

NEW MEXICO STATE BAR BANKRUPTCY SECTION NEWSLETTER

June 2004



NOTES FROM THE CLERK S OFFICE

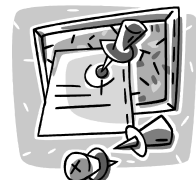
What's new in Court software development? The Clerk's Office is in the process of replacing its antiquated case management system. This is a 12 to 18 month project that involves almost all members of the Clerk's Office staff. This development effort should have very little direct impact on practitioners but it will provide many new resources for case management. This should improve the quality of case management and that benefits everyone. Unfortunately, the magnitude of this effort will require postponing ACE development issues like claims electronic filing and bulk case filing until after the new case management system goes live.

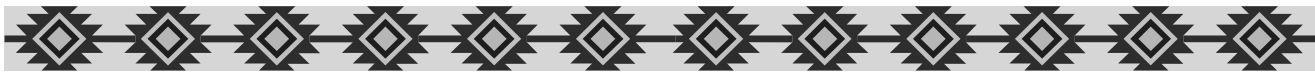
As always, the Clerk's Office needs your input. In particular, there are three opportunities for practitioners to comment:

1. The Clerk's Office has been "paperless" since January 2004. They are interested in hearing about how this has impacted your practice. An online survey is available on the Court's web site at www.nmcourt.fed.us/web/BCDOCS/bcindex.html or you can answer questions over the phone by contacting Sharon Kologie at 505-348-2443.
2. Judge Starzynski has initiated regular town hall meetings where practitioners have the opportunity to provide feedback on any aspect of Court operations. The next meeting will be held on Friday, July 9, 2004 from 3:30 to 5:00 in the Animas Courtroom. Details are outlined in the June 3, 2004 Notice to Practitioners.
3. The Clerk's Office has created a task force to address a proposal for mandatory electronic filing for attorney filers. If you are interested in participating in the task force, please contact Sharon Kologie at 505-348-2443.

The Clerk's Office continues to strive to provide excellent service. This is becoming increasingly difficult in the face of our mounting workload and limited budgets. We thank you for your consideration, and always appreciate your cooperation and help in achieving our mission.

Norman Meyer
Clerk of Court





SUPREME COURT DECIDES TWO CASES MAY 17, 2004

(from the American Bankruptcy Institute email newsletter)

Tennessee Student Assistance Corp. v. Hood

The Supreme held that the discharge of a debt, as an exercise of the bankruptcy court's in rem jurisdiction, does not infringe the state's sovereign immunity. The court did not address the underlying issue as to abrogation of the states sovereign immunity under section 106(a) of the bankruptcy Code.

The underlying case involved in adversary proceeding by the debtor, Pamela Hood, seeking the discharge of her student loans as constituting an "undue hardship" under section 523 (a) (8). A proof of claim was originally filed by Sallie Mae and later assigned to the Tennessee Students Assistance Corporation (TSAC). Because this was a no asset case, there was no active participation in the underlying bankruptcy case by TSAC, other than its acceptance of the assigned claim. Because the filing of a proof of claim has been held in previous cases to constitute submission to the bankruptcy court's jurisdiction, the debtor never advanced the argument that TSAC, as an agency of the state, waived its sovereign immunity. The Supreme Court, therefore, declined to address this specific issue.

The core holding focused on the nature of the bankruptcy court's jurisdiction with respect to the discharge of debts when it held that "a bankruptcy court's in rem jurisdiction permits it to 'determin(e) all claims that anyone, whether named in the action or not, has to the property or thing in question. The proceeding is 'one against the world'". In other words a state, regardless of its participation in the bankruptcy case, is bound by the bankruptcy court's discharge order and is no different than any other creditor whose debt is subject to that discharge.

Despite the acceptance of this basic concept, TSAC argued that the state's sovereign immunity was infringed upon by reason of the commencement of the adversary proceeding against TSAC and was therefore an unauthorized lawsuit within meaning of the 11th Amendment. The Supreme Court dismissed this argument, again focusing on the exercise of the bankruptcy courts jurisdiction over the res – not the persona of the state in this case.

