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How to Handle Challenging Clients and Conflict Issues in Individual Cases

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RECOGNIZING THE FRAILTIES IN YOUR CLIENTS

Over the course of my 37 years of practicing law, I have had two clients commit suicide. I sincerely believe that I neither directly nor indirectly was the cause of the suicides. On the other hand, with the benefit of hindsight and more sensitivity on my end, I may have been able to take certain steps which may have prevented the tragedies. I have written this article so that the practitioner will understand the available options and, upon identifying certain telltale signs, may be able to make a difference.

Though specific ethical rules will be referenced, this article will not delve into great detail regarding the psychology of what prompts somebody to considering killing himself/herself, but will assume that an experienced lawyer will know when to be concerned.

SIGNS TO LOOK FOR IN A CLIENT

I am fortunate that as an undergraduate a great number of my electives were devoted to psychology classes, and that during the course of my career, I have met with thousands of potential clients. Consequently, though I don't have any technical training in recognizing when someone may be suicidal, I have the benefit of consulting with a large number of individuals in very stressful situations. As a general proposition, anyone meeting with a lawyer could very well be stressed, but since the majority of my practice over the last 25 years has been in the area of bankruptcy and real estate restructuring, and individuals wanting to save their homes, many of my clients are mentally vulnerable from the onset. I also have specialized in the unique field of counseling divorcing and/or separating couples in the benefits of cooperating and seeking bankruptcy versus allowing the divorce proceedings to interfere with what is in their best financial interests.

Because I am committed to never having another client under my watch to commit suicide, at an initial consultation I intentionally allow a potential client to tell me something about their personal background which may be totally unrelated to the representation. If appropriate and the client is comfortable, I want to know about their family, leisure activities, and their long-term goals. Even in a stressful situation, individuals should be able to demonstrate at least some joy and optimism when discussing pleasant and positive topics.

I focus on the client's intentions once the client is extricated from the issues that brought the client to me. Most people love to discuss where they see themselves once the problems are resolved. If the individual cannot, this could be a sign of severe mental depression.

Oftentimes, especially after the initial consultation, I will tactfully suggest to a client who may have difficulty dealing with the pressure to talk to an expert. This is how I find out if the client is already speaking with a counselor or psychiatrist, which oftentimes is the case. If the client is not, and then asks for recommendations, this is a good sign. If a client reacts angrily to what is a subtle comment, I become concerned.

It is also invaluable to educate yourself about how the potential client has reacted to traumatic situations in the past. I ascertain what the client has done under previous difficult situations and whether the options are still available to the individual. If for whatever reason the previous alternatives available for the client to cope with the pressure are no longer available, this puts me on high alert.

When I'm meeting with divorcing individuals, I am hyper-sensitive about how the clients are reacting to what can be overwhelming pressure. You have to be very careful as you move into this line of questioning. If you alienate the individual, you probably will not get retained and will never have an opportunity to try to help. It's crucial to keep the client engaged if possible. If I can relate to what the client may be going through on a personal level, I never hesitate to tell the client that. If I have another client facing the same situation, I explain to the client how the other person was able to recover from what at the time was perceived to be untenable circumstances. I watch how the client reacts. You have to be careful to not have the client start thinking that he/she is a failure because others have been able to successfully face similar obstacles. Each case has to be treated differently and requires that you spend a substantial amount of the initial consult simply listening to the person.

So what are your options if you suspect your client may be capable of inflicting harm upon himself or even committing suicide?

OPTIONS FOR LAWYER

The goal is to provide assistance to a client while not violating your ethical responsibilities to that individual. Since you never know when you may confront such a client, knowing what you can do in advance of facing such a situation is extremely advantageous to you.

First of all, you need to spend the time to make sure that the client is not just venting, but rather may be sincere about his/her intentions. Notwithstanding the ethical implications if you make a mistake, most lawyers I have broached this subject with have told me that they would gamble on potentially improper disclosure versus risking the client's life. I found this rather refreshing in light of the ethical concerns. The ethical rules provide that you can reach out to certain individuals to advise them of the concern. See Ethical Rule 1.14(b)[1]. Especially because the Ethical Rules regarding confidentiality were never intended to mandate pure confidentiality in this situation, if you are acting in good faith, you should be fine. You do have to be careful as to exactly what you tell the third party to not disclose confidential information beyond what is needed to actually protect the client. This may be a confusing concept, but if a client reveals to you during the course of a confidential conversation that he has engaged in either criminally or civilly impermissible conduct and, as a result, is contemplating suicide, you have to give a lot of thought as to what you have to disclose in your communication with the third party. Especially because your communication to a third party could put your client in legal peril, the decision of what to say is not an easy one.

Years ago I had a client who was obviously mentally depressed. Once I realized that the client was a fairly active member of a church, I initiated contact with the spiritual leader of that

church. I was nervous about potential confidentiality, but I simply decided to take the chance because I was convinced that the individual was capable of harming himself or his spouse. Later on I confirmed that the spiritual leader contacted the client, and after that, all I could do was hope that the guidance from an individual that the client respected made a difference.

Please note that the standards are far different if you suspect that a client is capable of physically harming somebody else. In that case, Ethical Rule 1.6(d)[ii] not only allows you to disclose your concerns, but mandates you do so. Once again, in a close call, I believe that I would err on the side of disclosure irrespective of the potential ethical ramifications.

What about a situation in which you sense depression, but don't think that the situation is at a level that mandates intervention by third parties?

WHAT CAN YOU DO?

Most lawyers are not trained to recognize or diagnose psychological issues, but lawyers who regularly meet with clients learn over time to recognize certain problematic signs.

