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Too Broke for a Fresh Start

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Consumer bankruptcy was designed to provide a "new opportunity in life and a clear field for future effort."[1] In addition to erasing unsecured debt and stopping wage garnishment, chapter 7 increases debtors' employment outcomes by 12 percent,[2] and often improves access to credit after discharge.[3] In short, the fresh start is a powerful poverty-fighting tool.

However, over the last decade, chapter 7's fresh start has become steadily less accessible for low-income Americans. Since the financial crisis, the number of individual chapter 7 filings has steadily decreased.[4] While many factors account for this drop, one of the most significant factors is also among the least discussed: the rising cost of filing. Since 2005, added regulations have significantly increased the costs of providing legal services to chapter 7 debtors. In many markets, the cost of filing has more than doubled, putting a chapter 7 discharge outside the reach of many low-income debtors.[5]

Debtors who cannot afford a chapter 7 attorney might file a deficient *pro se* petition, fall prey to an unscrupulous bankruptcy petition preparer, or file a "no-money-down" chapter 13 case that is (in some jurisdictions) likely to be dismissed without any lasting debt relief. Lacking funds for the filing and attorney fees, these financially stressed debtors might not be able to file at all in some cases. In turn, they suffer from the lack of housing, food and basic utilities that often accompany severe debt.

Attorneys' fees are only likely to increase in the coming years, leading to a worsening of the problem. While the goal of finding a *pro bono* attorney to represent indigent debtors is laudable, history has shown that there are never enough *pro bono* attorneys to meet the demand. In this article, the current "too broke for a fresh start" problem will be discussed, and two experiments to increase access to chapter 7 using technology, electronic self-representation and online legal aid will be explored.

The Rising Costs of Chapter 7

In 2005, Congress passed the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA), which made a number of changes to bankruptcy law that were intended to prevent abuse of the bankruptcy system. Under BAPCPA, Congress significantly increased the amount of documentation that a debtor must provide their trustee to obtain a discharge, imposed personal liability on debtors' counsel for the accuracy of a debtor's bankruptcy forms, and required debtors to attend paid financial counseling sessions before and after filing in order to obtain a discharge (among other things).[6]

These new requirements significantly increased the cost of providing chapter 7 representation.[7] Obtaining financial documents from debtors and fact-checking the provided information are both a challenging and time-consuming process. Because attorneys "have nothing to sell besides their time," the cost of the additional time incurred was necessarily passed on to debtors, as was the cost of the new bankruptcy courses.

As a result, between 2003 and 2009, the national mean attorneys' fee in no-asset chapter 7 cases increased 48 percent from $654 to $968.[8] This increase is likely underestimated for 2018, as the cost of chapter 7 now often reaches $2,000 in some markets. This rise in filing costs has priced many debtors out of the bankruptcy system and, in the view of some scholars, has generated a permanent drop in the chapter 7 filing rate.[9]

Consequences of Increased Costs

Low-income debtors who cannot afford to pay chapter 7 attorneys' fees up front often face one of four negative outcomes: (1) remaining stuck in debt outside bankruptcy protection; (2) filing deficient *pro se* petitions; (3) falling prey to fraudulent petition-preparers; or (4) filing a no-money-down chapter 13 case that is likely to result in dismissal without any lasting debt relief.

Living in Debt

The most common approach to the unaffordability of chapter 7 is simply "doing nothing." This approach avoids the cost of attorneys' and court fees, but is not without other costs. Debtors who need a fresh start but live outside bankruptcy protection often go without health care, food and utilities, and lose homes and other property.[10]

1 *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934).
2 Daphne Chen and Jake Zhao, "The Impact of Personal Bankruptcy on Labor Supply," 26 *Review of Economic Dynamics*, 40-61 (2017).
3 Julapa Jagtiani and Wenli Li, "Credit Access After Consumer Bankruptcy Filing: New Evidence," FRB of Philadelphia Working Paper No. 14-25, Aug. 7, 2014 (average credit score of chapter 7 filers in 2010 study went from 538 to 620 after discharge).
4 *See* "Caseload Statistics Data Tables," U.S. Courts, *available at* uscourts.gov/statistics-reports/caseload-statistics-data-tables (unless otherwise specified, all links in this article were last visited on Jan. 3, 2019).
5 Stefania Albanesi and Jaromir Nosal, "Insolvency After the 2005 Bankruptcy Reform," FRB of New York Staff Reports, April 2015.
6 Lisa Guerin, "The New Bankruptcy Law: The Bankruptcy Reform Act of 2005," The Bankruptcy Site, *available at* thebankruptcysite.org/bankruptcy-law-changes.
7 Lois R. Lupica, "The Consumer Bankruptcy Fee Study: Final Report," 20 *ABI Law Review* 17 (Spring 2012), *available at* abi.org/member-resources/law-review.
8 *Id.*
9 *See* Albanesi and Nosal, *supra* n.5.
10 *See generally* Pamela Foohey, Robert Lawless and Katherine Porter, "Life in the Sweatbox," 94 *Notre Dame Law Review* (2018).

