the agency must provide “a clear and conspicuous written notice” that advises that:

- all information required in connection with the bankruptcy must be “complete, accurate, and truthful;”
- all assets and all liabilities must be “completely and accurately disclosed in the documents filed to commence the case,” and when the replacement value for an asset is required, this value must be provided and it must be based on a reasonable inquiry;<sup>19</sup>
- the debtor’s current monthly income, the amounts required for means testing under § 707(b)(2), and, in Chapter 13 cases, disposable income amounts will be required to be determined based on “reasonable inquiry” and provided as part of the bankruptcy; and
- information that an assisted person provides during their case may be audited, and that failure to provide such information may result in dismissal of the case or other sanction, including a criminal sanction.<sup>20</sup>

Section 527 requires a debt relief agency to maintain a copy of this notice for 2 years after the date on which the notice is given the assisted person.<sup>21</sup>

In addition to this notice, at the same time, i.e., within 3 business days of the date that bankruptcy assistance is offered, the debt relief agency must also provide the assisted person with the following statement, or one that is “substantially similar.” The statement must be “clear and conspicuous” and it must be given as a single document separate from other documents or notices provided to the assisted person:

***“IMPORTANT INFORMATION ABOUT BANKRUPTCY ASSISTANCE SERVICES FROM AN ATTORNEY OR BANKRUPTCY PETITION PREPARER.***

***“If you decide to seek bankruptcy relief, you can represent yourself, you can hire an attorney to represent you, or you can get help in some localities from a bankruptcy petition preparer who is not an attorney. THE LAW REQUIRES AN ATTORNEY OR BANKRUPTCY PETITION PREPARER TO GIVE YOU A WRITTEN CONTRACT SPECIFYING WHAT THE ATTORNEY OR BANKRUPTCY PETITION PREPARER***

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<sup>17</sup> Presumably the clerk’s duty under this section will be accomplished through disclosures contained on the official form and attested to by the debtor under 11 U.S.C. § 521.

<sup>18</sup> 11 U.S.C. § 342(b)(1).

<sup>19</sup> The actual language regarding this requirement provides that “the replacement value of each asset as defined in section 506 must be stated in those documents where requested after reasonable inquiry to establish such value.” *Id.*

<sup>20</sup> 11 U.S.C. § 527(a)(2).

<sup>21</sup> 11 U.S.C. § 527(d).

*WILL DO FOR YOU AND HOW MUCH IT WILL COST. Ask to see the contract before you hire anyone.*

*"The following information helps you understand what must be done in a routine bankruptcy case to help you evaluate how much service you need. Although bankruptcy can be complex, many cases are routine.*

*"Before filing a bankruptcy case, either you or your attorney should analyze your eligibility for different forms of debt relief available under the Bankruptcy Code and which form of relief is most likely to be beneficial for you. Be sure you understand the relief you can obtain and its limitations. To file a bankruptcy case, documents called a Petition, Schedules and Statement of Financial Affairs, as well as in some cases a Statement of Intention need to be prepared correctly and filed with the bankruptcy court. You will have to pay a filing fee to the bankruptcy court. Once your case starts, you will have to attend the required first meeting of creditors where you may be questioned by a court official called a 'trustee' and by creditors.*

*"If you choose to file a chapter 7 case, you may be asked by a creditor to reaffirm a debt. You may want help deciding whether to do so. A creditor is not permitted to coerce you into reaffirming your debts.*

*"If you choose to file a chapter 13 case in which you repay your creditors what you can afford over 3 to 5 years, you may also want help with preparing your chapter 13 plan and with the confirmation hearing on your plan which will be before a bankruptcy judge.*

*"If you select another type of relief under the Bankruptcy Code other than chapter 7 or chapter 13, you will want to find out what should be done from someone familiar with that type of relief.*

*"Your bankruptcy case may also involve litigation. You are generally permitted to represent yourself in litigation in bankruptcy court, but only attorneys, not bankruptcy petition preparers, can give you legal advice."<sup>22</sup>*

