IMPLEMENTATION OF THE BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT OF 2005

HEARING

BEFORE THE

SUBCOMMITTEE ON
COMMERCIAL AND ADMINISTRATIVE LAW

OF THE

COMMITTEE ON THE JUDICIARY
HOUSE OF REPRESENTATIVES

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JULY 26, 2005

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IMPLEMENTATION OF THE BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT OF 2005

TUESDAY, JULY 26, 2005

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Subcommittee met, pursuant to notice, at 2:12 p.m., in Room 2141, Rayburn House Office Building, the Honorable Chris Cannon (Chairman of the Subcommittee) presiding.

Mr. CANNON. I think we'll go ahead and begin. Thank you all for coming out. Quite a group. I'm a little surprised by the attendance here today.

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 was signed into law by President George W. Bush on April 20, 2005. The act represents one of the most comprehensive overhauls of the Bankruptcy Code in more than 25 years, particularly with respect to its consumer bankruptcy reforms. These consumer bankruptcy reforms include, for example, the establishment of a means test mechanism to determine a debtor's ability to repay debts and the requirement that consumer debtors receive counseling prior to filing for bankruptcy relief.

As we know, most of the act's provisions do not become effective until approximately 3 months from now on October 17, 2005. As we also know, the act directs the Executive Office for United States Trustees and the Judicial Conference to perform various tasks to facilitate the act's implementation. These responsibilities include the formulation and issuance of various rules, forms, guidelines, and procedures.

The purpose of today's hearing is to provide an opportunity for our Subcommittee to see how the Executive Office and the Conference are progressing toward fulfilling these critical responsibilities. For example, we are particularly interested in hearing how the Executive Office will ensure that only qualified credit counseling agencies and financial management course providers are approved. Unfortunately, some players in this industry have engaged in abusive practices and other wrongful behavior.

With respect to the act's means test reforms, which establish an income/expense screening mechanism for the purpose of determining a consumer debtor's ability to repay debts, the act requires the Executive Office to proactively identify abusive bankruptcy

cases and to conduct random audits of cases, as directed by the act. We would like to know how the United States Trustee Program will implement these responsibilities.

With respect to small business debtors, the act requires the United States trustee to conduct an initial debtor interview before the creditors for the purpose of investigating the debtor's viability and its business plan, among other matters. In addition, the act authorizes the United States trustee to inspect the debtor's business premises for the purpose of reviewing the debtor's books and records and verifying that the debtor has filed his tax returns. The methods by which the initial debtor interviews and inspections are of interest to us.

Like the Executive Office, the Judicial Conference is tasked by the act to play a critical role in its implementation. Much of the bankruptcy practice is guided by official rules and forms that are prescribed by the United States Supreme Court, subject to congressional disapproval or amendment.

The Supreme Court, in this endeavor, is largely guided by the Judicial Conference, which typically engages in a very prudential and public process from which draft rules and forms are proposed and finalized. Specifically, with respect to the development of bankruptcy rules and forms, the Conference receives guidance from the Advisory Committee on Bankruptcy Rules.

An integral part of the act's means test provisions is the requirement that a Chapter 7 debtor to file a statement setting forth his or her current monthly income and the calculations that determine whether a presumption of abuse based on the debtor's ability to repay arises. To implement this requirement, section 1232 of the act requires the Supreme Court to prescribe an official form for the income/expense disclosure statement and to promulgate general rules on the content of such statement. These rules and forms must be finalized and made available to the public by the act's effective date, namely, October 17, 2005.

Accordingly, we're very interested to learn about the process by which these rules and forms will be promulgated, whether the process will be completed in time to meet this deadline, and whether the public will have an opportunity to participate in this process. In addition, we would like to know the extent, if any, to which the court system will make the Internal Revenue expense standards and Census Bureau income statistics readily available to the public.

Another area of interest to us is the act's provision authorizing a court to waive the Chapter 7 filing fee for an individual and certain other fees under certain circumstances. In light of the fact that $45 of the Chapter 7 trustee's fee is paid out of this filing fee, we would like to know how Conference will treat the payment of trustee compensation in cases where the payment of the filing fee is waived.

Finally, the act requires certain personal information, such as the names of a debtor's minor children, and tax returns filed with the court to be safeguarded from public disclosure. We would like to know how the court system will ensure that this information does not fall into the wrong hands.

I now turn to my colleague Mr. Watt, who I suspect will have a statement for the record. We may recognize him later, when he arrives.

Without objection, any statement by him or other Members of the Committee will be placed in the record. Hearing no objection, so ordered.

[The prepared statement of Mr. Cannon follows:]

PREPARED STATEMENT OF THE HONORABLE CHRIS CANNON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF UTAH, AND CHAIRMAN, SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW

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With respect to the Act's means test reforms, which establish a income/expense screening mechanism for the purpose of determining a consumer debtor's ability to repay debts, the Act requires the Executive Office to proactively identify abusive bankruptcy cases and to conduct random audits of cases, as directed by the Act. We would like to know how the United States Trustee Program will implemented these responsibilities.

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Finally, the Act requires certain personal information, such as the names of a debtor's minor children, and tax returns filed with the court to be safeguarded from public disclosure. We would like to know how the court system will ensure that this information does not fall into the wrong hands.

Mr. CANNON. Without objection, the Chair will be authorized to declare recesses of the hearing at any point. Hearing none, so ordered.

I ask unanimous consent that Members have 5 legislative days to submit written statements for inclusion in today's hearing record.

At this time, I would like to offer into the record, on unanimous consent, a statement from the International Insolvency Institute concerning the transitional insolvency provisions to be codified in new Chapter 15 of the Bankruptcy Code. I believe a copy of this statement is included in the Members' packets.

[The material referred to is located in the Appendix.]

Mr. CANNON. In addition, on behalf of my colleague, Mr. Green, I would like to offer for submission into the record, a statement on behalf of the National Association of Bankruptcy Trustees.

As you all know, Mr. Green has been a staunch advocate for the bankruptcy trustees over the years. Although he personally wanted to be here to make this offer, his scheduling did not permit him to attend this afternoon's hearing.

A copy of this statement was distributed earlier today. It is also included in the Members' packets. Accordingly, I seek on Mr. Green's behalf unanimous consent that the statement be included in the record. Without objection, so ordered.

[The material referred to is located in the Appendix.]

Mr. CANNON. I am now pleased and honored to introduce the witnesses for today's hearing. Our first witness is Clifford White, who is the acting director of the Executive Office for United States Trustees. Over the course of his 25 years of public service in the Federal Government, Mr. White served as an assistant United States trustee and a deputy assistant attorney general within the Department of Justice. In addition, he was an assistant general counsel at the U.S. Office of Personnel Management. He is an honors graduate of George Washington University and the George Washington University Law School.

Our next witness is Judge Thomas Small, who appears on behalf of the Judicial Conference of the United States. Since 1982, Judge Small has served as a bankruptcy judge for the Eastern District of North Carolina. He received his undergraduate degree from Duke University and his law degree from Wake Forest University School of Law.

From 2000 until last year, Judge Small chaired the Judicial Conference's Advisory Committee on Bankruptcy Rules. He currently serves as the bankruptcy judge representative to the Conference. Judge Small was the president of the National Conference of Bankruptcy Judges from 2000 to 2001.

Our third witness is Travis Plunkett, who is the legislative director of the Consumer Federation of America. He appears today on behalf of the Consumer Federation of America, the National Consumer Law Center, and the U.S. Public Interest Research Group.

The Consumer Federation is a nonprofit association of 300 organizations that promotes consumer interests through advocacy and education. It has a defined membership of 50 million Americans. The National Consumer Law Center, is a nonprofit organization that specializes in consumer issues on behalf of low-income people. The U.S. Public Interest Research Group serves as a national lobbying office for State public interest research groups.

As the Federation's legislative director, Mr. Plunkett focuses primarily on financial issues, including credit reporting, bankruptcy, credit counseling, consumer privacy, and insurance. Mr. Plunkett previously served as the New York State legislative representative of the American Association of Retired Persons and the association legislative director of the New York Public Interest Research Group. He is a graduate of the University of Denver and served in U.S. Army Intelligence and Security Command.

Our final witness is George Wallace, who appears today on behalf of the Coalition for the Implementation of Bankruptcy Reform. Mr. Wallace has testified about the act's legislative predecessors on several occasions.

Welcome back. We also understand that you interrupted your vacation so that you could join us today, and we are most appreciative of your efforts to accommodate us on your schedule.

Mr. Wallace began his career as a law professor, teaching and writing about bankruptcy and consumer issues for 15 years at Tulane, Iowa, Virginia, Stanford, and Rutgers Universities. During this time, he started a legal aid clinic in Davenport, Iowa; testified in favor of the FTC's credit practices rule; was the principal draftsman of the Iowa consumer credit code; and handled various bankruptcy matters.

In 1982, he entered the full-time practice of law, where he represented lenders and debtors in commercial and consumer bankruptcy cases. From 1997 onward, his practice included representation of the Coalition for Consumer Bankruptcy Reform and its successors during the development and legislative refinement of the act. Currently, Mr. Wallace is the executive director of the Center for Statistical Research in Alexandria, Virginia. The center specializes in analyzing issues involving consumer credit, housing, and wealth distribution.

Mr. Wallace received his law degree from the University of Virginia Law School, where he was a member of the Order of the Coif and the Law Review. He received his undergraduate degree from Yale University, cum laude.

I extend each of you my warm regards and appreciation for your willingness to participate in today's hearing. In light of the fact that your written statements will be included in the hearing record, I request that you limit your oral remarks to 5 minutes. So feel free to summarize them.

And I may tap a pencil or something inconspicuous because we don't want you to just cut off, but to be aware of the time. I think we'll have several Members of the Committee here today, and they

will all want the opportunity to ask questions. And so, you'll have an opportunity to expand.

You have before you a lighting system that starts with a green light. After 4 minutes, it turns to yellow and then turns to red. And that will work for your 5 minutes as well as other Members. I would be a little more strict with Members' timing on their questions so that all Members will have an opportunity to ask questions if they wish.

After you have presented your remarks, the Subcommittee Members in the order they arrive will be permitted to ask questions of the witnesses. And pursuant to the directive of the Chairman of the Judiciary Committee, I ask the witnesses to please stand and raise your right hand to take the oath.

[Witnesses sworn.]

Mr. CANNON. The record will reflect that all of the witnesses answered in the affirmative. You may be seated.

And Mr. White, we'd be pleased if you would proceed with your testimony.

TESTIMONY OF CLIFFORD J. WHITE, III, ACTING DIRECTOR, EXECUTIVE OFFICE FOR UNITED STATES TRUSTEES, WASHINGTON, D.C.

Mr. WHITE. Good afternoon, Mr. Chairman and Members of the Subcommittee. I appreciate the opportunity to appear before you to discuss the work of the U.S. Trustee Program, our plans for implementing the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, and the fiscal year 2006 budget request that will provide the necessary resources for us to accomplish our goals.

During the past year, the U.S. Trustee Program has made substantial progress in achieving its mission to promote the integrity and the efficiency of the bankruptcy system. Beginning in April, our focus necessarily turned to implementing the new bankruptcy reform statute. Most provisions of the law become effective on October 17, and many of its key features will be enforced by the U.S. Trustee Program. We are currently engaged in a major effort to develop and to communicate the necessary policies and systems to effectively carry out our new duties.

Turning first to our major activities and achievements over the past year, I can report that combating fraud and abuse in the bankruptcy system has remained a key priority. The cornerstone of this effort has been our National Civil Enforcement Initiative, which addresses fraud and abuse and enhances protections for consumer debtors.

Although the ultimate goal of enhancing the integrity of the bankruptcy system does not lend itself easily to a quantitative measure, some numbers do help describe the magnitude of our success. In fiscal year 2004, the program took more than 52,000 civil enforcement and other actions that yielded more than $520 million in debts not discharged, penalties, and other monetary remedies.

Criminal enforcement is another key component of our strategy to combat fraud and abuse. Our 2-year-old Criminal Enforcement Unit, which is largely staffed by veteran career Federal prosecutors, has directly assisted United States attorneys in numerous prosecutions. Importantly, the unit has provided extensive training

to program staff, private trustees, and Federal law enforcement personnel.

In my written statement, I also describe many other major activities of the program.

These efforts provide a helpful springboard as we launch new initiatives to implement and enforce bankruptcy reform. Currently, our foremost responsibility is to implement the new statute. We've met with staff and trained staff at different levels in the organization and can report a very high level throughout the organization in energy, professionalism, and commitment to getting the job done.

Let me briefly highlight just two major areas of interest. First, in means testing. Congress prescribed new objective criteria for determining an individual debtor's eligibility for bankruptcy relief. The U.S. Trustee Program will be the primary enforcer to help ensure that debtors seeking Chapter 7 relief are not abusing the system.

It's critical that debtors file with the court new forms containing the information necessary to evaluate their eligibility. The U.S. Trustee Program is working closely with the courts to develop data-enabled, "smart" forms, which may be issued by the courts. Standardized, automated forms will enhance accuracy, timeliness, and cost efficiency for the benefit of debtors, creditors, the courts, and the U.S. Trustee.

Second, I'd like to highlight credit counseling and debtor education. The new law seeks to ensure that debtors are made aware of their options prior to filing bankruptcy and are equipped with more knowledge to avoid future financial difficulties before they exit bankruptcy. Under the law, the U.S. Trustee must approve eligible credit counseling agencies and debtor education courses.

As recently reported by a congressional Committee and elsewhere, some agencies within the credit counseling industry have engaged in abusive practices. To the maximum extent possible, we must screen out unscrupulous counselors without erecting unnecessary barriers that would limit the number of qualified providers who can assist debtors.

In June, we issued application forms for providers that we believe strike the appropriate balance. We may modify application requirements in the future as we learn from experience.

The new law also imposes many other duties on the U.S. Trustee Program. And, as the Chairman stated in his opening remarks, we will be taking on new responsibilities in areas such as small business Chapter 11 cases, debtor audits, and conducting numerous studies. We're moving forward with alacrity to carry out each of these mandates.

To continue our work and to implement bankruptcy reform in fiscal year 2006, the President's amended budget contains a request to fund the U.S. Trustee Program in the amount of $222.6 million. This proposal includes an increase of $37.2 million to fund our new bankruptcy reform responsibilities. The additional requested appropriations are within the revenue amounts that were provided under the recently enacted supplemental appropriations bill, which will add $241 million to the U.S. Trustee System Fund over the next 5 years.

Again, I thank the Subcommittee for the opportunity to testify. With adequate resources as contemplated by the new bankruptcy reform statute, the program looks forward to achieving its mission and successfully carrying out bankruptcy reform. I would be pleased to answer any questions from the Subcommittee.

[The prepared statement of Mr. White follows:]

PREPARED STATEMENT OF CLIFFORD J. WHITE, III

STATEMENT OF
CLIFFORD J. WHITE III, ACTING DIRECTOR
EXECUTIVE OFFICE FOR UNITED STATES TRUSTEES
UNITED STATES DEPARTMENT OF JUSTICE

BEFORE THE

SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW
COMMITTEE ON THE JUDICIARY
UNITED STATES HOUSE OF REPRESENTATIVES

July 26, 2005

Mr. Chairman and Members of the Subcommittee:

I appreciate the opportunity to appear before you to discuss the United States Trustee Program's plans for implementing the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. In describing the changes that are underway, it is important to provide an update on the ongoing work of the Program, including information on our fiscal year 2006 budget request and the resources needed to carry out our new responsibilities.

The United States Trustee Program is the component of the Department of Justice whose mission it is to promote the integrity and efficiency of the bankruptcy system by enforcing bankruptcy laws, providing oversight of private trustees, and maintaining operational excellence. Not only do we carry out numerous administrative, regulatory, and litigation responsibilities under title 11 of the United States Code (the Bankruptcy Code) and title 28 of the United States Code, but in the past four years, we have launched significant enforcement efforts to combat fraud and abuse in the system. Using a balanced approach, we have addressed debtor wrongdoing and sought protections for consumer debtors victimized by attorneys or others in a bankruptcy case. We have made great progress in accomplishing our goals, and our efforts provide a helpful springboard as we launch new initiatives to implement and enforce bankruptcy reform.

Implementing and Enforcing Bankruptcy Reform

The successful implementation and enforcement of bankruptcy reform is the most pressing responsibility now facing the United States Trustee Program. The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 provides the Program with new tools to enhance the integrity and efficiency of the bankruptcy system for the benefit of all parties and in the public interest. In cooperation with other governmental bodies with responsibilities under the new law, especially the federal court system, we will achieve the policy objectives of the new statute.

All Program personnel are currently engaged in a sprint culminating on October 17, 2005, when most provisions of the reform law become effective. A major effort is underway to develop the policies, protocols, associated technology systems or data systems/processes, and staffing patterns that will allow us to carry out our new responsibilities. Building upon work performed four years ago when reform seemed on the verge of passage, the past few months have been spent in a multi-faceted campaign to prepare for implementation. We have met with staff at all levels,

and we can report a high level of energy, professionalism, and commitment to getting the job done. We are in the midst of an unprecedented training effort that will reach nearly 800 employees and provide them with the necessary information and systems to effectively carry out and enforce our new responsibilities.

There are five major areas of bankruptcy reform in which the U.S. Trustee Program will play a key role. Program staff from both headquarters and the field are preparing our policies, procedures, and processes to implement the Act. A brief description of these areas follows.

– *Means Testing*: Congress prescribed new objective criteria for determining an individual debtor's eligibility for bankruptcy relief. Under the new statute, the United States Trustee Program must review petitions of debtors seeking chapter 7 relief to ensure they satisfy a means test and must file motions against those who have the ability to repay all or part of their debt. The new law sets forth a means test formula and specific requirements for the United States Trustee. The Program has worked closely with the Advisory Committee on Bankruptcy Rules of the Judicial Conference to develop model forms, which may be adopted by the courts in August, for use by debtors that will provide financial information required to determine their eligibility for chapter 7 relief.

