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*Legal Challenges to the Client Communication Provisions of  
the Bankruptcy Abuse Prevention and Consumer Protection  
Act of 2005*

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April 24, 2008

**Abstract.** Congress passed the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) in an effort to improve the U.S. bankruptcy system by curtailing perceived abuses. Some of the act's consumer protection provisions circumscribe the speech of attorneys who assist clients on bankruptcy matters. Several U.S. district courts have found that selected restrictions in these provisions violate the First Amendment right to freedom of speech. This report describes the relevant BAPCPA provisions and discusses the recent court decisions.

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# **Legal Challenges to the Client Communication Provisions of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005**

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## Summary

Congress passed the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) in an effort to improve the U.S. bankruptcy system by curtailing perceived abuses. Some of the act's consumer protection provisions circumscribe the speech of attorneys who assist clients on bankruptcy matters. Several U.S. district courts have found that selected restrictions in these provisions violate the First Amendment right to freedom of speech. This report describes the relevant BAPCPA provisions and discusses the recent court decisions.

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## Background and Introduction<sup>1</sup>

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005<sup>2</sup> made significant changes to the United States Bankruptcy Code.<sup>3</sup> Many changes were intended to remedy perceived abuses of the bankruptcy system. Several of BAPCPA's provisions regulate communications of the newly created category of "debt relief agencies" by both mandating certain disclosures and restricting the content of certain forms of advice. These communication provisions are found in Sections 526, 527, and 528 of the Bankruptcy Code. Some examples of these provisions are prohibiting advice to incur debt in contemplation of bankruptcy (§ 526), requiring disclosures of the types of services available from credit counseling agencies (§ 527), and requiring advertising to include the statement indicating that the advertiser is a debt relief agency and helps people file for bankruptcy relief (§ 528).

The statute neither explicitly includes nor explicitly excludes attorneys from the category of "debt relief agencies." If attorneys are considered "debt relief agencies," they would be subject to BAPCPA's communication provisions. These provisions would both restrict and compel attorneys' speech. The resulting question is "To what extent does the Constitution permit the government to regulate attorneys' speech?"

Critics challenge the communication provisions as unconstitutional, arguing that they have a chilling effect on attorney speech.<sup>4</sup> In addition, they claim that these provisions impede the ability of attorneys to best protect their clients<sup>5</sup> and increase confusion among those receiving attorneys' advice.<sup>6</sup>

This controversy involves tensions that were evident during BAPCPA's enactment. The legislative history indicates that some believed that the communication provisions were necessary to prevent debtors from taking advantage of loopholes in the bankruptcy system and to reduce the number of unnecessary filings.<sup>7</sup> Banks and other lenders who supported the adoption of the communication provisions contended that these provisions were necessary to eliminate bankruptcy mills, which, they argued, allowed bankruptcy attorneys to handle their clients' cases without having sufficient attorney-client contact.<sup>8</sup> Some opponents of the provisions worried that their burdensome

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<sup>1</sup> The original report, dated June 27, 2007, was written by Rebecca Smith, Law Clerk, under the general supervision of Robin Jeweler, Legislative Attorney.

<sup>2</sup> P.L. 109-8, 119 Stat. 23 (2005).

<sup>3</sup> 11 U.S.C. § 101 et seq.

<sup>4</sup> Joyce E. Cutler, *BAPCPA Provisions Chill Lawyers' Speech, Create Conflicts, Experts Say at NCBJ Forum*, 18 BNA BANKRUPTCY LAW REPORTER 1019 (2006).

<sup>5</sup> Samuel L. Bufford and Erwin Chemerinsky, *Constitutional Problems in the 2005 Bankruptcy Amendments*, 82 AM. BANKR. L.J. 1, 14-18 (2008) [hereinafter Bufford & Chemerinsky].

<sup>6</sup> *Id.* at 12-13.

<sup>7</sup> H.Rept. 109-31 at 5 (2005).

