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Messy Chapter 7s

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COMPLEX CHAPTER 7 CASES

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Intake of "Messy" Chapter 7 Cases

I. Initial Client Contact

Bankruptcy cases can vary from a simple no asset case to a complex case involving multiple businesses or suspicious transfers that necessitate review by the Chapter 7 Trustee. A bankruptcy attorney must be able to recognize the complex case and use the tools at his disposal to work with the client to minimize risk and maximize results. A critical aspect in recognizing the complex case is during the attorney's first contact with the client. In a complex case, the first telephone conversation is important so that the attorney can facilitate disclosure of as much pertinent information as practical so as to make the office consult productive. When handling a complex case the attorney should personally handle the phone consultation so that crucial information can be obtained regarding the assets, nature of the liabilities, and any transfers of property. Furthermore, by the attorney handling the initial phone consultation it builds a rapport with the client.

If a complex case deals with the ownership of a business the operation of the entity must be explored. A bankruptcy practitioner must calculate the solvency of the company; therefore, an analysis of the assets including hard assets, receivables, insurance policies, and deposits must be analyzed. An attorney must also calculate the debt of the company including any debts to taxing authorities, secured debt, and trade payables. Most businesses use some form of accounting software (usually QuickBooks) and it is crucial to have the potential client provide those documents and it is customary to have the client's bookeeper present for the first office consult. The most important documents are the company's list of payables, receivables, balance sheet, and profit and loss statement. A bankruptcy attorney must review any potential

loans to and from the company to the insiders. This information is usually found in company's internal documents or in a tax return.

Following the phone consult the next step is to attempt to verify the information provided by the client using online sources. One of the most important tools is to perform a UCC-1 search and a register of deeds search so that the order of priority of secured claims can be ascertained. Next an asset search on a database such as Westlaw or Lexis allows the attorney to verify the information and can be used to move the office consult into a strategy meeting rather than a fact finding exercise.

I think that it is important to state that attorneys should stay within their core competence. Attempting to veer outside of that runs the risk of malpractice or opens the client up to potential adversary proceedings.

II. Bankruptcy Code Implications

Bankruptcy is a highly technical practice that mandates particular expertise in order to adequately represent clients. The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA") effected numerous and significant revision to the Bankruptcy Code which imposed duties upon individual debtors and most importantly their counsel. Among the changes and additions, BAPCPA added section 707(b)(4)(C) and (D) of the Bankruptcy Code, which states as follows:

> (C) The signature of an attorney on a petition, pleading, or written motion shall constitute a certification that the attorney has-
>
> (i) Performed a reasonable investigation into the circumstances that gave rise to the petition, pleading, or written motion; and
>
> (ii) Determined that the petition, pleading, or written motion-
>
> (I) Is well grounded in fact and
>
> (II) Is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law and does not constitute an abuse under paragraph (1).
>
> (D) The signature of an attorney on the petition shall constitute **certification that the attorney has no knowledge after an inquiry** that the information in the schedules filed with such petition is incorrect.

While this section arguably did little more than codify an attorney's obligations pursuant Fed. R. Civ. P. 11 (Fed. R. Bankr. P. 9011), it certainly provided additional detail and evidenced strong Congressional intent to elevate the level of practice by debtor's counsel. As officers of the court, attorneys have a special responsibility for upholding the quality of justice within the judicial process. The Court depends on the veracity, integrity, and competence of the attorneys that practice before it. These sections, by their literal terms, impose numerous and significant obligations upon debtor's counsel and indeed the literal language of Section D obliges the attorney to proactively perform an investigation of the information supplied to counsel by a client prior to filing the petition.

In the preparation of bankruptcy schedules, debtor's counsel should take nothing for granted. The attorney should carefully investigate the affairs of the debtor and make certain that the attorney has all the information needed to prepare full and complete schedules.

By its very nature, Section 704(b)(4)(C) imposes a burden on the Debtor's counsel. Further, one court has held that the answers to the following questions are relevant to an inquiry of whether Section 704(b)(4)(C) has been violated:

> (1) did the attorney impress upon the debtor the critical importance of accuracy in the preparation of documents to be presented to the Court; (2) did the attorney seek from the debtor, and then review, whatever documents were within the debtor's possession, custody or control in order to verify the information provided by the debtor; (3) did the attorney employ such external verification tools as were available and not time or cost prohibitive (e.g., online real estate title compilations, on-line lien search, tax "scripts"); (4) was any of the information provided by the debtor and then set forth in the debtor's court filings internally inconsistent-that is, was there anything which should have obviously alerted the attorney that the information provided by the debtor could not be accurate; and (5) did the attorney act promptly to correct any information presented to the Court which turned out notwithstanding the attorney's best efforts, to be inaccurate. *In re Withrow,* 391 B.R. 217 (Bankr.D. Mass. 2008)

This suggest that an attorney conversely has a duty to perform these tasks, or risk violating Section 704(b)(4)(C).

III. Document Preparation and Review

It is not only the requirement that an attorney review the documents for accuracy that is important to be cognizant of the sheer weight of documents to be produced. Eastern District of Michigan Local Bankruptcy Rule 2003-2 requires an extensive list of documents to be produced from the preceding year (or as long as six) at the debtor's Section 341 first meeting of creditors. With production comes scrutiny by the Trustee. Furthermore, in any case that would be considered a complex chapter 7 case the document request by the Trustee would greatly exceed what is required under the Local Rule. Therefore, to the extent that a debtor has documents or the attorney can ascertain the documents from online sources an attorney must analyze the documents on their face and against the external data procured by an attorney for potential inconsistencies that go beyond the bankruptcy schedules themselves.

Before an attorney prepares a single bankruptcy schedule, the attorney must meet with the a client, analyze the documents and legal issues, and determine the advantages and risks imposed by filing. This practice allows the attorney to safeguard against any potential omissions in the schedules. As a practice a bankruptcy attorney must perform an online asset search, UCC-1 search, recorded documents search, credit report, watercraft search, and real property search. The attorney should also use bluebook, zillow, trulia, to help verify values of the client's subject property. More importantly, this practice allows the attorney to have access to any document that might be requested by a Chapter 7 Trustee. In my experience of representing Trustees and also as an observer of 341 hearings, many times attorneys do not have even the most basic records and essential documents such as relevant real estate documents or

bank records for the months prior to bankruptcy. This causes delay in the administration of the estate, frustration from the client's perspective, and additional cost to the estate.

Once the documents are secured, and the client has determined that a Chapter 7 filing is the most advantageous approach, a second office consult with the attorney to prepare the bankruptcy schedules is set up. In a complex chapter 7 case it is critical that the attorney prepare the Bankruptcy Schedules. In my practice, I personally input the client's responses in the bankruptcy software and the dialogue with the client allows for me to extract any potential issues with a Chapter 7 trustee. Although it is time consuming I find it to be a more successful approach than providing a client with a basic questionnaire and simply inputting the answers. That approach in a complex case is akin to opening pandora's box since if a client does not understand a question he will simply ignore or not answer accurately, which leads to omissions or inaccurate statements in the Bankruptcy Schedules.

After the preparation of the Bankruptcy Schedules it is of the utmost importance to review those Schedules with the client and ascertain verification that the client has reviewed and understands that the information is true, accurate, and complete. This exercise has two very important implications. First, your client understands the importance of full disclosure and that information provided is accurate. Second, by having the client verify the schedules in writing to you it provides the attorney a defense from the all too common " my attorney did that, I have no idea". This should be a strict policy of any bankruptcy attorney.

IV. KEEP THE CLIENT INFORMED

Most complex cases involve litigious creditors and/or a tremendous volume of creditors. Once retained the client should advise all creditors that attempt contact that

he has retained counsel and to relay all communications through the attorney. It is important that your client is informed of all aspects of his case and that you maintain contact regarding any important development.

In my practice I meet with the client on the eve of filing of the bankruptcy petition. In this meeting I like to stress the process, and inform the client of the likelihood of further document requests by a Chapter 7 Trustee, and explain what a Rule 2004 examination is and what the odds are of that occurring in his case. Clients are usually very receptive to this meeting because it offers them a roadmap of the next 30-60 days of the case.

