> he or she prepares potentially misleads the Court, the trustee and creditors, and distorts the bankruptcy process."
> *Merriam*, 250 B.R. at 733.

The *Merriam* court did, however, allow the fees to stand because the attorney had adequately disclosed the limits of his representation, the debtor had chosen the more limited option, the fees were not unreasonable and there was no harm done to the debtor by the limited representation.

Ultimately, the *Ruiz* court also cited *In re Castorena*, 270 B.R. 504 (Bankr.D.Idaho 2001), in which the Court stated:

> This Court agrees that there is no excuse for a lawyer, who counsels a debtor regarding a bankruptcy and prepares that debtor's petition, schedules and related documents, to fail to sign the petition. The attorney is responsible for what appears in such pleadings, and his signature is a required certification under Rule 9011(b)."
> *Castorena*, 270 B.R. at 515.

Finally, the Court distinguished the facts in *Torrens v. Hood (In re Hood*), 727 F.3d 1360 (11th Cir.2013) from those in *Ruiz*. In *Hood*, a secretary in the law firm filled out the blanks on the form petition and the debtor filed it without an attorney signature. The Eleventh Circuit held, in a very limited holding that the attorney did not violate the Florida Rules of Professional Conduct.

The *Ruiz* court held that the attorney could not evade his responsibilities under Local Rule 9011-1 by doing all the work and then giving the debtor the papers to file falsely pretending he is acting *pro se*, and, further, that the attorney was obligated to sign, and is deemed to have filed, the petition. The *Ruiz* court ordered the attorney to disgorge all fees and concluded by stating that "The Law Firm inconsistently agreed, on one hand, to provide full representation to the Debtor, but, on the other hand, refused to formally appear in the case, sign the petition, attend the meeting of creditors with the Debtor, or provide the normal legal services required of attorneys representing debtors in Chapter 7 bankruptcy cases." *Ruiz* at 364.

## IV. The Practice of Factoring Attorney Fees in Unbundled Cases

Related to unbundling is the emerging debtors' attorneys' practice of contracting with factoring companies to ensure the payment of attorney's fees in order to offer low or no money down Chapter 7 bankruptcies. Under the practice of factoring, the holder of accounts receivable sells them to the factor for a discounted amount, that is, an amount that is less than the face amount of the receivables. The factor then earns a profit by collecting the receivables.

In the context of consumer bankruptcy cases, the debtor's attorney might sell the post-petition accounts receivables for the unbundled or bifurcated services typically contracted under a post-petition attorney fee agreement. The use of factoring companies, however, has come

under scrutiny by the Office of the U. S. Trustee, and complaints filed in various enforcement actions highlight some of the potential issues.[1]

**A. Typical Factoring Contract Terms to Consider**

As with any contract, a factoring contract can take many different forms. The terms of a factoring contract between a Chapter 7 attorney and a factor will, like any contract, be determined by the parties. Certain terms are necessary, though. First, the parties must agree to a discount percentage that will be used to calculate the amount that the attorney will be paid once the amount of the receivable is determined. Second, the parties must agree to the terms of recourse that will be available to the factor in the event that the debtor fails to make the payments. In most instances, the agreement would provide the factor the right to prosecute an action for collection against the debtor. The parties might also address whether the factor would have recourse against the attorney if the debtor fails to make payments.

**B. Potential Issues Raised by Factoring**

The practice of factoring in the consumer debtor context raises a number of issues including: (1) whether the fees arising from post-petition Chapter 7 services are dischargeable, subject to the automatic stay, and may conceal the improper collection of attorney's fees for pre-petition services; (2) whether factoring causes the debtor to pay higher attorney's fees than the attorney otherwise would charge or than what may be deemed reasonable; and (3) whether the financial arrangement is properly disclosed in the schedules and statements filed with the petition.[2]

**1. Dischargeability, Stay Implications and the Bifurcation of Services**

The first issue that must be considered when a Chapter 7 attorney factors receivables owed by a debtor is whether the debtor's debt to the attorney, and hence the debtor's debt to the factor is dischargeable and subject to the stay imposed in 11 U.S.C. § 362. While all courts hold any unpaid debt based on a claim for pre-petition services to be dischargeable in Chapter 7, the courts are in in some disagreement, as described previously in this paper, regarding whether an attorney can collect unpaid fees for post-petition services based on a pre-petition contract. *Compare*, e.g., *Hines*, 147 F.3d. 1185 (9th Cir. 1998), with *Bethea*, 352 F.3d 1125 (7th Cir.2003). If the unpaid fees are dischargeable, then the factoring of the receivable arising from

[1] *See*, *e.g.*, Bloomberg Law, *Firm Sued by U.S. Trustee Over Billing Practices in Chapter 7s*, December 19, 2017, https://biglawbusiness.com/firm-sued-by-u-s-trustee-over-billing-practices-in-chapter-7s/, (referencing Adversary Proceeding No. 17-01271, filed in the case of *In re Gilmore*, pending in the U.S. Bankruptcy Court for the Central District of California), and Bloomberg Law, *U.S. Trustee Files Motion Against Lawyer's Fees in Chapter 7 Case*, February 27, 2018, https://biglawbusiness.com/us-trustee-files-motion-against-lawyers-fees-in-chapter-7-case/, (referencing the Motion to Examine Fees filed in the case of *In re Neufville*, Case No. 17-24812, pending in the U.S. Bankruptcy Court for the District of Maryland).