– *Credit Counseling and Debtor Education*: The new law seeks to ensure that debtors are made aware of their options prior to filing bankruptcy and are equipped with more knowledge to avoid future financial difficulties before they exit bankruptcy. As a condition of eligibility to file a bankruptcy petition, debtors must file a certificate from an approved credit counselor demonstrating that they received credit counseling. As a condition of receiving a discharge, debtors must complete an approved personal financial management course. Under the law, the United States Trustee must approve eligible credit counseling agencies and debtor education courses. The Program must also develop procedures to ensure compliance by debtors. These provisions hold much promise for ensuring that debtors are well informed about their decision to file bankruptcy and better equipped to avoid future financial difficulties. The agency approval process, however, will present many technical, administrative, and legal challenges for the Program. As recently reported by a Congressional Committee, and evidenced by enforcement actions taken by the Internal Revenue Service and Federal Trade Commission, some agencies within the credit counseling industry have engaged in abusive practices and other wrongful behavior. To the maximum extent possible, the Program must screen out unscrupulous counselors who would defraud individuals to the detriment of debtors and creditors. It will be a major challenge for the Program to review the large volume of applications it expects to receive and to approve only those who conscientiously and competently provide financial management advice and assistance to vulnerable debtors. The application forms for approval as a credit counselor or a debtor educator are posted on the Program's Internet site, and applications are being accepted.

- *Debtor Audits*: It is estimated that as a result of the Act, the United States Trustees will audit approximately 7,500 chapters 7 and 13 cases in the first year after the debtor audit provisions become effective. One of every 250 cases will be selected for random audit. In addition, the Program will target a sample of cases for audit based upon criteria prescribed in the law. This requirement is not effective until 18 months after enactment, but the data collection, procurement of contract auditors, and other preparatory work has commenced. The United States Trustee is currently reviewing the coverage of the audits to establish the necessary scope of the work.

- *Small Business Chapter 11 Cases*: The new law will subject businesses with debts of not more than $2 million to new requirements designed to expedite their progress through bankruptcy, and to dismiss or convert unsuccessful cases more quickly before assets are dissipated. Many of the duties imposed on the United States Trustee (e.g., initial debtor interviews and appropriate site visits) codify existing best practices. Nonetheless, the Program will need to devote additional attention to this area under the reform law.

- *Reports, Data, and Automation*: The United States Trustee Program is required to perform important studies on the effectiveness of the new law, such as reviewing the applicability of Internal Revenue Service expense standards in the conduct of means testing and studying the effectiveness of new financial education training programs. Moreover, the Program will need to develop new databases and collect additional types of data to perform these studies and to carry out statutory requirements. The standardization and automation of forms is critical to effective implementation, and accurate and timely case processing will benefit debtors and creditors alike. If "smart" forms (i.e., data-enabled forms) are fully implemented by the courts and the Program before the October 17, 2005, effective date, this innovation will expedite case analysis for means testing and will dramatically improve data collection by the Program and the courts. The United States Trustee Program is working closely with the court system to develop new forms and "smart" forms which may be issued by the Judicial Conference.

In addition to these major areas of activity, there are a number of other discrete provisions of the amended Bankruptcy Code requiring action by the United States Trustee Program, such as the appointment of health care and privacy ombudsmen and the standardization of forms. The Executive Office will issue policy and guidance wherever possible to ensure consistency in practice so that the new law is enforced uniformly and fairly in all districts where we have jurisdiction.

I believe that the United States Trustee Program, through its work over the past few years, has laid a solid foundation on which to successfully implement bankruptcy reform. As the discussion below will demonstrate, the significant progress we have made in several key areas will be further enhanced by the reform law, and has positioned the Program to assume our new responsibilities and satisfy our mandate.

Update on Major Activities of the United States Trustee Program

Civil Enforcement

Combating fraud and abuse in the bankruptcy system has been and continues to be a key priority of the United States Trustee Program. The cornerstone of this effort has been the National Civil Enforcement Initiative which was designed: (1) to root out and remedy debtor fraud and abuse by taking such actions as seeking dismissal for "substantial abuse" under § 707(b) and denial of discharge for the concealment of assets under § 727; and (2) to provide consumer protection by seeking the disgorgement of fees, fines, or other remedies against attorneys, bankruptcy petition preparers, and others who prey upon those in financial distress.

Although the ultimate goal of enhancing the integrity of the bankruptcy system does not easily lend itself to a quantitative measure, we have instituted and refined new systems to monitor the results of our work. In fiscal year 2004, the Program took over 52,400 civil enforcement and other actions that yielded more than $520 million in debts not discharged, penalties, and other monetary remedies. The number of actions and their dollar outcomes have grown impressively since we began tracking our efforts, and I believe our work in many jurisdictions has markedly improved compliance with the law. Through training and more refined guidance, we have focused on producing work products of the highest quality and have encouraged the strategic selection of cases to achieve the maximum deterrent effect. As a result of the diligence and expertise of Program attorneys, financial analysts, and other staff, we are filing more complex adversary actions that tend to produce the greatest financial benefit to the system.

Some recent examples of successful civil enforcement actions brought by U.S. Trustee offices that cover a variety of misconduct include the following.

> *Substantial Abuse*: In the District of Utah, the chapter 7 discharge of $606,756 in unsecured debt was prevented when a real estate agent agreed to dismissal of his case on the eve of a hearing on a substantial abuse motion filed by the U.S. Trustee. The debtor, who had an $800,000 home and gross annual income ranging from $130,000 to $300,000, wanted to retain a Hummer vehicle with a $900 monthly payment. He had paid no withholding tax for four years. The U.S. Trustee's review of his personal and business accounts did not support his claimed business budget and revealed wasteful extravagance.

> *False Statements and Concealment of Assets*: In the District of South Carolina, the Bankruptcy Court entered a judgment to prevent the chapter 7 discharge of almost $500,000 in unsecured debt, about half of which was credit card debt. The debtor had failed to disclose that, four months before filing bankruptcy, he pre-paid nearly $20,000 on a two-year lease of a 2004 Chrysler vehicle. He also failed to disclose transfers of a condominium in New York, a 2001 Chrysler, and two personal water craft, all of which were sold within five months of filing for a net profit of over $50,000. The debtor also gave false testimony at his section 341 meeting and failed to make numerous other material disclosures in his schedules and statements.

Bankruptcy Petition Preparers: In the District of Arizona, on motion of the United States Trustee, the bankruptcy court fined father and son bankruptcy petition preparers more than $2.1 million for 3,657 violations of § 110 and civil contempt. The preparers' violations included abandoning their clients; collecting filing fees from clients and then forging their signatures on applications to pay filing fees in installments; causing the dismissal of clients' cases through failure to timely prepare documents; and filing documents without client review. In addition to the civil penalties, a grand jury in Maricopa County, Arizona, indicted the preparers on 20 felony counts of theft and one count of fraudulent schemes and artifices. The father ultimately pleaded guilty to theft and was sentenced to three and a half years in state prison; the son pleaded guilty to attempted illegal enterprise and was sentenced to six months in jail and three years probation, and ordered to pay restitution. The U.S. Trustee referred the criminal matter to the county attorney and provided information leading to the arrest of the preparers.

Creditor Misconduct: The Program's National Civil Enforcement Coordinator issued a letter demanding that a law firm cease filing claims on behalf of a creditor based upon documentation that, on its face, evidenced no relationship to the individual(s) in whose case it was filed. United States Trustees from three regions had reported the pattern of abuse. The law firm responded by acknowledging that claims were filed in error in numerous cases, which they purported to be as a result of a data migration issue; that they were withdrawing the claims; and that the creditor had modified its business practices to require a manual review of each proof of claim prior to filing.

Attorney Misconduct: In the Central District of California, a lawyer who had filed over 1,200 bankruptcy petitions for clients in one year agreed to, among other things, a voluntary suspension from practicing bankruptcy law for 30 months. The bankruptcy court had previously found that the lawyer's non-attorney husband had provided legal advice to a debtor, and concluded that the lawyer had aided in the unauthorized practice of law by failing to adequately supervise the work of non-attorneys. The court also found that the lawyer and other attorneys in her office had failed to provide legal services to a debtor or meet with the debtor before filing a petition. The court referred the lawyer to the Discipline Panel for the Bankruptcy Court for the Central District of California, which approved the agreement. The U.S. Trustee's Los Angeles office assisted in the investigation of the matter.

As an enhancement to the Program's civil enforcement efforts, a bankruptcy prevention component has been added. We have partnered with the Credit Abuse Resistance Education (CARE) program developed by Chief Bankruptcy Judge John C. Ninfo II of the Western District of New York, as well as other financial literacy projects, to deliver educational programs to high schools and community groups across the country. We also developed and have distributed more than 20,000 brochures that provide information on a variety of financial literacy resources. Finally, the United States Trustee Program has encouraged chapter 13 trustees to provide financial management instruction to their debtors, and there are a number of trustees across the country who offer programs to debtors in their districts.

Criminal Enforcement

Criminal enforcement continues to be a key component of the Program's strategy to combat bankruptcy fraud and abuse. By statute, a United States Trustee must refer suspected criminal activity to the United States Attorney for prosecution. Program staff identify instances of suspected criminal behavior and assist United States Attorneys in the prosecution of such cases. To focus our efforts, two years ago, the Program established a Criminal Enforcement Unit headed by a veteran prosecutor working out of headquarters in Washington, DC. The Unit is assisted by a career Assistant U.S. Trustee who has been involved with the Program's criminal enforcement efforts for many years, three career Federal prosecutors in the field, and another headquarters-based attorney.

The Criminal Enforcement Unit has significantly strengthened our ability to detect, refer, and assist in the prosecution of criminal violations. The Unit has provided extensive training to Program staff, private trustees, and federal and local law enforcement personnel in courses at the National Advocacy Center, the Federal Law Enforcement Training Center, the Inspectors General Criminal Academy, and scores of district offices. In the past 12 months, staff of the Unit have participated in over 50 programs, including training for special agents of the FBI and Internal Revenue Service; Inspectors General at the Department of Housing and Urban Development, Social Security Administration, and Environmental Protection Agency; the United States Postal Inspection Service; and Immigration and Customs Enforcement.

On October 28, 2004, the Program announced the filing of 17 criminal cases against 21 defendants in 11 districts. Dubbed "Operation Silver Screen," the prosecutions demonstrated the breadth of bankruptcy crime enforcement actions taken by the Justice Department. The cases collectively involved the concealment of more than $7 million in assets. The alleged violations were committed by a variety of debtors, including an attorney, a certified public accountant, and a police officer. The criminal conduct charged included the use of false social security numbers, identity theft, the submission of forged court documents, false statements, and other fraudulent acts.

The following are examples of the Program's work in the criminal area.

- A former trading and investment firm executive was indicted in the Northern District of Illinois on multiple counts of bankruptcy fraud, wire fraud, and money laundering, and one count of using a fire to commit a felony. The indictment alleged that, in 2002, the defendant intentionally set fire to his residence to obtain insurance money and made it appear as if the fire was set by his elderly mother, who died in the fire. The indictment also alleged that the defendant concealed significant assets, including an off-shore account containing more than $300,000, when he filed bankruptcy in 2003. The Program's Regional Criminal Coordinator in Chicago is the lead prosecutor on this case.

- A husband and wife who operated a credit card bust-out scheme that resulted in $11 million in losses were sentenced in the Central District of California. A credit card bust-out is a criminal scheme used by individuals to fraudulently obtain

> numerous credit cards in their own names or in the names of businesses that they control, incur a large amount of debt over a short period of time with no intention of paying it back, use the credit cards to obtain cash advances and a variety of goods, and then file bankruptcy to receive a discharge of the debt incurred as a result of the scheme. The husband was sentenced to 41 months in prison and ordered to pay $4.9 million in restitution; the wife was sentenced to 12 months in prison and ordered to pay nearly $500,000 in restitution. The couple provided false information when they sought millions of dollars in credit for their business from credit card companies, banks, and high-end national retail stores. Once they obtained credit, the couple accumulated large balances with no intent to repay. They spent more than $350,000 of the fraud proceeds on luxury items such as watches, diamonds, and designer clothing. When the bust-out was complete, the couple filed bankruptcy for themselves and the company to avoid paying the debts. Related to this case, two other individuals pleaded guilty to conspiracy charges for participating in the bust-out scheme, as well as the schemes of three other companies that declared bankruptcy after millions of dollars worth of merchandise was purchased on credit. The Regional Criminal Coordinator in Los Angeles assisted on the case.

In early 2004, the Program developed and piloted a completely revamped automated data collection system to track the Program's criminal enforcement work. Implemented nationwide on October 1, 2004, the Criminal Enforcement Tracking System allows the Program to track the number of criminal referrals and analyze the types of referred violations. Over time, this will provide a more accurate measure of criminal enforcement actions, assist in trend identification, and permit management improvements through focused resource allocation.

<u>Chapter 11 Practice and Other Litigation</u>

Last year, the Program participated in more than 10,000 chapter 11 reorganization cases, ranging from small, single proprietorship cases to giant, multinational conglomerates. Without substituting our business judgment for that of parties with a monetary stake in a case, the Program focuses its attention to such areas as the appointment of official committees of creditors and equity holders; the retention of professionals under § 327; professional fee approvals under §§ 326, 330 and 331; and the adequacy of disclosure statements, especially in smaller cases. Issues regarding the retention and compensation of professionals are litigated not only in chapter 11, but in chapter 7 and chapter 13 cases as well. The following discussion addresses some examples of our work in these areas.

- Joining the Second, Seventh and Ninth Circuits, the United States Court of Appeals for the Sixth Circuit agreed with the United States Trustee Program that a debtor's attorney is not entitled to collect on unpaid pre-petition attorney fees because such fees are discharged under section 727(b) of the Bankruptcy Code. At the time of the filing of the bankruptcy case, the debtor owed her attorney unpaid fees for pre-petition work. Debtor's counsel argued he was entitled to collect on this debt based on 11 U.S.C. § 329. The United States Trustee opposed debtor's counsel on the grounds that section 329 constitutes a disclosure provision

that requires all attorneys for debtors to disclose the fees they have charged and will charge their clients and does not give the attorneys any rights to fees beyond the express provisions of the Bankruptcy Code.

- Issues pertaining to the retention of professionals in chapter 11 cases under section 327 continue to receive the attention of the Program. In New Weathervane Retail Corporation, a case pending in the District of Delaware, counsel for the debtor agreed to withdraw from its representation after the United States Trustee filed an objection challenging its retention for lack of disinterestedness and actual conflicts of interest. The firm also agreed not to seek approximately $160,000 in the value of services provided to the debtor or to seek reimbursement of its out-of-pocket expenses. The law firm regularly represented the largest shareholder, which held 62 percent of the debtor's equity securities and became a secured creditor within two months preceding the filing of the bankruptcy petition. In addition, the law firm simultaneously represented multiple parties, including the largest shareholder and the debtor's CEO, in a proposed merger transaction that terminated on the eve on bankruptcy. The firm failed to disclose much of this information in its application for retention, but other parties in the case brought some of this information to the attention of the United States Trustee.

- The Program also continues to monitor professional fees sought under sections 330 and 331 in large chapter 11 cases. One example involves a case where a financial advisor agreed to an $800,000 reduction of fees requested in its final compensation application after objections were filed by the U.S. Trustee, the unsecured creditors' committee, and an individual creditor. The financial advisor had been retained by the chapter 11 debtors, Homeland Holding Corporation and Homeland Stores. The U.S. Trustee argued that a requested "sale fee" was not earned and the requested compensation exceeded a reasonable amount compared to the benefit received by the estates from the financial advisor's services.

Trustee Oversight

United States Trustees are responsible for appointing and supervising about 1,400 private trustees who administer bankruptcy estates and distribute dividends to creditors. The Program trains trustees and evaluates their overall performance, reviews their financial operations, ensures the effective administration of estate assets, and intervenes to investigate and recover the loss of estate assets when embezzlement, mismanagement, or other improper activity is suspected or alleged.

The Program works closely with the various bankruptcy trustee associations to improve case administration and to address other matters of mutual concern and interest. These efforts have resulted in a marked improvement in the degree of cooperation and collegiality between the Program and the private bankruptcy trustees. Progress on this front is evident in a number of initiatives over the past few years, as exemplified by the following examples.

- Program staff and private trustees continue to work together successfully to develop critical management reports and financial reporting and record keeping procedures that reduce the administrative burden on the trustees while providing the Program the information it needs to fulfill its oversight duties. New annual reports, monthly reports, and budget forms have been adopted for standing trustees which have incorporated automation improvements to save time, reduce duplication of effort, and increase the usefulness of the reports.

- A new information technology security initiative has been developed for chapter 13 trustees, and other measures have been taken to assist trustees in adapting to the electronic case filing environment and to otherwise take advantage of technology.

- The Program developed policy to assist the trustees in adapting to the requirements of Check 21, the federal law enabling banks to process checks electronically.

Performance-Based Management

In addition to the substantive areas of activity addressed above, the United States Trustee Program has also made progress in programmatic and management areas. In fiscal year 2004, 615 participants attended 13 training courses sponsored by the Program's National Bankruptcy Training Institute (NBTI) of the Justice Department's National Advocacy Center in South Carolina. Over the past four years, the NBTI has hosted over 2,400 participants from within and outside the Program at 55 training courses ranging from one day to one week.

Moreover, the Program issued its new Strategic Plan for 2005 to 2010. The Strategic Plan links with the Department of Justice's Strategic Plan, incorporates elements of the President's Management Agenda and the Attorney General's Management Initiatives, and reinforces the statutory Government Performance and Results Act strategic planning and results measurement requirements.