While this case upholds the bankruptcy court's jurisdiction to determine the legal effect of a discharge in a bankruptcy case, there still remains for another day the all important issue of the application of section 106 (a) to issues involving sovereign immunity in proceedings where the state is seeking an affirmative recovery pursuant to a provision such as a preference action.

(Summary by Hon. Roger Whelan)

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Supreme Court decisions continued from page 2

Till vs. SCS Credit Corporation

The Supreme Court, apparently without resort to a calculator, decided the cram down interest issue by employing a formula approach.

Confronted by the difficult and arcane issue of what interest rate best satisfies the requirements of section 1325 (a) (5) (B) (ii) that the secured creditor receive "...the value, as of the effective date of the plan, of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim", the Court held that the so called formula approach (the prime rate plus a calculated risk factor) best meets the intent of Congress and the objectives of the bankruptcy Code.

The debtor's plan in this case, in dealing with a cram down of a secured claim that contained a pre-petition contract rate of interest of 21 %, proposed a three year plan payout of cash payments equal to the \$4,000 value of the collateral (a used truck) with a proposed interest rate of 9.5% (based on a national prime rate of 8% together with a court determined risk factor of 1.5%). The secured creditor countered with a contractual rate of its 21% pre-petition rate, because it represented the interest that "...it would obtain if it could foreclose on the vehicle and reinvest the proceeds in loans of equivalent duration and risk as the loan" originally made to petitioners.

Being confronted with four different approaches (the formula rate, the coerced loan rate, the presumptive contract rate, or the cost of funds rate) to determining the correct and appropriate interest rate, the Court determined that the least complicated approach and one most consistent with Congressional intent and promoting debtor rehabilitation, is the formula approach. The Court began by emphasizing that the Code does not set forth a defined "discount rate" or even the term "interest" in connection with the property to be distributed to the secured creditor over the lifetime of the plan. Rather, the sole command is to provide value of distributable property, as of the plans effective date, that is "...not less than the allowed amount of such claims;". In arriving at an appropriate discount rate for this "stream of differed payments", the Court held that "...we think Congress would favor an approach that is familiar in the financial community and that minimizes the need for expensive evidentiary proceedings." As a second consideration, the court recognized that there is a need to consider all "intervening changes and circumstances" when modifying the original terms of the, loan and finally, that the cram down provision requires resort to an objective rather than a subjective standard.

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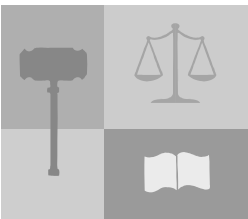


Supreme Court decisions continued from page 3

The analysis necessarily rejects the coerced loan approach, the presumptive contract rate and the cost of funds approach. The court instead adopted the formula approach by explaining that adherence to a “national prime rate” and, after a evidentiary hearing where the parties may present evidence about the “appropriate risk adjustment”, the court concluded that “...there is every reason that a properly risk-adjusted prime rate will provide a better estimate of the creditor’s current cost and exposure than a contract rate set in different times.”

Justice Scalia, in a well reasoned dissent, essentially argues that because all of the judges, (excluding Justice Thomas) argue that consideration of the risk factor is mandatory in determining a proper discount rate, adoption of the contract rate will best satisfy this requirement. When all is said and done the need for evidence on the critical element of risk will assure that even resort to a formula approach will not eliminate litigation.

(Summary by Hon. Roger Whelan)



**STAY HEARING PROCEDURES
FOR JUDGE STARZYNSKI’S COURT
(as of May 20, 2004)**

In an attempt to reduce the time and money that counsel and parties spend on prosecuting and defending stay relief motions, we are initiating the following procedures:

1. The current procedure for obtaining settings for stay hearings, set out in N.M.L.B.R. 9013-1(c) (eff. October 1, 1996), requires the moving party to request a setting from chambers. That procedure will continue.
2. It is also the current procedure that chambers will provide a setting for a preliminary hearing only, and that at the preliminary hearing, specific arrangements are made for the final hearing. This will continue to be the procedure used for ROSWELL AND LAS CRUCES cases. THE REST OF THIS (REVISED) PROCEDURE DEALS WITH ALBUQUERQUE CASES ONLY (although depending on circumstances and technology, the procedure may later be applied to Las Cruces also).
3. When a party calls chambers for a setting for a preliminary hearing on a stay motion, the party will ordinarily receive at that time two settings: one for the preliminary hearing and, if needed, one for the final hearing. The preliminary hearing will be set for a date within thirty days of the request (see N.M.L.B.R. 4001-1(b)), and the final hearing will be set for a date within thirty days of the preliminary hearing.

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Stay hearing procedures continued from page 4

4. The party obtaining the settings will be required to notice out both hearings, not just the preliminary hearing.

5. If the parties (creditor or other movant, debtor, and, as applicable, trustee and/or co-debtor) agree between or among themselves that they do not need a preliminary hearing, they may simply file an executed stipulation to that effect, continuing the automatic stay in effect until the final hearing. This stipulation will have the same effect as the order continuing the stay and setting a final hearing that usually results from the preliminary stay hearing. (Note that § 362(e) says “unless the court...orders such stay continued...” I believe this language is in the statute for the protection of the movant and thus can be waived by the movant. If instead of merely filing a stipulation, the parties wish to submit a stipulated form of order, requiring a judge’s signature, they may do so.)

6. We will assume, in the rare instance of a failure by any of the parties to appear at a preliminary hearing, that they have agreed to go directly to the final hearing with the stay remaining in place until further order of the Court. Notwithstanding the preceding sentence, when you stipulate to bypass the preliminary hearing, please notify us right away.

7. Any agreement between the parties to skip the preliminary hearing must be exactly that: an agreement. If one party does not want to skip the preliminary hearing (an example being the creditor wanting to obtain stay relief on a vehicle which the debtor has not insured), then the preliminary hearing will still take place. Should one party appear but not the other, then the usual practice in my court will prevail: if the creditor fails to appear, the stay motion will be denied; if the debtor fails to appear, then the matter will go on to the final hearing and debtor or counsel will face an order to show cause for the failure to appear. Note: there are times when the stay is modified at the preliminary hearing, such as for an uninsured vehicle (see Court Policies: The Main List, # 17 from my chamber’s website at www.nmcourt.fed.us.) or for some other reason. Nothing in this Notice to Practitioners is intended to change that policy.

8. If the parties wish to change the time for the final hearing to some date other than that received from chambers, they should either appear at the preliminary hearing and raise that issue, or, preferably, contact chambers to obtain an alternative setting. In the absence of an agreement between the parties or a court order for a new final hearing setting, the setting originally given by chambers will be the operable one. A creditor’s (movant’s) agreement to a final hearing date outside the thirty-day time limit provided by § 362(e) will be deemed to be a waiver of the thirty-day time limit.

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Stay hearing procedures continued from page 5

Please let us know whether these procedures work better for you than the previous ones; in particular, please let us know if there is anything we can do to improve on these procedures. (Voice: 505.348.2420; fax: 505.348.2432; e-mail: starzynski@nmcourt.fed.us.)

Preliminary Hearing

The Court will set a preliminary hearing on all contested motions for relief from stay. Movant should request a hearing: 1) after the objection deadline if general notice was given and one or more objections were filed, or 2) after receiving an objection (or non-concurrence) if general notice was not given.

As a general rule no testimony is taken or evidence presented at the preliminary hearing. The Court will, however, consider matters relating to whether there are grounds to continue the automatic stay in place pending the final hearing. If the collateral is not insured, the Court will seriously consider granting the motion at the preliminary hearing.

Movant should come prepared to support secured status (if contested), the amount of claim, and reason for claiming lack of equity (if alleged) or lack of adequate protection (if alleged).

The objecting party should be prepared to discuss value, necessity of the collateral and progress of reorganization (if applicable), and adequate protection.

Parties or counsel may appear by telephone if prior arrangements are made.

Preliminary stay hearings are usually set on trailing dockets.