In many cases, I have been successful in providing some relief by following the following practices:

1. Let the client talk and listen closely to what the client is telling you – Many individuals just need to vent. Occasionally, I recognize that a client simply needs to get it all out and I actually say to the client, "Talk to me off the clock." Since lawyers are legendary for "watching the clock," this sends a powerful message to an individual that you really do care and your desire to listen to their feelings is not based on generating revenue.

2. If appropriate, let the client know that it's not his or her fault – Many individuals are embarrassed and want to assess self-blame. In a surprisingly large percentage of cases, the blame is misplaced. Tell a client not to blame himself and back up that statement with an explanation. If an individual started a business that simply didn't work out, but that individual had a good faith belief that the business would be successful and was doing it to try to benefit his family, remind the client that he did nothing wrong; his family would forgive and understand what he did, and that even many famous and successful Americans failed early in life.

3. Remind them that many others have made the same mistake – I know it's a tired old figure of speech, but "misery loves companionship." During the real estate collapse, I faced scores of individuals who thought they were the only ones who foolishly placed all of their eggs in the real estate basket. I was pleasantly surprised at how relieved they were when I would tell the prospective client that I had literally talked to 30 other people that week who were facing that same situation. Time and time again, the client felt a lot better knowing that he was not the only one facing this situation.

4. If appropriate, try to personally relate to the issue – Tread carefully, but if you either directly or indirectly can relate to the client's concerns, you may want to let the client know. I have worked a lot with clients with horrendous gambling addictions. As a young adult,

I gambled too much and, even though I never lost control, I fully understand the jolt one gets when rolling the dice at craps when a large amount of money is on the pass line. Interestingly enough, I develop instant credibility when I can relate to what may be driving the client to financial disaster; and if the client is interested in knowing what I did to reverse the habit, I will let them know and the client is instantly more comfortable. Tread carefully in this area, but it can be a successful strategy.

CONCLUSION

Listen to your client. If you sense an issue, listen even more closely. Spend extra time in talking to the individual, look for certain hints, and when matters reach a point at which you perceive the client may harm himself, initiate contact with a third party and communicate whatever you can to that party without violating your ethical responsibilities.

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[i] Ethics Rule 1.14(b) When the lawyer reasonably believes that the client has diminished capacity, is at risk of substantial physical, financial or other harm unless action is taken and cannot adequately act in the client's own interest, the lawyer may take reasonably necessary protective action, including consulting with individuals or entities that have the ability to take action to protect the client and, in appropriate cases, seeking the appointment of a guardian ad litem, conservator or guardian.

[ii] Ethics Rule 1.6(d) A lawyer may reveal such information relating to the representation of a client to the extent the lawyer reasonably believes necessary:

(1) to prevent the client from committing a crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another and in furtherance of which the client has used or is using the lawyer's services;

(2) to mitigate or rectify substantial injury to the financial interests or property of another that is reasonably certain to result or has resulted from the client's commission of a crime or fraud in furtherance of which the client has used the lawyer's services;

(3) to secure legal advice about the lawyer's compliance with these Rules;

(4) to establish a claim or defense on behalf of the lawyer in a controversy between the lawyer and the client, to establish a defense to a criminal charge or civil claim against the lawyer based upon conduct in which the client was involved, or to respond to allegations in any proceeding concerning the lawyer's representation of the client; or

(5) to comply with other law or final order of a court or tribunal of competent jurisdiction directing the lawyer to disclose such information.

(6) to prevent reasonably certain death or substantial bodily harm.

(7) to detect and resolve conflicts of interest arising from the lawyer's change of employment or from changes in the composition or ownership of a firm, but only if the revealed information would not compromise the attorney-client privilege or otherwise prejudice the client.

PERILS OF DIVORCE/BANKRUPTCY REPRESENTATION

Attached to this short outline is Judge Wedoff's excellent overview and analysis of the ethics of joint bankruptcy filings and divorce. This outline focuses on specific issues I have faced when trying to counsel individuals as to bankruptcy options who are divorcing. I will start with a brief explanation of my practice in this area.

I admittedly have an unusual practice in that I represent a large number of individuals who are divorcing and are facing financial difficulties. I am not a divorce lawyer and don't handle divorce cases, but I do keep abreast of divorce law. Because this is such a specialized area, only one other lawyer in Arizona regularly practices in this area as well, and he has the benefit of having a wife who is a divorce lawyer.

MY CLIENTS

Over the years, divorce lawyers have learned that my background allows me to advise individuals who are encountering different degrees of marital difficulties, but are also facing financial problems as well. As a preliminary matter, anyone experiencing financial stress and personal trauma are normally under unbelievable stress. It therefore becomes crucial from the onset to be very cognizant of potential signs of mental instability. You have to be on the alert.

To some extent, what makes my practice unique is that I'm willing to speak with both spouses at the same time with the consent of their divorce lawyers. Or, in situations in which they have not retained attorneys, I'm willing to do so as long as both agree that they want to cooperate and work together. Without question, if each individual can cooperate with the other, a divorce can actually provide certain tools which could alleviate the financial stress, not exacerbate it. I have attached an article that I give to clients in this situation so that they have a grasp of the options and alternatives available to them.

If you want to try to counsel individuals in this situation, you have to be extremely sensitive about the conflict waiver you need to obtain. I will now discuss that matter in more detail.

CONFLICT WAIVER

Unlike some situations in which a conflict waiver may be a pro forma step, in this case, you need to be very careful from the day you first meet with the individuals as to the potential conflicts and their need to fully understand their rights and obligations in that regard. Because I've discovered that in about half the cases even initially cooperative clients become hostile towards each other very quickly, the clients need to have explained to them in great detail the benefits and detriments of having one lawyer represent them. As Judge Wedoff noted in his article, in certain instances, too much cooperation could actually lead to claims of fraudulent transfers and other improper conduct. I have been successful in avoiding those types of challenges by always making sure that the clients retained independent divorce counsel if they

proceed with dissolution of their marriage. It's simply too risky for me to try to advise them if they elect to proceed without independent lawyers.