Fiscal Year 2006 Budget Request

Last year, the Program oversaw 1.5 million bankruptcy cases filed in 88 judicial districts in 48 states, the U.S. Virgin Islands, the Territory of Guam, and the Commonwealths of Puerto Rico and the Northern Mariana Islands. (The Program does not have jurisdiction in Alabama and North Carolina.) To handle its work, the Program is structured with an Executive Office in Washington, DC; United States Trustees in 21 regions whose geographic jurisdiction is set in statute; and 95 field offices that cover 150 court sites and about 280 administrative meeting locations. The Program employs approximately 1,100 staff comprised of attorneys, financial analysts, and support staff, and more than 92 percent of its employees are located in the field.

The USTP is entirely self-funded through user fees paid by bankruptcy debtors. All revenues are deposited into the United States Trustee System Fund. The Program may expend funds as appropriated by Congress. Historically, 60 percent of the Program's funding is derived from quarterly fees paid in chapter 11 reorganization cases. The balance of the funds comes from

filing fees paid in chapters 7, 11, 12, and 13 cases, as well as interest earnings and other miscellaneous revenue. With the changes to the filing fees enacted by the Bankruptcy Abuse Prevention and Consumer Protection Act, as amended by the FY 2005 Emergency Supplemental Appropriations Act, the historic balance of revenue from quarterly fees and filing fees will change somewhat.

For fiscal year 2006, the President's budget requests $222,577,000 for the Program to cover 1,519 permanent positions (388 attorneys) and 1,351 work years. The request reflects the budget amendment transmitted to the Congress by the Office of Management and Budget on June 13, 2005, and includes $11.8 million in adjustments for rent, pay, and other mandatory increases necessary to maintain a current services base level, as well as $37,175,000, 321 positions (123 attorneys), and 161 work years to implement the Bankruptcy Abuse Prevention and Consumer Protection Act. The Act contemplated growth by the Program to implement bankruptcy reform, raising filing fees and allocating $241 million over five years to the United States Trustee Program. We appreciate your consideration of the FY 2006 budget request to ensure adequate funding for the Program.

* * * *

Over the past year, the United States Trustee Program has made substantial contributions to the efficiency and effectiveness of the bankruptcy system. Among other things, we have strengthened and expanded our civil and criminal enforcement efforts, as well as devoted attention to bankruptcy prevention. With adequate resources as contemplated by the new bankruptcy reform statute, the Program looks forward to successfully implementing the new law. We are in the midst of a six month effort to develop implementation systems and enforcement strategies, and we are confident that we will get the job done.

Thank you for the opportunity to testify on the recent major activities of the United States Trustee Program. I am pleased to answer any questions from the Subcommittee.

Mr. CANNON. Thank you, Mr. White.
Judge Small?

TESTIMONY OF THE HONORABLE A. THOMAS SMALL, UNITED STATES BANKRUPTCY JUDGE FOR THE EASTERN DISTRICT OF NORTH CAROLINA, ON BEHALF OF THE JUDICIAL CONFERENCE OF THE UNITED STATES, WASHINGTON, D.C.

Judge SMALL. Thank you, Mr. Chairman and Members of the Subcommittee. I'm pleased to have this opportunity this afternoon to advise you of the extraordinary efforts the judiciary has made to implement the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005.

I'm happy to report that those efforts are on schedule, and I anticipate that the bankruptcy system will be ready on October 17, when the act's major provisions become effective.

As you know, the rule-making process under the Rules Enabling Act is a deliberative one, with a long period provided for public comment and public hearings. Bankruptcy rules must be approved by the Advisory Committee on Bankruptcy Rules and by the Standing Committee, then by the Judicial Conference of the United States, and finally by the United States Supreme Court. And after that, there is a 7-month review period by Congress.

Typically, the process takes at least 3 years, and if everything goes according to plan, permanent rules and forms needed to implement the reform legislation will be in place on December 1, 2008. Until that date, interim rules and forms are needed. The judiciary has utilized interim rules in similar circumstances in the past, notably in connection with the Bankruptcy Reform Act of 1978 that became effective on October 1, 1979.

In mid August of '79, the Bankruptcy Rules Committee proposed suggested interim rules to implement the 1978 act, and they requested that those interim rules be adopted by each court as local rules. A similar approach will be followed this time with respect to the Reform Act of 2005. The only difference being that, in addition to having the approval of the Bankruptcy Rules Committee, the suggested interim rules and forms will be approved by the Standing Committee and the Judicial Conference as well.

On April 21, the day after President Bush signed the reform act, the Chair and several members of the Bankruptcy Rules Committee met in Washington to devise a plan for developing interim rules and forms. Their goal was to have the interim rules approved by the Bankruptcy Rules Committee at a special meeting during the first week in August.

Herculean efforts toward that goal have made—were made by the committee's chair, several subcommittees, the committee's reporter, two consultants, the administrative office staff, the Federal Judicial Center staff, and the Executive Office of the United States Trustee. And as a result, drafts of 40 to 50 interim rules and forms are almost ready. And as soon as those drafts are finalized, sometime this week, they will be submitted to all Members of the Bankruptcy Rules Committee, and they will also be posted on the Web site of the United States courts.

The full Committee will vote on those interim rules at its 2-day public meeting next week in Washington on August 3 and 4. When

the suggested interim rules and forms have been approved by the Bankruptcy Rules Committee, they will be sent first to the Standing Committee and then to the Judicial Conference for expedited consideration.

After the Judicial Conference approves the interim rules, probably in mid August, each local court will be asked to adopt them. The interim forms will be temporary forms, but pursuant to Bankruptcy Rule 9009, they will be official forms required for use by all courts until they are replaced by permanent official forms, which will have been adopted after the extensive public comment and public hearing process.

As I said before, the task force—the task before the Bankruptcy Rules Committee over the past 100 days has been formidable. And I can hardly overstate how much arduous work the committee has devoted to developing proposed interim rules and forms. But implementing the new law has involved much more than just rules and forms. Countless working groups of judges, clerks, deputy clerks, the staff of the administrative office, and the Federal Judicial Center have diligently been preparing for the coming changes on October 17.

Compliance with the new law requires extensive modification of the court's operating procedures, also demands complete reprogramming of the court's case management electronic case filing system. A particular challenge has been devising a reliable method for complying with the notice requirements of new Bankruptcy Code Section 342. And another necessity, and obviously a high priority, is the training of everyone involved in carrying out the provisions of the new act, especially judges, clerks, deputy clerks, case administrators.

Furthermore, bankruptcy administrators in the District of Alabama and North Carolina are preparing to assume their new responsibilities under the act, and the administrative office is working hard to find the space and facilities for the new and urgently needed bankruptcy judges. Getting ready hasn't been easy, but with an impressive ongoing effort, the judiciary will be ready on October 17, when the new law goes into effect.

[The prepared statement of Judge Small follows:]

PREPARED STATEMENT OF JUDGE A. THOMAS SMALL

Mr. Chairman and members of the subcommittee, I am A. Thomas Small, judge of the United States Bankruptcy Court for the Eastern District of North Carolina. I appear today on behalf of the Judicial Conference of the United States, the policy-making arm of the federal courts, to report on the actions taken by the federal judiciary to implement the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 [the "Act"], particularly the development of necessary new rules and forms. I serve as the bankruptcy judge representative to the Judicial Conference and am the immediate-past chair of the Advisory Committee on Bankruptcy Rules, having served in that capacity from 2000 to 2004. The present committee chair, Judge Thomas S. Zilly, is unable to attend because of pressing court business.

I appreciate this opportunity to share with you details of the hard work that the Judicial Conference and its committees have done so far in reviewing, understanding, and implementing this massive and complicated legislation within such a brief period of time. The Act exceeds 500 pages in length and affects virtually every aspect of bankruptcy cases. Among other things, it introduces the concept of a means test as a requirement of eligibility for chapter 7 relief, adds an entirely new chapter to the Code (chapter 15 governing cross border insolvencies), and creates new categories of debtors and cases (small business cases and health care businesses). The provisions of the Act generally take effect on October 17, 2005. Imple-

menting the legislation on a timely basis presents a tremendous challenge for the judiciary.

I will address the actions taken by the Advisory Committee on Bankruptcy Rules [the "Advisory Committee" or "committee"] to develop rules and forms implementing the Act, which I understand is one of the subcommittee's principal concerns. Later, I will briefly discuss the measures taken by other Judicial Conference committees and the Administrative Office of the United States Courts to implement the Act generally.

On April 21, 2005, (one day after the Act's enactment) the Advisory Committee held an organizational meeting here in Washington to devise a plan to carry out the Act's rules-related provisions. The Advisory Committee represents a wide spectrum of views and consists of 16 members appointed by the Chief Justice, who are well experienced and expert in bankruptcy law. The committee includes six article III judges, four bankruptcy judges, three private-sector attorneys, two law professors, and an official from the Department of Justice. In addition, the Director of the Executive Office for the United States Trustees and a bankruptcy clerk of court regularly attend and participate in the committee's meetings. The committee has been working closely and very productively with the Executive Office for the United States Trustees to develop the means testing form, a primary component of the Act. At the organizational meeting, the committee's chair tasked three subcommittees to address the business, consumer, and forms issues arising from the Act. Later, the chair tasked three additional subcommittees to address the Act's provisions on cross-border insolvencies, health care, and direct appeal provisions.

The Consumer Subcommittee met separately on May 6 and June 14; the Business Subcommittee met on May 5 and June 13; and the Forms Subcommittee met on May 6 and June 15. All the subcommittees have also conducted lengthy conference calls, usually lasting more than three hours. Their work product has been reviewed by a style subcommittee for clarity and consistency. The full Advisory Committee is holding a public meeting in Washington on August 3–4, 2005. At the meeting, the committee will consider approximately forty new or amended rules and changes to virtually all the Official Forms.

The groundwork for much of the Advisory Committee's work had been prepared and considered by the committee at its meetings in 2001 and 2002, when earlier versions of the Act appeared to be nearing passage in Congress. The committee worked on amendments to about thirty rules and changes to about twenty forms. Many of these earlier proposals remain largely unchanged or slightly refined and are part of the package now under consideration. Along with the committee's more recent consideration of the rules and forms, these records provide a rich source of information for anyone interested in the development of the rules and forms.

In accordance with established Judicial Conference procedures, all rules-related records are available to the public on request. Consistent with these procedures, the drafts of rules and forms considered by the committee at its earlier meetings, as well as all current draft rules and forms, have been and continue to be available to the public on request. The public may obtain a copy of any draft rule or form simply by contacting the Administrative Office. Likewise, all meetings of the full Advisory Committee are open to the public. Minutes of each meeting of the full Advisory Committee are posted on the judiciary's internet web site.

At the Advisory Committee's April organizational meeting, it was decided that a two-track process would be necessary to implement the Act because its impending effective date did not provide sufficient time to proceed under the regular rulemaking process, which ordinarily takes three years. The first track was to: (1) identify which rules-related provisions in the Act require an immediate response; and (2) develop interim rules and forms addressing these time-sensitive provisions well before the October 17 deadline so that the courts have adequate time to implement them. The second track will be to monitor the courts' experiences with the interim rules and forms, simultaneously proceeding with the regular rulemaking process and inviting public comment beginning in August 2006 on converting the interim rules to permanent federal rules. At the same time, the committee would also publish for comment additional proposed rule amendments not included as part of the time-sensitive interim rules package.

Under the first track, interim rules will be circulated in mid-August 2005 to the courts with a recommendation that they be adopted without change as part of a standing or general order. The Advisory Committee considered, but rejected, recommending model local rules implementing the Act because many of the model local rules would necessarily conflict with existing federal Bankruptcy Rules, which are based on pre-Act law. Local rules cannot be inconsistent with the federal rules. Any amendment of local rules will have to await amendment of the federal rules through the regular rulemaking process, which cannot be accomplished in time to meet the

Act's effective date. The committee concluded that the best vehicle to accomplish the Act's objectives was to develop interim rules and urge the courts to adopt them, while simultaneously monitoring the courts' experiences and working on permanent changes to the federal rules. The same process was followed on three separate occasions in the past when the Bankruptcy Code was amended in 1978, 1986, and 1994, and interim rules contemporaneous with the Act's effective date were issued. On each occasion, the courts uniformly adopted the committee's interim rules recommendations. I am confident that the courts will continue this tradition and adopt the interim rules now under consideration.

As a practical matter, the courts' discretion in adopting the amended and new rules is limited, because many of the Act's rules-related provisions will be implemented by amended or new Official Forms, which work in tandem with the interim rules and often are based on them. Unlike the recommended interim rules, however, the Judicial Conference itself authorizes the Official Forms, which courts must "observe" under Bankruptcy Rule 9009. Thus, courts will have a real incentive to adopt the recommended interim rules in order to facilitate compliance with the mandatory Official Forms.

Courts will require several weeks to train staff and make appropriate arrangements to implement the interim rules and forms. Major modifications must be made to the Case Management/Electronic Case Filing software, which has now been deployed in virtually all the bankruptcy courts. The judiciary must quickly accomplish many other time-consuming and burdensome tasks, which I later describe, all of which require significant lead time. In addition, legal publishing firms require at least 60 days to make appropriate software changes and arrangements to mass-produce amended or new Official Forms. To meet these demands, the Advisory Committee has been working on an expedited timetable that expects the interim rules and forms to be completed and circulated to the courts by mid-August 2005. Achieving this ambitious goal has imposed enormous burdens not only on the Advisory Committee, but on the Committee on Rules of Practice and Procedure [the "Standing Committee"] and the Judicial Conference, all of which must review and approve these actions. Then the ninety bankruptcy courts and their administrative staff will have to adopt all the changes in their local systems. Carrying out this legislation has severely strained the judiciary, which is already under enormous pressure to cope with its day-to-day responsibilities in the administration of justice. Nevertheless, the judiciary is committed to fully and faithfully execute the Act's provisions.

Recommending interim rules and authorizing Official Forms without going through the regular Rules Enabling Act rulemaking process is an unavoidable expedient compelled by the Act's fast-approaching effective date. To meet the Act's deadline, the Advisory Committee has devoted substantial time and effort in developing interim rules and forms that faithfully implement the Act. It has worked closely with the Executive Office for the United States Trustees. It has consulted with experts who participated in the legislation, who at times disagreed among themselves over the meaning of particular provisions in the Act, making the committee's job all the more difficult. It has reached out to many corners of the bar for assistance. It has relied on its members' varied experiences, including members who represent creditors and others who represent debtors in their private practice. All these efforts have been undertaken in an open fashion to ensure that the process remains transparent, a hallmark of the rulemaking process.

The Advisory Committee's work product is outstanding. But the committee recognizes the inherent limitations of its abbreviated review process. Any shortfalls in the committee's work will be identified and corrected beginning in August 2006, when the interim rules and the amended and new Official Forms will undergo the exacting scrutiny of the regular rulemaking process. The Rules Enabling Act rulemaking process is a painstaking and time-consuming process that ensures that the best possible rules are promulgated. Permanent changes to the Federal Rules of Bankruptcy Procedure and forms to implement the Act will take place during the second track in accordance with the rulemaking process as described below.

The Rules Enabling Act rulemaking process is set out in 28 U.S.C. §§ 2071–2077. In accordance with the regular process, the Advisory Committee will review the experiences of the bench and bar with the interim rules and forms with a view toward proposing permanent amendments to the Federal Rules of Bankruptcy Procedure and recommending any additional appropriate revisions to the Official Forms. At its spring 2006 meeting, the committee is expected to approve and transmit the interim rules as proposed amendments to the federal rules, with or without appropriate revisions, to the Standing Committee at its June 2006 meeting with a recommendation that it approve publishing them for public comment. In addition, the committee will request that the package include an opportunity for the public to comment on the forms authorized in 2005. If approved, the interim rules and forms will then be

published in August 2006 for a six-month period. Hearings will be scheduled at which the public can testify on timely request.

The Advisory Committee's reporter will summarize all comments and statements submitted on the proposed rules and forms. The committee will meet in spring 2007 and consider any changes to the proposed rules and forms in light of the public comment. If approved, the committee will transmit the proposed rules and forms to the Standing Committee in June 2007 with a recommendation that they be approved and submitted to the Judicial Conference at its September 2007 session. If approved by the Standing Committee and the Conference, the proposed rules will then be submitted to the Supreme Court for its consideration. Changes to the Official Forms, however, do not have to be approved by the Court and will take effect on a date designated by the Conference. The Court has until May 1, 2008, to prescribe the rules and transmit them to Congress. The rules then would take effect on December 1, 2008, unless Congress acts otherwise.

At each stage of the rulemaking process, the proposed rule amendments and forms will be subjected to exacting scrutiny. Participation of the bench, bar, and public in the rules process ensures that the procedural rules implementing the Act will be the best that we can conceive. The rules committees have completed a remarkable amount of first-rate work, yet much remains to be done. These accomplishments are all the more impressive because they represent the work of volunteers, many of whom incur substantial monetary sacrifices in terms of lost income and all of whom sacrifice enormous amounts of time for the public good.

I have alluded in earlier parts of my statement to many other projects that the judiciary has undertaken to implement the Act. I now turn to address some of these important matters.

Members of the judiciary, including members of several Judicial Conference committees, judges, clerks, and staff at the Administrative Office of United States Courts [the "AO"] and the Federal Judicial Center [the "FJC"], have worked tirelessly to implement the Act by its general effective date. This work involves a cross-section of disciplines within the judiciary that require expertise in such areas as rules and forms, clerk's office procedures, bankruptcy administration, budget and accounting, information technology, statistics, training, human resources, and judicial education.

Information on the Act was quickly transmitted to the courts and clerks as soon as the law was enacted. Thereafter, judges, clerks, and other members of the judiciary were kept informed of issues that arise from the changes to the Bankruptcy Code, and given reports of progress on the judiciary's implementation of the Act. In addition to memoranda to the courts, the AO and the FJC have established web sites where information and analyses of the Act are posted for review and study by members of the judiciary. In order to implement the Act in an orderly, methodical, and coordinated fashion, Director Mecham determined that the AO's Office of Judges Programs would coordinate the multi-faceted implementation work.