Generally the Court will ask the creditor to prepare an order setting the date and time of the final hearing, and providing that the automatic stay will remain in place to that final hearing.

Final hearing

Parties should mark their exhibits before the final hearing and supply three sets to Chambers. Often the Court will ask parties at the preliminary hearing to discuss exhibits in advance of the final hearing and submit a written list of exhibits which are admissible. This list should accompany the exhibits. If the Court has not requested such a list, the first order of business will be to establish whether there are stipulations regarding exhibits.

Witnesses should come prepared to testify at the time set for the hearing. If the hearing is set on a trailing docket the presence of witnesses is a factor the Court will consider in choosing the order in which the cases are taken.

If there will be expert testimony, the parties should consult before the hearing to determine if they can stipulate whether the expert qualifies as an expert witness. If the parties agree, appraisals or written reports may be introduced as direct testimony.

Editor's note: *The following is an article submitted by a third year law student on the 2003 bankruptcy legislation. While this legislation was not enacted, it is likely that this battle is not yet over, and we may see similar attempts to restrict access to Chapter 7 relief in the future.*

Closing the Book on Chapter 7: new eligibility requirements for the Chapter 7 debtor

Richard J. Moran
Third year student, UNM School of Law

On March 19, 2003, the Bankruptcy Abuse Prevention and Consumer Protection Act of 2003 cleared the House of Representatives by a vote of 315-113 and headed to the Senate, where many speculated that it would promptly be passed. Perhaps due to global events, as well as a Senate amendment by Sen. Charles Schumer (D-NY), which would prevent abortion clinic demonstrators from declaring bankruptcy to avoid paying fines incurred as a result of protests, the Act sat in the Senate without action. Despite inaction, however, as recently as September 29, 2003, Sen. Charles Grassley (R-Iowa) predicted that if the Senate failed to vote on the bankruptcy bill before recessing for the year, Sen. Orin Hatch (R-Utah) would insist the Senate reconvene during the first week in January to complete action on the bill, rather than waiting until after President Bush's State of the Union address. *See* Bankruptcy Reform Legislation News, *available at* <<http://www.bankruptcyfinder.com/bankruptcyreformnews.html>> (last visited November 14, 2003).

Admittedly, the new Act is intended to temper the dramatic increase in Chapter 7 bankruptcy filings seen over the past decade. For instance, in 1990, the number of total bankruptcy filings was 718,107, with Chapter 7 filings comprising 506,940 or 70% of the total. *See* United States Bankruptcy Statistics 1990-2002, *available at* <<http://www.abiworld.org/stats/1990nonbusChapter.html>> (last visited November 14, 2003). Since then, the number of filings has increased dramatically, with more than 1.5 million debtors filing for protection in 2002. *Id.* In 2002, over 1 million individuals filed under Chapter 7, again comprising roughly 70% of the filings. *Id.* In order to reduce the number of bankruptcy filings, the proposed Act seeks to change the eligibility requirements for Chapter 7 protection.

I. The Current Bankruptcy Law

The American bankruptcy system prides itself on its ability to provide a debtor with a fresh start, and this fresh start is most notably seen in the context of Chapter 7. The debtor's decision to file under a specific Chapter is usually influenced by the type of debt. For example, a debtor with mostly unsecured debt would choose Chapter 7, which would discharge the unsecured debts within 90 days of filing. *See* 11 USC §§ 341, 524, 727. Conversely, a debtor with more secured debt would likely file under Chapter 13. Under Chapter 13, a payment plan would be established and the debtor would have 3-5 years of payments. During the life of this plan, the debtor would first pay secured

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creditors, while applying any amount left over to unsecured creditors. In some cases, a debtor may file under Chapter 13 because of the unique advantages the Chapter offers. Specifically, the cramdown provisions of 11 USC § 1325^[1] allow the debtor to value a secured claim at replacement cost. The choice between Chapter 7 and Chapter 13 is placed squarely in the debtor's hands.