Messy Chapter 7 Cases | Moving the case along

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Moving a case along Post 341 Meeting of Creditors

A. Requests for Additional Information by the Trustee

Unfortunately, not every case will move forward to discharge as smoothly as others. At some point or another in our career as a Bankruptcy Attorney, we will receive a lengthy 2-3 page request by the Trustee assigned to your case for production of additional documents. This request is well within the rights of the said Trustee as they may ask for all documents necessary to perform their duties. Furthermore, it is the responsibility of the Debtor to assist the Trustee in obtaining the items necessary. See 11 U.S.C. § 521.

Should the Debtor fail to comply or produce the items necessary pursuant to the Trustee's request, the Trustee may move for a Rule 2004 Examination and request for production of documents. The Court has authority to compel the Debtor's testimony and the production of records pursuant to *Fed.R Bankr. P.2004*. A motion pursuant to Fed.R. Bankr. P. 2004 is a formal request to the court for production of the documentation or demand for the Debtor or other interested parties to attend an additional examination of the issues pertaining to the estate. *See Fed.R Bankr. P.2004.*

I recommend that you and your client avoid the necessity for the above referenced 2004 Examination. The 2004 Examination puts the Debtor in a position to have a court ordered time limit to produce specific documentation or face a motion for contempt or a motion to compel turnover of these items. Always try to avoid a Rule 2004 motion by the Trustee. Work with your client and the Trustee to resolve the inquiry. This will avoid your client from being held in contempt and sanctioned for failure to produce the documents, limit attorney fees, and cut down the time the Trustee and/or its counsel will have to spend on these issues. Additionally, if you decide to convert the case to a chapter 13 (to be discussed below) it will cut down on the Trustee's administrative claim.

The first step you should take when you receive the initial request by the Trustee is to contact the Trustee or their counsel; inquire what it is they are looking for and why they are requesting the production of these items. Trustees often make a request for a large amount of documents that can be more than needed to address their concern. There have been many cases where I contacted a Trustee and they have simply stated what they actually need and the reason for it. Having a candid and cordial conversation with the Trustee at the outset will establish good will with the Trustee and assure them of your intention to comply.

Although this is an adversarial system, having a dialogue with the Trustee is always to your client's benefit. Contacting the Trustee will narrow the scope of focus and many times bring to light what the issues are and what the Trustee is investigating in the case.

B. Contacting the client

Now that you have contacted the Trustee, narrowed the scope of their inquiry and established what it is that they are looking for, it is time to contact the client. If you have done a good job of preparing the client for these possible issues through your intake, investigated what may become issues with them and prepared the schedules properly, this phone call will be easy and one that you may both had anticipated. However, no matter how much investigation you do prior to the case and no matter how much you prepare the client there will sometimes be unforeseen issues that come up. Many times there are issues that your client didn't tell you. This is because the client did not understand, misinterpreted or had no knowledge of the matter.

The key here is keeping the client calm. Helping them understand the reason for the inquiry, the process moving forward, how this will affect their case and options they have in possibly resolving these matters will produce a cooperative relationship between you and your client. Find out what the client's

position would be on certain matters such as equity in property that the client no longer wants to keep or actions against insiders that the client will state they have no interest in protecting.

1. **Objections to Discharge**

The Debtor's failure comply with the terms of a Rule 2004 motion brought by the Trustee and ordered by the court may result in an objection to discharge. *See 11 U.S.C. § 727. Discharge*

> 11 U.S.C. § 727. Discharge
> (a) The court shall grant the debtor a discharge, unless—
> (1) the debtor is not an individual;
> (2) the debtor, with intent to hinder, delay, or defraud a creditor or an officer of the estate charged with custody of property under this title, has transferred, removed, destroyed, mutilated, or concealed, or has permitted to be transferred, removed, destroyed, mutilated, or concealed—
> (A) property of the debtor, within one year before the date of the filing of the petition; or
> (B) property of the estate, after the date of the filing of the petition;
> (3) the debtor has concealed, destroyed, mutilated, falsified, or failed to keep or preserve any recorded information, including books, documents, records, and papers, from which the debtor's financial condition or business transactions might be ascertained, unless such act or failure to act was justified under all of the circumstances of the case;
> (4) the debtor knowingly and fraudulently, in or in connection with the case—
> (A) made a false oath or account;
> (B) presented or used a false claim;
> (C) gave, offered, received, or attempted to obtain money, property, or advantage, or a promise of money, property, or advantage, for acting or forbearing to act; or
> (D) withheld from an officer of the estate entitled to possession under this title, any recorded information, including books, documents, records, and papers, relating to the debtor's property or financial affairs;
> (5) the debtor has failed to explain satisfactorily, before determination of denial of discharge under this paragraph, any loss of assets or deficiency of assets to meet the debtor's liabilities;
> (6) the debtor has refused, in the case—
> (A) to obey any lawful order of the court, other than an order to respond to a material question or to testify;
> (B) on the ground of privilege against self-incrimination, to respond to a material question approved by the court or to testify, after the debtor has been granted immunity with respect to the matter concerning which such privilege was invoked; or
> (C) on a ground other than the properly invoked privilege against self-incrimination, to respond to a material question approved by the court or to testify;
> (7) the debtor has committed any act specified in paragraph (2), (3), (4), (5), or (6) of this subsection, on or within one year before the date of the filing of the petition, or during the case, in connection with another case, under this title or under the Bankruptcy Act, concerning an insider;
> (8) the debtor has been granted a discharge under this section, under section 1141 of this title, or under section 14, 371, or 476 of the Bankruptcy Act, in a case commenced within 8 years before the date of the filing of the petition;
> (9) the debtor has been granted a discharge under section 1228 or 1328 of this title, or under section 660 or 661 of the Bankruptcy Act, in a case commenced within six years before the date of the filing of the petition, unless payments under the plan in such case totaled at least—
> (A) 100 percent of the allowed unsecured claims in such case; or
> (B)
> (i) 70 percent of such claims; and
> (ii) the plan was proposed by the debtor in good faith, and was the debtor's best effort;

(10) the court approves a written waiver of discharge executed by the debtor after the order for relief under this chapter;

(11) after filing the petition, the debtor failed to complete an instructional course concerning personal financial management described in section 111, except that this paragraph shall not apply with respect to a debtor who is a person described in section 109(h)(4) or who resides in a district for which the United States trustee (or the bankruptcy administrator, if any) determines that the approved instructional courses are not adequate to service the additional individuals who would otherwise be required to complete such instructional courses under this section (The United States trustee (or the bankruptcy administrator, if any) who makes a determination described in this paragraph shall review such determination not later than 1 year after the date of such determination, and not less frequently than annually thereafter.); or

(12) the court after notice and a hearing held not more than 10 days before the date of the entry of the order granting the discharge finds that there is reasonable cause to believe that—

(A) section 522(q)(1) may be applicable to the debtor; and

(B) there is pending any proceeding in which the debtor may be found guilty of a felony of the kind described in section 522(q)(1)(A) or liable for a debt of the kind described in section 522(q)(1)(B).

(b) Except as provided in section 523 of this title, a discharge under subsection (a) of this section discharges the debtor from all debts that arose before the date of the order for relief under this chapter, and any liability on a claim that is determined under section 502 of this title as if such claim had arisen before the commencement of the case, whether or not a proof of claim based on any such debt or liability is filed under section 501 of this title, and whether or not a claim based on any such debt or liability is allowed under section 502 of this title.

(c)

(1) The trustee, a creditor, or the United States trustee may object to the granting of a discharge under subsection (a) of this section.

(2) On request of a party in interest, the court may order the trustee to examine the acts and conduct of the debtor to determine whether a ground exists for denial of discharge.

(d) On request of the trustee, a creditor, or the United States trustee, and after notice and a hearing, the court shall revoke a discharge granted under subsection (a) of this section if—

(1) such discharge was obtained through the fraud of the debtor, and the requesting party did not know of such fraud until after the granting of such discharge;

(2) the debtor acquired property that is property of the estate, or became entitled to acquire property that would be property of the estate, and knowingly and fraudulently failed to report the acquisition of or entitlement to such property, or to deliver or surrender such property to the trustee;

(3) the debtor committed an act specified in subsection (a)(6) of this section; or

(4) the debtor has failed to explain satisfactorily—

(A) a material misstatement in an audit referred to in section 586(f) of title 28; or

(B) a failure to make available for inspection all necessary accounts, papers, documents, financial records, files, and all other papers, things, or property belonging to the debtor that are requested for an audit referred to in section 586(f) of title 28.