<sup>8</sup> Robert Wann Jr., Note, "Debt Relief Agencies:" *Does the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 Violate Attorneys' First Amendment Rights?* 14 AM. BANKR. INST. L. REV. 273, 274 (Spring 2006) (quoting Marcia Coyle, *Debtor's Attorneys See Red in Bankruptcy Bill; They See Malpractice Premium and Overhead Hikes; Judges' Workload Would Increase*, 179 N.J.L.J. 1126, March 21, 2005, at 12).

requirements singled out attorneys representing consumer debtors and would ultimately lead experienced bankruptcy attorneys to curtail their practices.<sup>9</sup>

Although two U.S. district courts found that attorney plaintiffs did not have standing to raise constitutional challenges to the communication provisions of BAPCPA, other courts have found that the chilling effect on an attorney's speech was sufficient injury to convey standing.

No circuit court of appeals has yet considered the constitutionality of BAPCPA's communication provisions; however the issue has been presented to several district courts. A survey of these cases reveals that district courts have been increasingly willing to find that one or more of the communication provisions violate the First Amendment right to freedom of speech. Attorney plaintiffs have argued that they are not included in the definition of "debt relief agencies," which would mean that the communication provisions would not apply to them at all. Alternatively, they have argued that if they are considered "debt relief agencies," the communication provisions are unconstitutional as applied to attorneys.

## Legal Issues

District courts have addressed four legal issues raised by BAPCPA's definition of "debt relief agency" and the communication provisions imposed on those agencies:

- whether attorney plaintiffs have suffered a sufficiently concrete injury to have standing to bring their claims;
- whether attorneys are included in the definition of a "debt relief agency";
- whether the prohibition against advising an assisted person<sup>10</sup> to incur additional debt in contemplation of filing for bankruptcy violates the First Amendment; and
- whether the mandate to make certain disclosures to assisted persons violates the First Amendment.

## Threshold Issue: The Standing Requirement

The Constitution does not allow federal courts to give "advisory opinions." Instead there must be a "case or controversy" before a federal court has jurisdiction to render a decision on a matter brought before it.<sup>11</sup> Additionally, a party in the case must have some concrete injury that can be remedied by the court. Without that, a plaintiff lacks standing and will not be heard.

Initially, two courts declined to address the constitutional challenges raised by the attorney plaintiffs, finding that the plaintiffs did not have standing.<sup>12</sup> Noting that no party had enforced any

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<sup>9</sup> Thomas Yerbich, *The Coming Exodus of Consumer Counsel*, 22 AM. BANKR. INST. J. 10 (July/August 2003).

<sup>10</sup> Defined in 11 U.S.C. § 101(3) as "any person whose debts consist primarily of consumer debts and the value of whose nonexempt property is less than \$150,000."

<sup>11</sup> U.S. CONST. art. III, § 2. *See also* Geisenberger v. Gonzalez, 346 B.R. 678, 683 (E.D. Pa. 2006).

<sup>12</sup> *Geisenberger*, 346 B.R. at 681; *In re McCartney*, 336 B.R. 588, 592 (Bankr. M.D. Ga. 2006).

of the communication provisions against them, both courts found that the plaintiffs failed to show they suffered a sufficient personalized injury that could be addressed by the courts.

Other courts, however, have found that attorney plaintiffs had standing even though no enforcement action had been taken against them. These courts concluded that the mere enactment of BAPCPA was a sufficient injury due to the chilling effect the statute had on attorneys' speech.<sup>13</sup>

## The Communication Provisions: Judicial Interpretations

### 11 U.S.C. § 101(12A): Definition of "Debt Relief Agency"

BAPCPA defines the term "debt relief agency" as any person who provides bankruptcy assistance to an assisted person for payment or who is a bankruptcy petition preparer.<sup>14</sup> This definition contains certain exceptions, none of which expressly includes attorneys.<sup>15</sup>

On October 17, 2005, the date that BAPCPA became effective,<sup>16</sup> the Bankruptcy Court for the Southern District of Georgia, on its own limited motion, considered whether "the members of the Bar of this Court [are] 'debt relief agencies.'"<sup>17</sup> The court concluded that they were not. It then found that the Bankruptcy Code's provisions regulating those agencies did not apply so long as the activities of the admitted attorneys "fall within the scope of the practice of law and do not constitute a separate commercial enterprise."<sup>18</sup> Two other courts have also determined that attorneys do not fall within the BAPCPA's definition of "debt relief agency."<sup>19</sup> Other courts, however, have found that attorneys are included in the definition of "debt relief agencies," and, therefore, would be subject to the communications provisions that are not unconstitutional.<sup>20</sup>

