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# 2019 Midwest Regional Bankruptcy Seminar

## Judicial Town Hall

**Hon. Gregory R. Schaaf, Moderator**

*U.S. Bankruptcy Court (E.D. Ky.); Lexington*

**Hon. John E. Hoffman, Jr.**

*U.S. Bankruptcy Court (S.D. Ohio); Columbus*

**Hon. Jeffery P. Hopkins**

*U.S. Bankruptcy Court (S.D. Ohio); Cincinnati*

**Hon. Cynthia A. Norton**

*U.S. Bankruptcy Court (W.D. Mo.); Kansas City*

**Bankruptcy Ethics Issues**

By Brittany Griffin Smith<sup>1</sup>

- I. Ethical issues related to advertising the practice.
  - A. Posts on social media may qualify as advertising. *See* Kentucky Supreme Court Rule 3.130(7.2); Ohio Rule of Professional Conduct 7.2.
  - B. Attorneys may not represent that they practice in an area if not authorized. *See* Kentucky Supreme Court Rule 3.130(5.5); Ohio Rule of Professional Conduct 5.5.
- II. Ethical issues related to agreements with a debtor.
  - A. Consumer debtors qualify as “assisted persons.” 11 U.S.C. § 101(3).
  - B. Attorneys qualify as debt relief agencies. 11 U.S.C. § 101(12A).
  - C. A “debt relief agency” must provide notices and copies of written employment agreements with “assisted persons.” 11 U.S.C. §§ 527-528.
- III. Ethical issues related to initial bankruptcy consultations and preparing the petition.
  - A. A “bankruptcy petition preparer” is someone who prepares petitions but is not the debtor’s attorney or supervised by the debtor’s attorney. 11 U.S.C. § 110(a)(1).
  - B. A bankruptcy petition preparer may not provide legal advice. 11 U.S.C. § 110(e)(2)(A).
  - C. Attorneys must investigate their clients’ financial condition before filing for bankruptcy. 11 U.S.C. § 707(b)(4)(C); *see also* FED. R. BANKR. P. 9011.
  - D. Attorneys should not advise their clients to incur additional debt in contemplation of a bankruptcy. 11 U.S.C. § 526(a)(4).
  - E. The fraudulent filing of a bankruptcy petition could give rise to criminal liability. 18 U.S.C. § 157.
  - F. Attorneys may withdraw if a client engages in fraud when filing the petition. *See* Kentucky Supreme Court Rule 3.130(1.16); Ohio Rule of Professional Conduct 1.16.
- IV. Ethical issues related to a pending bankruptcy case.
  - A. A reasonable attorney’s fee covers attorney’s attendance at the § 341 meeting. *See generally* Local Form 2016-2(a)(i)(16) (Eastern District of Kentucky); Order Governing Procedure for Allowance of Attorney’s Fees in Chapter 13 Cases Filed on and after June 1, 2007, Exhibit A, <https://www.ohnb.uscourts.gov/administrative-orders/order-governing-procedure-allowance-attorneys-fees-chapter-13-cases-filed-and> (Oct. 4, 2011) (debtors’ ‘Rights and Responsibilities’ forms, explaining that a chapter 13 attorney has responsibility to attend § 341 meetings).
  - B. Attorneys can limit the scope of representation. In Kentucky, the attorney must get informed consent from the client first. Kentucky Supreme Court Rule

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<sup>1</sup> Brittany Griffin Smith is a law clerk for the Hon. Gregory R. Schaaf, United States Bankruptcy Court, Eastern District of Kentucky. The following analysis is not intended to express the opinions of the Court, but merely to outline the issues and arguments raised by various courts and commentators.

- 1.30(1.2(c)). Ohio requires reasonable limitations that are in writing. Ohio Rule of Professional Conduct 1.2(c).
- C. Attorneys must understand the Code to competently represent debtors. *See* Kentucky Supreme Court Rules 3.130 (1.1), (1.3); Ohio Rule of Professional Conduct 1.1, 1.3; *see also* Kentucky Supreme Court Rule 3.130(3.2) (a lawyer must make reasonable efforts to expedite litigation consistent with the interests of the client).
  - D. Someone who appears in the case represents the debtor; thus, the use of appearance counsel may implicate conflict rules.
  - E. Attorneys must communicate with clients on the status of their cases. Kentucky Supreme Court Rule 3.130(1.4); Ohio Rule of Professional Conduct 1.4.
- V. Ethical issues related to conflicts with clients.
- A. Attorneys must consider whether creditors in the case may create conflicts with past or ongoing representations. Kentucky Supreme Court Rule 3.130(1.7); Ohio Rule of Professional Conduct 1.7 (an attorney may not represent one client if directly adverse to another client or there is a significant/substantial risk that representative will be materially limited).
  - B. A conflict could arise in chapter 11 cases between the debtor-in-possession and the sole equity owner.
  - C. Attorneys cannot represent both joint debtors if the joint debtors file for divorce.
  - D. A conflict can disqualify the attorney from employment under the Code. *See* 11 U.S.C. § 327 (a professional employed by the estate cannot have an interest adverse to the estate).
- VI. Ethical issues related to fees and the collection of fees.
- A. Attorneys must disclose all fees paid or agreed to be paid in contemplation of the bankruptcy. 11 U.S.C. § 329.
  - B. Attorneys must file detailed statements of expenses, services, and time expended to receive compensation. 11 U.S.C. §§ 327, 328, FED. R. BANKR. P. 2014, 2016.
  - C. Attorneys must not share compensation with attorneys outside the firm, unless otherwise authorized by statute. 11 U.S.C. § 504; *see also* Kentucky Supreme Court Rule 3.130(1.5(e)), Ohio Rule of Professional Conduct 1.5(e) (discussing when a fee may be divided between lawyers who are not in the same firm).
  - D. Any fees that are unpaid before filing a chapter 7 petition become dischargeable debts.
  - E. The collection of unpaid fees in a chapter 7 case could interfere with the stay or the discharge injunction. 11 U.S.C. § 524; 727.
  - F. Attorneys may only keep fees that are earned. Kentucky Supreme Court Rules 1.30(1.16(d)); Ohio Rule of Professional Conduct 1.16(e).
  - G. Parties who enter fee agreements to pay for bankruptcy services out of the assets of the estate may be subject to criminal liability. *See* 18 U.S.C. § 155.
- VII. Ethical issues related to disclosures in the bankruptcy case.
- A. Attorneys must investigate the information that is included in the schedules and correct them as needed. *See* 11 U.S.C. § 527(a)(2)(B) (a debt relief agency must