(e) The trustee, a creditor, or the United States trustee may request a revocation of a discharge—

(1) under subsection (d)(1) of this section within one year after such discharge is granted; or

(2) under subsection (d)(2) or (d)(3) of this section before the later of—

(A) one year after the granting of such discharge; and

(B) the date the case is closed.

C. Issues that May Arise

1. Actions Against Insiders

One of the most common source of issues to address in a Chapter 7 case would be actions against insiders of the estate. The concept of insider is defined by *11 U.S.C. § 101(31).* These insiders are of a

particular interest to the bankruptcy Trustee as certain payments and transfers to these individuals would be subject to surrender back to the estate.

> 11 U.S.C. § 101(a)(31).
>
> (31) The term "insider" includes— (A) if the Debtor is an individual— (i) relative of the Debtor or of a general partner of the Debtor; (ii) partnership in which the Debtor is a general partner; (iii) general partner of the Debtor; or (iv) corporation of which the Debtor is a director, officer, or person in control; (B) if the Debtor is a corporation— (i) director of the Debtor; (ii) officer of the Debtor; (iii) person in control of the Debtor; (iv) partnership in which the Debtor is a general partner; (v) general partner of the Debtor; or (vi) relative of a general partner, director, officer, or person in control of the Debtor; (C) if the Debtor is a partnership— (i) general partner in the Debtor; (ii) relative of a general partner in, general partner of, or person in control of the Debtor; (iii) partnership in which the Debtor is a general partner; (iv) general partner of the Debtor; or (v) person in control of the Debtor; (D) if the Debtor is a municipality, elected official of the Debtor or relative of an elected official of the Debtor; (E) affiliate, or insider of an affiliate as if such affiliate were the Debtor; and (F) managing agent of the Debtor.

If you have prepared your client prior to filing and have done proper intake; any payments made to an insider can be avoided by simply getting the property back from the insider and exempting that item in Schedule C. The main issue we have is that, in many instances, your client may conveniently forget to mention a fact or did not understand what you were asking them at the initial consult. Inevitably, you will have cases like this that come across your desk a few times each year.

Moving forward, you must find out the relationship between the Debtor and the alleged insider. I have had situations in which the Debtor simply does not mind if the Trustee brings an action against the insider. The Debtor has no interest in helping to resolve the matter or negotiate on the insider's behalf. In that case, get the information to the Trustee and essentially allow the action to move forward and secure the discharge of your client's debts. Your obligation will always be to your client and their best interests.

In most instances, the Debtor is eager to protect the insider and wishes to negotiate in order to avoid any strife between them and the alleged insider. This is where things become a bit more complex as you essentially are prohibited from litigating on behalf of the Insider due to any possible conflicts of

interest. The leverage you seek may not be there to negotiate. This puts you and your client in a precarious position. Rule 1.7 of the Michigan Rules of Professional Conduct States:

> Rule 1.7 Conflict of Interest: General rule
> (a) A lawyer shall not represent a client if the representation of that client will be directly adverse to another client, unless:
> (1) the lawyer reasonably believes the representation will not adversely affect the relationship with the other client; and
> (2) each client consents after consultation.
> (b) A lawyer shall not represent a client if the representation of that client may be materially limited by the lawyer's responsibilities to another client or to a third person, or by the lawyer's own interests, unless:
> (1) the lawyer reasonably believes the representation will not be adversely affected; and
> (2) the client consents after consultation. When representation of multiple clients in a single matter is undertaken, the consultation shall include explanation of the implications of the common representation and the advantages and risks involved.

Although the client and the insider may agree to it and allow you to proceed on behalf of the insider, there are instances where conflict comes about. In these situations, it would be in the best interest of all parties to have separate attorneys on this matter.

a. Preferences

Under *11 U.S. Code § 547 and 500* certain payments on a debt owed to an insider within a year prior to the filing of the Debtor's bankruptcy case over $600 may be avoided and recovered by the Trustee for distribution to creditors listed in the case.

> 11 U.S.C. § 547(b)
> (a) In this section—
> (1) "inventory" means personal property leased or furnished, held for sale or lease, or to be furnished under a contract for service, raw materials, work in process, or materials used or consumed in a business, including farm products such as crops or livestock, held for sale or lease;
> (2) "new value" means money or money's worth in goods, services, or new credit, or release by a transferee of property previously transferred to such transferee in a transaction that is neither void nor voidable by the debtor or the trustee under any applicable law, including proceeds of such property, but does not include an obligation substituted for an existing obligation;
> (3) "receivable" means right to payment, whether or not such right has been earned by performance; and
> (4) a debt for a tax is incurred on the day when such tax is last payable without penalty, including any extension.

(b) Except as provided in subsections (c) and (i) of this section, the trustee may avoid any transfer of an interest of the debtor in property—

(1) to or for the benefit of a creditor;

(2) for or on account of an antecedent debt owed by the debtor before such transfer was made;

(3) made while the debtor was insolvent;

(4) made—

(A) on or within 90 days before the date of the filing of the petition; or

(B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and

(5) that enables such creditor to receive more than such creditor would receive if—

(A) the case were a case under chapter 7 of this title;

(B) the transfer had not been made; and

(C) such creditor received payment of such debt to the extent provided by the provisions of this title.

(c) The trustee may not avoid under this section a transfer—

(1) to the extent that such transfer was—

(A) intended by the debtor and the creditor to or for whose benefit such transfer was made to be a contemporaneous exchange for new value given to the debtor; and

(B) in fact a substantially contemporaneous exchange;

(2) to the extent that such transfer was in payment of a debt incurred by the debtor in the ordinary course of business or financial affairs of the debtor and the transferee, and such transfer was—

(A) made in the ordinary course of business or financial affairs of the debtor and the transferee; or

(B) made according to ordinary business terms;

(3) that creates a security interest in property acquired by the debtor—

(A) to the extent such security interest secures new value that was—

(i) given at or after the signing of a security agreement that contains a description of such property as collateral;

(ii) given by or on behalf of the secured party under such agreement;

(iii) given to enable the debtor to acquire such property; and

(iv) in fact used by the debtor to acquire such property; and

(B) that is perfected on or before 30 days after the debtor receives possession of such property;

(4) to or for the benefit of a creditor, to the extent that, after such transfer, such creditor gave new value to or for the benefit of the debtor—

(A) not secured by an otherwise unavoidable security interest; and

(B) on account of which new value the debtor did not make an otherwise unavoidable transfer to or for the benefit of such creditor;

(5) that creates a perfected security interest in inventory or a receivable or the proceeds of either, except to the extent that the aggregate of all such transfers to the transferee caused a reduction, as of the date of the filing of the petition and to the prejudice of other creditors holding unsecured claims, of any amount by which the debt secured by such security interest exceeded the value of all security interests for such debt on the later of—

(A)

(i) with respect to a transfer to which subsection (b)(4)(A) of this section applies, 90 days before the date of the filing of the petition; or

(ii) with respect to a transfer to which subsection (b)(4)(B) of this section applies, one year before the date of the filing of the petition; or

(B) the date on which new value was first given under the security agreement creating such security interest;

(6) that is the fixing of a statutory lien that is not avoidable under section 545 of this title;

(7) to the extent such transfer was a bona fide payment of a debt for a domestic support obligation;

(8) if, in a case filed by an individual debtor whose debts are primarily consumer debts, the aggregate value of all property that constitutes or is affected by such transfer is less than $600; or

(9) if, in a case filed by a debtor whose debts are not primarily consumer debts, the aggregate value of all property that constitutes or is affected by such transfer is less than $5,000.[1]

(d) The trustee may avoid a transfer of an interest in property of the debtor transferred to or for the benefit of a surety to secure reimbursement of such a surety that furnished a bond or other obligation to dissolve a judicial lien that would have been avoidable by the trustee under subsection (b) of this section. The liability of such surety under such bond or obligation shall be discharged to the extent of the value of such property recovered by the trustee or the amount paid to the trustee.

(e)

(1) For the purposes of this section—

(A) a transfer of real property other than fixtures, but including the interest of a seller or purchaser under a contract for the sale of real property, is perfected when a bona fide purchaser of such property from the debtor against whom applicable law permits such transfer to be perfected cannot acquire an interest that is superior to the interest of the transferee; and

(B) a transfer of a fixture or property other than real property is perfected when a creditor on a simple contract cannot acquire a judicial lien that is superior to the interest of the transferee.