Implementing the new law has required substantial on-going coordination with the Executive Office for the United States Trustees and meetings or exchanges with other such agencies as the Internal Revenue Service, the Department of Health and Human Services, and the Census Bureau. Additionally, the AO has called upon many individuals and groups for assistance, including members of the Judicial Conference, article III and bankruptcy judges, clerks of court, and deputy clerks. Ad hoc working groups were created, new Judicial Conference subcommittees were formed, and a special advisory group of judges and clerks was called upon to help develop new policies and procedures for bankruptcy clerks' offices.

The implementation process is progressing according to projected time tables. At this point, we expect to meet all deadlines, although it will be a struggle to do so. It is not possible to provide a detailed recitation of all of the work in progress in this short testimony, but I can provide you an overview of some of the other major initiatives beyond the rules process.

CHANGES IN OPERATING PROCEDURES

Significant changes to the courts' operating procedures are underway. First, careful analyses of the Act to determine all the changes required in the courts' operating procedures were conducted. Thereafter, revised practices and procedures were developed to meet the requirements of the Act. Once a broad outline of the requirements and revised procedures were in place, significant changes were initiated to reprogram the judiciary's Case Management/Electronic Case Filing system. Additionally, the judiciary is developing guidelines and procedures to address various new procedures added by the Act, such as allowing in forma pauperis chapter 7 filings, han-

dling copies of debtor-tax returns filed with the court, and instituting procedures for nationwide noticing for creditors.

TRAINING

The FJC and the AO have planned and begun training for bankruptcy judges, bankruptcy clerks and bankruptcy administrators, and court staff, including case administrators in the clerks' offices who will use the revised CM/ECF system. Training occurs nationally at specifically designated seminars, at conferences, and via the "FJTN," the FJC's closed-circuit television broadcast channel. Many other groups have reached out to the AO for assistance or participation in their training plans.

BANKRUPTCY ADMINISTRATOR PROGRAM

The AO is working directly with the six bankruptcy administrator offices in the states of Alabama and North Carolina to prepare them to assume all the new duties and responsibilities required of them under the Act. First, careful analysis of the Act was conducted to pinpoint all the new duties, whether they are explicitly imposed on bankruptcy administrators by the Act or are needed to maintain parallel treatment with new duties imposed on United States trustees. The bankruptcy administrator offices must be educated as to the changes in the law, changes in the courts' operating procedures, and changes to the bankruptcy administrators' own duties and responsibilities, such as overseeing means testing and small business chapter 11 cases certifying consumer credit counseling and financial management courses, and taking on new audit and reporting responsibilities. The AO is in contact with each bankruptcy administrator office, and an inclusive seminar is planned for them well before the effective date of the Act. In addition, current bankruptcy administrator procedures and manuals will have to be revised substantially, and changes will have to be made to their automated case management systems.

STATISTICS

Major changes will be needed in the judiciary's statistical systems, both to adjust to the many changes in the bankruptcy system required in the Act generally and to comply with section 601 of the Act, which requires the AO to gather information and produce a whole new set of reports on consumer debtor cases. The AO has worked hand in hand with the Executive Office for the United States Trustees and with bankruptcy clerks to redesign the data input forms, reprogram the case management systems, design extraction programs, and build a whole new enterprise data system capable of receiving and processing the data.

ADDITIONAL JUDGESHIPS

Authorization of additional bankruptcy judgeships by the Act was effective upon enactment. The Judicial Conference has notified all affected circuits, including those that did not receive the bankruptcy judgeships recommended by the Conference to Congress in early 2005. Some circuits have begun the appointment process, advertising their new vacancies and receiving applications for the positions. The AO is working to identify adequate space and facilities for these new judges and chambers staff.

We share a common interest in ensuring that the bankruptcy system as a whole is prepared on October 17, 2005, when most of the provisions of the Act are effective. The amount of work required of the judiciary to implement the Act is immense and costly, especially considering the short time frame available to accomplish the extensive revisions required of the existing systems. The work to date has been impressive and remarkable, and we are confident that the deadlines will be met. Thank you.

Mr. CANNON. Thank you, Judge Small.

Mr. Plunkett, you are now recognized for 5 minutes.

TESTIMONY OF TRAVIS B. PLUNKETT, LEGISLATIVE DIRECTOR, CONSUMER FEDERATION OF AMERICA

Mr. PLUNKETT. Good afternoon, Mr. Chairman, Ranking Member Watt, and Members of the Committee.

I'm Travis Plunkett. I'm the legislative director of the Consumer Federation of America, and I appreciate the opportunity to offer

our comments and those of the National Consumer Law Center and the U.S. Public Interest Research Group today.

As you may know, our organizations opposed the Bankruptcy Abuse Prevention and Consumer Protection Act because we viewed it as an unbalanced law that erects dozens of new barriers that will likely keep many Americans who need a fresh start in bankruptcy from receiving it. However, since the law has yet to take effect, I would like to focus my comments on two new provisions in the law on which important implementation decisions are being made as we speak.

One has already been talked about. It requires consumers to receive credit counseling before filing for bankruptcy and then again before being discharged. The second requires broad disclosure of tax returns by debtors, which raises significant privacy concerns.

First, on credit counseling. Our organizations support credit counseling if it's properly administered, but this is a very dangerous time to be requiring over a million new consumers to see credit counselors. As you've heard, there have been serious problems in the industry affecting a number of agencies involving deceptive acts and practices, excessive cost, and abuse by these agencies of their nonprofit status. And a host of Federal and State agencies and regulators are investigating this industry.

Unless the shady operators and substandard agencies in the industry are completely shut out of offering credit counseling under this law, Congress could be creating a situation in which it has forced consumers into the hands of unscrupulous agencies. So I would strongly urge this Subcommittee to exercise vigorous oversight of the implementation of this requirement in the next year.

I would say that the Executive Office of the U.S. Trustees is working very hard, from what we could tell, to keep bad agencies from being approved. But they've got a monumental task before them. Let me point to four specific issues.

First, it's not at all clear that there is adequate capacity of quality credit counseling to meet the requirements of the law. So we're in a bind because, as you've heard, the Executive Office of the U.S. Trustees is working hard to ensure that there is adequate capacity.

We would hate to see a situation where, because of the demands of the law, inferior or unscrupulous agencies are approved. Conversely, we want to make sure, obviously, that adequate capacity exists not just for in-person counseling, which is allowed under the law; not just for telephone counseling, which is allowed under the law; or Internet counseling as well, but for all three throughout the country. That is a difficult task.

So we urge this Committee and the Executive Office of the U.S. Trustees to work hard to assure that, first, standards are applied to ensure that no substandard agencies or agencies that might cause harm are approved. And second, that adequate capacity for all three delivery channels—consumers need a choice here—is provided.

Second issue, affordability. Obviously, folks on the brink of bankruptcy are not in good financial shape. We know from much research that average incomes for Chapter 7 filers are in the low 20's. For Chapter 13 filers, in the high 20's.

It would be a mistake to assume that the ability to pay much, if anything, for credit counseling is significant here. So it's going to be up to the Executive Office of the U.S. Trustees to take affirmative steps to ensure that the law's requirements that the fees be reasonable are met and that appropriate fee waivers are provided for low-income consumers so that they don't have to pay anything for this service.

The executive office has not done that yet, and it's important that they lay out requirements for those fees, cap them, and ensure that a sliding scale is available based on ability to pay.

Third big issue, credit counselors and creditors need to do more to ensure that credit counseling actually works, that it's actually a viable alternative to bankruptcy. The key here is that they need to provide a significant break for consumers who enter credit counseling debt management plans on what they owe. Right now, creditors don't provide a break at all in the principal that is owed.

The law actually has a provision that we urge the Executive Office of the U.S. Trustees to enforce that requires the creditors offer—that provides an incentive, I should say, for creditors to offer a real break on what is owed on principal. And we urge the Executive Office of the U.S. Trustees to look hard at that provision and to ensure that creditors and credit counseling agencies are doing that.

Finally, let me say that privacy is going to be a major issue regarding the new law's requirements that tax forms be disclosed as part of the bankruptcy process by those filing. This is a huge potential privacy issue. The law clearly vests with the Administrative Office of the U.S. Courts the ability to restrict access to creditors who are allowed access upon request.

And the important—the most important thing here is that creditors should not be allowed carte blanche access for any reason that they choose based on filing of one form with the court to this tax information. They should be required by the courts to show cause. Otherwise, we could have very significant potential security breaches or the inappropriate uses of the extremely sensitive information on these tax forms.

I have a lot of detail on the specific steps we urge the Administrative Office to take to protect the privacy of tax forms, especially regarding creditors in my testimony, and I'll leave it at that.

Thank you.

[The prepared statement of Mr. Plunkett follows:]

PREPARED STATEMENT OF TRAVIS B. PLUNKETT

Good afternoon. My name is Travis B. Plunkett. I am the Legislative Director of the Consumer Federation of America.[1] I appreciate the opportunity to offer my comments on the implementation of the new bankruptcy law on behalf of CFA, the National Consumer Law Center[2] and the U.S. Public Interest Research Group.[3]

As you may know, our organizations opposed the enactment of the Bankruptcy Abuse Prevention and Consumer Protection Act because we feared that it would harm families hit by genuine financial misfortune, such as the loss of a job, crippling medical bills and divorce. We were concerned that this major overhaul of the Bankruptcy Code erects dozens of new barriers that will keep Americans who need a fresh financial start in bankruptcy from receiving it. We also pointed out that the law does virtually nothing to curb reckless and abusive lending practices by credit card companies that have contributed to the rising bankruptcy rate in this country.

Our organizations will be closely monitoring the implementation of this law over the next few years. We sincerely hope that our fears are not realized. Since the law has yet to take effect, I would like to focus my comments on two new provisions on which important implementation decisions will be made in the next few months. Both of these provisions have far-reaching consequences for debtors. One requires consumers to receive credit counseling before filing for personal bankruptcy, and then again before being discharged. This section is being implemented as we speak by the Executive Office of the United States Trustee. The second requires broad disclosure of tax returns by debtors, which raises significant privacy concerns. The Act gives the Administrative Office of the U.S. Courts significant discretion to restrict access to tax returns as necessary to protect privacy. I will address these issues individually.

I. Credit Counseling under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005

The Act includes two major new credit counseling requirements. The Bankruptcy Code (11 U.S.C.) is amended to require debtors to obtain a credit counseling "briefing" from an approved nonprofit organization within 180 days of filing for bankruptcy (section 109(h)(1)). Debtors are also required to complete a personal financial management "instructional course" before being discharged from chapter 7 (section 727(a) of the Code) or chapter 13 (section 1328). A new section 111 of the Code requires agencies that provide either the briefing or the instructional course to meet a number of specific standards regarding fees that can be charged, the management of finances, financial incentives provided to counselors, the provision of counseling and other criteria.

[1] The **Consumer Federation of America** is a nonprofit association of over 280 pro-consumer groups, with a combined membership of 50 million people. CFA was founded in 1968 to advance consumers' interests through research, advocacy and education.

[2] The **National Consumer Law Center** is a non-profit organization specializing in consumer issues on behalf of low income people. NCLC works with thousands of legal services, government and private attorneys, as well as community groups and organizations, who represent low-income and elderly individuals on consumer issues. These comments are submitted on behalf of NCLC's low income clients.

[3] The **U.S. Public Interest Research** Group serves as the national lobbying office for state public interest research groups, which are nonpartisan, nonprofit consumer and environmental advocacy organizations.

Our organizations strongly support credit counseling, if it is properly administered by a legitimate nonprofit agency that offers a range of services. Credit counseling and the credit card consolidated payment plans administered by credit counseling agencies can play an important role in helping some consumers pay down unsecured debt and start to recover from financial difficulties.

However, our organizations were among the first in the country to call attention to serious turmoil in the credit counseling industry that was harming consumers. In a report released in 2003,[4] the National Consumer Law Center and the Consumer Federation called attention to a number of serious problems in the industry.

- Starting in the mid-1990s, the credit counseling industry underwent an alarming transformation. Consumer demand for credit counseling grew, funding to agencies was sharply reduced, and an aggressive new class of credit counseling agencies emerged. As this new generation of credit counseling agencies gained market share, complaints about deceptive practices, improper advice, excessive fees and abuse of non-profit status grew.

- Traditional credit counseling agencies offered a range of services, including financial and budget counseling and community education, as well as debt consolidation plans, known as debt management plans, or DMPs. Newer agencies, in contrast, often pushed consumers into DMPs even if they did not benefit.

- New creditor policies, lax oversight of non-profit corporations by the states and the Internal Revenue Service, and consumer demand for contact with agencies via the telephone and Internet contributed to the rise of agencies that aggressively sell DMP services.

- Credit card banks and issuers significantly cut back funding for agencies during this period. As available revenue declined, most agencies curtailed the range of services they offered and increased the fees they charged to consumers. Creditors have recently made some efforts to stop the trend toward low-quality credit counseling "mills." However, in doing so, they have significantly increased the administrative burdens on and costs to agencies.

- Creditors also reduced the concessions they offer to those who enter a DMP, such as lower interest rates. Low creditor concessions cause more consumers to drop off DMPs and to declare bankruptcy. According to a survey by VISA USA, one-third of those who failed to complete a DMP would have stayed on if creditors had further lowered interest rates or waived fees.[5] Almost half of those who dropped off a DMP had or were going to file for bankruptcy.

[4] *Credit Counseling in Crisis: The Impact on Consumers of Funding Cuts, Higher Fees and Aggressive New Market Entrants*, National Consumer Law Center and Consumer Federation of America, April 2003.
[5] *Credit Counseling Debt Management Plan Analysis*, Visa U.S.A. Inc., January 1999.

- Not all new credit counseling agencies exhibited these problems. Some were above-board and have pioneered consumer-friendly practices, such as flexible hours, electronic payments and easy access by phone and by Internet.

Key problems highlighted in the report included:

- **Deceptive and Misleading Practices**. Consumer complaints and government investigations have focused on agencies that do not pay consumers' DMP payments on time, that deceptively claim that fees are voluntary, and that do not adequately disclose fees to potential clients.

- **Excessive Costs**. As creditors have reduced funding, some reasonable fee increases are to be expected. However, in an industry that rarely charged for counseling and other services a decade ago, one major counseling trade association, the National Foundation for Credit Counseling (NFCC) now reports that about eighty-eight percent of its agencies charge monthly DMP fees. A survey of non-NFCC agencies found that almost ninety-three percent said they charged some type of fee for debt management plans. Some agencies charge as much as a full month's consolidated payment simply to establish an account. Monthly DMP fees and costs for non-DMP services are also growing.

- **Abuse of Non-Profit Status.** "Non-profit" credit counseling agencies are increasingly performing like profit-making enterprises. Nearly every agency in the industry has non-profit, tax-exempt status. Nevertheless, many of these agencies function as virtual for-profit businesses, aggressively advertising and selling DMPs and a range of related services. Some agencies appear to be in clear violation of Internal Revenue Service (I.R.S.) rules governing eligibility for tax-exempt status. Credit counseling organizations should not qualify under I.R.S. rules if they are organized or operated to benefit individuals associated with the corporation or if they are not operated exclusively to accomplish charitable or educational purposes.

Since this report was issued, state and federal regulators have begun to root out unscrupulous agencies in the industry, but there are still significant problems. In March of this year, the Federal Trade Commission announced settlements with three debt services operations (including one credit counseling organization) that had scammed consumers out of more than one hundred million dollars.[6] It also announced that it had reached a settlement with the credit counseling agency AmeriDebt that it would shut down, because of numerous abusive practices in the last few years.[7] The Senate Permanent Subcommittee on Investigations recently issued the final results of its investigation of profiteering and abusive acts in the industry and called for

[6] "Debt Settlement Services Operations Settle FTC Charges," Federal Trade Commission News Release, March 30, 2005.

[7] "FTC Settles with AmeriDebt: Company to Shut Down," Federal Trade Commission News Release, March 21, 2005.

state and federal regulators to take a number of steps to prevent these problems in the future.[8] The IRS says that it is auditing 50 of the largest nonprofit agencies in the country. It has begun to revoke the non-profit status of a few existing agencies and to reject new applicants for this status.[9] In addition, a number of states have begun to enact new laws that attempt to better regulate these agencies.

Given the ongoing problems in the credit counseling industry, this is a very dangerous time to be requiring over a million new consumers to see credit counselors.[10] Unless the law is implemented rigorously, Congress could be creating a situation in which it has forced consumers into the hands of unscrupulous agencies. I strongly urge the Subcommittee to exercise vigorous oversight of the implementation of this requirement in the next year.

The Act does require the Executive Office of the U.S. Trustees (EOUST) and bankruptcy administrators to scrutinize agencies before allowing them to offer credit counseling. Among other things, agencies are required to:

- Maintain nonprofit status;
- Provide "adequate counseling;"
- Assist consumers without regard to their ability to pay. If the agency charges a fee, it must be "reasonable;"
- Fully inform consumers of their fees, funding sources, counselor qualifications and the possible impact of credit counseling on credit reports. Counselors must be adequately trained and not be paid more for placing consumers in a DMP; and
- Safeguard client funds, through employee bonding and an annual audit.

However, unless these requirements are rigorously enforced on a continuous basis, it is quite possible that a new bankruptcy law will only exacerbate the serious problems that currently exist in the credit counseling industry. The EOUST is certainly trying to avoid this outcome, but their implementation process is just beginning and it is too early to tell what will happen. The initial guidance they have offered regarding the criteria they will use to approve agencies for counseling under this requirement raises as many questions as it answers. To make matters worse, the EOUST has not responded to numerous requests by consumer representatives to discuss its plans for implementing and enforcing this section of the law. Our organizations have followed the credit counseling industry closely for a number of years and sincerely want to help ensure that this requirement works fairly and reasonably. We can't do that, however, if the EOUST does not respond to our inquiries.