- provide a disclosure telling assisted person that all assets should be disclosed); 11 U.S.C. § 707(b)(4)(D) (attorney's signature on the petition is a certification that attorney has no knowledge that the information in the schedules filed with the petition is incorrect); *see also* Kentucky Supreme Court Rule 3.130(3.3(b)) and Ohio Rule of Professional Conduct 3.3(b) (a lawyer who knows that a client intends to engage or is engaging in criminal or fraudulent conduct related to a proceeding shall take reasonable remedial measures).
- B. Concealing assets could lead to criminal liability. *See* 18 U.S.C. § 152.
  - C. Attorneys must fully disclose connections with the estate in their applications to employ. *See* 11 U.S.C. §§ 327-330, FED. R. BANKR. P. 2014, 2016, 2017.
- VIII. Ethical issues related to safeguarding property.
- A. Attorneys **must** have an escrow account. Kentucky Supreme Court Rule 3.130(1.15(a)); Ohio Rule of Professional Conduct 1.15(a).
  - B. The filing fee must be paid before the attorneys can be paid. Fed. R. BANKR. P. 1006(b)(3).
- IX. Ethical issues related to withdrawal from a case.
- A. Attorneys must withdraw if continuing the representation would force them to violate other ethics rules. *See* Kentucky Supreme Court Rule 3.130(1.16); Ohio Rule of Professional Conduct 1.16.
  - B. Representation continues unless attorneys formally withdraw.
- X. Authority to issue sanctions.
- A. Courts may order the return of any fees that are in excess of reasonable compensation for the value of services provided. 11 U.S.C. §§ 329(b), 526(c)(2); *see also* FED. R. BANKR. P. 2017.
  - B. Courts can void any contract that does not comply with the debt relief provisions. 11 U.S.C. § 526(c)(1).
  - C. Courts can order a debt relief agency to disgorge fees for inadequate representation. 11 U.S.C. § 526(c).
  - D. Courts can issue any other order to enforce its rules and prevent an abuse of the bankruptcy process. 11 U.S.C. § 105.
  - E. Court may also impose sanctions if attorneys file any pleading or petition for an improper purpose. *See* FED. R. BANKR. P. 9011(c).

**Hypothetical 1**

**FACTS:**

A Debtor receives a postcard in the mail from “John Doe Services” claiming it can stop a foreclosure sale of the Debtor’s home. He accepts the offer, pays \$600, and meets with a JDS representative to fill out paperwork.

When asked, the JDS representative says he will stop the sale for 6-9 months. The representative tells the Debtor to hurry and file the paperwork in time. The representative fills out all the paperwork, and the Debtor is rushed into signing.

The Debtor and JDS representative drive to the courthouse and the representative files the paperwork while the Debtor waits. The representative returns and tells the Debtor his home is safe.

The Debtor finds out that the paperwork started a chapter 13 bankruptcy filing after the Chapter 13 Trustee sends him a letter a short time later.

**FINDINGS:**

- JDS is both a bankruptcy petition preparer and a debt relief agency.
- JDS failed to identify itself on the petition and failed to disclose the fees it received.
- JDS intentionally misled the Debtor, misrepresenting the services it would provide and the ramifications of filing bankruptcy.
- JDS did not provide the required disclosures to the Debtor.
- The postcard advertisement did not disclose JDS’ bankruptcy services.
- JDS also failed to execute a written contract.

**ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

- 11 U.S.C. §110: A bankruptcy petition preparer must identify itself on the petition and disclose any fees it received from the debtor.
- 11 U.S.C. § 526(a)(2): A debt relief agency may not make any false or misleading statement.
- 11 U.S.C. § 526(a)(3): A debt relief agency may not misrepresent the services it will provide to an assisted person or misrepresent the benefits and risks of filing a bankruptcy petition.
- 11 U.S.C. § 527(a)(1),(2): A debt relief agency must provide a written notice that addresses everything required in § 342(b)(1) and the information specified in § 527(a)(2).
- 11 U.S.C. § 528(a)(1): A debt relief agency must execute a written contract with the assisted person.
- 11 U.S.C. § 528(a)(3): Advertising for a debt relief agency must disclose that its services are related to bankruptcy relief.