I will now elaborate on issues that can arise when you are trying to counsel individuals simultaneously who are divorcing.

POTENTIAL PITFALLS

Potential complications are probably unlimited, but the following is a list of the common ones that keep arising.

1. Fundamental disagreement – The clients may reach an impasse on material issues and this fundamental disagreement renders it impossible for you to try to counsel both of them. In most cases, if I have been representing both, this forces me to withdraw from all representation.

2. When a client may not be willing to file for bankruptcy – In a community property state, it's not unusual for just one spouse to file for bankruptcy if that filing will absolve the other client of any personal liability because of the community property discharge. If the spouse who should file refuses to do so, leaving the other spouse in peril, this refusal places the lawyer in an untenable position and the lawyer will have to withdraw.

3. Desire by one spouse to be indemnified by the other if a bankruptcy is filed – If the client not filing for bankruptcy demands that the filing spouse indemnify him or her, which is commonplace in a divorce proceeding, since that indemnification is non-dischargeable, this would render it impossible for a lawyer to represent both of the spouses.

4. Inability to decide on which spouse will fund a Chapter 13 Plan – Judge Wedoff has already pointed out that unless both clients agree as to which will ultimately have responsibility for the Chapter 13 Plan payments, joint representation is impossible and the lawyer will have to withdraw from representing both.

5. Super discharge of property settlement debt under 11 U.S.C. § 523(a)(15) – If one of the spouses elects to file for Chapter 13 and intends to otherwise discharge property settlement, unless the other spouse is then willing to file for bankruptcy, it's realistically impossible for the attorney to represent both or either.

6. Fighting over exemptions – Arizona allows the stacking of exemptions. If the filing spouse needs the benefit of a stacked exemption and the non-filing spouse refuses, the Court will not allow the filing spouse to stack the exemptions, which could lead to assets being exposed and which would create an irreconcilable conflict for the lawyer.

CONCLUSION

After reading what is rather an exhaustive list, an attorney may conclude that it's very difficult to try to represent both spouses when they are divorcing and filing for bankruptcy. That

initial reaction is absolutely accurate, but in certain instances, it can be done and can also be very advantageous for the clients. But they have to be willing to put aside their differences and cooperate in taking full advantage of the benefits of the Bankruptcy Code.

Attachments (Judge Wedoff outline, Interplay Between Divorce and Bankruptcy)

The Ethics of Joint Bankruptcy Filings and Divorce

Eugene R. Wedoff.[1]

Introduction

At first glance, it seems that couples contemplating a divorce would be wise to file a joint bankruptcy case first.

The advantages of a prior bankruptcy filing are set out in Nolo.com—"one of the web's largest libraries of consumer-friendly legal information."[2] "Filing for bankruptcy before a divorce" the website states, "can . . . simplify the issues regarding debt and property division and lower your divorce costs as a result."[3] Several websites for private attorneys repeat this advice, largely verbatim.[4]

The Nolo website also states the advantage of filing bankruptcy jointly:

> Bankruptcy filing fees are the same for joint and individual filings. So filing a joint bankruptcy with your spouse . . . can save you a lot on court fees. Also, if you decide to hire a bankruptcy attorney, your attorney fees will likely be much lower for a joint bankruptcy than if each of you filed separately.[5]

But there is a catch. Nolo cautions that "you should let your bankruptcy attorney know about your upcoming divorce as there may be a conflict of interest for him or her

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[1] U.S. Bankruptcy Judge, N.D.Ill. (ret.).

[2] *See* www.nolo.com, last visited March 29, 2016.

[3] *See* www.nolo.com/legal-encyclopedia/divorce-bankruptcy-which-comes-first.html, last visited March 29, 2016.

[4] *E.g,,* Bunch & Bock, Lexington Ky., http://www.bunchandbrocklaw.com/personal-bankruptcy/divorce-bankruptcy/, last visited April 2, 2016.

[5] *See* www.nolo.com/legal-encyclopedia/divorce-bankruptcy-which-comes-first.html.

to represent you both."[6] That advice only hints at the potential difficulties. There are several ethical problems that joint bankruptcy representation and divorce may present to a bankruptcy attorney: beyond potential conflicts of interest, there may be difficulties with the clients' expectations of confidentiality and a potential for fraudulent transfer liability. Each of these areas are outlined below, after a list of useful resources.

1. *Relevant material*

Although there are many opinions dealing with the treatment of property and claims in the intersection of bankruptcy and divorce, the following decisions and articles appear to be the ones most directly dealing with ethical issues arising from representing divorcing spouses in a joint bankruptcy case.

• *In re Disciplinary Proceedings Against Zablocki,* 635 N.W.2d 288 (Wis. 2001). An attorney who was facing suspension of his law license represented a woman in divorce proceedings without telling her of his imminent suspension; he also filed a joint bankruptcy petition for her and her husband while the divorce was pending. In this opinion, the Wisconsin Supreme Court issued a public censure and indefinite suspension of the license.

• *In re Green,* 1989 WL 1719956 (Bankr. S.D.Ga. Sept. 8, 1989). An attorney who had filed a joint Chapter 13 case later filed a divorce case on behalf of the wife. The bankruptcy court found that actions taken by the attorney to collect child support payments from the husband whom he was representing in bankruptcy violated the automatic stay. The opinion discusses in a footnote the apparent conflict of interests in the attorney's conduct, but states that this ethical issue was not before the court.