(2) For the purposes of this section, except as provided in paragraph (3) of this subsection, a transfer is made—

(A) at the time such transfer takes effect between the transferor and the transferee, if such transfer is perfected at, or within 30 days after, such time, except as provided in subsection (c)(3)(B);

(B) at the time such transfer is perfected, if such transfer is perfected after such 30 days; or

(C) immediately before the date of the filing of the petition, if such transfer is not perfected at the later of—

(i) the commencement of the case; or

(ii) 30 days after such transfer takes effect between the transferor and the transferee.

(3) For the purposes of this section, a transfer is not made until the debtor has acquired rights in the property transferred.

(f) For the purposes of this section, the debtor is presumed to have been insolvent on and during the 90 days immediately preceding the date of the filing of the petition.

(g) For the purposes of this section, the trustee has the burden of proving the avoidability of a transfer under subsection (b) of this section, and the creditor or party in interest against whom recovery or avoidance is sought has the burden of proving the nonavoidability of a transfer under subsection (c) of this section.

(h) The trustee may not avoid a transfer if such transfer was made as a part of an alternative repayment schedule between the debtor and any creditor of the debtor created by an approved nonprofit budget and credit counseling agency.

(i) If the trustee avoids under subsection (b) a transfer made between 90 days and 1 year before the date of the filing of the petition, by the debtor to an entity that is not an insider for the benefit of a creditor that is an insider, such transfer shall be considered to be avoided under this section only with respect to the creditor that is an insider.

The purpose of this section is to protect from unfair distribution to creditors of the Debtor. Essentially, you can not treat a certain creditor differently from the rest of your creditors.

This is a fact pattern that happens all too often during tax time. The most common questions at the section 341 meeting of creditors hearing from the Trustee will be about the tax refund. "Did you receive a tax refund?", " How much was the refund?" and of course "Did you pay anyone back with that refund money?" Always make sure to address the tax refund money with your client prior to filing the case. Otherwise this very situation will almost inevitably happen to you a few times each year.

Another area I find all too often is when a Debtor in bankruptcy is living with a family member or friend and contributing to the household. Payments to the Insider are often considered by a Trustee as a possible preference payment under *11 U.S.C. § 547(b)*. Again, make sure you prepare your client prior to their hearing by asking thorough and comprehensive questions about the nature of any payments in association with a rental obligation. While there may not be a lease agreement, there may be an understanding of an amount or contribution to the household in lieu of specific rental obligations that adhere to month to month.

One way to cure a situation such as this would be to have the insider execute an affidavit stating their understanding of the payments made to them in conjunction with any agreement that they may have had with the Debtor.

b. Fraudulent transfers

Once every few months, one question I seem to get from a potential client looking to hire our firm is "Well what if I just transfer the house to my Dad" My response to that is ALWAYS no, no, no and again NO. Attempts by Debtors to hide assets from their creditors is clearly a common occurrence. As attorneys, it is our responsibility to try to clean these issues up prior to the filing of the case or recommend other nonbankruptcy alternatives. Again, many times the client either does not realize what you are asking them at the initial intake or just does not think anyone will find out. So, it is essential that you hammer

this point home to them at the initial consult. Make sure they know that they are not clever enough to outsmart the bankruptcy code. If they hide the asset, they will lose it.

No matter how well you investigate the case and communicate to the client the importance of full disclosure prior to filing, fraudulent transfer issues may come across your desk after a case has been filed.

The Trustee may avoid transfers if there was actual fraud or constructive fraud. Actual fraud happens when the Debtor transfers an asset with the specific intent to hinder, delay or defraud his creditors. Constructive fraud occurs when the Debtor made the transfer for less than reasonably equivalent value and the Debtor was insolvent or became insolvent soon after the transfer. In the instance of constructive fraud, there is no intent needed with the act of transferring the asset.

> 11 U.S. Code § 548. Fraudulent transfers and obligations
> (a)(1) The Trustee may avoid any transfer (including any transfer to or for the benefit of an insider under an employment contract) of an interest of the Debtor in property, or any obligation (including any obligation to or for the benefit of an insider under an employment contract) incurred by the Debtor, that was made or incurred on or within 2 years before the date of the filing of the petition, if the Debtor voluntarily or involuntarily—
> (A) made such transfer or incurred such obligation with actual intent to hinder, delay, or defraud any entity to which the Debtor was or became, on or after the date that such transfer was made or such obligation was incurred, indebted; or
> (B)(i) received less than a reasonably equivalent value in exchange for such transfer or obligation; and
> (ii)(I) was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation;
> (II) was engaged in business or a transaction, or was about to engage in business or a transaction, for which any property remaining with the Debtor was an unreasonably small capital;
> (III) intended to incur, or believed that the Debtor would incur, debts that would be beyond the Debtor's ability to pay as such debts matured; or
> (IV) made such transfer to or for the benefit of an insider, or incurred such obligation to or for the benefit of an insider, under an employment contract and not in the ordinary course of business.

i. State of Michigan Statute – Fraudulent Transfers

One thing to address with your client prior to the filing of the case is the Michigan Uniform Voidable Transactions Act, *MCL 566.31 et seq* via *11 U.S.C. § 544(b) . MCL 600.5813* allows for additional look back time of 6 years prior to the filing of the bankruptcy case. This needs to be made clear to the Debtor. The issue that usually comes up is that the Debtor may not have been insolvent at the time of the transfer that is at issue.

2. **Equity Issues**

There are several duties that the Chapter 7 Trustees has when assigned to a case. *See 11 U.S.C. § 704*. The primary duty of any Trustee in a Chapter 7 bankruptcy case is to distribute any non-exempt assets. Any non-exempt assets are to be turned over to the bankruptcy Trustee for administration in a Chapter 7 case.

> 11 U.S.C. § 704
> The Trustee shall—
> (1) collect and reduce to money the property of the estate for which such Trustee serves, and close such estate as expeditiously as is compatible with the best interests of parties in interest;
> (2) be accountable for all property received;
> (3) ensure that the Debtor shall perform his intention as specified in section 521(2)(B) of this title;
> (4) investigate the financial affairs of the Debtor;
> (5) if a purpose would be served, examine proofs of claims and object to the allowance of any claim that is improper;
> (6) if advisable, oppose the discharge of the Debtor;
> (7) unless the court orders otherwise, furnish such information concerning the estate and the estate's administration as is requested by a party in interest;
> (8) if the business of the Debtor is authorized to be operated, file with the court, with the United States Trustee, and with any governmental unit charged with responsibility for collection or determination of any tax arising out of such operation, periodic reports and summaries of the operation of such business, including a statement of receipts and disbursements, and such other information as the United States Trustee or the court requires; and
> (9) make a final report and file a final account of the administration of the estate with the court and with the United States Trustee.

There are several exemptions that can be used to protect the assets of the Debtor. *See 11 U.S.C. § 522*. But, many times there will be a question as to whether or not all of the items that a Debtor owns are protected by the code. As always, your diligence and preparation in the intake with a client will help you determine the exposure and ensure that they know what to expect post filing.

You will want to research the advantages of State exemptions in the case. One in particular is the use of the Michigan homestead exemptions. These homestead exemptions can be useful in increasing the available exemptions with a primary residence, whether using tenancy by the entirety or simply using the state exemption to protect a larger portion of the equity in the home. Make sure you evaluate the use of State exemptions prior to the filing of the case. *See M.C.L. 600.5451.*

As with any potential actions against an insider, in many situations the Debtor will not mind if the Trustee liquidates the property for the benefit of his creditors. This is always an option with a home in bankruptcy. As always, make sure your contracts and disclaimers prior to filing are clear with the client about the potential of this happening. As a reminder, the Debtor is obligated to assist the Trustee in the liquidation process. See 11 U.S.C. § 521(a)(3).

3. Prior Divorce Agreements

The State of Michigan is not a community property state, this means that marital assets are to be divided up equitably according to the circumstances of the Divorce *See MCL § 552.401*. If this division can be proven to be unfair and inequitable, the Trustee may be able to avoid this transfer. Again, this may be an issue when your client will simply throw his hands up and say "go ahead and get it". In the circumstances where the Debtor is concerned, you may need to deal with when it comes to the negotiation of property in the estate.