Currently, the eligibility requirements for a debtor in Chapter 7 are minimal. Under 11 USC § 109, entitled "who may be a debtor," the only eligibility requirement to file under Chapter 7 is that the debtor reside in or have property within the United States and have debt. Likewise, under §109(e), a debtor may file under Chapter 13 if the debtor's noncontingent, liquidated, unsecured debts amount to less than \$290,525, while secured debts are less than \$871,550, and the debtor has regular income.

II. The Proposed Bankruptcy Act

The Proposed Act, in contrast, includes three provisions which have the combined impact of eliminating the debtor's option to file under Chapter 7.

A. Means Testing

Upon filing a Chapter 7 petition, the debtor's financial status is instantly subjected to scrutiny. If the debtor fails to overcome this scrutiny, and unless the debtor can attest to unavoidable special circumstances, the Chapter 7 petition is converted to Chapter 13, or Chapter 11, or dismissed entirely. *See* P 11 USC § 707(b)(2,7).^[2] The means test is almost wholly un-refutable by the debtor, as the debtor's financial status is calculated with an objective formula (current monthly income less expenses multiplied by 60)^[3]. The resulting product determines eligibility. A debtor may file under Chapter 7 only if the product is less than \$6,000. *See* P 11 USC §707(b)(2)(A)(ii). A debtor cannot file under Chapter 7 if the product is greater than \$10,000. *Id.* In the event the product is between \$6,000 and \$10,000, it must be less than 25% of the non-priority unsecured claims. *See* P 11 USC § 707(b)(2)(A)(i).

Furthermore, the allowable expenses included under this test are derived from IRS National and Local Standards. *See* Internal Revenue Service, *Allowable Expenses*, available at <<http://www.irs.gov/businesses/small/article/0,,id=104627,00.html>> (last visited November 16, 2003). Examples of permitted expenses are: apparel, food, housekeeping supplies, utilities, housing, and transportation costs. Other expenses, such as child care, life insurance, charitable contributions, and taxes are placed into a miscellaneous category. *See* P 11 USC § 707(b)(2)(A)(ii)(I-IV).

There are limited exceptions to the eligibility requirement under the means test. The means test would not be applied if the current monthly combined income of the debtor and the debtor's spouse, when multiplied by 12, is equal to or less than: (1) in a household of 1 person, the median family income of the applicable State for 1 wage earner as last reported

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by the Bureau of the Census; (2) in a household of 2, 3, or 4 individuals, the highest median family income of the applicable State for a family of the same number or fewer individuals as last reported by the Bureau of the Census; or (3) in a household exceeding 4 individuals, the highest median family income of the applicable State for a family of 4 individuals as last reported by the Bureau of the Census, plus \$525 per month for each individual in excess of 4. *See* P 11 USC § 707(b)(6-7).

B. Mandatory Credit Counseling

Under the proposed Act, 11 USC § 109 would be amended to require that the debtor, under any Chapter, during the 180-day period preceding the filing date of the petition, receive some sort of credit counseling. *See* P 11 USC § 109(h)(1). The requirement can be waived only if the debtor: (1) can show exigent circumstances; (2) can show some proof that although credit counseling services from an approved budget and credit counseling agency were requested, the debtor was unable to obtain the services during the 5-day period beginning on the date on which the debtor made the request; and, (3) the debtor satisfactorily proves the above to the court. *See* P 11 USC § 109(h)(3)(A)(i-iii). If one of the above requirements is met, the debtor must receive counseling within 30 days of filing the petition, which may be extended only 15 days by the court. After participating in credit counseling, the debtor must submit, at the time of filing the petition, a certificate from the approved non-profit budget and credit counseling agency describing the services provided to the debtor with a copy of the debt repayment plan. *See* P 11 USC § 521(b)(1-2). Furthermore, any payments made by the debtor to the credit counseling agency (on behalf of an unsecured creditor) could not be avoided by the U.S. Trustee. *See* P 11 USC § 547(h).