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[6] *Id.*

• C.R. "Chip" Bowles Jr., *Goldilocks, Bankruptcy and Divorce: Are the Adversarial Relationships too Much, not Enough or Just Right?* 21-JUN Am. Bankr. Inst. J. 20 (June, 2002). This article gives an excellent statement of the general rules on conflicts of interest in the bankruptcy/divorce intersection and discusses the potential for fraudulent transfer liability from property transfers in divorce decrees.

• Concurrent Session: Bankruptcy and Divorce, 111111 ABI-CLE 761 (2011), a general panel discussion that includes consideration of joint representation.

• Karmyn Wedlow & Jennifer Buchanan, Dual Representation Can Lead to a Duel with Your Clients, 55 S. Tex. L. Rev. 769 (2014), discussing ethical problems in joint representation and concluding that the economic benefits are outweighed by the ethical costs. The article outlines the potential consequences for a lawyer who fails to comply with ethical responsibilities: disqualification, monetary sanctions, and referral to disciplinary authorities. 55 S. Tex. L. Rev. at 775-77.

2. *Conflict of Interests*

a. *General rules*

The starting point for ethical representation of debtors in joint bankruptcy filings is conflicts of interest. The Model Rules of Professional Conduct, largely adopted in most states, provide a nuanced set of directives, first defining conflicts of interest and generally prohibiting representation when a conflict exists, and then providing the terms under which a conflict can be overcome by client consent.

Model Rule 1.7(a) provides the definition and prohibition. It states:

> Except as provided in paragraph (b), a lawyer shall not represent a client if the representation involves a concurrent conflict of interest. A concurrent conflict of interest exists if:

> (1) the representation of one client will be directly adverse to another client; or
>
> (2) there is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer.

It is important to recognize that this definition is not limited to clients whose interests are directly adverse in the matter for which the lawyer is retained, but extends to any situation in which the lawyer's ability to provide effective representation would be "materially limited" by responsibilities to another person or by personal interests of the attorney.

The potential for client consent is set out in Rule 1.7(b):

> Notwithstanding the existence of a concurrent conflict of interest under paragraph (a), a lawyer may represent a client if:
>
> (1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client;
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> (2) the representation is not prohibited by law;
>
> (3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and
>
> (4) each affected client gives informed consent, confirmed in writing.

This potential for consent is carefully limited. First, the attorney has to reach the personal conclusion that the conflict will not prevent effective representation; second, there must be no law prohibiting it (as there is in some jurisdictions for joint representation of parties to a divorce); third, the attorney may not pursue a claim by one client against another client in the same proceeding (so, for example, in a Chapter 11 case, a creditor client of the attorney for the debtor in possession could waive the attorney's conflict of interest, but a waiver would not allow the attorney to pursue a claim objection in the bankruptcy case against that creditor); fourth, the attorney must give

each client the information necessary for the client to make an informed decision about whether to consent to the representation despite the conflict; and finally, the client's consent must be in writing.

In the event that a conflict between the clients arises during joint representation, the attorney must withdraw from representing both clients, since continued representation would violate Rule 1.7(a). See Rule 1.16(a)("[A] lawyer . . . shall withdraw from the representation of a client if: (1) the representation will result in violation of the Rules of Professional Conduct . . . .") and Comment 4 to Rule 1.7 ("If a conflict arises after representation has been undertaken, the lawyer ordinarily must withdraw from the representation . . . ."). The attorney could continue representing one of the spouses while the other obtained a new attorney only with informed consent, as provided in Rule 1.9(a) ("A lawyer who has formerly represented a client in a matter shall not thereafter represent another person in the same . . . matter in which that person's interests are materially adverse to the interests of the former client unless the former client gives informed consent, confirmed in writing.").

b. *Divorce planned at the time of the bankruptcy filing*

The money-saving approach of a joint bankruptcy by a couple planning to divorce has the difficulty that the divorcing couple often disagree with one another, sometimes passionately. For example, in *In re Dube*, 2013 WL 1743849 (Bankr. C,D,Cal. April 23, 2013), a divorcing couple engaged in 13 years of litigation involving an individual Chapter 11 case filed by one of them. Even if spouses appear amicable when they seek bankruptcy advice in contemplation of a divorce, a joint bankruptcy carries the risk

of later conflicts between the two clients. Before filing a joint case—whether or not a divorce is contemplated—an attorney should take the following steps:

- *Assure that there are no bankruptcy issues in dispute between the spouses.* If there is any potential for a dispute between the spouses over a bankruptcy matter—such as an inter-spousal claim, the response to a particular creditor's claim, or ownership of property—a joint filing would be an ethical violation, because the representation of each party would be limited by the attorney's responsibilities to the other party, and the conflict could not be eliminated by consent, since any action that the attorney took would be against the other client's interest.
- *Give full disclosure to both clients regarding the potential for conflicts that might arise in the future and require the attorney's withdrawal.* This disclosure would reduce client resentment in the event of withdrawal, but a separate disclosure would have to be made to obtain any informed consent to continued representation of either party.
- *Do not represent either of the spouses in the subsequent divorce.* Although it might theoretically be possible to get informed consent from a client in the bankruptcy case to conflicting representation of one of them in the divorce case (because that would not be "in the same litigation" in which the attorney represented both clients), it would be extraordinarily difficult to be a client's advocate in bankruptcy and simultaneously the client's opponent in the divorce. This situation—albeit without an attempt to obtain informed consent—led to a suggestion of unethical conduct in *Green,* 1989 WL

1719956 at *6 n.1; and the imposition of ethical sanctions in *Zablocki,* 635 N.W.2d at 291.