If the debt relief agency prepares the bankruptcy petition and schedules for the assisted person, the agency is responsible for making "reasonably diligent inquiry of the assisted person or others so as to obtain such information reasonably accurately for inclusion on the petition, schedules or statement of financial affairs."<sup>23</sup>

If the debt relief agency is assisting the debtor to complete their own documents, within 3 business days of the date that bankruptcy assistance is offered, the agency must "to the extent permitted by nonbankruptcy law,"<sup>24</sup> provide each assisted person with "reasonably sufficient information" provided in a "clear and conspicuous writing" advising them how to provide all the information that will be required of them under § 521.<sup>25</sup> This advice must include:

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<sup>22</sup> 11 U.S.C. § 527(b).

<sup>23</sup> 11 U.S.C. § 527(c).

<sup>24</sup> Presumably, this takes into consideration state law that restricts the unauthorized practice of law.

<sup>25</sup> 11 U.S.C. § 527(c) (referencing the listing of the debtor's duties in 11 U.S.C. § 521).

- how to value assets at replacement value, determine current monthly income, determine the amounts specified for means testing in § 707(b)(2) and, in a chapter 13 case, how to determine disposable income;
- how to complete the list of creditors, including how to determine what amount is owed and what address for the creditor should be shown; and
- how to determine what property is exempt and how to value exempt property at replacement value as defined in § 506.<sup>26</sup>

Section 528 includes the explicit requirements that are imposed on debt relief agencies with respect to the services that they provide and the way that they advertise these services. With respect to the services that they provide to assisted persons, this section provides that within 5 business days of providing any bankruptcy assistance services to an assisted person, and prior to the filing of a bankruptcy petition, a written contract must be formed with the assisted person. This contract must explain “clearly and conspicuously” the services that the debt relief agency will provide to the assisted person, the charges for these services, and the terms of payment. The assisted person must be provided with a copy of the fully executed and completed contract.<sup>27</sup>

The provisions in § 528 regarding advertising require that any advertisement of “bankruptcy assistance services or of the benefits of bankruptcy that are directed to the general public” must clearly and conspicuously disclose that the services or benefits involve bankruptcy relief.<sup>28</sup> This section also provides that the advertisement must “clearly and conspicuously” include the statement, “We are a debt relief agency. We help people file for bankruptcy relief under the Bankruptcy Code.”<sup>29</sup>

Section 528 further provides that the phrase “an advertisement of bankruptcy assistance services or of the benefits of bankruptcy directed to the general public” includes descriptions of bankruptcy assistance in connection with a chapter 13 plan even if chapter 13 is not mentioned in the advertisement. It will also include advertisements that use statements such as “federally supervised repayment plan” or “federal debt restructuring help” or other statements that could lead a reasonable consumer to believe that debt counseling was being offered instead of bankruptcy assistance.<sup>30</sup>

Public advertisements offering assistance with respect to credit defaults, mortgage foreclosures, eviction proceedings, excessive debt, debt collection pressure, or inability to pay any consumer debt are required to disclose clearly and conspicuously that the assistance may involve bankruptcy and they must also include the statement “We are a debt relief agency. We help people file for bankruptcy relief under the Bankruptcy Code.”<sup>31</sup>

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<sup>26</sup> 11 U.S.C. § 527(c).

<sup>27</sup> 11 U.S.C. § 528(a).

<sup>28</sup> 11 U.S.C. § 528(a)(3).

<sup>29</sup> 11 U.S.C. § 528(a)(4).

<sup>30</sup> 11 U.S.C. § 528(b)(1).

<sup>31</sup> 11 U.S.C. § 528(b)(2).