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[8] *"Profiteering in a Non-Profit Industry: Abusive Practices in Credit Counseling,"* Permanent Senate Subcommittee on Investigations. April 13, 2005.

[9] "IRS Revokes Tax-Exempt Status of 4 Credit-Counseling Agencies," Washington Post, Wash Post, July 17, 2005.
[10] Although some debtors who declare bankruptcy now seek credit counseling first, the legislation is likely to dramatically increase the number of Americans in credit counseling. According to the Administrative Office of the U.S. Courts, just under 1.5 million people declared personal bankruptcy in last year.

There are three overriding consumer protection principals that the EOUST should seek to achieve in implementing this law:

- Financial abuses and violations of privacy should not occur.
- Debtors who need access to bankruptcy quickly should not be unduly delayed by the credit counseling requirement. To achieve this goal, it will be particularly important that the EOUST ensure the fair and reasonable implementation of exceptions to the credit counseling requirement for debtors facing "exigent" circumstances or unable to obtain credit counseling with five days from an approved agency (section 109(3)(A) of the Code.)
- Consumers should receive quality credit counseling and financial education courses at a price that they can afford.

Each of these particular principals poses a significant challenge for the EOUST, given the requirements of the law and pervasive problems in the credit counseling industry. Based on the initial guidance that EOUST has offered on its web site and in limited public remarks on this requirement, our organizations have several specific concerns.

Meeting the Counseling Capacity Requirements of the Law While Maintaining High Credit Counseling Standards

Given the problems in the industry that we have outlined, it is not at all clear that adequate capacity of quality counseling exists to meet the requirements of the law. To the best of our knowledge, the EOUST has offered no guidance on how it will determine that adequate credit counseling capacity exists, or what it will do if such capacity does not exist. Such a determination is very important. It would be catastrophic to many consumers if the EOUST approved inferior or unscrupulous agencies to offer counseling because it was trying to ensure that adequate counseling capacity existed.

Conversely, we would also be concerned if the EOUST did not ensure that adequate capacity of all three types of credit counseling existed. Under the law, counselors can offer in-person, telephone or internet based counseling to meet both the briefing and the instructional course requirements. In our view, it is very important that adequate capacity exist for each of these three separate delivery channels in all parts of the country. Some debtors will prefer to receive in-person counseling, while many others might find it more convenient to do their counseling on the phone. Debtors should have a meaningful choice about how they want to receive counseling, not be forced to talk to a counselor by phone or over the Internet because no in-person services are available on a timely basis in the area in which they live.

Assuring adequate counseling of high quality may prove to be an especially challenging task for pre-discharge instructional courses. Very few of these courses exist at the current time. It may require a significant amount of "due diligence" on the part of the EOUST to ensure that courses of high quality are offered throughout the country.

We urge the EOUST to offer its guidelines immediately for assuring adequate counseling for both counseling requirements – and regarding a back-up plan if adequate counseling does not exist. We urge the Office to seek public and agency comment on these guidelines.

Affordability of Counseling Services

As mentioned above, agencies approved for credit counseling under the law must offer services at "reasonable" fees without regard for the ability of a debtor to pay. The EOUST has yet to offer much guidance on how either of these requirements will be administered. At the same time, the EOUST has determined that the average length of a pre-filing "briefing" should be 90 minutes. Our organizations strongly support the provision of thorough, effective counseling, but it will not be cheap for agencies to provide high-quality sessions of one and one-half hours. Moreover, as stated above, many of the abuses that have occurred in the industry have involved overcharging. It will be very important that the EOUST issue detailed guidelines soon on how much agencies can charge for pre-filing "briefings" and pre-discharge "instructional courses" and on serving debtors without ability to pay.

Assuming that most debtors considering bankruptcy have much, if any, "ability to pay" would be a mistake. Studies have consistently shown that the average income of chapter 7 filers hovers around $20,000 a year, well below the national median. Chapter 13 filers have slightly higher incomes but are still earn less than $30,000 yearly.[11] Research has also shown that the vast majority of individuals who enter bankruptcy do so because of a significant loss in income, high medical bills or divorce, meaning that their ability to pay for credit counseling will likely be very limited.

The reasonableness of fees for the pre-petition briefing and the financial education instructional course must also be viewed in the context of the other substantial increases in the costs of bankruptcy relief brought about by the 2005 Act. As a result of section 325 of S.256, and section 6042 of H.R. 1268, the total filing fee for a chapter 7 bankruptcy case will be increased from $209 to $274, as of October 17, 2005. In addition to this $65 increase and the new counseling costs, many bankruptcy attorneys have indicated that their fees for representation of clients will increase as a result of the new filing requirements and other burdens imposed by the 2005 Act. And while programs that provide pro bono representation are helpful, they assist only a small percentage of low-income consumers, and many pro bono coordinators have stated that they will lose many of the their volunteers as a result of the new attorney liability provisions.

If the EOUST does not take affirmative steps to ensure that the new counseling fees are truly reasonable and that appropriate fee waivers are available, many low-income consumers will be shut out of the bankruptcy system due to the substantial new costs. Agencies will be tempted to "cherry pick" the clients that they believe can pay higher fees. In establishing these fees, the EOUST should not just consider the direct costs of providing the service by agencies. The

[11] *Personal Bankruptcy: A Report on Petitioners' Ability-To-Pay*, Monograph #33, John M. Barron, Michael E. Staten, Credit Research Center, Georgetown School of Business, Georgetown University, 1997, p. 16. Barron and Staten reported that average household income for surveyed chapter 7 filers was $19, 620, after-taxes. Chapter 13 filers had an average income of $26, 334.

nonprofit organizations that will be providing briefings prior to a bankruptcy filing are required by law to be charitable in nature and to seek diverse funding sources for their services.[12]

We suggest that EOUST require agencies to administer a sliding scale of fees based upon a fair and rigorous assessment of ability to pay, and that it cap the amount that can be charged for a counseling session. We also urge the EOUST to develop the capacity to affirmatively investigate whether agencies are truly charging based on ability to pay in individual cases. This is a far more effective approach than passively providing agencies with a "safe harbor" if they can prove that they are not charging a certain percentage of the clients that see them. Given the vast demographic and regional differences that affect the ability of debtors to afford credit counseling, such a number would be hard to set fairly. It would also encourage agencies to violate the law and not serve particular consumers, once that target number is met.

Ensuring that Agencies and Creditors Offer Meaningful DMP Concessions

The EOUST should be complimented in its decision not to require approved counseling agencies to offer debt management plans. However, in setting out the minimum requirements for adequate credit counseling services by those agencies which do provide debt management plans, the EOUST should require that approved agencies make such plans available to consumers in a manner that is consistent with the intent of Congress as reflected in section 502(k). In this new section of the Bankruptcy Code, the debtor may attempt to negotiate through an approved nonprofit budgeting and credit counseling agency a "reasonable alternative repayment schedule." If the creditor unreasonably refuses to negotiate such a schedule, a debtor who later files bankruptcy, perhaps as a result of the creditor's unreasonableness, may ask the court to reduce the creditor's claim by 20 percent.

As stated above, the National Consumer Law Center and Consumer Federation of America have documented in recent years how creditors have actually reduced the concessions they offer to consumers in repayment plans, such as lower interest rates (while telling Congress that too many debtors were irresponsibly ignoring alternatives to bankruptcy like credit counseling).[13] This provision is clearly premised on the assumption that creditors must do more to offer viable alternatives to bankruptcy.

For this provision to apply, the consumer's offer must be made at least 60 days before a bankruptcy is filed and it must provide for payment of at least 60 percent of the amount of the outstanding debt over a period not to exceed the debt's repayment period. Importantly, by setting out these requirements, section 502(k)(1) provides that a repayment schedule is reasonable even if it offers payments by the consumer of an amount less than 100% of the debt. In fact, an offer of 60 percent of the amount owed may be deemed reasonable and invoke the court's authority under this provision to reduce the creditor's claim.

Moreover, by requiring that the offer must be made at least 60 days before filing through a nonprofit agency approved under section 111, it is clear that Congress intended for consumers

[12] *Credit Counseling in Crisis: The Impact on Consumers of Funding Cuts, Higher Fees and Aggressive New Market Entrants*, National Consumer Law Center and Consumer Federation of America, April 2003, p. 28.
[13] Ibid, p. 22.

to be able to negotiate repayment schedules that involve a compromise of the debt as part of the new credit counseling sessions.[14] Thus, section 502(k) must be read in connection with the new credit counseling requirements, and it apparently reflects the intent of Congress to encourage both debtors and creditors to take steps before bankruptcy which might actually prevent the bankruptcy filing. Given this purpose, the EOUST should require that approved counseling agencies which offer debt management plans must be prepared, if the consumer requests, to offer reasonable alternative repayment schedules that are consistent with the requirements of such offers under section 502(k).

Credit Counseling Agencies and Bankruptcy "Advice"

The credit counseling requirements of the bankruptcy law place several requirements on agencies regarding the kind of counseling they must offer during the pre-filing briefing. Section 111(c)(2)(E) requires agencies to provide "adequate counseling with respect to a client's credit problems that includes an analysis of such client's current financial condition, factors that caused such financial condition, and how such client can develop a plan to respond to the problems without incurring negative amoritization of debt."

There is not a single requirement in the Act that agencies provide debtors with substantive advice about whether or not to file bankruptcy, and for good reason. For one thing, agencies that did so might well violate state laws against practicing law without a license. Even if these laws didn't exist, credit counselors typically know very little about the bankruptcy process. After all, credit counseling was created by the credit card industry as an alternative to bankruptcy. Credit counseling agencies still receive a significant amount of "fair share" funding from credit card issuers based on the quantity of credit card debt each agency handles. Even legitimate, reputable credit counseling agencies often have counselors with an imperfect understanding of the bankruptcy process and of its benefits and hazards, not to mention an institutional bias against it. (Just as bankruptcy attorneys often have an institutional bias against credit counseling.) Unscrupulous agencies have a bigger problem: a conflict of interest. They allow the funds they receive from creditors to bias the recommendations they offer to consumers.

For all of these reasons, we believe it is very important that EOUST monitor approved agencies carefully to ensure that they are not exceeding the requirements of the law and offering specific bankruptcy advice to debtors, and that any information that agencies do provide about bankruptcy is accurate and balanced.

Nonprofit Status of Agencies that Offer Pre-Filing Briefings

Section 111(c)(2) of the Act requires that agencies that are approved to offer pre-filing briefings are "nonprofit". (No such requirement exists for organizations that offer pre-discharge instructional courses.) The Act does not specify that agencies that offer briefings be 501(c)(3)

[14] It is worth noting that Congress did not require the use of counseling agencies approved by the EOUST in all of the new provisions in the 2005 Act which involve repayment plans. For example, new section 362(i) states that a case may be considered filed in good faith if it is filed after an earlier case dismissed due to the creation of a repayment plan, but there is no requirement that the plan be negotiated through an approved counseling agency.

nonprofit organizations, as approved by the IRS. This lack of exclusivity could be a positive factor if it encourages a variety of nonprofit organizations, such as social welfare organizations (501(c)(4)), business leagues (501(c)(6)), credit unions (501(c)(15)), and legal services clinics (501(c)(20)) to offer quality credit counseling under the Act. It would be an especially positive development if these other types of nonprofits offered promising new forms of credit counseling or counseling without the provision of a DMP.

However, given all of the abuses that have occurred in the industry by profit-oriented "nonprofits", it is absolutely essential that the EOUST establish tight standards to ensure that profiteering by phony nonprofits does not occur. We strongly encourage the EOUST to propose these standards immediately and to request public comment on them.

II. Protecting Debtor Privacy under the Act

The Act has a number of new provisions dealing with access to and the privacy of information submitted by debtors in a bankruptcy proceeding. The most far-reaching privacy issue raised by the Act involve new provisions requiring the disclosure of tax returns by debtors. The Act requires debtors to provide tax returns or transcripts of returns to the trustee (Section 521(e) 11 U.S.C., the Bankruptcy Code) and, under certain conditions, to file them with the court (section 521(f) of the Code). Both sections require debtors to provide these returns to creditors upon request. However, this requirement is subject to section 315(c) of the legislation (S. 265), which mandates that the Administrative Office of the U.S. Courts "shall establish procedures for safeguarding the confidentiality of any tax information provided," which "shall include restrictions on creditor access." These procedures must be in place within 180 days of the date of enactment of the Act – October 17, 2005.

In order to fulfill the intent of the Act <u>and</u> protect the privacy of the Americans who file bankruptcy every year, it is essential that the Administrative Office restrict the disclosure of tax filings to creditors and limit their use of this information. The primary purpose of requiring debtors to produce tax filings under the Act is to allow the bankruptcy trustee, supervised by the U.S. Trustee Program of the Department of Justice, to verify the accuracy of the income and expense information that debtors will now be required to provide for both chapter 7 and chapter 13 bankruptcies. Creditors should only be allowed access to tax returns in limited circumstances when they can show that there is a specific need for the creditor – as opposed to the Trustee – to have access to the information.

The reason that creditor access to tax filings has to be controlled so closely is that the information is exceedingly sensitive; much of what is provided on tax filings is not relevant to a bankruptcy proceeding and this information could easily be misused or abused on a broad scale that causes substantial harm to debtors. These documents include unique personal identifiers and information that is particularly susceptible to misuse and abuse.

First, the extraordinarily large and frequent security breaches of confidential information held by creditors, retailers and data brokers that have come to light in recent months clearly illustrate how vulnerable sensitive financial data is to theft and abuse right now. Imagine what

this country's increasingly sophisticated identity thieves[15] could do if they were able to breach creditor databases that contained the mother lode of all financial and personal information: tax filings. Filings contain information like Social Security Numbers, dates of birth, bank account numbers, income and other tax information, market value of real property and other assets, alimony and support payments, expenses, purchases and personal spending habits.

Second, tax filings contain much information that has no bearing on bankruptcy filings in most cases, such as information about children, past medical treatment and about the finances of spouses who are not in bankruptcy. This information could be subject to inappropriate secondary uses by the creditor, its employees, its affiliated companies or even third parties. Creditors, for example, will be tempted to use tax information for marketing purposes (including, with unscrupulous lenders, the provision of predatory loans) unless access to filings is strictly limited to the specific requirements of the Act and not allowed to be aggregated in the firm's general shared administrative databases.

Further, under no circumstances should the Administrative Office allow this sensitive information to be sold to data aggregators, incorporated into an internal marketing database or distributed to affiliated entities by creditors.

We suggest that the Administrative Office apply the following specific standards to the distribution and use of tax filings as soon as possible, so that they are in place when the Act takes effect:

1. **No tax returns or transcripts should be in public files or available on the Internet.** The procedures for handling tax returns could track those already in use for Social Security Numbers, in which the numbers are submitted to the court but not placed in public files.

2. **Creditors must be required to show cause to gain access to a particular tax filing.** Creditors should not be able to file a form request in every case giving them access to millions of debtor tax returns. We do not object to disclosure of tax returns in appropriate cases, as defined by narrow rules under section 315(c) of the legislation. However, a determination of appropriateness must be made on an individualized basis by requiring creditors to show cause. They should be required to state why a Trustee cannot adequately check a debtor's filings for accuracy, why the tax information is relevant to a particular claim the creditor has, and that the information that the creditor seeks cannot be obtained from other sources. It is important to note that much information is already widely available to creditors in bankruptcy, including a debtor's income and expenses (including 60 days of pay stubs), ages of children, and prior residences.

3. **Interested parties should be forbidden from redistributing the information in any fashion unless approved by the court, including to affliates**. This would include, at a minimum, creditors and panel trustees. There are currently no rules limiting the use of

[15] A 2003 survey sponsored by the Federal Trade Commission suggests that incidents of identity theft are on the rise in the United States. The survey reveals that 12.7% of Americans have been victimized by some form of identity theft in the last five years, and that the total cost of this crime is estimated at $50 billion per year.

information creditors obtain in bankruptcy cases. There should be strict guidelines restricting the disclosure of the information to only the creditors' counsel and the few people in the creditor's organization who are actually participating in the bankruptcy case.

4. **Creditors should be required to keep a record of the receipt of all tax information and of each internal disclosure or use (within the company) that is made of this information**. The court, the United States Trustee and the debtor should have access to this database.

5. **Interested parties should also be required to meet security requirements regarding the use and storage of this information.** This would, at a minimum, include creditors and panel trustees. A good model for this standard would be the security requirements that government agencies have to meet under subsection (e)(9) of the Privacy Act. They must "establish appropriate administrative, technical, and physical safeguards to insure the security and confidentiality of data and to protect against any anticipated threats or hazards to their security or integrity which could result in substantial harm, embarrassment, inconvenience, or unfairness to any individual." Such a requirement should also establish rules of conduct for all persons allowed to access this information by creditors.

Mr. CANNON. Thank you, Mr. Plunkett.
Mr. Wallace?

TESTIMONY OF GEORGE WALLACE, ESQ., COALITION FOR THE IMPLEMENTATION OF BANKRUPTCY REFORM, WASHINGTON, D.C.

Mr. WALLACE. Good afternoon, Chairman Cannon, Ranking Member Watt, and Members of the Subcommittee.

My name is George Wallace. It's my pleasure to appear before you today to discuss the important topic of implementing the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005.

I am testifying on behalf of the Coalition for the Implementation of Bankruptcy Reform, which is comprised of major trade associations and companies that represent the full range of consumer credit businesses interested in bankruptcy reform.

The coalition is fully committed to working with all interested parties to ensure that the act is implemented as Congress intended. Our most important objective is to ensure that an improved bankruptcy process enables consumers to fully and efficiently obtain bankruptcy relief. At the same time, this improved process should afford a meaningful opportunity for consumers who can resolve their financial difficulties through counseling or other means to do so.