<sup>13</sup> Olsen v. Gonzalez, 350 B.R. 906, 913-915 (D.Or. 2006), *reconsidered, adhering to original decision*, 368 B.R. 886 (D. Or. 2007); Zelotes v. Martini, 352 B.R. 17, 21-22 (D. Conn. 2006), *reconsidered, adhering to original decision*, 363 B.R. 660 (D. Conn. 2007); Milavetz v. U.S., 355 B.R. 758, 762 (D. Minn. 2006); Hersh v. U.S., 347 B.R. 19, 22 (N.D. Tex. 2006).

<sup>14</sup> 11 U.S.C. § 101(12A).

<sup>15</sup> 11 U.S.C. § 101(12A)(A)-(E).

<sup>16</sup> BAPCPA was enacted on April 20, 2005 and its provisions generally became effective 180 days later. P.L. 109-8 § 1501(a).

<sup>17</sup> In re Attorneys at Law and Debt Relief Agencies, 332 B.R. 66, 68.

<sup>18</sup> *Id.* at 71.

<sup>19</sup> *Milavetz*, 355 B.R. at 769 ("Moreover, the Court finds the debt relief agency provisions of BAPCPA inapplicable to attorneys."); In re Reyes, 361 B.R. 276, 281 (Bankr. S.D. Fla. 2007) ("[This] Court does not believe Congress intended the scope of the statute to include attorneys. If Congress wanted 'attorney' included in the definition, it could have accomplished same by adding the word to 11 U.S.C. § 101(12A).").

<sup>20</sup> *Olsen*, 350 B.R. at 912; *Zelotes*, 352 B.R. at 19; *Hersh*, 347 B.R. at 22-23; In re Irons, 379 B.R. 680, 685 (Bankr. S.D. Tex. 2007).

## 11 U.S.C. § 526(a)(4): Restrictions on Advice to Clients

BAPCPA prohibits a debt relief agency from advising assisted persons either to incur additional debt in contemplation of filing for bankruptcy or to pay an attorney or bankruptcy petition preparer fees in exchange for bankruptcy services.<sup>21</sup>

Attorney plaintiffs have had success in challenging the constitutionality of this provision. Four U.S. district courts have held that the provision violates the First Amendment's guarantee of freedom of speech.<sup>22</sup> These courts all concluded that the provision is too broad in scope because it restricts more speech than is necessary to prevent debtors from being able to manipulate the system. Therefore, the courts have reasoned, this restriction prevents attorneys from being able to best protect their clients. Advising a client to incur additional debt is not illegal so long as there is no intent to avoid repaying the debt.<sup>23</sup> There may be legitimate, non-abusive reasons to counsel a client to incur additional debt. A client might be able to at least postpone and possibly avoid bankruptcy by refinancing a mortgage at a lower rate. Purchasing a car with financing might be necessary to enable a client to continue to commute to a job.<sup>24</sup> Other legitimate reasons to incur additional debt include acquiring a secured loan or borrowing from family or friends to hire an attorney or pay the filing fee so as to begin the bankruptcy process and benefit from the protection of the automatic stay provisions.<sup>25</sup>

At least one court has also argued that the restriction could also be found unconstitutional because it is under-inclusive. Non profit organizations are excluded from the definition of "debt relief agency," and may, therefore, freely advise debtors to incur more debt in contemplation of bankruptcy.<sup>26</sup>

## 11 U.S.C. § 527: Required Disclosures of Information on the Bankruptcy Process

BAPCPA compels debt relief agencies to notify assisted persons of the following:

- the costs and benefits of proceeding under chapters 7, 11, 12, and 13 of the bankruptcy code;
- the types of services available from credit counseling agencies;
- the requirement that the assisted person provide only complete, accurate, and truthful information;
- the requirement that all assets and liabilities be disclosed;

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<sup>21</sup> 11 U.S.C. § 526(a)(4).

<sup>22</sup> *Olsen*, 350 B.R. at 916; *Zelotes*, 352 B.R. at 24-25; *Milavetz*, 355 B.R. at 765-66; *Hersh*, 347 B.R. at 25.

