

OBLIGATIONS OF ATTORNEYS UNDER 11 U.S.C. § 707(b)(4)

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I. Overview

Attorneys have always been subject to rules governing their conduct, including state rules of professional responsibility, 18 U.S.C. § 157, Fed. R. Civ. P. 11, and related Fed. R. Bankr. P. 9011. BAPCPA² added § 707(b)(4) to hold attorneys responsible for the accuracy and truthfulness of the information contained in clients' schedules of assets and liabilities, and possibly impose sanctions and even civil penalties if a consumer bankruptcy case is dismissed by the court. Additional duties and certifications of the consumer attorney are also added by § 707(b)(4), and that section appears as part of one of the more revised sections of the Bankruptcy Code³ under BAPCPA.⁴ The question persists — “does § 707(b)(4) add anything new that was not possible under Fed. R. Bankr. P. 9011”?

Specifically, § 707(b)(4) reads:

(A) The court, on its own initiative or on the motion of a party in interest, in accordance with the procedures described in rule 9011 of the Federal Rules of Bankruptcy Procedure, may order the attorney for the debtor to reimburse the trustee for all reasonable costs in prosecuting a motion filed under section 707(b), including reasonable attorneys' fees, if—

- (i) a trustee files a motion for dismissal or conversion under this subsection; and
- (ii) the court—

(I) grants such motion; and

(II) finds that the action of the attorney for the debtor in filing a case under this chapter violated rule 9011 of the Federal Rules of Bankruptcy Procedure.

(B) If the court finds that the attorney for the debtor violated rule 9011 of the Federal Rules of Bankruptcy Procedure, the court, on its own initiative or on the motion of a party in interest, in accordance with such procedures, may order—

- (i) the assessment of an appropriate civil penalty against the attorney for the debtor; and

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² “BAPCPA” refers to the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. The new § 707(b)(4) is effective in cases filed on or after October 17, 2005.

³ Unless otherwise indicated, the terms “Bankruptcy Code,” “section,” “subsection” and “§” refer to Title 11 of the United States Code, 11 U.S.C. § 101 *et seq.*, as amended by BAPCPA.

⁴ Section 707 is captioned “Dismissal of a case or conversion to a case under chapter 11 or 13” and, through BAPCPA, has grown from 243 words to 2611 words. See *In re Robertson*, 370 B.R. 804, 806 (Bankr. D. Minn. 2007).

(ii) the payment of such civil penalty to the trustee, the United States trustee (or the bankruptcy administrator, if any).

(C) The signature of an attorney on a petition, pleading, or written motion shall constitute a certification that the attorney has—

(i) performed a reasonable investigation into the circumstances that gave rise to the petition, pleading, or written motion; and

(ii) determined that the petition, pleading, or written motion—

(I) is well grounded in fact; and

(II) is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law and does not constitute an abuse under paragraph (1).

(D) The signature of an attorney on the petition shall constitute a certification that the attorney has no knowledge after an inquiry that the information in the schedules filed with such petition is incorrect.

11 U.S.C. § 707(b)(4).

Prior to BAPCPA, debtor's counsel did not guarantee the accuracy of the information contained in the bankruptcy petition, or the schedules of assets and liabilities, nor were they expected to do so. Given the often times hurried nature of consumer filings (due to imminent foreclosure sale, *etc.*), no special due diligence was required of debtor's counsel. While it is not clear whether § 707(b)(4) really adds anything new to what was already expected of an attorney, it is worth reviewing to understand (a) why, in light of Fed. R. Bankr. P. 9011, these obligations were added, (b) what is required of consumer attorneys under § 707(b)(4), and (c) how courts have interpreted § 707(b)(4). The initial fear of counsel to consumer debtors was, of course, personal liability for a client's misstatement. While this fear may have initially driven some attorneys from doing debtor work or *pro bono* work, it seems that the initial apprehension has subsided as bankruptcy filings are once again on the rise.

II. Why was § 707(b)(4) added?

Why was the addition of § 707(b)(4) necessary if bankruptcy courts already had several mechanisms in place to sanction an attorney's conduct? For instance, while § 707(b)(4) codifies a court's ability to sanction an attorney, Fed. R. Bankr. P. 9011 already gave a court that discretion and has always imposed the same duties on bankruptcy lawyers as other lawyers. For example, Fed. R. Bankr. P. 9011(b)(3) requires a lawyer to certify that, to the best of the lawyer's knowledge,

information and belief, "formed after an inquiry reasonable under the circumstances . . . the allegations and other factual contentions have evidentiary support or, if specifically so identified, are likely to have evidentiary support after a reasonable opportunity for further investigation or discovery[.]" Fed. R. Bankr. P. 9011(b)(3).