My remarks today are focused upon implementation of the consumer bankruptcy provisions of the act. Although the act brings much needed fundamental change to this area, it must be appropriately and efficiently implemented to fully accomplish its goals. Let me now discuss some of the most significant elements of the consumer bankruptcy implementation process. I have approximately six points to make.

The act, with regard to credit counseling, which has been discussed before, the act requires consumers to obtain credit counseling, of course, before they file bankruptcy from a nonprofit budget and credit counseling agency approved by the United States trustee. This is one of the most important consumer benefits included in the act. For this provision to be effective, only counseling agencies of the highest quality can be approved by the United States trustee.

In our view, the United States Trustee Program has taken important steps to achieve this goal. We urge, however, consideration of two modifications to its current draft requirements. First, the proposed bonding requirements may be given excessive—may be excessive, given the limited resources of many of the nonprofit counseling agencies. One possible solution would be to cap bonding requirements based on a variety of factors, including the resources of the counselor and other bonds and fidelity insurance it already has in place—for example, under State law requirements. We under the U.S. Trustee Program is already reviewing its requirements in this regard.

Second, counselors are appropriately required to properly identify consumers when they seek counseling. But how is that done when the counseling is conducted remotely, such as by Internet or phone? One solution would be to require that when the consumers seek counseling remotely, the consumers need to be verified by com-

paring information the consumer provides to information in a consumer report or similar document.

The second issues is needs-based bankruptcy. An essential component of the reforms that are needs-based is the form system. Congress designed the needs-based process so that it could be implemented efficiently without imposing undue burdens on those who administer the bankruptcy process. In order for the clerks, United States trustees, and bankruptcy administrators, the Chapter 7 trustees to perform their required functions efficiently, the needs-based bankruptcy forms must be properly crafted.

The forms should be simple and easy for consumers to understand, court officials to use, and creditors to review, and should provide a clear indication whether the presumption of repayment capacity is triggered. Section 1232 of the act requires no less. Development of this and other forms to implement the act is delegated in the first instance of the Judicial Conference. The first Advisory Committee on Bankruptcy Rules meeting will be held August 3 of this year, and the steps then proposed will permit us to evaluate how well this important task is being performed.

In addition, whenever a trustee determines that the presumption is triggered, a motion to dismiss the case should be filed unless special circumstances required by the act are clearly demonstrated. It is important to note that any deviations from the means test enacted by Congress are unnecessary because Congress already built into the needs-based test sufficient flexibility in the repayment thresholds and through the special circumstances provisions.

Thirdly, with regard to audits, the act requires the attorney general and Judicial Conference to establish an audit program to determine the accuracy, veracity, and completeness of petitions, schedules, and other information that the debtor required—is required to provide in individual bankruptcy cases. These audit functions are an extremely important part of the proper implementation of the act because the information filed by individuals in a bankruptcy case is essential for the proper working of the new bankruptcy process. Without appropriate audits, the lack of reliability Congress found to exist during the enactment process will continue unabated.

Fourthly, information filed with the bankruptcy case. As part of the efforts to address the unreliability of information filed in bankruptcy cases, the act requires that individual debtors must file tax returns and pay stubs in Chapter 7 and Chapter 13 cases. In order to ensure that congressional intent is implemented, the trustees must make sure that procedures are in place to ensure that creditors in the case are able to access the tax return and other information efficiently.

Fifthly, reaffirmation agreements. The act includes new provisions clearly defining and standardizing process for reaffirming a debt. While the act sets out verbatim the specific disclosures that must be made in connection with the reaffirmation agreement, it would be very helpful in ensuring uniform nationwide implementation if the Administrative Office of the United States Courts, which now provides a nonmandatory form for reaffirmations, would promptly revise and publish a new form, faithfully following the new statutory requirements.

And last, improving bankruptcy statistics. Section 601 of the act requires the clerk of the court to collect statistics regarding debtors or individuals with consumer debts seeking relief under Chapters 7, 11, and 13. In addition, the attorney general must issue rules requiring uniform forms for final reports by trustees in cases under Chapters 7, 12, and 13. And then there is a provision for the collection of this information and reporting it.

It is critical that these data collection tasks be fully implemented. In future years, the resulting data will provide a solid information basis on which to build constructive bankruptcy policy.

Conclusion. I have highlighted some of the most important implementation tasks, but I have hardly been exhaustive. The act's reforms require cooperation by several separate governmental and quasi-governmental agencies if the legislation's goals are to be promptly realized.

The Bankruptcy Rules must be revised in several respects, and since the formal process to do so takes some time, uniform interim rules that can be adopted by each local bankruptcy court should be proposed. Forms and procedures must be developed. Issues, as they arise, must be resolved. Many entities have important functions to perform, either in cheerfully making the new system work or examining how well it does work.

We appreciate the interest the Subcommittee has shown in overseeing the process and encouraging the involved parties to work together in good faith to implement the legislation. I would like to thank the Subcommittee for the opportunity to appear before you today to discuss this important topic. I would be happy to answer any questions you may have.

[The prepared statement of Mr. Wallace follows:]

PREPARED STATEMENT OF GEORGE WALLACE

TESTIMONY OF GEORGE WALLACE
BEFORE THE
SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW
OF THE
COMMITTEE ON THE JUDICIARY
U.S. HOUSE OF REPRESENTATIVES

Oversight Hearing on the
Implementation of the
"Bankruptcy Abuse Prevention and Consumer Protection Act of 2005"

July 26, 2005

Good morning, Chairman Cannon, Ranking Member Watt, and Members of the Subcommittee. My name is George Wallace and it is my pleasure to appear before you to discuss the important topic of implementing the "Bankruptcy Abuse Prevention and Consumer Protection Act of 2005" (the "Act"). I am testifying on behalf of the Coalition for the Implementation of Bankruptcy Reform (the "Coalition"), which is comprised of major trade associations and companies that represent the full range of consumer credit businesses interested in bankruptcy reform.

The Coalition is fully committed to working constructively with all interested parties to ensure that the Act is implemented as Congress intended. Our most important objective is to ensure that an improved bankruptcy process enables consumers to fully and efficiently obtain bankruptcy relief. At the same time, this improved process should afford a meaningful opportunity for consumers who can resolve their financial difficulties through counseling or other means to do so.

The Act represents the most important set of changes to the Bankruptcy Code since 1978 when Congress enacted the Bankruptcy Reform Act of 1978. It realigns commercial and consumer bankruptcy policy in a number of ways, including introducing a formal means test and credit counseling requirements into consumer bankruptcies, and imposing significant reforms in the areas of health care providers, retailers, and small businesses. Important new provisions deal with cross border insolvencies, financial contracts, and family farmers and fishermen, as well as with misbehavior of corporate officers on the eve of bankruptcy.

My remarks today are focused upon implementation of the consumer bankruptcy provisions of the Act. Although the Act brings much needed fundamental change to this area, it must be appropriately and efficiently implemented to fully accomplish its underlying goals. Below I discuss some of the more significant elements of the consumer bankruptcy implementation process.

Consumer Credit Counseling

During the 9 years of deliberations on the Act, it became all too clear that many consumers file for bankruptcy without ever realizing that it is possible to resolve their financial difficulties in more constructive ways. The Act seeks to address this issue by requiring consumers to obtain basic education before filing for bankruptcy. In particular, Section 106 of the Act requires consumers to obtain a briefing that outlines the opportunities for available credit counseling and assists them in performing a related budget analysis. The briefing must be obtained from a "non-profit budget and credit counseling agency" approved by the United States Trustee (or bankruptcy administrator if applicable). This is one of the most important consumer benefits included in the Act. It creates an opportunity for consumers to avoid filing for bankruptcy if their financial condition enables them to do so. In order to ensure that this provision is effective, it is imperative that only counseling agencies of the highest quality are approved by the U.S. Trustee.

On June 30, 2005 the U.S. Trustee Program took an important step to achieve this objective when it announced that it would begin accepting credit counseling applications. The application and accompanying materials published by the U.S. Trustee go a long way towards ensuring that the congressional intent of Section 106 is properly implemented. The U.S. Trustee is to be strongly commended for its efforts. We urge, however, that the U.S. Trustee consider modifications to its application package in two respects. First, we are concerned that the bonding requirements included in the application materials may be excessive given the limited resources of many non-profit counseling agencies. In some cases, these requirements could divert tens of thousands of dollars of resources that non-profit counseling agencies would otherwise be able to devote to counseling efforts. We understand that the U.S. Trustee has acknowledged this issue and is considering ways to address it. One possible solution would be to impose a cap on the bonding requirements of an individual credit counselor based on a variety of factors including the resources of the counselor and other bonds it already has in place, for example, under state law requirements.

Second, the application materials appropriately indicate that counselors must ensure that they properly identify consumers when they seek the counseling mandated under Section 106. This is an important provision, and we commend the U.S. Trustee for including it in the application materials. We note, however, that many counselors are seeking guidance on how to obtain proper identification of consumers particularly when the counseling is conducted remotely, such as by Internet or phone. One possible solution to this issue would be to provide guidance that counselors will be deemed to have properly identified a consumer who appears for counseling in person by checking a government-issued I.D. presented by the consumer, such as a driver's license or passport. For consumers who obtain counseling remotely, a consumer should be deemed to be adequately identified if the counselor is able to verify the consumer's identity information by comparing it to a consumer report from a consumer reporting agency or similar document obtained from other verification sources.

The requirements of Section 106 do not apply in any district where the U.S. Trustee determines that approved non-profit budget and credit counseling agencies are not available to individuals in that district. We recognize that some parties may be concerned that counseling services may not be available in some areas when the requirements take effect on

October 17, 2005. Non-profit counseling agencies across the country are working diligently to ensure that they have adequate capacity to provide these important services when required to do so. We are confident that the non-profit counseling agencies will be able to meet this challenge, and we urge the U.S. Trustee to continue its efforts to ensure that only top-quality counselors are approved.

Needs-Based Bankruptcy

Another essential component of the reforms contained in the Act is found in Title I which establishes a new "needs-based" bankruptcy process. In particular, Section 102 of the Act creates a presumption that a Chapter 7 proceeding should be dismissed for "abuse" if over 5 years, the debtor has the ability to repay the lesser of: (i) $10,000; or (ii) 25% of the debtor's total non-priority, unsecured claims (but which must be at least $6,000). The debtor's ability to repay is based on a relatively simple "means test" calculation which takes the debtor's average income over the last 6 months, and deducts certain allowable expenses set by the IRS, as well as categories of the debtor's actual expenses and actual payments for secured debts and priority debts. Congress carefully crafted the means test to ensure that it provides appropriate flexibility for debtors who have "special circumstances" that "justify" adjustments to income or expenses for which there is "no reasonable alternative."

Congress designed the needs-based process so that it could be implemented efficiently without imposing undue burdens on those that administer the bankruptcy process. Under the needs-based system, each debtor is required to include the means test calculations in the bankruptcy schedules filed at the beginning of the bankruptcy case. The debtor also is required to provide his or her paystubs covering the 60 days prior to filing and the debtor's most recent federal tax return. Based on the information filed with the court, the clerk must notify all creditors within 10 days of filing if the information filed indicates the presumption of abuse is triggered. In order for the clerks to be able to execute their duties efficiently, it is imperative that the needs-based bankruptcy forms be properly crafted. The forms should be simple and easy for consumers to understand and should provide a clear indication to the clerks as to whether the presumption of repayment capacity is triggered.

Properly crafted forms also will assist the trustees and bankruptcy administrators in fulfilling their duties. When a consumer files for bankruptcy, the trustee or bankruptcy administrator is required to review the schedules and, 10 days after the first meeting of creditors, file a report with the court as to whether the case would be presumed to be an abuse because the debtor has filed in Chapter 7 but has the capacity to repay. The court must provide a copy of that report to all creditors within 5 days. In those cases where the application of the means test indicates a presumption of abuse (and the debtor's income is above the applicable state median income level), the trustee or administrator has 30 days to file with the court either a motion to dismiss the case or a statement as to why no motion is being filed. Based on the carefully crafted provisions enacted by Congress, it would be anticipated that trustees and bankruptcy administrators will file such a motion in the overwhelming majority of cases where the presumption of abuse is triggered. Guidance from the Department of Justice to the trustees may be helpful in clarifying this point. In particular, use of any additional tolerances above the means test enacted by Congress should be avoided. In this regard, it is reported that in prior Administrations, there was discussion about requiring the debtor to have an additional 10 or 15%

repayment capacity above that enacted by Congress before a trustee would bring a motion based on the means test. Such deviations from the clearly defined means test enacted by Congress are unnecessary because Congress already built into the needs-based test sufficient flexibility in the repayment thresholds and through the "special circumstances" provisions noted above.

Audits

During the deliberations on the Act, there was wide agreement that much of the information filed in individual bankruptcy cases is largely unreliable notwithstanding existing penalties against filing false information in a bankruptcy case. In order to address this issue, Section 603 of the Act requires the establishment of procedures "to determine the accuracy, veracity, and completeness of petitions, schedules, and other information that the debtor is required to provide in individual bankruptcy cases." These procedures must be established by the U.S. Attorney General (in judicial districts served by the United States Trustees) and the Judicial Conference of the United States (in judicial districts served by bankruptcy administrators). The procedures must include audits in accordance with generally accepted auditing standards and the audits must be performed by independent certified public accountants or independent licensed public accountants. The Attorney General and Judicial Conference, however, may develop alternative auditing standards within the 2 years after the date of enactment of the Act.

The procedures required by Section 603 must establish a method of selecting appropriate qualified persons to enter into contracts to perform the audits. In addition, the procedures must establish a method of randomly selecting at least 1 out of every 250 cases to be audited in each federal judicial district. The procedures also must require audits of schedules of income and expenses that reflect greater than average variances from the statistical norm of the district in which the schedules were filed. Finally, the procedures must provide for reports at least annually concerning the aggregate results of the audits, including the percentage of cases, by district, in which a material misstatement of income or expenditures is reported.

These audit provisions are an extremely important part of proper implementation of the Act because the information filed by individuals in a bankruptcy case is essential for the proper working of the new bankruptcy process. Without appropriate audits, the lack of reliability Congress found to exist will continue unabated.

Information Filed With Bankruptcy Case

As part of the efforts to address the unreliability of information filed in bankruptcy cases, the Act requires that individual debtors must file tax returns and paystubs in Chapter 7 and Chapter 13 cases. Congress recognized the importance of this information, particularly in connection with administration of the controls on abusive use of Chapter 7, including the needs-based bankruptcy test. Under the Act, the paystubs must be filed with other materials as part of the bankruptcy filing, such as the list of creditors, and must be provided to parties in interest to the case. Debtors also must file their most recent federal tax return and the debtor or trustee must provide a copy of such return to the debtor's creditors upon request. In order to ensure that congressional intent is implemented, the trustees must make sure that

procedures are in place to ensure that creditors in the case are able to access the tax return and other information efficiently.

Reaffirmation Agreements

The extensive hearing record on the Act reflects that many consumers who file for bankruptcy have a strong desire to reaffirm some of their debts. Many bankruptcy judges, however, disfavor reaffirmation agreements and have adopted their own reaffirmation rules and have made it difficult for debtors to reaffirm.

To address this issue, the Act includes new provisions clearly defining and standardizing the process for reaffirming a debt. While the Act sets out verbatim the specific disclosures that must be made in connection with a reaffirmation agreement, it would be very helpful in ensuring uniform nationwide implementation if the Administrative Office of United States Courts which now provides a non-mandatory form for reaffirmations would promptly revise and publish a new form faithfully following the new statutory requirements.[1]

Improve Bankruptcy Statistics

Section 601 of the Act requires the Clerk of the Court to collect statistics regarding debtors or individuals with consumer debts seeking relief under Chapters 7, 11, and 13. Those statistics must include the total assets and liabilities of consumer debtors, the income and expense figures for such debtors, and the aggregate amount of debt discharged for consumer debtors.

Under Section 602 of the Act, the Attorney General must, within a reasonable time after the effective date (18 months after enactment of the Act), issue rules requiring uniform forms for final reports by trustees in cases under Chapters 7, 12, and 13. Each report must be designed to facilitate compilation of data and maximum possible access to the public. The reports must include information to evaluate the efficiency and practicality of the bankruptcy system.

Conclusion

I have highlighted some of the most important implementation tasks, but I have hardly been exhaustive. What is important to understand is that the Act's reforms require cooperation by several separate governmental and quasi-governmental agencies if the legislation's goals are to be promptly realized. The Bankruptcy Rules must be revised in several respects, and since the formal process to do so takes some time, uniform interim rules that can be adopted by each local bankruptcy court should be proposed. Forms and procedures must be developed. Issues, as they arise, must be resolved. The bankruptcy judges, bankruptcy court clerks, United States Trustees, bankruptcy administrators, Chapter 7 and Chapter 13 trustees, U.S. attorneys in each district, as well as the Federal Reserve Board, the Government Accountability Office, Internal Revenue Service, and the Administrative Office of United States Courts all have important functions to perform, either in cheerfully making the new system work,

[1] There should be two different versions of the form to reflect the different treatment for credit unions as compared to other types of creditors.

or examining how well it does work. We appreciate the interest the Subcommittee has shown in overseeing this process, and encouraging the involved parties to work together in good faith to implement the legislation.

I would like to thank the Subcommittee for the opportunity to appear before you today to discuss this important topic. The Coalition is fully committed to working with the Subcommittee and other interested parties to ensure that the Act is implemented efficiently and fairly. I would be happy to answer any questions you may have.

Mr. CANNON. Thank you, Mr. Wallace.

As Chair, let me suggest the following order for questions. If someone has a commitment and would like to be recognized out of this order, we'd appreciate hearing about it now. But first of all, Mr. Gohmert, then Mr. Watt, then Mr. Franks, Mr. Delahunt, Mr. Chabot, and then Mr. Nadler. And if there is anything left to ask, I will follow up with questions.

Mr. Gohmert? You are recognized for 5 minutes.

Mr. GOHMERT. Thank you, Mr. Chairman.