**SANCTIONS:**

- The following sanctions are appropriate:
  - Disgorgement of fees pursuant to § 526(c)(2);
  - Voiding of contracts pursuant to § 526(c)(1);
  - Enjoining the business against providing debt relief services that violate the debt relief provisions; pursuant to § 526(c)(5) and
  - Treble damages pursuant to § 110(l)(2).

*See In re Apollos Nwankaire Njoku*, Case No. 18-30558, 2018 Bankr. LEXIS 2453 (Bankr. N.D. Ohio Aug. 14, 2018).

**Hypothetical 2**

**FACTS:**

Two Debtors refuse to turnover their vehicle to the Chapter 7 Trustee. The Chapter 7 Trustee commences an adversary proceeding objecting to their discharge. A default judgment is entered. The Debtors contact attorney John Doe and orally agree to pay him \$1,000 to move for relief from default.

Doe files the motion and negotiates a settlement with the Chapter 7 Trustee that will enable the Debtors to receive a discharge and keep their vehicle.

The Debtors reject the settlement. Doe moves to withdraw. The Debtors object, arguing that the attorney entered negotiations without their consent. They also request the court order him to return the \$1,000 they paid.

**FINDINGS:**

- Doe is a debt relief agency.
- Doe did not provide a written fee agreement.
- A fee agreement would have explained the expectations of the legal representation and what would happen to the fees if Doe had a fundamental disagreement with the Debtors.

**ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

- 11 U.S.C. § 528: A debt relief agency must execute a written contract that details the fees charged for its services.

**SANCTION:**

- The following sanction is appropriate:
  - Return \$500 of the \$1,000 that the Debtors paid for legal services, pursuant to § 329(b).

*See In re Payton*, Case No. 12-18215, 2014 Bankr. LEXIS 4701 (Bankr. N.D. Ohio Nov. 12, 2014).

**Hypothetical 3**

**FACTS:**

John and Jane Doe search online and find John Smith Law Services, a law firm that offers bankruptcy services to prospective debtors in multiple jurisdictions. The Does hire JSLS to file their bankruptcy petition. JSLS appoints Local Attorney to represent them. Local Attorney meets with the Does and provides them with the necessary information.

Months go by with no word from JSLS. Eventually, Local Attorney tells the Does that he can no longer help them. Jane Doe's wages are garnished. Finally, the Does find someone new to help them file a petition.

**FINDINGS:**

- JSLS is a debt relief agency.
- JSLS promised to provide bankruptcy services to the Does, including filing a petition.
- Local Attorney is also a debt relief agency.
- Local Attorney promised to provide bankruptcy services to the Does.
- JSLS and Local Attorney failed to provide any of the promised bankruptcy services.

**ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

- 11 U.S.C. § 526: A debt relief agency may not fail to provide any service that it promised an assisted person it would provide in connection with a bankruptcy case.

**SANCTIONS:**

- The following sanctions are appropriate:
  - Disgorgement of fees pursuant to § 329 and Fed. R. Bankr. P. 2017;
  - Voiding the agreement pursuant to § 526(c)(1); and
  - Imposing a civil penalty equal to the amount of expenses the Debtors incurred, multiplied by three, pursuant to § 526(c)(5)(B).

*See In re Hanawahine*, 577 B.R. 573 (Bankr. D. Haw. 2017).

**Hypothetical 4**

**FACTS:**

A law firm uses clerical staff to meet with clients. One staff member, Jane Doe, meets with Debtor for an initial consultation. The Debtor discloses a structured settlement payment. Doe adds this information to an intake sheet.

An attorney signs her petition and the case is filed. But the attorney never reviewed the intake sheets. The petition does not disclose the structured settlement payment.

The Chapter 7 Trustee discovers that the Debtor failed to disclose this asset and files an objection to discharge.

**FINDINGS:**

- The attorney was required to perform a reasonable investigation into the case.
- A reasonable investigation requires doing more than finding out “just the basics” about a prospective debtor’s case.
- The attorney bore responsibility for his role in the false information in the filings.

**ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

- 11 U.S.C. § 707(b)(4)(C): An attorney’s signature on the petition is a certification that he or she performed a reasonable investigation into the circumstances and the petition is grounded in fact and warranted by the law.
- 11 U.S.C. § 707(b)(4)(D): An attorney’s signature on the petition also certifies that he or she has no knowledge, after an inquiry, that the information in the schedules is incorrect.

**SANCTIONS:**

- The following sanctions are appropriate:
  - Electronic case filing privileges in bankruptcy court suspended; and
  - Required ethics training.

*See In re Moffett*, Case No. 10-71920, 2012 Bankr. LEXIS 824 (Bankr. C.D. Ill. March 2, 2012).

**Hypothetical 5**

**FACTS:**

The Debtors approach Suspended Attorney about filing a bankruptcy petition. Suspended Attorney has lost her electronic filing privileges. She agrees to represent these Debtors anyway.

She explains that she cannot file the pleadings, but they could execute the filings as *pro se* Debtors. Both Debtors sign petitions stating they are not represented by counsel.