The U.S. Trustee has broad discretion to approve a credit counseling agency based on a minimum set of criteria. Proposed 11 USC §111 requires a credit counseling agency (1) be a non-profit entity; (2) have a board of directors, a majority of which are not employees and do not benefit from the outcome of the services; (3) charge a reasonable fee or provide services regardless of the ability of the debtor to pay; (4) perform annual audits on client accounts; (5) disclose to the debtor the costs and the impact services will have on credit reports; and, (6) provide counseling and services addressing the debtor's financial situation, the causes of the debt, and a budgetary remedy to resolve the debt. *See* P11 USC § 111(c)(2)(A-G).^[4]

C. Greater Burdens on Debtor's Attorney

The Proposed Act classifies bankruptcy attorneys as "debt relief agencies." *See* P 11 USC § 101(12)(A). Attendant to this definition are numerous requirements regarding how the attorney may advertise to the public and what must be disclosed to the client and the

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court. These requirements make the attorney susceptible to a broad range of damages for willful or negligent conduct. Perhaps the most burdensome addition is the requirement that the attorney certify the values included in the petition. Under proposed 11 USC § 527(c), a bankruptcy attorney must conduct a reasonable inquiry into the values included in the petition. The attorney may provide the debtor with the methods for determining disposable income, the amount owed, values of the assets, exempt property, and for the means test. If the attorney accepts the debtor's valuations, section 707(b)(4)(C) would require the attorney, by signing the petition, to certify "the attorney has no knowledge after an inquiry that the information in the schedules filed with the petition is incorrect." Sanctions and costs can follow if an attorney fails to meet these requirements.

III. The Effect of the Proposed Act is the Potential Elimination of Chapter 7

The requirement that the debtor participate in credit counseling is fraught with problems. The industry as a whole currently is under heavy scrutiny from the Internal Revenue Service and the Federal Trade Commission. As recently as October, 2003, the IRS issued two consumer bulletins advising potential clients of some of the hazards associated with doing business with these entities. In IR-2003-120, the IRS expressed concern that some of the agencies are using their tax-exempt status to circumvent state and federal laws designed for consumer protection. *See* IRS Bulletin IR-2003-120 (10/14/2003). Likewise, in FS-2003-17, the IRS stated that the majority of the agencies engaged in credit counseling offer little, if any, meaningful education or counseling. In fact, the bulk of the agencies simply place clients on payment plans. The IRS suggests that, although these organizations may have qualified for tax-exempt status in the past, because very little counseling or education occurs, they would not be able to obtain tax-exempt status for simply serving as a payment conduit to unsecured creditors. *See* IRS Bulletin FS-2003-17 (10/2003). Furthermore, even as the proposed Act waits in the Senate, the Chairman of the Senate Government Affairs Committee Permanent Subcommittee on Investigations, Sen. Norm Coleman (R-Minn.), has announced plans to hold oversight hearings on consumer protection issues associated with the credit counseling industry. *See* 22-SEP Am. Bankr. Inst. J. 3.

It is also difficult to perceive the credit counselors as objective participants. The credit counseling industry is relatively new, starting out in the early 1970's. *See* 21-FEB Am. Bankr. Inst. J. 14, 15. By 1998, the largest entity in the industry, the National Foundation for Consumer Credit, had relationships with 1.6 million individuals. *See* 53 Consumer Fin. L. Q. Rep.191. From their inception, these credit counseling agencies have placed clients on 100% repayment plans, receiving their compensation from the creditors (at one time receiving as much as 15% of the debt they managed). *See* 21-FEB Am. Bankr. Inst. J. 14. Yet, in recent years, creditors have reduced the amount they pay these agencies (now the rate varies between 10% and 7% percent). As a result, the agencies have required clients pay for the services to defray the "costs." *Id.* Although the proposed Act would require the entities to charge a "reasonable fee" or no fee at all, it is easy to speculate that whatever fee is charged to clients, creditors will augment the shortfall.