Mr. Plunkett, let me ask you a question. You had indicated that we should be involved in significant oversight to help—these weren't your words—but basically to keep the charlatans out of the consumer counseling business. What amendments, if any, do you think would help make that possible?

Mr. PLUNKETT. Well, at this point, it appears to be a question of implementation. The standards laid out in the law for quality, although quite general, are fairly good. For example, it——

Mr. GOHMERT. Well, but I'm just asking—my question is, do you see any amendments that would help keep charlatans out of the consumer counseling business?

Mr. PLUNKETT. At this point, I would suggest that what's needed is really tough oversight.

Mr. GOHMERT. Okay. You'll go back to my original question.

Mr. PLUNKETT. Yes.

Mr. GOHMERT. Besides oversight. So listen to me. Besides oversight, what amendments, if any, do you think would help keep charlatans out of consumer counseling?

Mr. PLUNKETT. I wouldn't recommend anything at this point. As I mentioned, the standards are fairly good. However, if it's not properly implemented, we're still going to have the charlatans offering credit counseling.

Mr. GOHMERT. Okay. Thank you. And you also mentioned that you want to protect basically tax information from creditors unless they were to show cause before they got it. And it's been years, before I ever went on the bench as a judge that I'd been in bankruptcy court with clients, but—and that was usually from an FDIC standpoint.

Is it currently required that debtors file any tax information?

Mr. PLUNKETT. It will be under this act.

Mr. GOHMERT. No, but I mean right now. There is no requirement like that. Is that correct?

Mr. PLUNKETT. Not that I know of.

Mr. GOHMERT. All right. What, in your opinion, would be good cause to require the furnishing of the tax information?

Mr. PLUNKETT. There needs to be either a cause showing that the trustee, which is allowed access to the tax information, can't adequately verify the income and expense information required by the law. General verification of accuracy is the issue, and it needs to be a creditor, for instance, that is requesting this tax information needs to show that the trustee can't do that verification, first and foremost.

Second, the creditor needs to show a particular need based on the specifics of the individual's, that is the debtor's, problem. This should not be a form request for all cases that the creditor is a

party and interest to. That is, it needs to be an individualized decision. We have no problem, of course, because the law requires it, with the requirement that where there is cause that creditors have access to this information.

But that is going to—the issue is——

Mr. GOHMERT. Well, the question was, though, what cause? Thank you.

Mr. White—and I'm sorry to be sharp in cutting off when it is not germane to the question, but our time is so limited. Mr. White, you know, you've—well, Mr. Plunkett in his written testimony had indicated that given the ongoing problems in the credit counseling industry, and I think most of us would acknowledge there have been some, this is a very dangerous time to be requiring over a million new consumers to see credit counselors. What would be your response to that?

Mr. WHITE. I'd look at it in two ways, Congressman. First, in terms of the possibilities for salutary effect, it's quite significant because what's being done here, in many respects, is a consumer protection provision that will ensure that debtors will come into the system after first receiving counseling services so they know what their options are to go into bankruptcy or to develop other budget or alternative repayment methods. That can be very salutary.

But, as all of us know, there have been significant problems in the industry. We, at the end of June, just a few weeks ago, issued for the first time the application materials under the standards set forth in the statute. What we tried to do was to strike the appropriate balance, and we'll be learning. We've learned a lot since April. We'll learn a lot as we go along and adjust standards as necessary. But what we have done is we've put forth applications for providers to come to us to show that they are qualified and in such areas as, for example, qualifications. Are the counselors certified?

Bonding requirements, which some have suggested and Mr. Wallace did in his statement. Perhaps he believes they are a bit too stringent. There are certain background check requirements for those who are handling money or giving advice to debtors on what to do with their money. We also are requiring——

Mr. GOHMERT. But as far as the background check, who does that?

Mr. WHITE. That would have to be performed by the provider. So when they hire employees, certain employees whom we define would have to have a background check. If it is a debt management plan provider——

Mr. GOHMERT. So, in other words, you'd be looking only to the four corners of what they provide, what information they provide to determine whether or not they are legitimate, should be doing consumer counseling. Is that fair?

Mr. WHITE. We've set out certain requirements, and they would file certifications with this instant backup documentation. Yes, sir.

Mr. GOHMERT. But you're still looking only to what they provide. You do no background investigation yourself?

Mr. WHITE. We do not do the background checks. No, sir.

Mr. GOHMERT. So if they can fill out a form and do it in such a way that they sound good on paper, then they're in?

Mr. WHITE. Well, the applications will be signed under penalty of perjury, yes.

Mr. GOHMERT. And we all know that keeps everybody from perjuring themselves.

Mr. WHITE. Right. The point——

Mr. CANNON. The gentleman's time has expired. Does the gentleman——

Mr. GOHMERT. Thank you. Thank you, Mr. Chairman.

Mr. CANNON. Thank you. The Chair recognizes the gentleman from Massachusetts for 5 minutes.

Mr. DELAHUNT. Yes, I really enjoyed the line of questioning by my friend from Texas. Speaking about signing under the pains and penalties of perjury, just for my information, how many cases have been referred for criminal prosecution in the course of the past year, 2 years, 5 years?

Mr. WHITE. I believe in fiscal year 2004, it may have been in the neighborhood of 700 cases. I can provide for the record——

Mr. DELAHUNT. Out of how many, approximately?

Mr. WHITE. Out of how many cases being filed nationally? About 1.5 million or more cases were filed nationally.

Mr. DELAHUNT. So that's a very small percent. I bet—I bet that former judge down there in Texas that he could have found—you let him loose, he could have done a lot more than 700. I dare say that it's not very reassuring to me that the only protection in terms of quality control is, you know, within the four corners of an application form.

Mr. WHITE. Well, if I may say, Mr. Delahunt, if I said that is all we are doing or will do, then I've misspoken. What I'm saying is that we have an application; we do not perform background checks. The application says that the provider will perform and certify. It performs background checks, and we set out requirements.

We can get continuing information on an annual basis and, in addition, as to monitoring that is done between. The approval period is for 1 year. We have not determined what monitoring can feasibly be done during the 1-year period. We are still putting together all of our implementation plans.

But what we did issue in a very short period of time were application materials that set forth the standards consistent with what is in the statute and requiring documentation that would allow us to make a reasoned decision to see whether there is documentation to support the certifications that the standards set forth in statute have been met, that the provider is qualified and should be approved and, therefore, be able to provide the services and issue the certificates to debtors.

Mr. DELAHUNT. Mr. White, what's the price tag for this legislation?

Mr. WHITE. Well, for the U.S. Trustees——

Mr. DELAHUNT. No. The whole enchilada?

Mr. WHITE. I don't have a number.

Mr. DELAHUNT. You don't have a number?

Mr. WHITE. I don't.

Mr. DELAHUNT. Has CBO scored it different ways? Judge Small?

Judge SMALL. I don't know. I don't have a number.

Mr. DELAHUNT. Mr. Wallace, it's good seeing you back here again.

Mr. WALLACE. Nice to see you, sir.

Mr. DELAHUNT. Good to see you. Mr. Plunkett?

Mr. PLUNKETT. Don't know.

Mr. DELAHUNT. You know, there was considerable testimony—I remember, Mr. Chairman—about $500 million, possibly $1 billion. But none of you panelists have a figure. Mr. White?

Mr. WHITE. Mr. Delahunt, with regard to what the costs are to—direct costs to Government agencies and any loss to the Treasury through the——

Mr. DELAHUNT. Yes, give me that.

Mr. WHITE.—filing fees we'll provide for the record. In the supplemental appropriation recently enacted, there were filing fee increases that were designed to address the funding needs of the U.S. Trustee Program, the court system, and any other loss from the Treasury.

Mr. DELAHUNT. What was the percentage of increase in the——

Mr. WHITE. It was a significant percentage. Maybe, in the filing fee for Chapter 7, maybe in the nature of 25 or 30 percent. The U.S. Trustee cost over 5 years, at least as reflected in our budget request, is for an additional $37 million for fiscal year 2006. That's what our budget request is.

The filing fees enacted by Congress, the increase, the allocation to the U.S. Trustee Program is, over a 5-year period, $241 million.

Mr. DELAHUNT. $241 million. To get to the issue of creditor access to tax returns, the proposal put forth by Mr. Plunkett, what's your—what's your opinion of his suggestion?

Mr. WHITE. I don't have any instant reaction. We're talking with our trustees with regard to new responsibilities they'll have under the Code. So, for example, with regard to the tax returns, I think there is an assumption in Mr. Plunkett's testimony, perhaps, that the trustees will retain tax returns in all cases. I don't know that that's the case at all.

The trustees who we oversee—we appoint and oversee—will receive tax returns for purposes of verifying information. But certainly, any privacy concerns with regard——

Mr. DELAHUNT. But you wouldn't——

Mr. WHITE. I am not endorsing——

Mr. DELAHUNT. Do you share his concern about creditors receiving that information?

Mr. WHITE. The bankruptcy bill contains on balance, including in those provisions, many consumer protections and other salutary provisions. I'm not suggesting any changes at this time.

Mr. DELAHUNT. I'm not asking you that. I'm asking you whether you share——

Mr. CANNON. Would the gentleman like to ask an additional—unanimous consent for an additional 2 minutes?

Mr. DELAHUNT. Yes, I would, Mr. Chairman.

Mr. CANNON. Without objection.

Mr. DELAHUNT. Mr. White, I am asking you a concern about the privacy implications as it relates to tax returns. Do you share his concern?

Mr. WHITE. I think I would share a concern that private information that is provided on debtors ought to be addressed in the U.S. Trustee's implementation, and our oversight of the trustees ought to be foremost in our minds. And that is why, for example, in the bankruptcy bill there are numerous other privacy provisions: to ensure that private information is not put out into the public domain.

Section 107 of the Bankruptcy Code was changed, and there were other provisions. So, there are very important policy considerations. I don't——

Mr. DELAHUNT. But——

Mr. WHITE. Go ahead.

Mr. DELAHUNT. But there is no—as I understand it, it's my understanding that there's no provision in terms of the release of tax returns to creditors. There is no privacy protection incorporated into the act as passed. Is that—is that a fair statement?

Mr. WHITE. I would want to go back before I gave you a firm answer, but I am not offhand aware of what the restrictions are that a creditor would have.

Mr. DELAHUNT. Judge Small?

Judge SMALL. Well, I think you're right. It is a huge and important concern, and the director of the Administrative Office is coming up with guidelines. It is a huge and important consideration, and the director of the Administrative Office is coming up with guidelines to help protect the privacy.

There are privacy provisions. There's a privacy policy that personal information should be redacted from documents that are filed with the court, and also the court system is trying to devise a system where if a document is filed, it's not available to anybody.

Mr. DELAHUNT. Would you agree with Mr. Wallace that the creditor should have access to the IRS return?

Judge SMALL. I think the law requires that.

Mr. DELAHUNT. And is it your opinion, Mr. Plunkett, that the law requires that?

Mr. PLUNKETT. It's my opinion that the law requires it. The law also says specifically that the Administrative Office of the U.S. Courts, and I am quoting here, "Shall establish procedures for safeguarding the confidentiality of any tax information provided" and—quote—"shall include restrictions on creditor access."

So what I'm commenting on are the kinds of restrictions that I think the Administrative Office should be placing on creditor access.

Mr. DELAHUNT. Okay. Mr. Wallace, I'd feel remiss if I didn't ask you a question.

Mr. WALLACE. I was waiting for you, sir. If I could comment on this last one, I'd appreciate it.

Mr. DELAHUNT. No, because I think I know your answer there.

Mr. CANNON. Without objection, the gentleman is recognized for an additional 1 minute.

Mr. DELAHUNT. Just one final question. Thank you. What can we expect in terms of interest rate reduction from the major credit card companies as a result of the passage of this act?

Mr. WALLACE. I'm not——

Mr. DELAHUNT. Or the correct implementation of it?

Mr. WALLACE. That will be handled by the market, sir. And the marketplace presumably will take into account the savings that occurs, and competition will lower prices as appropriate if, in fact, lower prices are justified.

Mr. DELAHUNT. Right. I don't think I'm too hopeful. But thank you. I expected that answer, Mr. Wallace.

I yield back.

Mr. CANNON. Thank you.

Mr. Franks? The gentleman is recognized for 5 minutes.

Mr. FRANKS. Thank you, Mr. Chairman.

Mr. White, I know that there are sometimes people who are called on in this world to be implementers. And you have a great challenge in front of you, and I'm sure that, at this point, you have done more than a cursory analysis of the legislation that you have to implement. And again, I don't envy your job because, you know, people who make legislation in theory, and then you have to turn around and try to turn it into reality.

Having said that, did we goof anywhere? Are there any areas that you feel like are going to especially be challenging in the logistical implementation?

Mr. WHITE. We have no specific—excuse me. We have no specific suggestions to make to Congress at this time. If, as we go forward in the implementation we find there are, we certainly would discuss that with the Department and provide them to Congress.

But you're absolutely right, and I appreciate the sentiment. There is a great deal of work for the U.S. Trustee Program, and if I just may say that there has been a great deal of professionalism and enthusiasm on the part of the staff, the 1,100 people of the U.S. Trustee Program, to move forward with our implementation plans.

We've just finished a round of three regional training sessions, 2-day programs, with our senior managers going over the major provisions of the statute and the outlines of our implementation. And, in a few weeks, we'll embark upon 10 sessions, reaching almost all members of the U.S. Trustee Program to ensure that they are thoroughly familiar with the provisions of the law and those responsibilities Congress has given to us to implement and enforce the law.

Mr. FRANKS. Let me just, if you had to point to any one aspect of the legislation as the biggest challenge you had, no matter what your opinion of it is, what do you think is the biggest logistical challenge that you have?

Mr. WHITE. Well, there are two major challenges, and they have been pointed out by the Members and in the statements we've heard. Cornerstone issues for us, among others, are means testing, because there is a significant volume of work, and credit counseling. I do not wish to minimize for one moment the importance of us eventually being able to strike that right balance in ensuring that we are protecting debtors from scam operations or abusive operations, but setting rules that do not unnecessarily create barriers because we do want the capacity in the system to serve the debtors.

We've taken our initial effort. We've issued those applications in June, and we are going to be watching that very carefully. But we

are new to this area, and it is a major challenge, and we'll keep it at the top of our attention.

Mr. FRANKS. Well, thank you, sir.

And to that point, Mr. Plunkett, you gave us a couple of statistics related to I think the majority of the Chapter 7 bankruptcies being for those with a median income of—or an income of under $20,000.

Mr. PLUNKETT. Just around.

Mr. FRANKS. And then the rest of them for Chapter 13, under $30,000. Is that correct?

Mr. PLUNKETT. Yes.

Mr. FRANKS. You mentioned that part of the protocol is that the creditors, under some type of consumer credit counseling process, would hopefully offer incentives to the debtor. It doesn't sound like any incentives are actually required. If not required, what incentive would be the one that you would call for if you were writing the regulation that might follow the legislation?

Mr. PLUNKETT. New Section 502(k) of the Code provides an incentive for creditors to actually reduce the principal that is owed for people who enter credit counseling debt management plans. I'm going to summarize here, but it essentially says that a 60 percent—or a 40 percent reduction, 60 percent of what you owe, would be deemed a reasonable repayment plan. And the incentive is that if the creditor doesn't offer such a repayment plan and the consumer ends up in bankruptcy, they can seek a 20 percent reduction in what is owed.

So it's an attempt to incent creditors to offer more in the way of reductions in credit counseling. Right now all they offer, and it's fairly minimal for many creditors, is a break in interest, not in principal.

The reason more people don't use credit counseling is because creditors typically have been fairly stingy in offering these breaks. So if they do better, then more people will choose credit counseling as an alternative. If it's not financially viable for them to do so, they'll end up in bankruptcy.

Mr. FRANKS. So if I understand, those creditors that did not offer an incentive to the debtor would be diminished in their position in an actual bankruptcy?

Mr. PLUNKETT. That's the idea behind the provision.

Mr. FRANKS. Thank you, Mr. Chairman.

Mr. CANNON. I thank the gentleman.

Mr. Nadler, would you seek recognition?

Mr. NADLER. Yes, I do.

Mr. CANNON. The gentleman is recognized for 5 minutes.

Mr. NADLER. Thank you, Mr. Chairman.

Mr. Wallace, I want to follow up on Mr. Delahunt's question. We heard for any number of years prior to the passage of this bill that every adult or maybe it was every family, I forget which, in the United States paid a $400 premium in higher interest costs because of the cheating that was going on, which this bill would eliminate. And we heard that from you, among others, I think.

So would you agree that we ought to see now a $400 reduction in interest costs per family or per individual if this bill is properly implemented?

Mr. WALLACE. In the event that—although those statistics were developed back in the early period of the act, yes, I would assume that on the whole, there would be that kind of savings develop——

Mr. NADLER. And if we don't see it—and if we don't see it, then we would assume either that the bill is not being properly implemented or that the bill was fallacious?

Mr. WALLACE. I think implementation is going to be a real challenge, but I think it can be done well. And if it is done well, then there will be substantial improvement in the bankruptcy system that will——

Mr. NADLER. I didn't ask about substantial improvement. I asked about a lowering of interest rates.

Mr. WALLACE. Well, there needs to be an improvement in the bankruptcy system in order for there to be a lowering to cost.

Mr. NADLER. But you are saying that there will be that lowering of costs?

Mr. WALLACE. If the implementation is effective and as full as——

Mr. NADLER. And if we don't see it, we can assume that either the implementation was ineffective in ways that we could point out or that the bill was defective in some way?

Mr. WALLACE. On the whole, that should be the case. Yes.

Mr. NADLER. Okay. Thank you.

Mr. White, when we were considering the legislation, some Members of the Committee—myself included, former Chairman Hyde—were concerned that a debtor who was found ineligible for Chapter 7—he flunked the means test—but who could not confirm or complete a plan in Chapter 13. In other words, he might be—would be ineligible for relief under any chapter. In other words, colloquially, too rich for Chapter 7, too poor for Chapter 13.