**FINDINGS:**

- The Suspended Attorney did not effectively limit her representation.
- Her attempt to limit the representation was not reasonable under the circumstances.
- The Suspended Attorney's participation in a bankruptcy case is a material fact that is relevant to the proper administration of the case.
- Her knowing misrepresentation of her participation constituted dishonest conduct.
- Presenting a petition as *pro se* to avoid the attorney's obligation of certifying the claims is an improper purpose within the scope of Fed. R. Bankr. P. 9011.

**ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

- Tennessee Rule of Professional Conduct 1.2(c); Kentucky Supreme Court Rule 1.30(1.2(c)); Ohio Rule of Professional Conduct 1.2(c): A limitation on the scope of representation must be reasonable.
- Tennessee Rule of Professional Conduct 8.4(c), Kentucky Supreme Court Rule 1.30(3.3), Kentucky Supreme Court Rule 1.30(8.4(c)); Ohio Rule of Professional Conduct 8.4(c): A lawyer may not engage in conduct involving "dishonesty, fraud, deceit, or misrepresentation."
- Fed. R. Bankr. P. 9011: An attorney who represents a debtor must sign the petition, certifying that the petition is not presented for an improper purpose.

**SANCTIONS:**

- The following sanctions are appropriate:
  - The attorney agreed to waive any attorney's fees;
  - Continued ethics education; and
  - Payment of attorney's fees and expenses for the UST, Chapter 13 Trustee and Debtors.

*See In re Smith*, Case Nos. 12-11603, 12-11857, Chapter 13, 2013 Bankr. LEXIS 368 (Bankr. E.D. Tenn. Jan. 30, 2013).

**Hypothetical 6**

**FACTS:**

Attorneys at Law Firm agree to represent joint Debtors in a chapter 11 case. The Attorneys file the petition, but never obtain wet signatures from the Debtors on their petition or schedules.

The Attorneys file an Application to Employ but the proposed order is rejected because it has an incomplete certificate of service. An amendment is filed. Neither Application reveals that the mother of one of the Debtors paid the attorneys' retainer. The Applications also do not reveal that the Debtors and their closely-held companies owe \$150,000 in prepetition legal fees to the Firm.

**FINDINGS:**

- Attorneys must have a strong knowledge of technical requirements of the Bankruptcy Code.
- These Attorneys did not demonstrate that knowledge.
- The Attorneys failed to review and verify the statements and schedules.
- The Attorneys' disclosure statement failed to identify the source of the retainer.
- The Attorneys failed to disclose their financial connections with the Debtors, which created an adverse interest with the estate.

**ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

- Tennessee Rule of Professional Conduct 1.1; Kentucky Supreme Court Rule 1.30(1.2(c)); Ohio Rule of Professional Conduct 1.2(c): A lawyer must provide competent representation.
- Fed. R. Bankr. P. 9011: The attorney's signature on the petition represents that the legal contentions are warranted, and the factual contentions have evidentiary support.
- 11 U.S.C. § 327; Fed. R. Bankr. P. 2014: A professional person employed in a case must not hold an interest adverse to the estate.
- 11 U.S.C. § 329; Fed. R. Bankr. P. 2016: The application must reveal the source of funds.

**SANCTIONS:**

- The following sanctions are appropriate, pursuant to Fed. R. Bankr. P. 9011 and § 105:
  - Disgorgement of legal fees and the retainer;
  - Inability to file a claim as a creditor in the case;
  - Denial of the employment application;
  - Requirement to attend continuing legal ethics education; and
  - Requirement to self-report to the applicable state board of professional responsibility.

*See In re Morton*, Case No. 3:15-bk-30892-SHB, 2015 Bankr. LEXIS 3309 (Bankr. E.D. Tenn. Sept. 30, 2015).

**Hypothetical 7**

**FACTS:**

Joe Doe agrees to represent a Debtor in a chapter 7 case. He never executes a written fee agreement with the Debtor.

The Debtor tells Doe that she owes money to her mother. Doe instructs the Debtor to not repay her mother, but if she does, “stick with the story” that the payment did not happen.

The Debtor tells Doe that she owns horses. Doe does not identify any horses on the Debtor’s schedules.

**FINDINGS:**

- Doe is a debt relief agency.
- Doe misled the court.
- Doe failed to execute a written agreement.
- Doe failed to perform a reasonable investigation into the information included in the schedules.

**ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

- 11 U.S.C. § 526(a)(2): A debt relief agency may not make false or misleading statements in a bankruptcy case.
- 11 U.S.C. § 528(a): A debt relief agency must execute a written contract with an assisted person.
- 11 U.S.C. § 707(b)(4)(C),(D): An attorney’s signature on a petition certifies that the attorney has no knowledge that the information in the schedules is inaccurate.
- Fed. R. Bankr. P. 9011: An attorney’s signature is certification that he or she has performed a reasonable investigation into the filing.

**SANCTIONS:**

- The following sanction is appropriate:
  - Disgorgement of fees at three times the amount of fees he collected in the case, pursuant to § 105 and § 526(c)(5).

*See Gargula v. Bisges (In re Clink)*, Case No. 10-21489-DRD-7, 2013 Bankr. LEXIS 1663 (Bankr. W.D. Mo. April 23, 2013), *aff’d*, 497 B.R. 44 (W.D. Mo. 2013), *aff’d*, 770 F.3d 719 (8th Cir. 2014).

**Hypothetical 8**

**FACTS:**

John Smith agrees to represent a chapter 11 debtor. He files a voluntary chapter 11 petition with the wrong name. He then files an amendment to correct the mistake.