The costs of remaining in debt are not just financial. Research indicates that living in a state of financial scarcity impedes the ability to lead a productive life because simply determining how one will survive day to day depletes mental resources for dealing with anything else, including one's job.[11]

Deficient *Pro Se* Petitions

Many debtors who cannot afford chapter 7 counsel attempt to file *pro se* by downloading forms from court websites and completing them on their own. The results are often poor, with missing forms, "chicken-scratch" schedules and incomplete creditor-counseling courses. These and other mistakes often lead to cases being dismissed for routine mistakes that could have been easily avoided with the assistance of counsel.

Unscrupulous Petition-Preparers

Steep attorney and court fees for chapter 7 also lead many debtors to bankruptcy petition-preparers, who promise a fresh start at rock-bottom prices. Although there are many competent petition-preparers,[12] too many provide debtors with inaccurate and incomplete schedules. *Pro Publica* recently documented an industry of petition-preparers in Los Angeles who violate bankruptcy law regulations and skirt enforcement by having multiple related individuals acquire a fractional interest in a property subject to foreclosure before filing a chapter 13 case for each individual, thereby delaying the foreclosure process for days or months.[13]

Bankruptcy courts in other parts of the nation with high numbers of *pro se* filings — such as Phoenix, Atlanta, Detroit and Milwaukee — also have similar fraud problems with unscrupulous petition-preparers who flout the unauthorized-practice-of-law rules and overcharge for their services, particularly for minority and immigrant debtors.[14] As Bankruptcy Judge **Maureen A. Tighe** (C.D. Cal.; Woodland Hills) told *Pro Publica*, "There are all these people [who] need the relief of the bankruptcy system, who can't afford it. And they fall prey to these fraudster [petition-preparers]. If we had adequate access to our legal system, there would not be this wonderful ripe field for picking by the fraud artists."[15]

No-Money-Down Chapter 13s

Lastly, many debtors who are unable to afford chapter 7 end up filing a no-money-down chapter 13 case that is likely to face dismissal without lasting debt relief. Data from a national study suggests that these filers pay $2,000 more and have their cases dismissed at a rate 18 times higher than if they had filed chapter 7.[16]

This problem is particularly prevalent among one segment of U.S. debtors: According to public data, low-income African-Americans in the South are far less likely to attain lasting debt relief from bankruptcy because steep up-front chapter 7 fees force them to choose chapter 13 plans that are ultimately more expensive and far more likely to fail.[17] Specifically, the odds of African-American debtors choosing chapter 13 instead of chapter 7 were more than twice as high as for Caucasian debtors with a similar financial profile.[18] Once they chose chapter 13, the odds of their cases ending in dismissal were about 50 percent higher.[19]

Once these debtors' cases are dismissed and they leave chapter 13 protection, they are often in a far worse financial position. The interest on their debt continues to compound, so they wind up paying the costs of bankruptcy anyway — attorney and court fees and a seven-year flag on their credit report — without receiving the main benefit of bankruptcy: a fresh start.

Potential Improvements

Given the severity of the current access problem, we must consider new approaches to make chapter 7 more accessible. The bad news is that there is no quick fix. All approaches must be balanced with the need to protect debtors who do