But, courts imposing sanctions against debtor's counsel under Fed. R. Bankr. P. 9011(b)(3) have generally done so where the lawyer has committed a bad act, not where a lawyer has innocently overlooked a misrepresentation by the debtor. *See, e.g., In re Phillips*, 317 B.R. 518 (B.A.P. 8th Cir. 2004) (affirming award of sanctions under Fed. R. Bankr. P. 9011(b)(3), where attorney electronically filed debtor's Chapter 13 petition without a signature from debtor, holding that absence of signature indicated lack of evidentiary support for petition); *In re Brown*, 328 B.R. 556 (Bankr. N.D. Cal. 2005) (awarding \$250 sanction against attorney who had electronically filed amended Chapter 13 plan without signature); *In re American Telecom Corp.*, 319 B.R. 857 (Bankr. N.D. Ill. 2004) (imposing sanctions against lawyer for Chapter 7 debtor who filed petition in bad faith in order to thwart collection efforts against non-debtor insiders).

Regardless of the prior use of Fed. R. Bankr. P. 9011, it appears that some members of Congress viewed it as inadequate. According to the debates held in Congress, § 707(b)(4) was added because of perceived abuses of the federal bankruptcy system by attorneys who were thought to be pushing people into bankruptcy. During final debate on the bill, several United States Senators expressed their displeasure with members of the consumer bankruptcy bar.

Unfortunately, this misconduct is all too often encouraged by a bankruptcy bar that ushers people into chapter 7 without ever fully considering the client's ability to repay. [T]he U.S. trustees had to pursue 653 actions seeking disgorgement of debtors' attorney's fees in fiscal year 2002. At the same time, they pursued 243 other actions for attorney misconduct that resulted in \$533,813 in sanctions. Over 75 attorneys were referred to State bar associations or other disciplinary boards. In the Eastern District of Pennsylvania, a U.S. trustee review discovered that in bankruptcy filings it was common to have boilerplate information entered without regard to the individual debtor's circumstances, internally inconsistent information, and

missing financial information. These are bankruptcy factories that appear to attempt to get as many as possible into chapter 7.

109 Cong. Rec. S1843 (2005) (statement of Sen. Hatch).

[T]here are advertisements all over America in newspapers and late night TV and cable: Come on down. Wipe out your debts. You don't have to pay what you owe. Just come on and talk to old Joe, your good, friendly bankruptcy attorney, and he will just wipe them all out. Do you know what they tell them when they come in there? They say: Take out your credit card. I want you to take your paycheck that is coming in now, you pay that to me, pay my fee, and you put everything else on your credit card. Then when you are bankrupt you just wipe that out and you don't have to pay the credit card company. That is the way it works. We know that. People are following the advice of their lawyer. Lawyers are giving them advice based on what the law allows them to do.

Id. (statement of Sen. Sessions).

A few Senators objected to the new attorney liability provisions arguing:

What this bill does to catch the very small number of potential abusers — most of whom can be caught and screened out under the existing system — is to impose huge new paperwork and filing and counseling and other barriers on all those who seek to enter the system, whether they are above or below the median income level, and whether or not there is the slightest indication that they are trying to game the system. Why else would the bill place such strict and intolerable personal liability on the bankruptcy lawyer for mistakes made in the detailed information provided by the client? In Boston and throughout the country, pro-bono lawyers from leading firms now lend a hand with bankruptcy filings to people down on their luck. The sponsors know that if this bill passes, those firms will not let their lawyers do that public interest work, because the risk will be too high.

109 Cong. Rec. S2202 (2005) (statement of Sen. Kennedy).

Pointing out the obvious, another Senator stated:

Under existing law, attorneys are already required to certify that pleadings, motions, and other materials have factual support pursuant to bankruptcy rule 9011. Attorneys are also prohibited from knowingly making any legal or factual misrepresentation to the court or assisting a client in any abuse. If we want to address misconduct by attorneys, what we need is better enforcement of those existing rules. If we want to address abuse by debtors in submitting their lists of assets, we should seek to hold those individuals responsible. My amendment would do that by making specific debts nondischargeable if the debtor lied about them in their bankruptcy schedule.

109 Cong. Rec. S2319 (2005) (statement of Sen. Bingaman).

III. What is Required of Consumer Attorneys Under § 707(b)(4)?

So, in light of the victory of Senator Hatch and the passage of BAPCPA, what is now required of a consumer bankruptcy attorney? Section 707(b)(4)(A) requires that debtor's counsel may be required by the court to reimburse the trustee for all costs under § 707(b), if the court finds that counsel violated Fed. R. Bankr. P. 9011. Since the court must also find a violation of Fed. R. Bankr. P. 9011, it is unclear what § 707(b)(4)(A) really adds to an attorney's responsibilities. In addition, § 707(b)(4)(B) further provides for a civil penalty against debtor's counsel in the event the attorney violated Fed. R. Bankr. P. 9011, and the court may order payment of such civil penalty to the trustee, the United States Trustee, or the bankruptcy administrator. Again, § 707(b)(4)(B) seems to just restate what was already possible under Fed. R. Bankr. P. 9011.