D. Negotiation of a possible Settlement

Now that we have discussed several common areas where a Trustee may be able to bring actions against insiders of the Estate and/or liquidation of assets, what do you do to help your client? How do we approach the issue to make this situation as easy as possible for them?

1. Equity in property

Once we establish the issues that may be on the forefront of the Trustee's inquiry, we must first discuss how to minimize risk and maximize results. The Debtor's equity in his house is the main issue we deal with now that the housing market has made a turnaround in the last 10 years. A house is clearly more to people than four walls and a roof. The possibility of losing their home terrifying for most people. You need to be compassionate toward the client and make sure he or she knows you will do whatever you can

to help. In negotiation regarding an asset that has an emotional attachment it is important to maintain a good bedside manner. Often times, a Debtor has a hard time "seeing the forest through the trees".

Many times, you would need to help them come to the realization that having to settle with the Trustee and pay to protect their home is a small sacrifice when compared to discharging the debt. Make sure to keep the client issues in perspective. This will help you to move the case forward and avoid the Debtor daring the Trustee to put the house on the market.

The fact that the Trustee has the ability to put the house and any other property of the estate up for sale leaves the Debtor in a difficult situation. However, here are some key points to remember when negotiating with the Trustee:

- If you are using Federal exemptions, you can change at any point in time during the case to State exemptions that allow for higher exemptions ceilings on a homestead.
- Always remember to run a liquidation analysis on any values for the home and make sure to take into account closing costs, realtor commissions, Trustee fee, and Trustee's professional fees.
- Make sure to get a realistic valuation from a realtor or if practical an appraisal. It's nice to have a low number as a bargaining tool. But, the bottom line is that if it's not realistic the Trustee will know and the Trustee may feel you are negotiating in bad faith.
- A house is only worth what someone is willing to pay for it. So, if your client is willing to take a risk, it may be worth allowing the Trustee to put the house on the market and ask for the first right of refusal on an accepted purchase agreement from a pre-approved buyer. If you truly believe the value you are using, this will allow you to let the Trustee see that your valuation is the proper amount and give your client the option of matching it before the sale. The Trustee

should be willing to move forward on that as they would much rather have your client buy it back or remortgage than wait anxiously to see if the house sale will actually close.

- A Chapter 7 Trustee might be willing to work out some sort of arrangement where your client pays a small amount for a few years until they rebuild their credit. Then, they are able to take on an equity line of credit to pay the Trustee off.
- Although it may be easier to just convert the case, the benefits of keeping the settlement payment in a Chapter 7 allow you more flexibility on payments plans, balloon payments and more or less creatively financing the settlement.

The main point here is that you need to try and get creative in working out a settlement agreement. At worst, your client will need to convert the case to a Chapter 13. The Chapter 7 Trustee (attorney) may be allowed an administrative claim in the case once it is converted to a Chapter 13. Just make sure to explore all viable options before you convert. You may be able to save your client a great deal of time and money.

2. Negotiating Preference payments and Fraudulent Transfer issues

It would seem to reason that the process of negotiating a settlement in an equity issue case would be the same as a case involving an insider. However, I have found that negotiating cases involving actions against insiders and other fraudulent transfers are easier to navigate. Here are some reasons why I believe you may have more leverage in negotiating these issues:

- The relationship between the Debtor and the insider can often times be more a strained relationship. As discussed above, the Debtor is often times more willing to just let the Trustee take any action they want against the insider.

- Even if you would find that the relationship is one that you would consider close between the two, the Trustee simply can't count on that. Their job is to maximize money to be paid to the creditors. The old expression of "a bird in the hand is worth two in the tree" applies here. The Trustee may be more willing to take a smaller amount now rather than proceed through litigation against the insider. Even if they obtain an Order, they still have to go through the process of collecting. If any of you have done any collection work, I'm sure you can attest that it is not an easy or pleasant experience.

E. 11 U.S. Code § 554. Abandonment of Property of the Estate

11 U.S.C. § 554 allows a party in interest to ask the court to order abandonment of any property of the estate as burdensome to the estate. This is of particular interest to Debtors whose cases may not be moving forward in an expeditious manner for a variety of reasons, such as lawsuits that the Trustee has taken over, sale of certain specific assets of the estate, etc. In particular, the Debtor may want the Trustee to abandon any real estate that is not subject to the Trustee's current investigation. With the exception of a market crash 10 years ago, property values have a tendency to rise in value. The Trustee in bankruptcy may benefit from the increase in value of a home from the time of filing up to and including the time that a property is sold. Therefore, you must monitor the estate even after discharge of the debt. If the Trustee, in essence, sits on the estate, and doesn't take any action aside from filing timely reports, it's on the Debtor to bring a motion to compel the abandonment of the property.

> 11 U.S.C. § 554. Abandonment of property of the estate
> (a) After notice and a hearing, the Trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate.
> (b) On request of a party in interest and after notice and a hearing, the court may order the Trustee to abandon any property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate.
> (c) Unless the court orders otherwise, any property scheduled under section 521(a)(1) of this title not otherwise administered at the time of the closing of a case is abandoned to the Debtor and administered for purposes of section 350 of this title.
> (d) Unless the court orders otherwise, property of the estate that is not abandoned under this section and that is not administered in the case remains property of the estate.

Even if the Trustee has not expressed any interest in the Real Estate or other property of the estate and if there is no abandonment of the property; the Trustee can come back and sell that property if you do not take action. Make sure to monitor the property of the estate from start to finish whether or not the Trustee takes action.

Fee Agreements in Chapter 7 Cases

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Fee Agreements

A. The importance of a written fee agreement

A fee agreement is important for a number of reasons, not the least of which is that § 528 of the Bankruptcy Code requires every "debt relief agency"[1] to execute a written contract with an "assisted person"[2] not later than 5 days after providing "bankruptcy assistance".[3] The contract must specify clearly and conspicuously the services the agency will provide, the fees for such services, and the terms of payment. *See* 11 U.S.C. § 528(a).

Even if not required by statute, a written statement concerning fees is recommended for the simple reason that it reduces the possibility of misunderstanding.

But regardless of how detailed the § 528 written contract is, it will not protect your unpaid fees from being discharged. *See Bethea v. Robert J. Adams & Assocs*, 352 F.3d 1125 (7th Cir. 2003); *Rittenhouse v. Eisen*, 404 F.3d 395 (6th Cir. 2005). The Bankruptcy Code specifically identifies the types of pre-petition debts that survive discharge in § 523(a), and the debt for services rendered under a pre-petition fee agreement is not one of them.

B. Types of fee agreements

Before addressing the issue of how to get paid for services rendered post-petition, it is important to understand the types of retainers that apply to legal fees.

(1) A classic retainer, also referred to as a true or general retainer, is paid to secure the lawyer's availability, not to compensate the lawyer for services to be rendered. *In re McDonald*

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[1] Attorneys are "debt relief agencies." *See Milavetz, Gallop & Milavetz, P.A. v. United States*, 559 U.S. 229, 236-37 (2010)

[2] An "assisted person" is "any person whose debts consist primarily of consumer debts and the value of whose nonexempt property is less than $192,450." 11 U.S.C. § 101(3).

[3] "'Bankruptcy assistance' means any goods or services sold or otherwise provided to an assisted person with the express or implied purpose of providing information, advice, counsel, document preparation, or filing, or attendance at a creditors' meeting or appearing in a case or proceeding on behalf of another or providing legal representation with respect to a case or proceeding under [title 11]." 11 U.S.C. § 101(4A).

Bros. Constr., Inc., 114 B.R. 989, 998 (Bankr. N.D. Ill. 1990). The classic retainer is earned when paid and immediately becomes the lawyer's property. A classic retainer, paid pre-petition, is outside the estate and outside the purview of § 330, though it remains subject to disclosure and reasonableness review under § 329 of the Bankruptcy Code. *Barron v. Countryman*, 432 F.3d 590, 595-96 (5th Cir. Tex. 2005).