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11 Sendhil Mullainathan and Eldar Sharif, *Scarcity: Why Having Too Little Means So Much*, 1-52 (2013) (discussing how lack of valuable resource like money "captures the mind" and reduces a person's IQ by equivalent of 13-14 points).
12 Hon. Maureen A. Tighe, "Seeking Innovation to Address Low-Income Access to Bankruptcy," XXXVII *ABI Journal* 11, 38-39, 60, November 2018, *available at* abi.org/abi-journal.
13 Paul Kiel, "How to Get Away with Bankruptcy Fraud," *Pro Publica*, Dec. 22, 2017.
14 *Id.*
15 *Id.*
16 Katherine Porter, Pamela Foohey, Robert Lawless and Deborah Thorne, "'No Money Down' Bankruptcy," 90 *S. Cal. L. Rev.* 1055 (2017). For condensed version of this article, *see* Pamela Foohey, Robert M. Lawless, Katherine Porter and Deborah Thorne, "Attorneys' Fees and Chapter Choice: Exploring 'No Money Down' Chapter 13 Bankruptcy," XXXVI *ABI Journal* 6, 20, 62-63, June 2017, *available at* abi.org/abi-journal.
17 Paul Kiel, "How Our Bankruptcy System Is Failing Black Americans," *Pro Publica*, Sept. 27, 2017.
18 *Id.*
19 *Id.*

Problems in the Code: "Substantial Contribution" Test for Indenture Trustees

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receive payment only from either the exercise of the charging lien or upon satisfaction of the substantial contribution test in § 503(b)(3)(D) and (b)(4).[12]

The court approved the payments, stating that the parties provided a substantial contribution,[13] further stating that it could authorize the indenture trustees' fees outside of § 503 and without court review as to reasonableness, citing *In re Adelphia Communications Corp.*[14] While the court said it did not reject the reasoning of *Adelphia*, it concluded that § 503 was satisfied.[15]

This ruling followed *Lehman I*,[16] where the plan provided for the payment of indenture trustees' professional fees under § 1129(a)(4) for their service on the official creditors' committee.[17] The U.S. Trustee objected to payment under § 1129(a)(4), arguing that the trustees had to satisfy § 503(b)(3)(D) and (b)(4).[18] However, the court disagreed with the U.S. Trustee and allowed payment under the plan, following the decisions in the *Adelphia* and *AMR* cases that allowed payments under §§ 1104(a)(4) and 1123(b)(6).[19]

In reversing on appeal, the district court held that § 503(b) is the "sole source of administrative expenses," requiring indenture trustees (and others) that seek administrative expense payments for work on a creditors' committee to satisfy the substantial-contribution standard.[20] However, this decision is inconsistent with the aforementioned decision in *Southeastern Grocers*.

A Legislative Solution: Remove the "Substantial Contribution" Requirement

To avoid inconsistent approaches, § 503(b)(4) and (b)(5) should be amended to delete the requirement that indenture trustees must make a substantial contribution in order to be reimbursed directly from the debtor's bankruptcy estate. This would not only resolve the inconsistent standards placed on indenture trustees in having fees and expenses approved, it would provide fair treatment to indenture trustees *vis-à-vis* other administrative creditors. Indenture trustees should only be required to satisfy the same standard for administrative expense claims as other administrative creditors. abi

12 *See id.* at 34-35, 80-81 (court discussing U.S. Trustee's argument regarding payment via charging lien or via showing of "substantial contribution").
13 *See id.* at 36-37.
14 441 B.R. 6 (Bankr. S.D.N.Y. 2010).
15 *Id.*
16 *In re Lehman Brothers Holdings Inc.*, 487 B.R. 181 (Bankr. S.D.N.Y. 2013), *rev'd*, 508 B.R. 283 (S.D.N.Y. 2014).
17 *Id.*
18 *Id. See* U.S. Trustee's Objection to the Fifth Amended Joint Plan of Reorganization of Energy Future Holdings Corp., *et al.*, Pursuant to Chapter 11 of the Bankruptcy Code and the Motion of Energy Future Holdings Corp., *et al.*, to Approve a Settlement of Litigation Claims and Authorize the Debtors to Enter into and Perform Under the Settlement Agreement, *In re Energy Future Holding Corp., et al.*, Case No. 14-10979 (Bankr. D. Del. 2014) ECF No. 6705.
19 *Id.* at 190-93. *See Adelphia*, 441 B.R. at 22-23; *In re AMR Corp.*, 497 B.R. 690 (S.D.N.Y. 2013).
20 *Davis v. Elliott Mgmt. Corp. (In re Lehman Bros. Holdings Inc.)*, 508 B.R. 283, 290 (S.D.N.Y. 2014). *Davis* could be narrowly viewed in that it did not address whether indenture trustees could be paid for their work in a case unrelated to service on the creditors' committee.