<sup>23</sup> *Bufford & Chemerinsky*, *supra* note 6, at 16. *See also* Megan A. Taylor, Comment, *Gag Me with a Rule of Ethics: BAPCPA's Gag Rule and the Debtor Attorney's Right to Free Speech*, 24 BANK. DEV. J. 227, 246 (2008).

<sup>24</sup> *Hersh*, 347 B.R. at 24.

<sup>25</sup> *See Zelotes*, 352 B.R. at 24.

<sup>26</sup> *Olsen*, 350 B.R. at 916.

- the requirement that an assisted person be able to choose to hire an attorney, hire a bankruptcy petition preparer, or represent himself or herself, but that only attorneys and not petition preparers can render legal advice;
- information on the process of filing for bankruptcy; and
- information on how to value assets, complete bankruptcy schedules, and determine what property is exempt.<sup>27</sup>

Each of the two courts to have considered the question have found that the disclosure requirements in Section 527 pass constitutional muster.<sup>28</sup> Both courts reasoned that subjecting attorneys to regulation of their professional activities is justified by the government's significant interest in ensuring that debtor clients are adequately informed.<sup>29</sup>

The courts applied intermediate scrutiny analysis: (1) Is there a substantial government interest? (2) Does the legislation advance that interest? (3) Is the restriction reasonable in proportion to the interests served? Intermediate scrutiny is generally applied to restrictions on commercial speech, content neutral speech, and where there is an incidental burden on expression.

Some in the legal community question whether it was appropriate to apply intermediate scrutiny when analyzing the constitutionality of requiring the disclosures. Instead, they would argue that strict scrutiny should have been used since the speech was mandated and not content neutral.<sup>30</sup> Under a strict scrutiny analysis, the government interest must be compelling rather than significant and the statute must be narrowly tailored to advance that compelling interest. "Requiring a long list of lawyer disclosures ... cannot be reconciled with the First Amendment... [This provision] is [un]likely to survive the strict scrutiny applicable to mandated ... speech."<sup>31</sup>

## 11 U.S.C. § 528: Required Contract and Advertising Disclosures

BAPCPA mandates that a debt relief agency do the following:

- within five days of first providing bankruptcy advice to an assisted person, execute a written contract with the person describing the services that will be provided and the corresponding fees;<sup>32</sup>
- explain in its advertisements that its services are with respect to bankruptcy relief under the Bankruptcy Code;<sup>33</sup>
- include the following, or a "substantially similar," statement in its advertisements: "We are a debt relief agency. We help people file for bankruptcy relief under the Bankruptcy Code."<sup>34</sup>

<sup>27</sup> 11 U.S.C. § 527 (2006).

<sup>28</sup> *Hersh*, 347 B.R. at 27; *Olsen*, 350 B.R. at 917-19 (quoting *Hersh*, 347 B.R. at 26-27).

<sup>29</sup> *Hersh*, 347 B.R. at 27; *Olsen*, 350 B.R. at 918 (quoting *Hersh*, 347 B.R. at 27).

<sup>30</sup> Bufford & Chemerinsky, *supra* note 6, at 21.

<sup>31</sup> Bufford & Chemerinsky, *supra* note 6 at 22.

<sup>32</sup> 11 U.S.C. § 528(a)(1).

<sup>33</sup> 11 U.S.C. § 528(a)(3)

<sup>34</sup> 11 U.S.C. § 528(a)(4).

It appears that this provision of BAPCPA has not generated as many challenges as the other communication provisions. One district court has found § 528 to stand up under a four-pronged intermediate scrutiny analysis.<sup>35</sup> However, another court, applying the same test, held that the section “fail[ed] constitutional scrutiny” as applied to attorneys.<sup>36</sup> It found that the provision both failed to advance the government’s stated interest and was not narrowly drawn.<sup>37</sup>

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<sup>35</sup> *Olsen*, 350 B.R. at 919-20 (applying the test prescribed in *Central Hudson Gas & Electric Corp. v. Public Service Commission of N.Y.*, 447 U.S. 557, 566).

<sup>36</sup> *Milavetz*, 355 B.R. at 766-67.

<sup>37</sup> *Id.* at 767.