(2) A security retainer is paid for prospective services. This type of retainer remains the property of the client and must be deposited in a trust account and kept separate from the lawyer's own property until the lawyer applies it to services that are actually rendered. Because the debtor retains an interest in these funds, they become property of the estate at filing subject to §§ 329 and 330. *See McDonald Bros.*, 114 B.R. at 1000-02; *In re James Contracting Grp., Inc.*, 120 B.R. 868, 872 (Bankr. N.D. Ohio 1990).[4]

(3) An advance payment retainer, also known as a flat or fixed fee, is a payment to the lawyer in exchange for the commitment to provide legal services in the future. Whether ownership of these funds passes immediately to the lawyer upon payment or remains with the client depends on the jurisdiction. A number of courts follow the rule that an advanced payment retainer is earned upon receipt; thus, it is the lawyer's property and does not flow through a trust account. *See McDonald Bros.*, 114 B.R. at 1000-02; *White v. Coyne, Schultz, Becker & Bauer, S.C. (In re Pawlak)*, 483 B.R. 169, 177 (Bankr. W.D. Wis. 2012); *In re Blackburn*, 448 B.R. 28, 38 (Bankr. D. Idaho 2011); *Barron*, 432 F.3d at 596. Because it is the lawyer's property; the advance payment retainer does not become property of the estate when a case is filed. Although the trend seems to

[4] The issue of whether a debtor's interest in a retainer is property of the estate is a question of federal law. *McCarthy, Johnson & Miller v. N. Bay Plumbing, Inc. (In re Pettit)*, 217 F.3d 1072, 1078 (9th Cir. 2000). However, bankruptcy courts must look to state law to determine whether and to what extent the debtor has any legal or equitable interests in property as of the commencement of the case. *See Butner v. United States*, 440 U.S. 48, 55 (1979) ("Property interests are created and defined by state law.").

be moving toward allowing ownership of advance payment retainers to pass immediately to the lawyer, there are still cases that hold otherwise. *See, e.g., In re Doors & More, Inc.*, 127 B.R. 1001 (Bankr. E.D. Mich. 1991) [5]; *In re Printing Dimensions, Inc.*, 153 B.R. 715, 720-22 (Bankr. D. Md. 1993); *In re NBI, Inc.*, 129 B.R. 212, 221 (Bankr. D. Colo. 1991); *In re Hathaway Ranch P'ship,* 116 B.R. 208, 216-17 (Bankr.C.D. Cal. 1990).

One thing is clear: a lawyer who charges a soon-to-be debtor a security retainer must either deplete the retainer before filing the petition or turn over any balance remaining on the petition date to the Chapter 7 trustee.[6] Either way, the attorney may not collect for any post-petition services under the pre-petition retainer agreement. The better option, in those jurisdictions recognizing earned-upon-receipt advance payment retainers, is to charge a flat fee that does not have to pass through a trust account. But even then, it is difficult to determine the appropriate fee to charge given the uncertainty of the amount of services that will be required post-petition, and the fees are still subject to review for reasonableness under § 329 and ethical guidelines.

C. Limited Scope Representation ("Unbundling")

Instead of handling a bankruptcy case in its entirety, some lawyers provide limited scope representation, limiting the parts of a case that the lawyer will handle. Limited scope services are also known as "unbundled" services. Filing only a bare-bones petition and schedules is an example of limited scope representation.

Whether a lawyer may provide limited scope representation in a bankruptcy case, and to what extent, depends on two bodies of rules. The first is the ethical rules of the particular

[5] However, in 2008, the Michigan Supreme Court held that, a non-refundable retainer is permissible so long as the fee agreement memorializing the retainer is unambiguous. *Griev. Adm'r v. Cooper*, 757 N.W. 2d 867 (Mich. 2008). *Contra In re O'Farrell*, 942 N.E.2d 799, 807 (Ind. 2011) (finding lawyer violated Rule 1.5(a) by charging and collecting flat fees that were wholly nonrefundable.)

[6] The retainer must be disclosed on Schedule B and, if possible, should be claimed as exempt on Schedule C.

jurisdiction in which the lawyer practices. Some ethical rules do not allow attorneys to provide limited scope representation; others allow it only under certain conditions. Most jurisdictions do require attorneys to outline clearly in their written retainer agreements what activities they will and won't provide for the fees charged.

The second is the rules of the particular bankruptcy court in which the attorney is practicing. Most bankruptcy courts have "local" rules dealing with issues not addressed by the Federal Rules of Bankruptcy Procedure. Some courts have rules that directly address limited scope representation.

The ABA Model Rules of Professional Conduct, largely adopted in some form in most states, permit limited scope representation under certain, defined circumstances. On September 20, 2017, the Michigan Supreme Court adopted rules providing clearer direction to attorneys offering limited scope representation. These rules became part of the Michigan Rules of Professional Conduct, effective January 1, 2018. The primary Rules on the subject of limited scope representation are Rule 1.1 (requiring competent representation), Rule 1.2(b) (permitting limited scope representation if reasonable and client gives informed consent), Rule 1.4(b) (requiring proper communication), and Rule 1.5(a) (prohibiting a lawyer from charging or collecting an unreasonable fee).

1. Limitation of Representation by Task

Several district courts and bankruptcy courts have local rules addressing the obligations a lawyer takes on by appearing in a case. Some rules provide that attorneys who appear in a case must represent debtors in all related matters, including adversary proceedings. *See, e.g.,* Bankr. E.D.M. Local Rule 9010-1 (requiring debtor's attorney to attend and represent the debtor at the meeting of creditors, any hearing on reaffirmation agreements and all hearings within the scope of

representation.) Others exclude representation in adversary proceedings from those duties imposed merely by appearing in the case. *See, e.g.,* Bankr. N.D. Ill., Local Rule 2090-5(B); Bankr. W.D.N.C., Local Rule 2091-1.

Regardless of whether permissible by local rule, a lawyer seeking to limit the scope of representation must also fulfill ethical duties. It would seem almost impossible to fulfill those duties if the scope of representation is limited by task, particularly if the excluded task is routine or fundamental to the bankruptcy case.

Even if the lawyer gets past the duties of communication and informed consent by explaining in terms understandable to the client the tasks the lawyer will perform, those the lawyer won't perform, the potential problems that may arise in any given case, and the difficulties of addressing those problems as a pro se debtor, the attorney still has to provide competent representation.[7] And any limitation on the scope of services to be performed must be reasonable.[8]

At least one court has interpreted the ethical duty of competence to mean that the lawyer is required "to provide services that are necessary to achieve the basic fundamental objectives of the representation." *In re Egwim*, 291 B.R. 559, 572 (Bankr. N.D. Ga. 2003). In most if not all bankruptcy cases, the objective is to obtain a discharge. Given this broad objective, the attorney is arguably required to represent the debtor on any matters that might stand in the way of that discharge.

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[7] MRPC 1.1 provides: A lawyer shall provide competent representation to a client. A lawyer shall not: (a) handle a legal matter which the lawyer knows or should know that the lawyer is not competent to handle, without associating with a lawyer who is competent to handle it; (b) handle a legal matter without preparation adequate in the circumstances; or (c) neglect a legal matter entrusted to the lawyer."

[8] MRPC 1.2(b) provides: "A lawyer licensed to practice in the State of Michigan may limit the scope of a representation, [] if the limitation is reasonable under the circumstances and the client gives informed consent, preferably confirmed in writing."

Even if the duty of competence poses no obstacle, the limited representation still has to be reasonable. What is reasonable? Is it reasonable to exclude amending schedules if the debtor omitted an asset, whether by mistake or on purpose? Is it reasonable to exclude defending an objection to exemptions, particularly when the debtor relied on the attorney to assert proper exemptions? Picking and choosing between tasks that will be performed and those that won't is a problematic and uncertain exercise.

So how can an attorney strike that delicate balance between protecting their economic interests while providing competent representation to clients?

2. Limitation of representation based on pre- and post-petition services

There is some support for limiting services in a bankruptcy case by the time they are rendered—pre-petition versus post-petition. *In re Slabbinck*, 482 B.R. 576 (Bankr. E.D. Mich. 2012); *see also Bethea*, 352 F.3d 1125. In *Slabbinck,* the court found a limitation on services reasonable where separate contracts were entered into for pre-petition and post-petition services. *In re Slabbinck*, 482 B.R. 576. Such a limitation is only permissible, however, when a debtor has been fully advised of

> (1) the specific services debtor's counsel will perform as part of the pre-petition agreement to represent the debtor; (2) the specific services debtor's counsel will perform post-petition; (3) the necessity of a separate post-petition agreement regarding payment of those services; (4) the consequences to the debtor if the debtor chooses not to retain counsel post-petition; and (5) the consequences to the debtor if debtor retains counsel post-petition i.e. that fees for post-petition services survive discharge. *In re Abdel-Hak*, No. 12-46329-MBM, 2012 Bankr. LEXIS 5393, 18 (Bankr. E.D. Mich. Nov. 16, 2012) (citations omitted).