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file. However, there is good news: There are experiments that can be quickly implemented and tested to measure their efficacy. Two such experiments are electronic self-representation (eSR) and online legal aid.

Electronic Self-Representation

To improve access to chapter 7 for low-income filers, the Administrative Office of the U.S. Courts is piloting an eSR system in the U.S. Bankruptcy Courts for the Central District of California, District of New Jersey and District of New Mexico.[20] This is a free online tool to help individuals complete a chapter 7 petition upon deciding to file for bankruptcy without an attorney. Similar to "Turbotax for bankruptcy," eSR allows debtors to answer questions that complete all relevant bankruptcy forms. There are helpful prompts and definitions, as well as the ability to save the document online for review with an attorney at a self-help desk or finish filling out as time allows. The debtor is allowed to file electronically, although local forms and payment must be dropped off by the debtor in person at the courthouse.

Critics of eSR note that in making a simple online filing system available, the bankruptcy courts using it might be seen as endorsing self-representation and encouraging debtors to undertake significant legal decisions without counsel.[21] However, bankruptcy court websites using eSR repeatedly warn debtors of the risks of *pro se* filings and the need for representation by counsel where feasible.[22] According to the most recent data available in the Central District California, 81.5 percent of eSR debtors have received a chapter 7 discharge.[23] This discharge rate is significantly better than that of *pro se* chapter 7 filings undertaken without the benefit of eSR.[24] In addition, eSR will be rolled out to all bankruptcy courts using the NextGen system over the next few years, allowing for the measure of its efficacy and efficiency.

Online Legal Aid

Brick-and-mortar legal-aid organizations have long provided free legal assistance to low-income Americans.

20 *See* "Electronic Self-Representation (eSR) Bankruptcy Petition Preparation System for Chapter 7," U.S. Bankruptcy Court (C.D. Cal.), *available at* www.cacb.uscourts.gov/esr.
21 Andrew Mansfield, "eSR: A False Sense of Safety and Competence?," *Central District of California Bankruptcy Law Blog*, Dec. 9, 2016, *available at* mansfield.law/bankruptcyblog.
22 For example, the U.S. Bankruptcy Court for the Central District of California's website provides the following warning: "Bankruptcy has serious long-term financial and legal consequences and hiring a competent attorney is strongly recommended. The Bankruptcy Court is not permitted to provide legal advice. Individuals filing for bankruptcy without an attorney are still responsible for knowing and following all of the legal requirements. Low or no cost legal resources are available in all divisions of the bankruptcy court." *See* "Electronic Self-Representation (eSR) Bankruptcy Petition Preparation System for Chapter 7," *supra* n.20.
23 "*Pro Se* Report: 2015-2016," U.S. Bankruptcy Court for Central District of California, p. 11.
24 *Id.*

However, their resources are limited and most cannot provide bankruptcy assistance in significant volumes.

In 2016, the nonprofit Upsolve was founded out of Harvard Law's Access to Justice Lab to remedy this problem. Upsolve is an online legal aid organization that provides chapter 7 assistance for low-income debtors who need a fresh start but cannot afford counsel. This service was designed with input from an advisory board of leading bankruptcy academics, judges, trustees and practitioners. Similar to eSR, Upsolve is free, thanks to federal funding from the Legal Services Corp. (LSC).[25]

To start the process, debtors are screened online or by Upsolve's network of brick-and-mortar legal-aid organizations across the U.S. Once qualified, debtors enter their financial information and upload financial documents on Upsolve's website. The website asks debtors a series of questions using plain language and visual depictions of complex concepts. These approaches were originally designed by Profs. **Lois R. Lupica** of the University of Maine School of Law (who served as ABI's Resident Scholar in the fall of 2014), D. James Greiner of Harvard Law School and **Dalié Jiménez** of the University of California-Irvine School of Law (a 2018 ABI "40 Under 40" honoree) in connection with the Financial Distress Research Project.[26]

Next, Upsolve attorneys review the resulting bankruptcy forms for accuracy and reach out to the debtor with questions before the debtor files *pro se* by bringing the forms to the courthouse. Their cases are then tracked on PACER after the filing, and debtors are assisted with amendments and other support when necessary.