Under § 707(b)(4)(C), an attorney's signature constitutes a certification that he has performed a reasonable investigation of the circumstances giving rise to the petition, pleading, or motion being filed and that the papers are well grounded in fact. "This section applies to all attorneys, not just those representing debtors, and is applicable to all motions and pleadings filed in Chapter 7 cases." 6 Lawrence P. King, *Collier on Bankruptcy*, ¶ 707.06[1] (15th ed. rev. 2007). However, it does not appear to apply to the schedules of assets and liabilities. *Id.* This is not really new, because Fed. R. Bankr. P. 9011 already required lawyers to make an "inquiry reasonable under the circumstances."

Under § 707(b)(4)(D) an attorney's signature is a certification that the attorney has no knowledge after inquiry that the information in the schedules of assets and liabilities is incorrect.

This is a relatively low standard that every debtor should meet; a violation requires actual knowledge, not just a belief or suspicion, that the schedules are inaccurate. It requires an inquiry, which should be no greater than for other pleadings, perhaps less, since it does not use the word "reasonable."

Collier on Bankruptcy, ¶ 707.06[2].

But again, under Fed. R. Bankr. P. 9011, an attorney already had an obligation to make an inquiry and was subject to sanctions for knowingly filing incorrect schedules. See *In re Cossey*, 172 B.R. 597 (Bankr. E.D. Ark. 1994). However, *Colliers* suggests that § 707(b)(4)(D) might have been added because “it was not clear whether Rule 9011 of the Federal Rule of Bankruptcy Procedure previously applied due to the exclusion of schedules and statements in Rule 9011(a).” *Collier on Bankruptcy*, ¶ 707.06[2]. In a passing reference, another court suggested that § 707(b) simply imposes the standards of Fed. R. Bankr. P. 9011 on the debtor’s attorney in preparing the schedules of assets and liabilities and statement of financial affairs. See *In re Close*, 2008 WL 836160, *10 (D. Kan. March 28, 2008). However, a review of § 707(b)(4) does not reveal any mention of the statement of financial affairs. Furthermore, § 707(b)(4)(D) merely references “schedules.”

Unfortunately, BAPCPA does not define either “reasonable investigation” under § 707(b)(4)(C) or “inquiry” under § 707(b)(4)(D).⁵ And given the small amount of case law guidance, it is unclear what type of investigation or inquiry will be sufficient to enable debtor’s counsel to avoid issues under § 707(b)(4). Does an attorney have to visit a client’s home? Is debtor’s counsel expected to have the knowledge and skill of a trained appraiser? Is the attorney responsible for hidden assets (*i.e.*, is clairvoyance required)?

To date, it appears that attorneys have not taken such drastic steps. Some lawyers have implemented new measures, including subscribing to a commercial asset locator service, obtaining credit reports, searching public records such as registries and courts, and requiring clients to fill out and sign property inventories. See Helen W. Gunnarsson, *Bankruptcy Practice After Bankruptcy Reform*, 94 Ill. B.J. 12 (January 2006). It is likely that “reasonable investigation” and “inquiry” for purposes of § 707(b)(4) will ultimately be tested through case law and will vary depending on the facts and circumstances of each case. It also seems likely that case law interpreting counsel’s

⁵ Both *Collier on Bankruptcy*, ¶ 9011.04[2] and 2 *Moore’s Federal Practice*, § 11.11[2] (3d ed. Matthew Bender) use the words “inquiry” and “investigation” interchangeably.

investigative duties under Fed. R. Bankr. P. 9011 may be helpful guideposts in interpreting the duties imposed by § 707(b)(4).

IV. Post-BAPCPA Decisions Interpreting § 707(b)(4).

There are very few decisions on this topic, but a few courts have given some sense of how allegations of attorney misconduct may be handled. One of the few post-BAPCPA decisions involving § 707(b)(4) is *In re Robertson* 370 B.R. 804 n.8 (Bankr. D. Minn. 2007). In *Robertson*, the court reasoned that § 707(b)(4)(C) might put more teeth into the assumption that debtor's and their counsel have presented accurate information in the schedules of assets and liabilities, and that attorneys are automatically certifying the merits of each case they file. The court further explained:

This certification [under § 707(b)(4)(C)] is analogous to that long imposed by Fed. R. Bankr. P. 9011(b), though the statute uses part of the language from an earlier version of that rule. Another automatic certification is imposed by new § 707(b)(4)(D). It is triggered by counsel's signature on the client's bankruptcy petition, which activates a deemed representation that "the attorney has no knowledge after an inquiry that the information in the schedules filed with such petition is incorrect." Though this new verbiage has no directly-associated enforcement mechanism, § 707(b) now contains a basis in statute for the bankruptcy court to impose sanctions. These can take the form of "all reasonable costs" incurred by a successful movant under § 707(b), where "the action of the attorney for the debtor in filing a case under [the Bankruptcy Code] violated rule 9011 of the Federal Rules of Bankruptcy Procedure." 11 U.S.C. § 707(b)(4)(A)(i)-(ii). It also provides for "the assessment of an appropriate civil penalty against the attorney for the debtor," § 707(b)(4)(B)(i), payable to the trustee or the UST, § 707(b)(4)(B)(ii), if "the attorney for the debtor violated rule 9011 of the Federal Rules of Bankruptcy Procedure," 11 U.S.C. § 707(b)(4) (prefatory language).

The court, apparently not impressed with the language used also stated:

These provisions are worded in a cumbersome fashion and they are clumsily organized. With them being references to readily-amendable rules of court procedure that were not legislatively adopted, their mere placement in a statute is somewhat counterintuitive. It is not clear exactly how they are to be applied, and they may not be as baleful as they first may seem. *See* David Gray Carlson, *Means Testing: The Failed Bankruptcy Revolution of 2005*, 15 AM. BANKR.INSTIT. L.REV. 223, 294-295 (2007); Henry J. Sommer, *Making Sense Out of Nonsense: Representing Consumers Under the "Bankruptcy Abuse Prevention and Consumer Protection Act of 2005,"* 79 AM. BANKR.L.J. 191, 204-206 (2005).

But, their general drift is clear: debtors' counsel are to exercise significant care as to the completeness and accuracy of *all* recitations on their clients' schedules, after they have made a factual investigation and legal evaluation that conforms to the standards applicable to any attorney filing a pleading, motion, or other document in a federal court. The content of a debtor's petition and schedules is relied on, and should have the quality to merit that reliance. (Critic Sommer, 79 AM. BANKR.L. J. at 206, questioned whether the new verbiage worked any change from preexisting law. He had a point, though an academic one only.)

Robertson 370 B.R. at 804; *See also In re Ovalle*, 2008 WL 926080, *4 (Bankr. E.D. Calif. April 4, 2008) (citing *Robertson*).

In re Alvarado, 363 B.R. 484, 491-92 (Bankr. E.D. Va. 2007), provides several examples of attorney misconduct including failure to become familiar with BAPCPA, signing the debtor's name to the statement of financial affairs, receiving the filing fee from the client and then failing to use it, failing to act when informed that the case had been dismissed for failure to pay the filing fee, attempting to blame a subordinate, and filing a second petition without the debtor's authorization. The *Alvarado* court held that the debtor's counsel violated (a) §707(b)(4)(C) by failing to make a reasonable inquiry into the facts giving rise to the second petition, (b) Fed. R. Bankr. P. 9011 by filing the second petition without the debtor's signature, and (c) the Virginia Rules of Professional Conduct. The court further stated that it had the power to sanction these violations under § 105, as well as Fed. R. Bankr. P. 9011(c)(2). Unfortunately, that decision does not really discuss the interaction of all of the court's powers and whether the outcome would be different if the court were proceeding only under Fed. R. Bankr. P. 9011, rather than also § 707(b)(4).

In *In re Cherry*, 2007 WL 4893497 (Bankr. N.D. Ind. 2007), the United States Trustee filed a motion under both § 707(b)(4) and Fed. R. Bankr. P. 9011, because the debtor's attorney failed to verify the debtor's income. The debtor's case was eventually dismissed and the United States Trustee moved for sanctions. The case eventually settled for a payment of \$350.00 by debtor's counsel.

V. **Conclusion**

It seems we are left with a general sense that § 707(b)(4) makes explicit what was implicit under Fed. R. Bankr. P. 9011, and applicable rules of professional responsibility, when preparing and filing petitions and schedules of assets and liabilities. Notwithstanding the lack of case law guidance, the language of § 707(b)(4) alone appears to make it incumbent upon debtor's counsel to take every reasonable step to verify the accuracy of the information he receives from the client. Thus, the days of taking a client at their word as to their assets, income, and liabilities, may well be over. The passage of over two years with little case law addressing § 707(b)(4) may also be an indication that courts are more likely to proceed under Fed. R. Bankr. P. 9011 to penalize attorneys believed to be engaged in seriously deficient conduct, with the provisions of § 707(b)(4) as additional ammunition to sanction that conduct.

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