He fails to comply with several local filing requirements. He fails to obtain authority for the Debtor to use cash collateral. Finally, after two primary creditors get stay relief, the Debtor voluntarily dismisses the case.

The Debtor then complains to the U.S. Trustee that Smith did not provide accurate information about the case and also filed things without authorization.

**FINDINGS:**

- Smith failed to follow basic filing rules.
- Smith failed to perform a reasonable investigation into the facts prior to filing the petition.
- Smith failed to inform his client about the case.

**ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

- Missouri Rule of Professional Conduct 4-1.1, Kentucky Supreme Court Rule 3.130(1.1), Ohio Rule of Professional Conduct 1.1: An attorney must provide competent representation.
- Missouri Rule of Professional Conduct 4-1.4, Kentucky Supreme Court Rule 3.130(1.4), Ohio Rule of Professional Conduct 1.4: An attorney must keep a client reasonably informed.
- 11 U.S.C. § 329: An attorney's compensation cannot exceed the reasonable value of services.
- Fed. R. Bankr. P. 9011: An attorney must perform a reasonable investigation into the allegations in a pleading before filing.

**SANCTIONS:**

- The following sanctions are appropriate, pursuant to Fed. R. Bankr. P. 9011, § 105, and the court's inherent authority:
  - Denial of application for fees;
  - Disgorgement of fees; and
  - Indefinite suspension from bankruptcy court and revocation of electronic filing privileges.

*See Needler v. Casamatta (In re Miller Auto. Grp. Inc.), 536 B.R. 828 (B.A.P. 8th Cir. 2015).*

**Hypothetical 9**

**FACTS:**

John Smith files a Debtor's chapter 11 petition. The Debtor currently awaits sentencing in a federal criminal tax evasion pleading. Smith does not review any of the pleadings in the criminal case.

The Debtor has no equity in his property and no ability to fund a chapter 11 plan.

Further, the disclosure of compensation, Statement of Financial Affairs, and Application to Employ each conflict on the amount the Debtor paid Smith for his services.

**FINDINGS:**

- A reasonable investigation prior to filing the petition would have revealed that filing a bankruptcy in these circumstances was bad faith.
- That investigation would also reveal that the Debtor did not have a viable chapter 11 case.
- Thus, Smith's services could not benefit the estate.
- Smith's disclosures were also inaccurate.

**ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

- 11 U.S.C. § 329; Fed. R. Bankr. P. 2016: An application for compensation must accurately disclose the amount agreed to be paid and that compensation cannot exceed the reasonable value of the services.

**SANCTIONS:**

- The following sanctions are appropriate, pursuant to § 329 and Fed. R. Bankr. P. 2016:
  - Denial of the application for compensation; and
  - Disgorgement of fees.

*See In re Small*, Case No. 18-40362-can11, 2018 WL 2938517 (Bankr. W.D. Mo. June 7, 2018).

**Hypothetical 10**

**FACTS:**

John Smith agrees to represent two Debtors in a chapter 13 case. His disclosure of fees provides that the Debtors paid him \$3,000 for his services.

Three months later, Debtors convert to chapter 11. Smith requests and receives an additional \$8,011.40. He does not file an amended disclosure in the chapter 11 case.

Debtors later convert to chapter 7. The chapter 7 trustee learns of this additional compensation and requests an order of disgorgement.

Smith then files a disclosure revealing the additional compensation.

**FINDINGS:**

- Attorneys must disclose the amount and source of all compensation received.
- Smith actively solicited the additional compensation.
- Smith then failed to disclose this compensation until after the Chapter 7 Trustee sought disgorgement.

**ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

- 11 U.S.C. § 329; Fed. R. Bankr. P. 2016: Attorneys must disclose the amount and source of all compensation received.

**SANCTIONS:**

- The following sanctions are appropriate:
  - Disgorgement of \$10,011.40 Smith received in fees pursuant to § 329 and Fed. R. Bankr. P. 2016.

*See Schroeder v. Rouse (In re Redding)*, 263 B.R. 874 (B.A.P. 8th Cir. 2001), *amended by* 265 B.R. 601 (B.A.P. 8th Cir. 2001).

**Real Life Bankruptcy Ethics Examples from the Eastern District of Kentucky**

By Brittany Griffin Smith<sup>1</sup>

**I. Case No. 15-51918 (procedurally consolidated), ECF Nos. 150, 162**

**A. FINDINGS:**

1. The Attorney is a debt relief agency.
2. The Debtors in five consolidated cases are all assisted persons.
3. One Debtor gave the Attorney funds for the purpose of paying off her chapter 13 plan.
4. The Attorney deposited the Debtor's funds into a business account, then wrote checks to cash and deposited those checks into his personal account.
5. Therefore, the Attorney intentionally misappropriated these funds.
6. The Attorney accepted the full amount of filing fees from other Debtors, and then filed applications to pay the filing fees in installments.
7. The Attorney never paid the filing fees in these cases.
8. The cases were subsequently dismissed for failure to pay the filing fees.