- *Do not file a joint Chapter 13 case if divorce is anticipated.* Chapter 13 would not eliminate the need to address the allocation of claims against the spouses in the divorce case because there would be no prompt discharge of those claims. And in Chapter 13, disagreements could arise not only about property interests and claims, but also about allocation of payments to the trustee and the need for—and terms of—any plan modification. If one of the spouses wishes to retain jointly-owned property that is collateral for a loan, Chapter 13 might be necessary for that spouse, but the other would likely be best served by a separate Chapter 7 filing.

c. *Marital dispute first arising after a joint filing*

Just as a joint bankruptcy can be filed on behalf of spouses anticipating a divorce, a joint bankruptcy can be maintained on behalf of spouses who first decided to divorce while their bankruptcy case is pending. Unexpected marital discord is most likely to occur in Chapter 13 cases, because of the longer time before these cases conclude. In such cases, the attorney should have informed the spouses at the outset of the case that any disputes between them over bankruptcy matters would require the attorney to withdraw from their representation. If bankruptcy-affecting disputes do arise—likely over the plan modification and allocation of trustee payments—the attorney would have to withdraw and advise the clients to retain separate bankruptcy counsel unless informed consent is given—which is unlikely if the clients are in a contentious dispute.

3. *Confidentiality*

a. *General rules*

Rule 1.6(a) of the Model Rules of Professional Responsibility sets out the general prohibition against attorney disclosure of client confidences: "A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent, [or] the disclosure is impliedly authorized in order to carry out the representation . . . ."

Rule 1.6(b) sets out exceptions to the prohibition that would not generally apply in joint bankruptcy representation, but the two exceptions set out in Rule 1.6(a) itself do apply. First, the exception for "impliedly authorized" disclosure would allow the attorney to disclose to one of the spouses whatever relevant information the attorney received from the other spouse. *See Securities Investor Protection Corp. v. R.D. Kushnir & Co.,* 246 B.R. 582, 588 (Bankr. N.D.Ill. 2000) ("Under the 'joint defense doctrine' if the same lawyer jointly represents two or more clients with respect to the same matter, those clients have no reasonable expectation that their communications to the lawyer with respect to the joint matter will be kept secret from each other."). Second, the exception for "informed consent" would allow either spouse to require the attorney to disclose information that either spouse conveyed to the attorney in confidence. *See* Teresa Stanton Collett, *The Promise and Peril of Multiple Representation*, 16 Rev. Litig. 567, 579 (1997) ("[A]ny joint client can require the attorney to testify about such disclosures when a dispute arises between the joint clients.").

Rule 1.9(c) imposes a confidentiality limitation on continued representation of one spouse after the attorney withdraws from representation of the other: "A lawyer

who has formerly represented a client in a matter . . . shall not thereafter . . . reveal information relating to the representation except as these Rules would permit or require with respect to a client." See Comment 7 to Rule 1.9 ("Independent of the question of disqualification of a firm, a lawyer changing professional association has a continuing duty to preserve confidentiality of information about a client formerly represented.")

b. *Effect on joint bankruptcy representation*

A major concern for an attorney representing spouses in a joint bankruptcy is the potential for their not realizing the limits on confidentiality that the law has established. It is critical for the attorney to advise the clients at the outset of the representation that no statements they make to the attorney in connection with the bankruptcy case can be withheld from their spouse and that either of them can require the attorney to disclose their confidential statements in any controversy that may arise between them in the future.

4. *Fraudulent transfer liability*

One potential benefit of a divorce in connection with bankruptcy is that it typically divides the property of the spouses between them, and, in this way property that was subject to the claims against only one of the spouse can be freed from those claims by being awarded to the other spouse. Even if the divorce court order makes a substantially unequal division of the marital property, the division may be seen as supported by reasonably equivalent value to both spouses, and so immune from challenge as a constructively fraudulent transfer under § 548(a)(1)(B). *See, e.g., In re Kimmell,* 480 B.R. 876, 889-90 (Bankr.N.D.Ill.2012). However, courts are sensitive to the possibility that spouses may use the divorce process to facilitate an actual intent to

defraud creditors. The authorities are collected in *Shaudt v. United States,* 2013 WL 951138, at *5 (N.D. Ill. March 11, 2013):

> Courts have recognized that divorce can be used to lend an air of legitimacy to an otherwise fraudulent transfer. *See, e.g., In re Chevrie,* 2001 WL 120132, at *10 (Bankr.N.D.Ill. Feb.13, 2001) (finding the transfer of a marital home pursuant to a divorce settlement fraudulent because the transfer was made for the purpose of placing the home outside of the reach of the IRS). Such sham divorces often share certain "badges of fraud," including: (1) a quickly agreed upon property division; (2) the completion of the divorce proceeding on a "fast-track;" (3) the fact that only one of the spouses is represented by counsel in the divorce proceeding; (4) the fact that the spouses continue to live together after the divorce decree in the very house that was transferred; (5) the fact that the transferor spouse continues to pay the mortgage, taxes, and other costs on the transferred house; and (6) the inequitable distribution of debts and assets in the divorce. *Id.; see also In re Pilcher,* No. 05–8044, 2008 WL 2682858, at *4 (Bankr. C.D.Ill. Jun.25, 2008); *In re Hill,* 342 B.R. 183, 199–200 (Bankr.D.N.J.2006); *In re Zamudio,* No. 04 A 02922, 2005 WL 2035969, at *9–10 (Bankr. N.D.Ill. Aug.23, 2005); *In re Rodgers,* 315 B.R. 522, 531 (Bankr. N.D. 2004); *In re Boba,* 280 B.R. 430, 434–35 (Bankr. N.D.Ill. 2002); *In re Dunham,* No. 98–1466–MWV, 99–1054–MWV, 2000 WL 33679421, at *4 (Bankr. D.N.H. 2000).