## Enforcement Provisions

Section 526(c) sets forth the enforcement provisions applicable to violations of §§ 526, 527, or 528. It provides that “[a]ny contract for bankruptcy assistance between a debt relief agency and an assisted person that does not comply with the material requirements” of these sections “shall be void and may not be enforced by any Federal or State court or by any other person, other than such assisted person.”<sup>32</sup>

Section 526(c) further provides that a debt relief agency will be liable to the assisted person for fees paid for the bankruptcy assistance received, for actual damages, and for reasonable attorneys’ fees and costs if the debt relief agency is found to have -

- intentionally or negligently failed to comply with any provision of §§ 526, 527, or 528 with respect to bankruptcy proceeding for the assisted person;
- provided bankruptcy assistance to an assisted person in a bankruptcy proceeding that is dismissed or converted because of such agency’s intentional or negligent failure to file a required document including those specified in § 521; or
- intentionally or negligently disregarded the material requirements the Bankruptcy Code or the Federal Rules of Bankruptcy Procedure.<sup>33</sup>

The state is authorized take action, in addition to its state law remedies, whenever it has “reason to believe” that a person has violated § 526 and may bring an action to enjoin the violation or bring an action on behalf of its residents to recover the actual damages of assisted persons arising from the violation. In the case of a successful action in either instance, the state “shall be awarded the costs of the action and reasonable attorneys’ fees as determined by the court.”<sup>34</sup> The U.S. district courts of the United States for districts located in the State are given concurrent jurisdiction over these actions.<sup>35</sup>

Section 526 also provides that notwithstanding any other provision of Federal law and in addition to any other remedy, if the court finds that a person intentionally violated § 526 or engaged in a clear and consistent pattern or practice of violating it, the court may enjoin the violation or impose an appropriate civil penalty. The court may take such action on its own motion, on the motion of the United States trustee, or on the motion of the debtor.<sup>36</sup>

Section 526 concludes by providing that no provision of §§ 526, 527, 528 can “annul, alter, affect, or exempt any person subject to such sections from complying with any law of any State except to the extent that such law is inconsistent with those sections, and then only to the extent of the inconsistency.”<sup>37</sup> It provides that no provision shall be “deemed to limit or curtail the authority or ability of a State or subdivision or instrumentality thereof, to determine and enforce qualifications for

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<sup>32</sup> 11 U.S.C. § 526(c)(1).

<sup>33</sup> 11 U.S.C. § 526(c)(2).

<sup>34</sup> 11 U.S.C. § 526(c)(3).

<sup>35</sup> 11 U.S.C. § 526(c)(4).

<sup>36</sup> 11 U.S.C. § 526(c)(5).

<sup>37</sup> 11 U.S.C. § 526(d)(1).

the practice of law under the laws of that State; or of a Federal court to determine and enforce the qualifications for the practice of law before that court.”<sup>38</sup>

### **Challenges to the Inclusion of Attorneys in the Definition of Debt Relief Agency**

On October 17, 2005, the date when most provisions of the new act took effect, Judge Lamar W. Davis, Chief Judge of the Bankruptcy Court for the Southern District of Georgia issued an order holding that attorneys licensed to practice law who were members of the bar of the Bankruptcy Court were not “covered by the provisions of the Code regulating debt relief agencies.”<sup>39</sup>

The court noted that the definition of “debt relief agency” did not include the word attorney or lawyer; that it included “bankruptcy petition preparer;” and that the definition of “bankruptcy petition preparer” specifically excluded attorneys and their staff.<sup>40</sup> The court further noted that “attorney” is also defined in the act, with no reference to “debt relief agency.”<sup>41</sup> The court then tried to reconcile this with the inclusion of “legal representation” within the definition of “bankruptcy assistance.” The court admitted that this seemed to imply that attorneys would be included, but explained this away by suggesting that “legal representation” was used to authorize the bankruptcy courts to take action against the unauthorized to practice law. Judge Lamar found the debt relief agency restrictions to be “intended to regulate that universe of entities who assist persons but are not attorneys.”<sup>42</sup>