By using technology and allowing for remote access, Upsolve can help traditional brick-and-mortar legal-aid offices expand their service capacities. During 2018, Upsolve assisted more than 300 chapter 7 debtors with a 98 percent discharge rate, which compares favorably to the national chapter 7 discharge rate of 96 percent.[27] Upsolve has been recognized by the American Bar Association as a top tool for improving access to justice.[28]

Although Upsolve offers an advantage over eSR's pure *pro se* model in the form of attorney review, it has a far more limited service capacity than eSR. Most significantly, Upsolve can only serve low-income debtors who cannot afford an attorney, and its policy is that if one can afford an attorney, one should be obtained. In addition, Upsolve currently cannot serve debtors who require joint filings, own real estate or expensive cars, are seeking to discharge student loan debt, or have other complicating factors requiring full representation.

Too Broke for a Fresh Start

Since BAPCPA, the cost of counsel for a routine chapter 7 case has increased beyond the reach of many people to pay for it.[29] As a result, many low-income Americans, particularly financially vulnerable minority communities, remain trapped in debt because they cannot access chapter 7.[30] *There is no reason to believe that this access problem will improve in the future*; in fact, just the opposite would appear to be true as bankruptcy attorneys' fees must keep pace with those in other areas of the law.

This crisis of being "too broke for a fresh start" has significant implications on public confidence in the bankruptcy system. Chapter 7 is "a worthless solution if you can't pay because you don't have money," according to one debtor in Indiana. "It's a sad realization that the legal system isn't there for us."[31] Put differently, the bankruptcy courts risk losing their legitimacy in the eyes of the public when chapter 7 can only be meaningfully accessed by debtors with money.

There are no easy answers to this access crisis. Good attorneys must be paid for their time, and efforts to expand the access for the truly broke must also ensure that debtors who do file have the help they need. However, these challenges should not stop us from experimenting with new approaches to improve access.

The approaches outlined in this article — and others not discussed here[32] — deserve to be tested with data so we can see what works for those who cannot afford counsel. As stewards of the bankruptcy system, we have an obligation to find a better path forward for low-income debtors. **abi**

25 In addition to LSC, Upsolve is funded by the Robin Hood Foundation, Public Welfare Foundation, Harvard University, and the foundations of Google Chairman Eric Schmidt and Facebook CEO Mark Zuckerberg.
26 *See* Greiner, Jiménez and Lupica, "Self-Help Reimagined," 92 *Indiana L.J.* 119 (2017).
27 *See* Paul Kiel, "Data Analysis: Bankruptcy and Race in America," *Pro Publica*, Sept. 27, 2017.
28 Stephen Rynkiewicz, "Best Web Tools of 2018," *ABA Journal* (December 2018), *available at* abajournal.com/magazine/article/best_legal_apps_2018.
29 *See* Albanesi and Nosal, *supra* n.5.
30 *See* Kiel, *supra* n.17.
31 Paul Kiel, "When You Can't Afford to Go Bankrupt," *Pro Publica*, March 2, 2018.
32 *See, e.g.*, Tighe, *supra* n.12 (exploring other options for increasing access to chapter 7 for low-income debtors, including certification of petition preparers); Daniel E. Garrison, "Liberating Debtors from 'Sweatbox' and Getting Attorneys Paid: Bifurcating Consumer Chapter 7 Engagements," XXXVII *ABI Journal* 6, 16, 66-68, June 2018, *available at* abi.org/abi-journal (arguing that bifurcation of attorneys' fees is a promising solution for increasing access to chapter 7).

Legislative Update: Cross-Border Professionals Respond to Chapter 15 Proposals

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Ltd. held that COMI should be determined as of the commencement of the foreign proceeding.[2] Other courts, including the district court in *Fairfield Sentry Ltd.*, held that a bankruptcy court should determine COMI as of the chapter 15 filing date. The Second Circuit resolved this issue and held that a court (1) should determine COMI as of the date of the filing of the chapter 15 petition, and (2) may consider actions taken in the foreign proceeding when determining COMI.[3]

Following the Second Circuit's ruling, foreign representatives from the offshore jurisdictions have on numerous occasions sought and obtained recognition under chapter 15 based on activities occurring in the foreign proceeding.[4] If the NBC's proposed amendment regarding COMI is adopted and those proceeding-based activities can no longer be considered when determining COMI, many offshore foreign proceedings will not be entitled to recognition.

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2 *See Millennium Global Emerging Credit Master Fund Ltd.*, 458 B.R. 63 (Bankr. S.D.N.Y. 2011).
3 *See In re Fairfield Sentry Ltd.*, 714 F.3d 127 (2d Cir. 2013).