[2] A further issue that is top of mind at least to most debtors is whether the factor will report payment delinquencies to the credit services. One factoring provider, BK Billing, states on its website, www.bkbilling.com that it reports on time payments positively to the credit bureaus, but it is not as clear from the website whether it also reports payment delinquencies to the credit agencies.

the debt does not change the analysis. The factored receivables would be discharged and subject to the automatic stay.

To minimize the risk of the discharge of fees, factoring companies suggest to debtors' counsel a two contract practice model.[3] The skeletal petition would be filed for low or no money down, and then the debtor would be offered the opportunity to contract, post-petition, for the services of the attorney needed to complete the case. Attorneys endorsing such a practice would note that it is not dissimilar from a *pro se* debtor that seeks out and hires competent counsel for the completion of the case and schedules after the debtor files his or her own basic petition. Under such a scenario, the fees due under the post-petition contract would not be dischargeable. *See*, Garrison, Daniel, *Liberating Debtors from "Sweatbox" and Getting Attorneys Paid, ABI Journal*, Vol. XXXVII, No. 6, June 2018, at p. 66. However, is a different analysis required when the same attorney is involved pre and post-petition in the planning of two legal services separate contracts?

Critics might argue that the planned division of services with the only substantial fees charged post-petition is a fiction because significant legal work is required before a petition may properly be filed. Competent representation requires review of assets, income and liabilities prior to filing even a skeletal petition. Thus, is the bifurcation of the work and ultimate factoring of the fees arguably concealing the improper collection of attorney's fees for pre-petition services?

Of course, if any issue as to the dischargeability of the fees remains an open question in a particular jurisdiction, the attorney would need to properly inform the client. In some actions, the Office of the United States Trustee has, in fact, asserted that the attorney in these scenarios has not properly advised the debtor regarding the automatic stay or the discharge.

**2. Increased Attorney's Fees and Review of Reasonableness**

Another issue that arises in the factoring scenario is whether the debtor is forced to pay a higher amount in attorney's fees. If the attorney would accept the reduced amount from the factor, he or she should also accept the same reduced amount from the debtor according to the Utah State Bar Ethics Committee. *See*, Advisory Opinion No. 17-06, at ¶ 2.c., September 27, 2017. In addition to implicating ethical responsibilities, increasing attorney's fees to compensate for the factoring of fees may run afoul of the reasonableness of fees requirements of 11 USC § 329(b). The fact that the attorney is willing to accept an amount that is discounted from what he is asking the debtor to pay might support the notion that the fees that the debtor is being charged are high. "If the lawyer is willing to do the work with a thirty percent discount, we question (but do not resolve) whether the total fee is reasonable." *Id.*, at ¶ 17. Of course, the other side of this coin is that the debtor could possibly pay less in a post-petition fee arrangement than he or she would pay through garnishment, which in many cases may in some jurisdictions be as much as 25% of a debtor's gross wages. *See*, *Liberating Debtors from "Sweatbox" and Getting Attorneys Paid,* at p.67.

[3] The complaint of the U.S. Trustee in the *In re Gilmore* case includes as an attachment a "welcome memo" from the factoring company which describes the suggested two contract approach. *See*, p. 29 of 147 of the Complaint at Docket Entry No. 1, December 12, 2017, Adversary Proceeding No. 17-01271.

**3. Disclosure of the Financial Arrangement and Informed Consent**

Clear disclosure of the bifurcation of the legal services and the factoring of the attorney's fees must be made both to the debtor and the Court. The American Bar Association's Model Rules of Professional Conduct Rule 1.2 (c) allows attorneys to limit the scope of their representations as long as the limitation is reasonable and the client gives informed consent after full disclosure. Further, Bankruptcy Rule 2016(b) mandates disclosures for payments made "in a case under this title, or in connection with such a case."

In addition, bifurcating legal services under a two contract system requires particular timing. The post-petition contract must in fact be executed after the date of the Chapter 7 filing and requires the informed consent of the debtor to the arrangement. This would likely need to include the clear disclosure to the debtor of the other options that he or she may have, including proceeding *pro se* or hiring another lawyer to complete his or her case. *See*, *Walton II*, at 386.

As with many thorny issues in the practice of bankruptcy, different approaches are developing that seek to accomplish the same goal: the payment of reasonable attorney's fees by debtors in an affordable and appropriate manner so that debtors may have access to the relief they need and also the benefit of competent legal advices during their cases. Case law is rapidly developing in this area that provides some guidance to practitioners, and the topic continues to be an active one in academic and professional publications. From these sources and others, counsel must be mindful of the relevant issues and ethical considerations as they establish procedures in their own firms for handling consumer debtor cases.