On the other hand, it has been held that a regularly conducted divorce proceeding, with no indication of collusion, is entitled to a presumption of validity. *Batlan v. Bledsoe (In re Bledsoe),* 569 F.3d 1106, 1112 (9th Cir. 2009) ("[A] state court's dissolution judgment, following a regularly conducted contested proceeding, conclusively establishes 'reasonably equivalent value' for the purpose of § 548, in the absence of actual fraud."); *Ingalls v. Erlewine (In re Erlewine),* 349 F.3d 205, 212 (5th Cir.2003) ("[W]e should hesitate before we impute to Congress an intent to upset the finality of judgments in an area as central to state law as divorce decrees.").

This state of the law makes it important for attorneys representing a spouse in a divorce case to avoid uncontested transfers of property obviously subject to

enforcement of judgment. If spouses seek bankruptcy representation after such a transfer, bankruptcy counsel should warn of the potential liability for a fraudulent transfer.

Though not directly involving a divorce proceeding, *In re Prince,* 40 F.3d 356 (11th Cir. 1994), provides an example of the difficulty that bankruptcy counsel may face in this situation. In *Prince,* a Chapter 11 debtor had made a large transfer to his wife, and the law firm for the debtor had earlier represented both the husband and wife in estate planning matters. The court held that because the wife was potentially a defendant in a fraudulent transfer action, and because the attorney had previously represented the debtor's wife, the firm had a conflict of interest in representing the husband in his Chapter 11 case, and on that basis all fees for the bankruptcy representation were denied. "By representing Prince in his bankruptcy proceedings, [the firm] deprived Prince of a conflict-free, impartial, independent evaluation of the potential claims of and against his estate." *Id.* at 360. This decision is questionable; another lawyer would have faced the same difficulty, since the debtor had a personal interest in allowing his wife to keep the transferred property that would have interfered with his duty to the estate. A key to avoiding denial of fees in this situation is full disclosure of all transfers made by one spouse to the other in the bankruptcy schedules and in any application to be retained as counsel.

INTERPLAY BETWEEN DIVORCE AND BANKRUPTCY

Not surprisingly, and often tragically, individuals seeking bankruptcy relief also end up divorcing or the reverse is true, *i.e.*, a divorcing couple encounters the need to file for bankruptcy. This occurs because a divorce oftentimes creates or exacerbates the financial troubles of the individuals, or the monetary pressures leading to bankruptcy drives couples apart. This is especially true in today's economic climate in which so many citizens are unemployed or underemployed and real estate can no longer be relied upon as a lifeline and the lending industry has cut off the availability of cheap credit.

This outline is designed to highlight issues which arise in cases in which a bankruptcy is filed during the pendency of a divorce or parties decide to divorce after filing for bankruptcy. It was drafted for bankruptcy lawyers, but divorce lawyers should find it valuable.

I. IMPACT OF AUTOMATIC STAY OF 11 U.S.C. § 362

Much confusion has arisen regarding the scope of the automatic stay in divorce proceedings. This confusion probably results from lawyers having been taught all these years that the filing of a bankruptcy prevents action being taken against a debtor unless stay relief is procured from the Bankruptcy Court. Although it is true that the automatic stay normally prevents such action from going forward, the Bankruptcy Code does include a number of exceptions directly relating to divorce proceedings. Those exceptions include the commencement or continuation of a civil action proceeding – (1) for the establishment of paternity, (2) for the establishment or modification of an order for domestic support obligations, (3) concerning child custody or visitation, (4) for the dissolution of a marriage, except to the extent that such proceedings seek to determine the division of property of the estate or, (5) regarding domestic violence.

The automatic stay also does not apply to the collection of a domestic support obligation from property that is not property of the estate or the withholding of income that is property of the estate or property of the debtor for payment of domestic support obligation under judicial or administrative order or statute.

The exceptions to the automatic stay are broad and have been expanded over recent years. The legislature has determined, probably correctly, that bankruptcy has been used inappropriately in many instances to frustrate the non-filing debtor from enforcing his or her rights in divorce court. Because of a strong public policy of allowing the completion of divorce proceedings and of insuring that such individual's rights are not impaired or impeded by bankruptcy, the automatic stay does not prevent one spouse from pursuing or enforcing most monetary entitlements.

Notwithstanding the clear wording of the Bankruptcy Code, many Superior Court judges are very hesitant to permit a divorce proceeding to continue once one party files for bankruptcy protection. That is why in instances in which a non-bankruptcy judge

expresses concern, it is normally more expedient to simply seek stay relief in Bankruptcy Court so that you can then return to State Court with a Federal Court Order specifically ratifying your client's right to proceed against his or her spouse notwithstanding a bankruptcy filing. Even though the debtor may oppose such stay relief, I have found over the years that bankruptcy judges will summarily grant a stay motion because those judges understand their fellow brethrens' hesitation to proceed without clear guidance from them and bankruptcy judges have no interest in interfering with efforts to enforce and protect rights under divorce law.

Confusion has arisen as to what occurs when, in the midst of a divorce proceeding, a spouse attempting to enforce his or her rights files for bankruptcy. Interestingly enough, when a party files for bankruptcy who is not the one actually commencing or continuing a civil proceeding against the other spouse, the automatic stay does not apply. However, as a practical matter, since State Court judges are extremely uncomfortable when a bankruptcy is filed in a divorce proceeding and oftentimes the commencement or continuation of a proceeding by one spouse leads to counterclaims being filed by the other, stay relief is sought as well.

II. SCOPE OF PROPERTY OF THE ESTATE AND IMPACT ON LIABILITIES WHEN A BANKRUPTCY IS FILED DURING A DIVORCE

Divorce lawyers may have heard horror stories or actually had clients experience the ramifications of one spouse filing for bankruptcy during a divorce proceeding. Unlike some horror stories that are primarily fictional, these oftentimes are real for the following reasons.