But, although it may be appropriate to distinguish between services rendered and charged for pre-petition and those rendered and charged for post-petition, carrying out that distinction may prove difficult. In *Slabbinck*, the debtors agreed to the pre-petition/post-petition division of

services and fees. They signed the pre-petition agreement and signed the post-petition agreement. What happens if the debtor doesn't sign the post-petition agreement? Under the local rules of most courts, the attorney of record is still on the hook to represent the debtors in the case until an order is entered authorizing the lawyer to withdraw. Consequently, any legal services required between the petition date and the date of an order authorizing the lawyer's withdrawal must be performed without compensation (assuming the debtor receives a discharge). If the debtor objects to the withdrawal and a hearing is required, there will be further delay and thus the possibility that more services will be required pending withdrawal. And then there is also the possibility that the court will not permit the withdrawal.

Under MRPC 1.16, in a matter that does not involve a crime, fraud, or a fundamental disagreement, a lawyer may withdraw from representation if withdrawal can be accomplished without material adverse effect on the interests of the client, or if;

> (5) the client fails substantially to fulfill an obligation to the lawyer regarding the lawyer's services and has been given reasonable warning that the lawyer will withdraw unless the obligation is fulfilled;
>
> (6) the representation will result in an unreasonable financial burden on the lawyer or has been rendered unreasonably difficult by the client; or
>
> (7) other good cause for withdrawal exists.

In the Bankruptcy Court for the Eastern District of Michigan, an attorney who has appeared on behalf of a party may not withdraw without permission of the court. L.B.R. (E.D.M.) 9010-(g). Whether refusal to enter into a post-petition retainer agreement falls within one of the permissible reasons for withdrawal remains to be seen. But, since the alternative is to not get paid for post-petition work and there is no way of knowing how much post-petition work there may be, the best option is to divide the services and fees down the pre-petition/post-petition line.

D. Drafting the pre-petition fee agreement

Here are some recommendations for preparing your pre-petition fee agreement:

1. Clearly state that the fee is a flat fee and not a security retainer.

2. Explain that the flat fee is earned upon receipt, and that it will not be held in trust but instead deposited into the lawyer's operating account as it is the lawyer's property (if permitted in your jurisdiction).

3. Describe the specific services the lawyer will perform as part of the pre-petition agreement to represent the debtor and how the fees/expenses will be applied.

4. Describe the specific services the lawyer will *not* perform as part of the pre-petition agreement[9] but may perform under a post-petition agreement, if retained;

5. Explain that unless the debtor enters into a post-petition agreement after the case is filed, the lawyer will request permission from the court to withdraw from the case.

6. Explain what may happen if the debtor chooses not to retain the lawyer post-petition, including the technical aspects, legal ramifications, material risks, and available alternatives.

7. Explain that the debtor has the option of hiring any lawyer post-petition, and if the debtor exercises that option, the post-petition fees will not be discharged in the bankruptcy case.

8. At least one author cautions lawyers never to describe any retainer or flat fee as "non-refundable," even if it is to be earned upon receipt. *See* Douglas R. Richmond, *Understanding Retainers and Flat Fees*, 34 J. Legal Prof. 113, 142 (2009). He explains that any

[9] If a retainer agreement is silent or ambiguous on the subject of representing a debtor-client in bankruptcy adversary proceedings, the lawyer will be required to provide that representation. *See* Michigan Ethics Opinion RI-184, 1994 WL 27231 (Jan. 19, 1994).

fee may be reduced or ordered to be refunded if it is unreasonable; thus, branding any retainer or flat fee non-refundable is misleading.

> Describing a retainer or flat fee as non-refundable potentially violates Model Rule 1.5(a), which requires that all fees be reasonable; Model Rule 1.15(d), which controls lawyers' duty to return to clients any funds to which they are entitled and to account for such funds when requested to do so; Model Rule 1.16(d), which governs lawyers' duties upon termination of a representation; Model Rule 8.4(c), which prohibits 'dishonesty, fraud, deceit, or misrepresentation;' and even Model Rule 8.4(d), which forbids conduct that is 'prejudicial to the administration of justice'. *Id.*

In Michigan, however, the word "non-refundable" controls whether the fee becomes property of the attorney that is not subject to deposit into a trust account. *See Griev. Adm'r v. Cooper*, 757 N.W. 2d 867 (holding that a non-refundable retainer is permissible so long as the fee agreement memorializing the retainer is unambiguous); *Devolder v. Lee*, No. 14-10624, 2014 U.S. Dist. LEXIS 116212 (E.D. Mich. Aug. 21, 2014) (following *Cooper*, but noting criticism of non-refundable retainers).

9. Finally, even when charging flat fees, an attorney should keep contemporaneous time records and document expenses. Such records are essential if the attorney is called upon to demonstrate the reasonableness of their fees.

E. Fee Disclosure

1. 11 U.S.C. § 329(a)

11 U.S.C. 329(a) provides that "[a]ny attorney representing a debtor in a case under this title, or in connection with such a case, whether or not such attorney applies for compensation under this title, shall file with the court a statement of the compensation paid or agreed to be paid, if such payment or agreement was made after one year before the date of the filing of the

petition, for services rendered or to be rendered in contemplation of or in connection with the case by such attorney, and the source of such compensation."

***Mapother Mapother v. Cooper (In re Downs)*, 103 F.3d 472 (6th Cir. 1996):** the disclosure requirement under §329(a) applies to post-petition and pre-petition compensation or agreements.

2. Fed. R. Bankr. P. 2016(b)

Bankruptcy Rule 2016(b) provides that "[e]very attorney for a debtor, whether or not the attorney applies for compensation, shall file and transmit to the United States trustee within 14 days after the order for relief, or at another time as the court may direct, the statement required by §329 of the Code including whether the attorney has shared or agreed to share the compensation with any other entity. The statement shall include the particulars of any such sharing or agreement to share by the attorney, but the details of any agreement for the sharing of the compensation with a member or regular associate of the attorney's law firm shall not be required. A supplemental statement shall be filed and transmitted to the United States trustee within 14 days after any payment or agreement not previously disclosed."

3. Form of Fee Disclosure

Form B2030 is an official form issued under Fed. R. Bankr. P. 9009. The use of this Form may be required by local court rules or general orders, but it otherwise exists for the convenience of the parties and should be modified as needed. If debtor's counsel uses Form B2030 with no modification, counsel should be prepared to represent the debtor in connection with all aspects or the bankruptcy case.

In the Eastern District of Michigan, Local R. Bankr. P. 9010-1(d) requires debtor's counsel to use its Statement of Attorney for Debtor(s) Under F.R.Bankr.P. 2016(b).

The Western District of Michigan does not require a specific form; however, its Local Bankr. R. 2016-1 details the information that must be included in the required disclosure of compensation.

Pre-Petition Bankruptcy Fee Agreement—Chapter 7

This agreement explains the terms of your retention of _____, ("the Firm") as your attorney in your Chapter 7 bankruptcy case.

The Firm specializes in bankruptcy, but it cannot guarantee the outcome of your bankruptcy case. We will explain the process to you and describe what is likely to happen in your case. Please ask us any questions you have. Because bankruptcy cases are complex and may involve a number of hearings and negotiations, this agreement may not adequately cover all aspects of the case.

1. Flat Fee. A flat fee of $_____ must be paid to engage the services of the Firm. The fee is not a security retainer, but a fee earned upon receipt that will be deposited into the Firm's operating account. The flat fee is property of the Firm and will not be held in trust. An additional $_____ is required for the court filing fee.

2. Services. The Firm will provide the following limited services:

   a. analyze your financial situation, and render legal advice to determine whether to file a Chapter 7 petition in bankruptcy;

   b. prepare and file a Chapter 7 bankruptcy Petition, Bankruptcy Petition Cover Sheet, Notice to Individual Consumer Debtor, Form 21 Statement of Social Security Number, and a Creditor Matrix;

   c. prepare and file bankruptcy Schedules A-J, Statement of Financial Affairs, Statement of Intent, and Form 22A (Means Test);

   d. file your certificate of credit counseling after you have completed the required course;

   e. advise you of your duties as a debtor in bankruptcy;

   f. represent you with respect to any reaffirmation agreements (service required by Admin Order No 09-32, Eastern District of Michigan); and

   g. attend your first meeting of creditors (section 341 hearing) where you will be questioned under oath about your property interests and financial affairs.