The court found that because § 526(c) authorizes the court on its own motion to enjoin violations of the debt relief agency provisions or to impose civil penalties on a violator, the court must also have the authority to interpret who should not be found in violation. This authority “complements the inherent authority of a Court to regulate the practice of the members of its bar.”<sup>43</sup> The court noted that it would be a “breathtakingly expansive interpretation of federal law to usurp state regulation of the practice of law via the ambiguous provisions of this Act, which in no clear fashion lay claim to the right to do any such thing.”<sup>44</sup> If Congress meant to “ensnare attorneys in the thicket of §§ 526, 527, and 528, it would have used the term ‘attorney’ and not ‘debt relief agency.’”<sup>45</sup>

In the case of *Milavetz, Gallop & Milavetz, P.A. v. United States*, No. 05-CV-2626 (D. Minn.) (filed Nov. 10, 2005), a Minneapolis law firm that represents consumers in bankruptcy challenged the application of the “debt relief agency” provisions to attorneys as unconstitutional. The action alleges that the provisions limit an attorney's ability to ethically and competently advise and represent clients, illegally restrict an attorney's right to free speech, and illegally restrict the public's right to receive information from attorneys, presumptively protected under the First Amendment of the United States Constitution. The plaintiffs also allege that the provisions are unconstitutionally vague. Other similar actions are anticipated.

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<sup>38</sup> 11 U.S.C. § 526(d)(2).

<sup>39</sup> *In re Attorneys at Law and Debt Relief Agencies*, 332 B.R. 66 (Bankr. S.D. Ga. 2005).

<sup>40</sup> *Id.* at 69.

<sup>41</sup> *Id.* (referencing the definition of attorney at 11 U.S.C. §101(4)).

<sup>42</sup> 332 B.R. at 70.

<sup>43</sup> *Id.* at 67, 68 n.1.

<sup>44</sup> *Id.* at 71.

<sup>45</sup> *Id.*

## Did Congress Really Intend the Application of These Provisions to Attorneys?

That attorneys would be “debt relief agencies” is not intuitive. In fact, in line with Judge Lamar’s arguments, in the Office of Management and Budget’s analysis of the bill, reference is made to “bankruptcy attorneys, creditors, bankruptcy petition preparers, debt-relief agencies, consumer reporting agencies, and credit and charge-card companies,” as though listing six different categories.<sup>46</sup>

The Bankruptcy reform bill was massive - over 500 pages of detailed and complex amendments to an already complex code. Could the inclusion of the attorney language be an inadvertent error or oversight? Apparently not. On the floor of the House on the day that the new act passed, Representative Melvin Watt from North Carolina proposed an amendment that would have removed attorneys from the definition of debt relief agency. As he described his amendment,

Amendment 05 corrects the provisions that would require bankruptcy attorneys to identify and advertise themselves as debt relief agencies and comply with intrusive new regulations that would interfere with the confidential attorney-client relationship. Sections 227 and two twenty—through 229 of the bill would seriously interfere with the attorney-client relationship by prohibiting debtor’s bankruptcy attorneys and many non-bankruptcy attorneys from giving their clients certain proper bankruptcy planning advice. These provisions would also have a chilling effect on debtor’s lawyers and their firms by requiring all of their newsletters, seminars, advertising materials to include awkward and misleading statements identifying themselves as debt relief agencies.”<sup>47</sup>

The amendment was voted down on a voice vote and shortly thereafter, the new act, including the debt relief agency requirement was passed.<sup>48</sup>

## Conclusion

As with any new legislation, the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ushered in a host of new issues and considerations for policy makers, attorneys, and other bankruptcy professionals. One such issue is when an attorney or law firm will be a “debt relief agency” under the new act. Until the scope of who or what can be a “debt relief agency” is resolved, practitioners should be aware of the “debt relief agency” provisions and requirements. Hopefully, input from practitioners, scholars, and policy makers and legal challenges such as *Milavetz* will help clarify the scope of who or what entity may be a “debt relief agency” under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005.

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<sup>46</sup> Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, *Rept. of the Comm. on the Judiciary*, H.R. Rep. No. 109-31, 109<sup>th</sup> Cong. at 38 (Apr. 8, 2005).

<sup>47</sup> *Id.* at 524.

<sup>48</sup> *Id.*