Under 11 U.S.C. § 341, property of the bankruptcy estate of one spouse includes not only that spouse's sole and separate property, but community property as well in almost all instances. In most cases, because of the strong community property presumption under Arizona law and other community property states, almost all of that couple's property will fall within the jurisdiction of the Bankruptcy Court. Consequently, when one spouse files for bankruptcy without warning or preparing the other, even though the filing spouse may have engaged in some basic pre-bankruptcy planning, the other spouse would not have the benefit of this strategy. A bankruptcy filing by one spouse could therefore result in the non-filing spouse getting caught with a substantial amount of money in a bank account in excess of the exemption or even worse, other non-exemption assets which could have easily been converted to exempt ones if the non-filing spouse had known of the inevitable bankruptcy filing. In situations in which the divorce is especially acrimonious, the non-filing spouse may find himself or herself having to turn over to the bankruptcy trustee monies in a checking account which would have been spent if that spouse would have been given the opportunity to allow outstanding checks to clear.

One may ask why one spouse would file for bankruptcy without telling his or her spouse in advance so that the non-filing spouse could engage in some prophylactic steps. Sadly, it is not uncommon for one spouse to deliberately time the bankruptcy filing in

hopes of catching the other spouse off guard and inflicting as much pain as possible on the other spouse, purely out of anger or acrimony.

On the other hand, a bankruptcy filing initiated by one spouse during a divorce proceeding can be of great benefit to the non-filing spouse. That is because not only are the filing spouse's sole and separate debts discharged in a bankruptcy filing, but community obligations are discharged as well. This leads to a strategy which can allow a non-filing spouse to directly benefit from a bankruptcy filing by the other spouse. Arizona law provides that one spouse can bind the community in many instances but cannot bind the other spouse in a sole and separate capacity unless the other spouse has signed for the indebtedness or has specifically agreed to be responsible for it. Therefore, in such instances, which are very common in cases of credit cards or similar debts, if the non-filing spouse is not liable in a sole and separate capacity, a bankruptcy proceeding commenced during the divorce case could effectively wipe out the non-filing spouse's exposure on such debts, thereby allowing that spouse to avoid bankruptcy.

This leads to a very serious malpractice pitfall for divorce lawyers. Arizona law specifically provides that in most instances, once a divorce is completed, community obligations become sole and separate obligation of each of the spouses. *See Community Guardian Bank v. Janice Hamlin*, 182 Ariz. 627, 898 P.2d 1005. This makes sense to some extent because once the divorce is completed, the community ceases to exist. However, a spouse who may not have signed or taken on any other community obligations now will find himself or herself liable in a sole and separate capacity once the divorce is completed. Each of the spouses would then have to file for bankruptcy protection since a filing by one will not shield the other. Contrast this to what occurs if the spouse who is primarily responsible for the debts files for bankruptcy while the divorce is proceeding. By cooperating and working together, one spouse may not have to file at all since that spouse would receive the benefits of the other spouse's community discharge.

III. DISCHARGEABILITY OF CERTAIN DIVORCE BASED DEBTS

This is one area where recent changes of the bankruptcy law should eliminate any confusion. In a Chapter 7 proceeding, a spouse cannot discharge any support obligations under 11 U.S.C. § 523(a)(5) and also cannot discharge any indemnification obligations under 11 U.S.C. § 523(a)(15). This bar to discharge is automatic and does not require a spouse to file a complaint under U.S.C. § 523 to preserve such rights. If a spouse agrees to assume certain indebtedness of the marriage and then files for bankruptcy protection upon the completion of the divorce, that individual would be liable to his or her former spouse under 11 U.S.C. § 523(a)(15). For this reason, it is crucial for divorce lawyers to fully understand the ramifications of the statutes because if their clients are contemplating bankruptcy after divorcing, their ability to reap the benefits of the bankruptcy proceeding could be severely impaired if attention is not paid to the division of the debt. In such cases, it is better for the spouses to be totally candid with each other regarding their future intentions. Future aggravation can be avoided if the possibility of bankruptcy is

discussed from the onset so that appropriate verbiage can be incorporated into the operative divorce documentation.

IV. SCOPE OF DISCHARGE: DANGERS OF CHAPTER 13

The scope of the discharge in a Chapter 13 is probably misunderstood more than any other aspect of Chapter 13 by divorce lawyers. When the Bankruptcy Code was dramatically modified in 2005, and the Code increased the power of a spouse to enforce domestic support obligations, the legislature did not address an individual's ability to discharge non-support obligations in a Chapter 13. I am convinced this was purely an oversight because the legislative intent was very clear that it did not want individuals to be able to modify domestic relations obligations in a bankruptcy proceeding. Nevertheless, notwithstanding massive changes in the Bankruptcy Code, the legislature left intact the power of a Chapter 13 debtor to treat non-support obligations as general unsecured debt. That is because, whereas in a Chapter 7 property equalization payments and indemnity obligations are not dischargeable under 11 U.S.C. § 523(a)(15), they are clearly dischargeable in a Chapter 13.

Why is this so precarious for both the divorcing client and the attorney involved? Time and time again, I have clients come to me who are relying upon either the property equalization payment or indemnification rights to ensure that they are receiving their fair share of the community estate. Once the filing spouse is able to discharge that indebtedness, the result is normally a dramatic imbalance in distribution of assets and liabilities. For example, in the case of a husband who is allowed to keep his business in return for agreeing to pay the business debt and then compensating his wife for the value of the business, that husband's Chapter 13 filing could permit that individual to discharge the obligation to indemnify his wife and pay the equalization payments. This could be extremely unfair, especially in situations in which the husband retains exempt assets, be it the equity in the house or a disproportionate amount of retirement funds in return for indemnifying his wife or by paying a disproportionately large equalization payment. I have handled cases in which the opposing spouse has shrewdly reaped the upside of the divorce and none of the downside by careful planning and by lulling the other spouse into a property settlement agreement in which the spouse contemplating bankruptcy accepts a large amount of the debt in return for retaining certain of the exempt assets.