   The following services are <u>not</u> part of this fee agreement:

   a. attendance at any Bankruptcy Rule 2004 examinations (similar to a deposition);

   b. attendance at any court hearings, except for hearings on reaffirmation agreements;

   c. preparation and filing of amended schedules or other bankruptcy forms, including the pre-discharge financial education certificate;

d. representation regarding reaffirmation agreements (if not a required performance);

e. representation in any objection to claim of exemptions;

f. representation in defending any motions for relief from stay, including motions for relief from the stay filed by secured creditor to foreclose on real property or repossess collateral;

g. representation in pursuing or defending any motions, including motions to compel abandonment of assets, motions to dismiss, or motions to avoid judicial liens on property;

h. representation for any type of tax advice, opinion, negotiation, or any other matters pertaining to the discharge of any tax under any state or federal law;

i. representation in any adversary proceedings

3. Post-Petition Representation. Many of the above services are necessary to obtaining a discharge and retaining exempt property. You must attend to them whether you do so on your own or with the representation of an attorney. If you desire to retain the Firm to represent you post-petition, the Firm requires that you enter into a post-petition fee agreement in the form attached as Exhibit "A". If the post-petition fee agreement is not signed, the Firm will ask the bankruptcy court for permission to withdraw from your case.

4. Credit Counseling. You must attend pre-petition credit counseling before the bankruptcy petition is filed. You must also attend post-petition counseling after the bankruptcy petition is filed and within the time frame allowed by statute. Your debts will not be discharged if a post-bankruptcy credit counseling certificate is not filed with the court within the statutory time frame.

5. Meeting of Creditors. Shortly after your bankruptcy is filed with the court, you will receive a notice of the time and place that your Meeting of Creditors will be held. You must appear at this meeting or your bankruptcy case will be dismissed. The purpose of this Meeting is to give the creditors and the trustee an opportunity to question you under oath about your assets and the information contained in your bankruptcy schedules. This meeting lasts about ten minutes but because several other meetings may be scheduled before yours, you can assume that the entire proceeding will last about an hour.

6. Full disclosure. You are required to completely disclose all of your assets and all liabilities, and to provide all documents and information requested by the Firm before the bankruptcy petition and schedules can be prepared and filed with the court. If you fail to schedule a debt, it may not be discharged in your bankruptcy.

7. Non-Dischargeable Debts. Certain debts cannot be discharged in bankruptcy. You will be liable to repay any debt not discharged by your bankruptcy. The debts listed below are common examples of the types of debts that cannot be discharged in bankruptcy. The list of non-

dischargeable debts may be expanded by legislation or court decisions, and the Firm has no control over the type of debts that may be or become non-dischargeable.

a. Certain types of taxes, custom duties, or debts to pay taxes or custom duties.
b. Student loans.
c. Debts owed for spousal or child support.
d. Debts owed to the spouse, former spouse, or child in a domestic relations proceeding.
e. Debts arising from a previous bankruptcy wherein discharge of that particular debt was waived.
f. Debts owed for money, property, services, extension-or-removal, or refinancing of credit, if obtained by false pretenses, or false representations, or actual fraud.
g. Consumer debts for luxury goods obtained within 90 days of the date of filing of the bankruptcy petition.
h. Cash advances obtained within 70 days of the date of the filing of the bankruptcy petition.
i. Debts owed for fraud or defalcation while acting in a fiduciary capacity, or embezzlement or larceny.
j. Debts owed for fines, penalties, or forfeitures payable to and for the benefit of governmental entity.
k. Debts owed for death or personal injury arising from the operation of a motor vehicle, boat, or aircraft while intoxicated by drugs or alcohol.

8. Liens. Filing bankruptcy does not automatically discharge or remove liens from any real estate. The Firm will not take any action to avoid (remove) any lien on real estate unless you enter into a written agreement to retain the Firm to do so.

9. Audits. You may be subject to an audit by the U.S. Trustee.

10. Delay. The Firm may charge additional fees if you wait longer than 60 days from the first date the Firm is retained to finalize the bankruptcy petition and schedules due to additional due diligence and other update work required to finalize the bankruptcy.

I have read this fee agreement, understand its contents and agree to its terms and conditions.

Dated: _____

_____ _____
Attorney Signature Client Signature

_____
Client Signature

Post-Petition Bankruptcy Fee Agreement—Chapter 7

The agreement explains the terms of your retention of _____ ("the Firm") as post-petition counsel in your Chapter 7 bankruptcy case

The Firm cannot guarantee the outcome of your bankruptcy case. Since bankruptcy proceedings are complex and may involve numerous kinds of hearings and negotiations, this letter may not cover all aspects of the case.

You have agreed to pay hourly for the Firm's services at the Firm's current hourly rates ranging from $___ to $___ depending on the attorney working on your case. Costs will be billed separately and may include court costs, courier services, postage, photocopies, facsimile, and telephone call charges. You will receive monthly statements showing the time expended and costs incurred on your case. All billing statements must be paid in full within 15 days after the statement date. Overdue balances will accrue interest at 12% per year, and you will be responsible for all costs of collection, including attorney fees, for any action necessary to collect the costs and fees incurred in the course of the Firm's representation. There will be a $30 charge for all checks returned for insufficient funds.

In return for the above fees, the Firm will represent you in all matters arising in your Chapter 7 bankruptcy case, including:

1. Attending any Bankruptcy Rule 2004 examinations;
2. Filing motions or responses to motions;
3. Attending court hearings after the initial Meeting of Creditors;
4. Recovering garnishments from creditors; and
5. Negotiating with your Trustee regarding your case.

This agreement does not include representation in any adversary proceedings. An adversary proceeding is a formal lawsuit which is litigated in the bankruptcy court. If an adversary proceeding is filed, we may discuss the possibility of the Firm representing you at that time, however, a retainer will be required in an amount to be established based upon the nature of the litigation and is payable in advance.

I have read this fee agreement, understand its contents and agree to its terms and conditions.

Dated: _____

_____ _____
Attorney Signature Client Signature

_____
Client Signature

POST-PETITION FEE AGREEMENT WITH RETAINER – CHAPTER 7

The purpose of this agreement is to explain and establish the terms of your retention of _____ ("the Firm") as post-petition counsel in your Chapter 7 bankruptcy case.

The Firm cannot guarantee the outcome of your bankruptcy case. Since bankruptcy proceedings are complex and may involve numerous kinds of hearings and negotiations, this agreement may not cover all aspects of the case.

You have agreed to pay an initial retainer in the amount of $_____. The retainer will be deposited into our Client Trust Account and held as an "evergreen" retainer, securing payment of prospective fees. You will be billed on a monthly basis at the Firm's usual hourly rate of $___-____, depending upon the attorney performing the services. Each monthly bill will be paid from the retainer on hand at the time the billing statement is generated. Upon receipt of the billing statement, you will be required to replenish the retainer in an amount necessary to restore the retainer balance to $_____. In the event a monthly bill exceeds the amount of the evergreen retainer, the balance due will be $_____ plus the difference of the billing statement. Any unused retainer will be refunded upon completion of the Firm's services. Overdue balances will accrue interest at 7% per year, and you will be responsible for all costs of collection, including attorney fees, for any action necessary to collect the costs and fees incurred in the course of the Firm's representation.

In return for the above fees, the Firm will render post-petition legal services for certain aspects of the bankruptcy case, including:

1. Attending any Bankruptcy Rule 2004 examinations:
2. Filing motions or responses to motions;
3. Attending Court hearings after the initial Meeting of Creditors;
4. Recovering garnishments from creditors; and
5. Negotiating with your Trustee regarding your case.

This agreement does <u>not</u> include representation in any adversary proceedings. An adversary proceeding is a formal lawsuit which is litigated in the bankruptcy court. If an adversary proceeding is filed, we may discuss the possibility of the firm representing you at that time, however, an additional retainer will be required in an amount which will be established based upon the nature of the litigation and is payable in advance.

By: _____
The Firm

I (we) have received a copy of this retainer agreement, understand its contents and agree to its terms and conditions.

Dated: By: _____

_____