# Faculty

**Hon. Janet E. Bostwick** is a U.S. Bankruptcy Judge for the District of Massachusetts in Boston, appointed on Sept. 27, 2019. Prior to her appointment, she practiced as a bankruptcy attorney with more than 30 years of experience with financially troubled companies, dealing with chapter 11 business reorganizations, liquidations and wind-downs, loan workouts and creditor negotiations. From 2001-19, Judge Bostwick practiced at her own firm, Janet E. Bostwick, PC, which focused on business bankruptcy and restructuring. Before launching her firm, she practiced at the Boston firms of Goldstein & Manello, PC and Sherin and Lodgen, LLP. During her career, Judge Bostwick has been active in professional and bar associations and is a member of the Boston Bar Association, the American Bar Association and ABI. In 2007, she became a Fellow of the American College of Bankruptcy. She serves as a director of the American College of Bankruptcy and serves on its Pro Bono Committee. Judge Bostwick is actively involved in other professional organizations and frequently lectures on bankruptcy topics. She is a member of the American Bar Association, for which she serves as co-chair of the Administration and Courts Subcommittee of the its Business Bankruptcy Law Committee. She also is a member of the National Conference of Bankruptcy Judges, for which she serves on its Membership and Next Generation Committees. Judge Bostwick is a longstanding member of the International Women's Insolvency & Restructuring Confederation (IWIRC) and she served its IWIRC Chair (2002-04) and as a director. She also is the founding chair of the IWIRC-New England Network. Judge Bostwick received her B.A. in economics and mathematics from the State University of New York at Albany and her J.D. from Cornell Law School.

**Aria Eee** is executive director of Maine's Board of Overseers of the Bar in Augusta, Maine. Her primary responsibilities include assisting the Board in its fiduciary obligations, advising Maine lawyers on ethical concerns, and presenting legal education programs. Previously, Ms. Eee served as Maine's Bar Counsel and for several years in the Bar Counsel's office. She began her career as a NAPIL fellow assisting Passamaquoddy Tribal clients, then as counsel for the Passamaquoddy Tribe's Housing Authority (Pleasant Point). She also was a solo practitioner in Washington County, Maine, before serving for several years as an assistant attorney general. Ms. Eee teaches professional responsibility as an adjunct professor at Maine Law, from which she graduated in 1994. She is also a subject-matter expert for the National Conference of Bar Examiners. Ms. Eee is a member of the ABA, the MSBA (including its BIPOC and WLS sections), the Gignoux Inn of Court and various affinity bar groups. She received her undergraduate degree from the University of Alabama and her J.D. in 1994 from the University of Maine School of Law.

**Stephen G. Morrell** is an assistant U.S. Trustee with the Office of the U.S. Trustee for Region 1 in Portland, Maine, which supervises the administration of bankruptcy cases in the federal districts created for Massachusetts, Maine, New Hampshire and Rhode Island. Prior to that, he concentrated his private practice in business planning, bankruptcy and commercial litigation for 28 years. Mr. Morrell chaired the Bankruptcy section of the Maine State Bar Association and chaired panels of the Maine Board of Bar Overseers' Fee Arbitration and Grievance Commissions. He withdrew from private practice in 2006 to accept an appointment as Assistant U.S. Trustee, responsible for the administrative oversight of bankruptcy cases, supervision of trustees and legal representation of the U.S. Trustee in Maine. Mr. Morrell is a member of the Local Rules Advisory Committee for the Maine

Bankruptcy Court and ABI, and he is Board Certified in Business Bankruptcy Law by the American Board of Certification. He received his B.A. in government and legal studies from Bowdoin College in 1975 and his J.D. in 1978 from the University of Maine Law School.

**Nina M. Parker** is the founder of the firm of Parker & Associates in Winchester, Mass., and has been a member of the bar since 1981 practicing in the areas of personal and corporate bankruptcy, specializing in small business and individual chapter 11 plans of reorganization, chapter 13 wage-earner plans and other insolvency options. Since 2002, she has been Board Certified in Consumer Bankruptcy Law by the American Board of Certification. In 2016, Ms. Parker was inducted as a Fellow of the American College of Bankruptcy and in 2019 was named by *Massachusetts Lawyers Weekly* as a Top Woman of Law for her contributions to the practice. In addition, she served as commissioner on the American College of Bankruptcy's Diversity, Equity and Inclusion Commission in 2021-22 and now sits on the Committee formed in 2022. Ms. Parker is a member of the District of Massachusetts Bankruptcy Court Advisory Committee for the Local Rules, as well as the Bankruptcy Court Diversity Initiative Task Force. In addition, she is an active member of the Boston Bar Association's Bankruptcy Section having served as its co-chair, and she currently serves as member of its Strategic Thought Leadership Committee. Ms. Parker formerly served as a member of ABI's Board of Directors on its Education Committee, served on ABI's Civility Task Force and Individual Chapter 11 Task Force, and co-chaired its Consumer Committee. She currently serves on the advisory board of ABI's Northeast Bankruptcy Conference and Consumer Forum. Ms. Parker received her B.A. from Washington University in St. Louis and her J.D. from New England Law School in Boston.