So what can be done to prevent this from happening? There are basically three ways to keep this from happening. They are:

1. Try to ensure that any indemnification of property equalization payment is fully secured. If you are securing the obligation, perfect the security agreement since the last thing in the world you want to do is agree to a secured arrangement just to have the bankruptcy debtor avoid the transaction.

2. Try to label as much of the obligation as domestic support (alimony, maintenance, or other support), since domestic support is not dischargeable even in a Chapter 13. In certain cases, this may not be possible or practical, but in other situations,

by treating and labeling the obligation as domestic support, you increase your client's protection. Although labels do not control, and bankruptcy courts look to the substance of the underlying agreement rather than the label alone, if you are able to appropriately label the obligation as domestic support, this should help your client.

3. Do not let your client enter into a property settlement agreement which is dependent upon the other spouse not filing for bankruptcy unless you have conducted an independent analysis and can opine that that spouse is really not eligible for bankruptcy relief. This would normally require the intervention of bankruptcy counsel, because an individual may look to be solvent but can quickly become insolvent with proper planning.

V. IMPORTANCE OF PAYING DOMESTIC SUPPORT OBLIGATIONS

A Chapter 13 debtor's failure to pay domestic support obligations that become due after filing affects the debtor's ability to get a plan confirmed and can lead to dismissal of the debtor's case.

A Chapter 13 plan cannot be confirmed unless the debtor has paid domestic support obligations that become due after the filing. One of the requirements of confirmation is that the debtor has paid all domestic support amounts that are required to be paid after the date of the filing.

The 2005 Amendments included protection of future support obligations in Chapter 13 cases. Prior to the Amendments, failure to pay maintenance obligations was already a ground for dismissal of a Chapter 7 case. The 2005 Amendments added § 1307(c)(11), which provides a ground to dismiss a Chapter 13 case for the debtor's failure to pay domestic support obligations that first come due after the filing of a bankruptcy case.

VI. ATTORNEYS' FEES AND DISCHARGEABILITY

Divorce attorneys must be aware of certain attorneys' fees issues that may arise if a client or client's spouse or former spouse files bankruptcy. A frequently litigated issue under 523(a)(5) and 523(a)(15) is the dischargeability of attorneys' fees. Support obligations must be owed directly to the former spouse or children to be nondischargeable.

However, there is an exception for attorneys' fees for the representation of the former spouse or child where the spouse or child was awarded support that is nondischargeable in a bankruptcy. The determination rests on the nature of the fees and whether or not they are considered "support." Most courts have concluded that attorneys' fees and costs incurred in divorce actions between ex-spouses or matters involving child support or custody are in the nature of support under 523(a)(5).

Some courts have allowed the discharge of attorney's fees in certain situations.

The Ninth Circuit held in one case that an attorney-creditor lacked standing to bring an action under section 523(a)(15) because the attorney-creditor was not a spouse, former spouse, or child of the debtor. The attorney-creditor had represented the debtor in divorce proceedings. The non-debtor spouse and children did not have liability on the attorney-creditor's claim. The Ninth Circuit noted that the attorney-creditor would have standing under 523(a)(5) where the non-debtor spouse or children had liability on the creditor's claim – in other words, if the attorney-creditor had represented the non-debtor spouse or children.

VII. WHICH SUPPORT OBLIGATIONS ARE EXEMPT

Arizona law has been amended over the years to provide that support obligations are 100% exempt, be it child support or spousal maintenance. The exemption applies to amounts past due and even amounts once collected. The scope of this exemption is very broad and provides a vehicle for pre-bankruptcy planning in that if a party contemplating bankruptcy avoids comingling support with non-exempt monies, the support money is protected even upon the filing of a bankruptcy petition. The scope of this statute also provides an avenue for potential planning between the spouses, but that discussion is beyond the scope of this outline.

VIII. POST-DISSOLUTION STATE COURT RELIEF

Because of the possibility of one spouse's rights being severely impaired by the bankruptcy filing by the other spouse, Arizona case law specifically permits a damaged spouse to return to State Court to attempt to modify the divorce decree because of the bankruptcy filing by the other spouse. Seeking such relief in many instances may not be of much benefit if the bankrupt spouse is otherwise not collectable, but it is an option you need to be aware of because there are situations in which it could benefit your client. The seminal case which specifically authorizes a spouse to seek post decree modification in Arizona is *Judith A. Birt v. John Mark Birt*, 208 Ariz. 546, 96 P.3d 544.

IX. CONCLUSION

It is almost impossible for a divorce lawyer to be sufficiently familiar with bankruptcy law to properly and accurately advise his client of the impact of bankruptcy. Therefore, if a divorce lawyer has any concern that a bankruptcy may be filed by the other side, which today is not unusual, then it is strongly recommended that independent bankruptcy counsel is retained to avoid the unpleasantry of an unexpected bankruptcy filing. As importantly, if the spouses are willing to work together notwithstanding the emotional turmoil of the divorce, in many instances a properly timed and prepared bankruptcy filing could actually help facilitate the divorce proceeding by reducing exposure and potential costs for both sides.

Divorce lawyers also need to understand how a Chapter 13 filing can impact on his client's rights, as well, in regards to non-support obligations of the filing spouse.