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Furthermore, the additional requirements on bankruptcy attorneys may have negative effects on a debtor's ability to obtain representation. In a March 4, 2003 letter addressed to the Chairman of the House Judiciary Committee, Robert D. Evans of the American Bar Association expressed concern over the detrimental effects the bill would have on attorneys. The requirements could increase the cost of representation, in some cases by as much as 40%. Amy Borrus, *Personal Bankruptcy: Beware the Next Chapter*, Business Week, (September 30, 2002). Normally, Chapter 13 representation costs are significantly higher than those costs associated with Chapter 7. Although it is standard practice for attorneys to collect their fees up front in a Chapter 7, in a Chapter 13 the fees can be built into the plan. The increased burdens could require Chapter 7 debtors to pay a greater amount up front, something very few debtors would likely be able to do. As Mr. Evens states, "the practical effect of these provisions will be to deny debtors timely, effective, and affordable representation just when they [debtors] need it most." See American Bar Association, *March 4, 2003 Letter to House of Representatives Judiciary Committee* available at <<http://www.bankruptcyfinder.com/article%20folder/aba-letter.pdf>>(last visited November 20, 2004).

When the additional requirements are combined, they effectively place a majority of debtors into Chapter 13 who would otherwise seek protection under Chapter 7. First, a debtor who is contemplating filing bankruptcy must participate in credit counseling for the 6 months before filing, even if the debt load is entirely unsecured. The task of the credit counseling agency is nominally to prepare a repayment plan, not unlike the contents of a Chapter 13 plan. The debtor then makes payments according to the plan for the period before filing. At the conclusion of the 6 month period preceding the petition, the debtor can choose between continuing to adhere to the payment plan and filing for bankruptcy.

Once the decision to file for bankruptcy is made, the debtor must find an attorney for representation, as the burdens of gathering documentation, applying the means test, and absorbing liability for certification of values will most likely be too great for the lay bankruptcy preparer. Attorneys, driven by market forces, must either continue to allow the debtor to make payments through a Chapter 13 plan or require payment up front for Chapter 7. The debtor, who has been paying into a payment plan preceding the decision to file, will likely have even fewer resources. With this in mind, the rational debtor will likely chose to file under Chapter 13.

Even for those debtors who have built up some savings, and who can afford Chapter 7 representation, they must still satisfy the means test. If, at the time of filing, the debtor has greater than \$166.67, or the debtor has at least \$100 but less than \$166.67, and at least 25% of the payments on unsecured debt, see *section II(A) supra*, then the petition is automatically converted to Chapter 13. See P 11 USC § 707(b)(2)(A)(i).^[5] Theoretically, the debtor who

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seeks Chapter 7 protection can satisfy the means test by increasing expenses to offset income. As a result, greater expenses provide the debtor with a better chance of falling below the \$100 ceiling. Yet, a closer look at the expense standards envisioned by the means test suggests that the two potentially most useful expenses, unsecured payments made during the credit counseling period and attorney's fees for the bankruptcy petition, will not be considered in the application. According to IRS Publication 529, legal fees are allowable expenses only if they are: (1) necessary to protect one's job; (2) for representation before the IRS; or, (3) for the health or welfare of the taxpayer. Similarly, payments to unsecured creditors are not deductible unless the taxpayer can justify and substantiate the expense. Therefore, the debtor's real expenses -such as legal fees and unsecured payments- would not be considered expenses under the means test.

IV. Conclusion

The effect of the proposed "reform" Act is that only the truly indigent debtor can satisfy the means test. Yet such a concept is an oxymoron, as the truly indigent debtor could not afford the scope of representation required under the proposed Act. If and when the new act is passed,^[6] Chapter 7 will become a seldom used relic of a bygone era – an era when debtors were given a fresh start. Chapter 13 filings will increase, however, there will likely be a sharp decrease in filings as most debtors will simply chose to continue the mandatory credit counseling payment plans. The Act will have satisfied it purpose of decreasing the number of bankruptcy filings – at the expense of the premises underlying the Act itself.

^[1] It is noteworthy, however, that a proposed addition to the "cramdown" provisions of Section 1325 would remove the ability to pay less than the balance of a PMSI in vehicles incurred within 5 years (House version) or 3 years (Senate version) before filing, or for anything else of value if incurred within 1 year before filing.

^[2] The sections of the proposed Act will be preceded by "P" to distinguish them from those sections currently in effect.