**B. ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

1. 11 U.S.C. § 526(a)(1) (failing to perform services);
2. 11 U.S.C. § 526(a)(2) (untrue statements in bankruptcy filings; specifically, applications to pay filing fees in installments),
3. 11 U.S.C. § 526(a)(3) (misrepresenting the services the attorney will provide);
4. 11 U.S.C. § 527 (failing to provide required notices);
5. 11 U.S.C. § 528 (failing to execute written contracts required with assisted persons);
6. Kentucky Supreme Court Rule 3.130(1.1) (competence);
7. Kentucky Supreme Court Rule 3.130(1.15) (failing to maintain IOLTA accounts and failing to safeguard property); and
8. Kentucky Supreme Court Rule 3.130 (3.3) (lack of candor, through false statements in the attorney's motions to pay filing fees in installments).

**C. SANCTIONS:**

1. Disgorgement of all fees received in the five matters that were consolidated; and
2. Permanent disbarment.

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<sup>1</sup> Brittany Griffin Smith is a law clerk for the Hon. Gregory R. Schaaf, United States Bankruptcy Court, Eastern District of Kentucky. The following analysis is not intended to express the opinions of the Court, but merely to outline the issues and arguments raised by various courts and commentators.

II. Case No. 12-51391, ECF Nos. 216, 234

A. FINDINGS:

1. The Attorney is a debt relief agency.
2. The Debtors in this case are assisted persons.
3. The Attorney represented the Debtors in a chapter 13 bankruptcy.
4. The Debtors' plan was confirmed.
5. A Creditor later got relief from stay and filed a foreclosure action against the Debtors.
6. The Debtors thought their Attorney was representing them in the foreclosure.
7. The Attorney failed to file an answer, and the Creditor filed for default judgment.
8. The Debtors asked for the Attorney's help with a loan modification.
9. The Debtors wired him funds for the loan modification to his business account. This account was not an IOLTA account.
10. The Attorney withdrew the funds and used them for personal expenses.
11. The Attorney was suspended from practice while the Debtors' case was pending, but he did not inform the Debtors.
12. The Attorney filed a late response to the foreclosure complaint, and signed the Debtors' name "*pro se*," without their consent.
13. The Attorney did not appear at a hearing and therefore, default judgment was entered.
14. The Attorney entered a request to vacate the default judgment under another attorney's name.
15. The Creditor filed a request for summary judgment.
16. The Attorney did not file a response.
17. The Attorney requested to vacate the order of sale, under another attorney's name.
18. No one appeared at the hearing and the request was overruled.
19. The Debtors completed plan payments and sent the plan completion report to the Attorney.
20. The Attorney lied and said he had uploaded the documents.
21. When the Debtors' house was sold, they requested a refund of the money they paid the Attorney for the loan modification.
22. The Debtors' case was closed without discharge, because the Attorney never filed the plan completion paperwork.
23. The Attorney never repaid the amounts he received from the Debtors.

**B. ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

1. Sections 526(a)(1) (failing to perform a service, including filing a plan completion report);
2. Section 526(a)(3) (misrepresenting the services the attorney will provide, because he was suspended and could not file the report);
3. Kentucky Supreme Court Rule 3.130(1.1) (competency);
4. Kentucky Supreme Court Rule 3.130(1.3) (diligence);
5. Kentucky Supreme Court Rule 3.130(1.15) (failing to deposit into an IOLTA account until fees were earned and failing to safeguard client property);
6. Kentucky Supreme Court Rule 3.130(4.1) (knowingly making a false statement to a third person, specifically the parties in the state action where he filed pleadings under a false name);
7. Kentucky Supreme Court Rule 3.130(5.5) (unauthorized practice of law); and
8. Kentucky Supreme Court Rule 3.130(8.4) (conduct involving dishonesty, fraud, deceit, including filing pleadings in state court under a false name).

**C. AGREED SANCTIONS [ECF NO. 234]:**

1. Disgorgement of \$10,500 taken from Debtors; and
2. Permanent disbarment.

**III. Case No. 16-60054, ECF No. 97, 137**

**A. FINDINGS:**

1. The Attorney allowed non-attorney staff to meet with prospective debtors.
2. The Attorney allowed non-attorney staff to provide legal advice when preparing petitions.
3. The Attorney allowed non-attorney staff to file petitions without supervision.

**B. ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

1. Kentucky Supreme Court Rule 3.130(1.1) (competency); and
2. Kentucky Supreme Court Rule 3.130(5.5) (unauthorized practice of law).

**C. AGREED SANCTIONS [ECF NO. 137]:**

1. Resolved through agreement to return fees to certain clients and cease all relationship with non-attorney staff who filed petitions without the Attorney's knowledge.

**IV. Case No. 13-30601, ECF Nos. 104, 113, 131, 132, 133**

**A. FINDINGS:**

1. Partner and Associate (“Attorneys”) were a debt relief agency.
2. The Debtors in several consolidated cases were assisted persons.
3. The Attorneys failed to provide copies of written contracts to prospective debtors.
4. The Attorneys accepted fees to file bankruptcy petitions but did not always file the petitions.
5. The Attorneys accepted filing fees, but then filed Applications to Pay the Filing Fees in Installments.
6. The Attorneys did not provide the required notices that they offer bankruptcy assistance.
7. The Attorneys did not maintain an IOLTA account.
8. The Attorneys allowed unlicensed, non-attorney staff to counsel clients.
9. The Attorneys did not obtain wet signatures before filing petitions and schedules.
10. The Attorneys sometimes failed to attend confirmation hearings and meetings of creditors.

**B. ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

1. Sections 526(a)(1) (failing to perform a service, namely attending the 341 hearings);
2. Section 527 (failing to provide required notices);
3. Section 528 (failing to provide written contracts);
4. Kentucky Supreme Court Rule 3.130(1.15) (failing to maintain an IOLTA account and failing to safeguard property); and
5. Kentucky Supreme Court 3.130(3.3) (failing to show candor to the court).

**C. AGREED SANCTIONS [ECF NOS. 131, 133]:**

1. Disgorgement of legal fees;
2. Waiver of Partner’s right to discharge of any debt for these sanctions in his personal bankruptcy;
3. Permanent disbarment;
4. Payment of a \$5,000 civil penalty.

**Upright Law Cases**  
By Brittany Griffin Smith<sup>1</sup>

- I. *In re Banks*, Case No. 17-10456, 2018 Bankr. LEXIS 315 (Bankr. W.D. La. Feb. 2, 2018); *aff'd sub nom Law Sols. Chi. LLC v. United Stats Tr.*, 592 BR 624 (W.D. La. 2018); *aff'd*, No. 18-33145, 2019 U.S. App. LEXIS 13599 (5th Cir. May 7, 2019).

A. FINDINGS:

1. Upright Law and the Local Attorney assigned in this case were debt relief agencies.
2. The Debtor is an assisted person.
3. Upright Law made several oral promises to this Debtor, which were inconsistent with the terms of its retainer agreement.
4. Upright Law did not provide a copy of the retainer agreement, as required by Louisiana Code of Professional Responsibility Rule 1.5.
5. Upright Law did not file her case until she had paid the full retainer, which conflicted with its promise to provide immediate relief.
6. Upright Law allowed non-attorney staff members to advise the Debtor.
7. Upright Law promised the Debtor a local attorney, but she was actually assigned a Local Attorney who practiced 350 miles away.
8. The Local Attorney did not file the petition for six months.
9. In that time a judgment was issued against the Debtor.
10. Local Attorney failed to file the Debtor's credit counseling certificate, and her case was dismissed.
11. Local Attorney failed to file a proper motion to reconsider the dismissal and the case stayed dismissed.
12. Local Attorney intentionally misled the Debtor into thinking she was contacting judge's chambers to resolve the dismissal.
13. Local Attorney did not communicate with her for three months.
14. Upright Law continued to mispresent the facts of her case over the phone.
15. Local Attorney re-filed the petition without a wet signature.
16. Local Attorney failed to file the Debtor's personal financial management certificate.
17. Local Attorney failed to attend the Debtor's 341 meeting.
18. Local Attorney failed to file other necessary documentation, so the Debtor's case was dismissed again.

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<sup>1</sup> Brittany Griffin Smith is a law clerk for the Hon. Gregory R. Schaaf, United States Bankruptcy Court, Eastern District of Kentucky. The following analysis is not intended to express the opinions of the Court, but merely to outline the issues and arguments raised by various courts and commentators.

**B. ETHICAL ISSUES IMPLICATED BY THESE FACTS:**

1. 11 U.S.C. § 526: A debt relief agency may not fail to provide services promised to provide to an assisted person.
2. 11 U.S.C. § 528: A debt relief agency must execute a written contract with an assisted person.
3. Louisiana Rules of Professional Conduct 1.1 (competence).
4. Louisiana Rule of Professional Conduct 1.3 (diligence).
5. Louisiana Rule of Professional Conduct 1.4 (communication).
6. Louisiana Rule of Professional Conduct 1.5 (fees).
7. Louisiana Rule of Professional Conduct 5.1 (responsibilities of partners).

**C. SANCTIONS:**

1. They were ordered to disgorge all attorney fees pursuant to § 329 and Fed. R. Bankr. P. 2017.
2. The contract was voided pursuant to § 526(c)(1).
3. Upright agreed to disgorge all fees paid by the Debtor, refund the \$30 the Debtor paid for credit counseling, and pay a \$5,000 civil penalty. The Court approved this agreement and ordered these sums to be paid within 14 days.
4. The Local Attorney and Upright Law were suspended for 90 days.
5. The Local Attorney's electronic filing privileges were revoked until she completed 15 hours of bankruptcy-related legal education.
6. Upright Law was prohibited from accepting payment from any residents of that district who have not had a thorough and adequate consultation with an attorney licensed in that district who is able to represent them.
7. Upright Law's future retainer agreements and contracts must conform to the Louisiana Rules of Professional Conduct.
8. All attorneys who act on behalf of Upright Law were ordered to file all documents signed by a client with a scanned, original signature.
9. Every employment contract for debt relief between Upright Law and its clients must contain the wet signatures of the client and a licensed attorney who is in charge of the case. Upright Law may not accept a retainer before that contract is executed.
10. Every attorney affiliated with Upright Law who files a pleading on the firm's behalf must contact the clerk and either update the account or create a duplicate so that the docket reflects the firm's name as Upright Law.

- II. *In re White*, Case No. 17-40093-JJR, Chapter 7, Case No. 17-40462-JJR, Chapter 7, Case No. 17-40599-JJR, Chapter 7, Case No. 17-00999-DSC, Chapter 7, Case No. 16-72114-JHH, Chapter 7, Case No. 17-70171-JHH, Chapter 7, 2018 Bankr. LEXIS 1187 (Bankr. N.D. Ala. April 19, 2018), *aff'd sub nom, Law Sols. Of Chi., LLC v. Corbett*, Case No. 1:18-cv-00677-AKK, 2019 U.S. Dist. LEXIS 39335 (N.D. Ala. March 12, 2019).