^[3] A peculiar provision to this proposed statute is that the means tests applies the debtor's current monthly income minus expenses and then multiplies the product by 60, suggesting that the debtors income and expenses have remained the same over a 5 year period.

^[4] It is noteworthy to mention that the debtor must complete a financial management course in order to receive a discharge. P 11 USC § 727(a)(11), 1328(g-i). The provider of the course is initially placed on a 6 month probationary period. P 11 USC § 111(b)(3). During this 6-month period, the course must provide education designed to assist debtors in understanding personal financial management. P 11 USC § 111(d)(1). After this period, in order for the course to maintain its approval status, it must demonstrate to the U.S. Trustee that it has been effective and will continue to be effective in helping a substantial number of debtors. P 11 USC § 111(d)(2). The proposed Act gives the U.S. Trustee broad discretion in determining the goals and success rates of the courses

^[5] This calculation is based on the proposed statutory figures, although the statute does not directly use these numbers. In Proposed 11 USC § 707, the means test is income less expenses times 60. See footnote 3. The conclusion is that only if the debtor's monthly income minus expenses is \$100 or less (as \$100 multiplied by 60 is \$6000) or at the maximum \$167.67 (as \$1667.67 multiplied by \$10,000).

^[6] The bill would go into effect six months from the date the President signs it.



Case Summary

Judge McFeeley recently issued an opinion in the case *In re Modrall*, 7-00-12951 on the issue of dismissal of a case when the debtor dies after filing the petition but prior to the §341 meeting. The case was originally filed by the husband and wife debtors as a Chapter 13 case and was converted to Chapter 7. Both debtors attended the §341 meeting in the Chapter 13, but only the wife attended the §341 meeting held by the Chapter 7 trustee, as the husband died shortly after the conversion to Chapter 7. Judge McFeeley denied the motion to dismiss and held that, despite the mandatory directive contained in §343 that the debtor attend the §341 meeting, Rule 1016 (which provides that death or incompetency of the debtor shall not abate a Chapter 7 case, and the bankruptcy estate should be administered and the case concluded as far as possible) controls. The court also noted that the debtors attended the §341 meeting while the case was a Chapter 13 case, so the requirements of §343 were met.



Editor's note:

The editor is Alice Nystel Page, formerly Corporate Counsel for Sun Healthcare Group, Inc., now trial attorney for the Office of the U.S. Trustee in Albuquerque. The new phone number for submitting story ideas is 505-248-6547.



Judge McFeeley Inducted as Fellow of The American College of Bankruptcy

Judge McFeeley was inducted this year as a Fellow of the American College of Bankruptcy at its induction ceremony in the Great Hall of the Supreme Court in Washington, D.C.. Forty-three inductees from the United States and abroad were inducted into the Fifteenth Class of College Fellows. All are being honored and recognized for their professional excellence and their exceptional contributions to the fields of bankruptcy and insolvency.

The American College of Bankruptcy is an honorary professional and educational association of bankruptcy and insolvency professionals. College Fellows include commercial and consumer bankruptcy attorneys, insolvency accountants, corporate turnaround and renewal specialists, law professors, judges, government officials and others involved in the bankruptcy and insolvency community.

Nominees for Fellows are extended an invitation to join based on a record of achievement reflecting the highest standards of professionalism. The College now has 607 Fellows, each selected by a Board of Regents from among recommendations of the Circuit Admissions Council in each federal judicial circuit and specially appointed Committees for Judicial and International Fellows. This is a very special honor for Judge McFeeley, especially because attorneys and fellow judges are not permitted to nominate judges from within their own districts.

New Mailing Address for Taxation and Revenue Department

New Mexico Taxation and Revenue Department
Bankruptcy/Support
P.O. Box 80688
Albuquerque, NM 87198



Section Picnic

Preliminary plans are in the works for a Bankruptcy Section picnic to be held in mid to late September. Members of the planning committee are Manny Lucero, Jerry Velarde, and Nancy Cusack. Contact the committee members if you have any suggestions for the picnic. Another announcement to the Section will be forthcoming after picnic plans are finalized.

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