A. FINDINGS:

1. Upright Law and the Local Attorney were debt relief agencies.
2. The Debtors in these cases were assisted persons.
3. Upright Law's Sperro Scheme, *infra* Part XI.f.1.a, was likely an intentional conversion of the secured creditor's collateral.
4. The scheme could have exposed prospective debtors to civil and criminal liability and jeopardized their right to a discharge.
5. Upright and any participating attorneys were encouraging debtors to engage in criminal or fraudulent conduct.
6. Further, Upright Law and the Local Attorney filed retention agreements that disclosed a flat fee was paid but that fee did not include routine bankruptcy matters.
7. The U.S. Trustee sued Upright Law to address these issues.
8. Upright Law and the Local Attorney settled after agreeing to pay between \$25,000-\$50,000 each to the Trustee in the relevant cases, to not file new cases for six months, and to provide all legal services they had routinely excluded from their fee arrangements without charging additional fees.
9. An audit revealed that Upright Law and the Local Attorney continued to require additional fees for these routine legal services.
10. Upright Law and the Local Attorney did not act in good faith, because the settlement required them to deviate from their "high-volume, monolithic business model," which they did not do.

B. ETHICAL ISSUES IMPLICATED BY THESE FACTS:

1. 11 U.S.C. § 526(a)(2): A debt relief agency cannot file false or misleading statements.
2. Fed. R. Bankr. P. 9011: An attorney's signature is verification that the information in the pleading is accurate and for a proper purpose.

**C. SANCTIONS:**

1. A civil penalty of \$150,000 was assessed against Upright Law and the Local Attorney, jointly and severally.
2. Upright Law and the Local Attorney were ordered to return all fees paid in any cases filed after this settlement within 21 days.
3. Upright Law's was suspended in that district for 18 months. It could not make referrals and upon being contacted by potential debtors, it was ordered to inform them that it was prohibited from filing in that district and from making referrals.
4. Upright Law was ordered to refund all fees it had received in that district from prospective debtors whose cases were not yet filed and inform those individuals that Upright Law's right to file was revoked. Upright Law was ordered not to refer them elsewhere. Upright Law was also ordered to provide copies to the bankruptcy administrator of the letters to these prospective debtors informing them of these facts.
5. The Local Attorney was suspended for 60 days.

III. *In re Foster*, 586 B.R. 62 (Bankr. W.D. Wash. 2018)

A. FINDINGS:

1. Upright Law and a Local Attorney were debt relief agencies.
2. The Debtor in this case is an assisted person.
3. Upright Law and a Local Attorney helped this Debtor to file and settle a Fair Debt Collection Practices Act lawsuit prior to filing bankruptcy.
4. Upright Law and the Local Attorney failed to disclose money they had collected for these services before the petition was filed.
5. Upright Law and the Local Attorney also failed to disclose payments from the settlements.
6. The settlement fees were received in contemplation of a bankruptcy filing.
7. Upright Law and the Local Attorney did not accurately disclose the scope of services that were excluded from the base fee.

B. ETHICAL ISSUES IMPLICATED BY THESE FACTS:

1. 11 U.S.C. § 329; Fed. R. Bankr. P. 2016: An attorney must disclose all compensation.
2. 11 U.S.C. § 526(a)(2): A debt relief agency may not make false or misleading statements in a bankruptcy filing.
3. Fed. R. Bankr. P. 9011: An attorney's signature is verification that the information in the pleading is correct.

C. SANCTIONS:

1. Upright Law took corrective action to avoid similar inaccuracies and disgorged fees associated with the case.
2. No further sanctions were imposed.

- IV. *Robbins v. Delafield (In re Williams)*, Case No. 15-71767, Adv. No. 16-07024, Case No. 16-50158, Adv. No. 16-05014, Adv. No. 16-07024, 2018 Bankr. LEXIS 382 (Bankr. W.D. Va. Feb. 12, 2018).

A. FINDINGS:

1. Upright Law collects fees from prospective debtors throughout the country for bankruptcy services.
2. Upright Law connects prospective debtors with local attorneys.
3. Upright Law participated with a repossession company to create the “Sperro Program.”
4. The Sperro Program allowed a prospective debtor who wanted to surrender a car to turn it over to the repossession company, who then paid the debtor’s legal fees.
5. The repossession company would move the car out of state.
6. The repossession company would then notify the lienholder that it could use the repossession company’s auction services or else pick up the car after paying unnecessary storage and towing fees.

B. ETHICAL ISSUES IMPLICATED BY THESE FACTS:

1. 11 U.S.C. § 329; Fed. R. Bankr. P. 2016: An attorney must disclose the source of any compensation.

C. SANCTIONS:

1. Upright Law was ordered to return all fees.
2. Upright Law and its principals were suspended for five years.
3. Upright Law and their principals were collectively fined \$250,000.
4. One of these principals was fined an additional \$50,000 for his participation in the repossession scheme.
5. One of the local attorneys who took a case from Upright Law was suspended for a year and fined \$5,000.
6. Another attorney who took cases from Upright Law was suspended for 18 months and fined \$5,000.
7. The repossession company was ordered to disgorge all funds it received in connection with the sale of any property or the recovery of any property in connection with any bankruptcy case in that court.