Mr. Wallace, among others, assured this Committee these concerns were unfounded. What guidance will the executive office provide to ensure that the discretion it has under the legislation will be used so as to make Mr. Wallace's predictions not untrue? In other words, to make sure that nobody is too rich for Chapter 7, too poor for Chapter 13.

Mr. WHITE. You are very correct, Mr. Nadler, that although we are dealing with a formula under the Code with regard to the presumption on the means test that, in fact, the U.S. Trustee has a responsibility to exercise some level of discretion in deciding whether to file a motion or if it doesn't file a motion to dismiss in Chapter 7, to provide reasons for that.

We've been studying those issues, and we will be working with our field to try to ensure that all appropriate factors are taken into account. The Congress has clearly made a change in the standard. It is also indicated clearly in the statute that even if the means test shows disposable income, if the reasons for that were catastrophic medical issues, military service, and so forth, that should not be the basis for pursuing a motion based upon a presumption.

I don't have a precise answer to your question——

Mr. NADLER. But I understand that, and I appreciate that. I'm concerned sort of about the further application of that. In other words, if someone has enough income so that he doesn't meet the means test, then you would direct him to Chapter 13 rather than

Chapter 7. But he has too much income to be able to confirm a plan under—not too much income. The Chapter 13, there are requirements in the law that say that the plan, that any plan that is confirmed must enable him to pay certain things, and it may very well be that the income is not sufficient to enable him to pay those things. So you couldn't confirm Chapter 13.

How can you make sure that he isn't directed to Chapter 13 when you can't confirm a plan because the means test is just as rigid in Chapter 13 as it is in Chapter 7?

Mr. WHITE. There is no formula we can then issue to our field to say that we can take care of all particular circumstances in every case. Every case, before a motion is filed, should be the basis of a reasoned judgment by an attorney looking at the totality of circumstances in a case.

Mr. NADLER. But before you file a motion, what I am really asking is before you file a motion under Chapter 7, could you look at whether that means test applied to both Chapter 7 and Chapter 13 would allow a plan to be confirmed under Chapter 13? If the answer is no, not file the objection to go into Chapter 7.

Mr. WHITE. I'm not going to suggest that in every Chapter 7 case that we are going to do a hypothetical 13 plan and run it through to the Nth degree.

Mr. NADLER. Why not? Why not?

Mr. WHITE. I don't think that's a feasible alternative. I am saying, Mr. Nadler, that you are absolutely correct that we should not be filing a motion based strictly upon a formula that doesn't take into account what the statute tells us to take into account, which are appropriate factors and the debtor also having an opportunity to rebut.

I just don't want to commit that we can come up with some formula or some magic wand to say that in all cases that we'll have properly taken into account all factors and done it right 100 percent of the time the first time around. You are correct. And we believe, and we've talked to our attorneys. We'll continue to counsel them and watch the performance in the field to ensure that we are exercising prudent discretion.

And a debtor in some cases, for example, sir, who perhaps doesn't qualify for 13 might—and I can not anticipate all circumstances—might be able to confirm an 11 plan. There are all kinds of possibilities out there. There is no way we can reduce it to a simple formula.

Mr. NADLER. I must say, if you can't afford a 13, I can't imagine how you can do an 11.

Let me ask one quick question to Mr. Small—or to Judge Small, excuse me. Judge Small, for debtors who fit into one of the safe harbors, that is debtors not subject to the means test or whose cases cannot be dismissed under the means test, will the forms and schedules reflect this fact? Or will debtors be required to bear the paperwork burden of the means test even if they're exempt from it?

Judge SMALL. Well, as I understand the forms, and Mr. White can answer this as well, I believe that if it's shown that their income is below the median income, that would be the end of it. They

wouldn't have to go forward and fill out the rest of the means test because the means test just simply wouldn't apply to them.

Mr. NADLER. Okay. That applies, I assume, to some of the other——

Mr. CANNON. Would the gentleman like to ask unanimous consent for an additional minute or two?

Mr. NADLER. I would like to ask unanimous consent for an additional 30 seconds. That's all I think I require.

Mr. CANNON. Without objection.

Mr. NADLER. My only other question was that there are a number of safe harbors. And your answer, I assume, applies to the other safe harbors, not just the means test?

Judge SMALL. If the means test is not applicable to them, I don't see why they should have to fill out the rest of the means test.

Mr. NADLER. Thank you. I yield back.

Mr. CANNON. The gentleman yields back. Mr. Watt?

Mr. WATT. Am I the last one on the horizon?

Mr. CANNON. More or less.

Mr. WATT. Oh, next to you. I'm sorry.

First of all, let me just apologize to the witnesses for being in and out. Unfortunately, there are a number of other things going on in the world at the same time.

So I saw some estimates, when we were considering this bill, that suggested that the amount of paperwork and administrative obligation to administer this new system was going to be fairly high. Do you all remember what those projections were or have an estimate of what the additional cost of administering our bankruptcy system is likely to be compared to what it was before this reform?

Mr. White, maybe?

Mr. WHITE. In answering a similar question before, I do not know the overall number. In the recent supplemental appropriations bill, Congress has changed the filing fee structure to provide additional funding for the courts and the U.S. Trustee. We will get an additional $241 million over 5 years, and the President has requested $37 million for us in the next fiscal year to implement bankruptcy reform.

Mr. WATT. And what part of that is it anticipated will be covered by the filing fees?

Mr. WHITE. All of the costs of the U.S. Trustee Program will be fully covered by filing fees, just as all of the costs of our previous budgets have been covered by filing fees.

Mr. WATT. So you anticipate that, basically, this will just be a pass-through then. The appropriation and the income that comes from filing fees should pay for the entire bankruptcy system?

Mr. WHITE. Well, the budget we have out, it will have revenues that will at least match what we expect it will cost us to administer bankruptcy reform next year. Yes, Mr. Watt.

Mr. WATT. Next year and going forward or——

Mr. WHITE. Well, the President's budget is for fiscal year 2006. With regard to any out-years, all I can say is that there is the $241 million in the filing fee increase. So we are being given growth revenues, growth by 20 percent or more because of bankruptcy reform.

Mr. WATT. Okay. How many new additional bankruptcy judges do you anticipate will be necessary to administer the reform part of this?

Mr. WHITE. We don't have any estimates on that. The growth of our staff will be approximately 320 additional staff.

Mr. WATT. Judge Small?

Judge SMALL. Well, I think the Judicial Conference projected 47 judges would be needed, and I know 28 were included in the bill. So I think there is a need for more judges.

Mr. WATT. And the cost of those judges will be offset by the filing fees also, do you anticipate?

Judge SMALL. I can't answer that question.

Mr. WATT. Mr. White, do you anticipate the cost of the judges will be covered by the filing fees also?

Mr. WHITE. That is not a matter within, sir, my knowledge.

Mr. WATT. Mr. Plunkett or Mr. Wallace, have any idea about that?

Mr. WALLACE. No, sir.

Mr. WATT. Okay. The supply of credit counseling agencies—well, before I get to the supply, let me just try to figure out who is paying for that cost. Anybody care to venture an answer for that? Mr. Plunkett, you seem like you were about to say something.

Mr. PLUNKETT. Well, the cost will be borne by debtors and potentially by agencies. There are two requirements in the law. Fees must be reasonable, but agencies are not allowed to turn away debtors because of inability to pay.

What I've said in my testimony is that we anticipate that a significant number of those who are required to go to credit counseling will have little ability or an inability to pay. And so, that presents a whole series of problems. For the agencies, some of them may have to bear that cost if they are properly complying with the law. If they aren't, they may be doing what we call cherry-picking. That is finding sophisticated ways to provide counseling to people they believe can pay whatever fee it is that they're charging while subtly turning away people who can't. And that presents a problem.

Mr. WATT. I ask unanimous consent for 2 additional minutes.

Mr. CANNON. Without objection, so ordered.

Mr. WATT. I'm looking at a newspaper article from the Seattle Times, dated July 24, 2005, Mr. Plunkett, in which you estimated 2 million to 9 million additional credit counselors or credit counselors who would be needed. Am I misreading what you estimated?

Mr. PLUNKETT. Those are the broad estimates that have been made over the last few years about how many people seek assistance.

Mr. WATT. Oh, that is how many people seek assistance from credit counselors.

Mr. PLUNKETT. From credit counseling agencies.

Mr. WATT. Before the bankruptcy reform?

Mr. PLUNKETT. Correct. Now if we look at the number of people who filed for bankruptcy last year, Chapter 7 or Chapter 13, that would be just under 1.5 million. We assume that some portion of those people will have already met at least the first requirement,

that they receive a credit counseling briefing within 6 months of filing.

One can safely assume that somewhere around a million people, maybe a little more, maybe a little less, are going to be new to the system.

Mr. WATT. So I'm bankrupt, and then I seek credit counseling. That's supposed to do something good for me, I presume. I mean, is your experience with credit counselors that they can perform those Houdini reversals, or what is your experience with credit counseling? Maybe I shouldn't lead the witness. Judge Small is saying I'm leading the witness.

Mr. PLUNKETT. Well, we've looked at the industry hard for the last 5 years, and our experience is that if credit counseling is delivered at the right time by a reputable agency that provides good quality counseling, it can help some people. But if they——

Mr. WATT. Okay. Well, let's evaluate the components of that. What is the right time?

Mr. PLUNKETT. Well——

Mr. WATT. What is the capable person, and what are the some people?

Mr. PLUNKETT. Okay. The right time is early. That is probably before the person is on the brink of bankruptcy to the point where they are actually considering bankruptcy. And those are many of the people that will be seen by credit counselors right now.

So I'm not sure that this requirement is going to work as those who drafted it think it will because I think many people are simply going to view the credit counseling requirement as a college student would a required class that they have to sit through. They are too far gone financially to benefit from what counseling can do.

Who are the "some people?" Well, if their secured debts aren't too high and their unsecured debts, creditors offer a reasonable repayment plan on unsecured debt, a debt management plan, a credit card consolidation plan over 3 to 5 years can give those people enough breathing room to pay down their unsecured debts and start to work their way back away from the financial brink. That's some people, but that's not many people who are on the brink of bankruptcy.

Mr. WATT. Just one final question, Mr. Chairman. Now does the credit counseling requirement apply to people above the means test and below, or just to people——

Mr. PLUNKETT. It applies to everyone.

Mr. WATT. Everybody. Okay.

All right. Thank you, Mr. Chairman.

Mr. CANNON. The gentleman yields back.

Is there a more compelling voice than that sotto voce that we just heard asking insightful questions? I am trying to learn from the Ranking Member to speak more slowly and carefully myself.

Without objection, the record will be kept open for 5 additional days for any follow-up questions for the witnesses.

Mr. WATT. Would the Chairman consider extending that to 7?

Mr. CANNON. Oh, sure. Without objection, the record will be kept open for 7 legislative days for follow-up questions for the witnesses.

Mr. WATT. Thank you.

Mr. CANNON. And so ordered.

One concern I have is privacy, and so I'm going to ask a question to the whole panel, and I hope that you can all comment. But principally for those organizations that are involved in overseeing this, what organizational steps are you taking—and this will be both for you, Mr. White, and for you, Judge Small—how are you creating a function to evaluate and to continue evaluating issues of privacy?

And then, Mr. Plunkett and Mr. Wallace, if you could comment on those comments, and we'll come back for a final follow-up from the two of you, if you could? Thank you, Mr. White.

Mr. WHITE. Mr. Chairman, the responsibility in that matter that falls to us would generally be in the nature of the oversight of the trustees who would look at the tax returns. And so we have been discussing and will continue to discuss with the trustees the protocols for their handling. And it may well be that the trustees, who need the tax returns primarily for purposes of verification, should not, in most instances, retain the tax returns. They should return them at the 341 table or destroy them.

But we're very cognizant of the delicacy of that matter, and I believe our appointed trustees are as well, and we will continue to develop the appropriate protocols with them.

Mr. CANNON. Will you have someone assigned to do that in the structure of your office?

Mr. WHITE. We hadn't decided that that was necessary, but that is a point well taken.

Mr. CANNON. Let me suggest that for both the Department of Homeland Security now and the recent reauthorization of the Department of Justice, we have created a privacy officer. We've learned a great deal about that. I think Kelly O'Connor, who has done that job at DHS, has done a remarkable job in improving the way the whole department works. And this is an area where I see the potential for a huge problem.

So without a legislatively mandated officer, it may be good to think in terms of having a person or a place where the responsibility lies because, over time, you are going to see new ways of abuse, new permutations of the problem, and evolution of forms. And so, to have someone to come back and be responsible to go through a process, saying how does this affect privacy, might be a good idea.

Did you have anything you wanted to add to that, Mr. White?

Mr. WHITE. No. Point is well taken, Mr. Chairman. I appreciate it.

Mr. CANNON. Judge Small?

Judge SMALL. The director of the Administrative Office has the statutory duty to come up with some guidelines to protect the privacy, and I can give you those guidelines in about 2 weeks. The Judicial Conference is going to approve those guidelines.

Mr. CANNON. But my concern is not the guidelines so much, but the person who would be looking at those guidelines over time to say are these adequate? Given the changes in what is happening, are we doing an adequate job? In other words, some person—it could be a part-time position—somebody who exists there to occasionally come back and look at privacy.

Judge SMALL. I don't know that there is a specific person other than the director. And the director's staff has the obligation to do

these guidelines, and I assume that he'll be constantly reviewing them as we go along.

Mr. CANNON. As you create those guidelines, it might be good to keep in mind that a place with a job description with that element of the job description might actually be helpful.

Judge SMALL. I'll mention that to the director.

Mr. CANNON. Thank you. Mr. Plunkett?

Mr. PLUNKETT. Mr. Chairman, your point is well taken. I know under the privacy act, Federal agencies have to have such a privacy officer, and I think it would help ensure that as changes are made and as the situation develops that the courts can respond very quickly.

Just so you know, some of the other steps we're urging the Administrative Office to take, starting with the obvious, tax returns and transcripts shouldn't be put on the Internet or placed in public files. But also there needs to be a system of transparent recordkeeping by interested parties that receive these tax returns. And they should be able—they should be required to disclose upon request exactly who has access and has seen this information. That is a fairly inexpensive way of ensuring compliance.

We also think interested parties should be completely forbidden from redistributing this information in any fashion unless it's approved by the court. What we want to avoid is a situation, either through sloppiness or intent, where this information is lying in files or in a database somewhere where it can be accessed inappropriately. We certainly don't want creditors to be tempted to include any of this information in their internal databases.

Mr. CANNON. I suspect, Mr. Plunkett, that you would actually like to have somebody in the oversight process looking at privacy so that your groups could contact and say, hey, here is a thing you ought to look at and maybe you ought to consider?

Mr. PLUNKETT. I think that would be very helpful.

Mr. CANNON. Mr. Wallace, did you have any comments?

Mr. WALLACE. Oh, yes, sir. On the whole, I think that this discussion assumes that creditors have no interest in seeing those tax returns, and that's not the case. We approach this from a history in which despite the good interests and the good intentions of both the trustees—the Chapter 7 trustees and the U.S. Trustee—there has not been enforcement of the means test which was in the old act. That is the substantial abuse standard under 707(b).

For a number of years, creditors were basically left holding the bag. And therefore, the bill specifically, the act specifically provided that creditors could enforce, under certain circumstances, the means test. And they can also raise with by reporting to the United States trustee or to a trustee, a Chapter 7 trustee, if they think that there is an abusive case for appropriate action to be taken, regardless of whether the means test is triggered.

In order to perform that function, which is an important enforcement function and vital to their interests as well as the society as a whole in keeping the system honest, they need to have access to those tax returns. And that's important. That's an important function, a governmental function, which the bill recognized. Those provisions were contested. These issues were fully debated during the enactment process. The privacy concerns with regard to the tax re-

turns were always an issue, and the compromises were made as described.

Now the bill says creditors have access to those tax returns. They need to have access to them. It's an important function for them to do that. They are subject to the Gramm-Leach-Bliley Act, which once—this is personal, private information. Once they get that information, there is a whole host of Federal regulations that are triggered in, that apply to this information.

They cannot pass it on. They can't disseminate it. There is no such thing as putting this stuff on a Web site. Nobody is suggesting that kind of an approach. That would be ridiculous.

So everybody is very sensitive to this information, but there is a vital function that the creditors have, and this act preserved the ability of the creditor to do this because Government had failed, year in and year out, in the enforcement of 707(b).

Mr. CANNON. Thank you. Let me just say that I think everybody concurs that there's going to be a problem with privacy, that we need to watch it, that there needs to be input from outside groups. And having somebody responsible I think will be very, very important.

Mr. WALLACE. And we agree with that, sir.

Mr. CANNON. Yes, in particular, you guys want a system that will work and be above reproach. So absolutely.

The Ranking Member is recognized for an additional 5 minutes.

Mr. WATT. No, I don't need 5 minutes. I just wanted to inquire about one thing, which was the increased filing fee. What was the cost of the filing fee for bankruptcy under the old system, under the current system, and what is the projected cost under the new system?

Mr. WHITE. I'm afraid I don't have right at the tip of my tongue all of the exact numbers. I think the filing fee for Chapter 7—all fees put together, filing fees and other fees that must be paid at filing—is in the neighborhood of $275 for Chapter 7. It's somewhat less for Chapter 13.

Under the bill, the fee went up for 7. It went down for 13.

Mr. WATT. You mean we set the fee, the new filing fee in the bill?

Mr. WHITE. You did, and that——

Mr. WATT. As opposed to you all doing it administratively?

Mr. WHITE. Yes. And the supplemental appropriations bill made further adjustments in the filing fee structure and allocation of the filing fees between the court, U.S. Trustee, and general treasury.

Mr. PLUNKETT. Mr. Watt, the current fee is $209. It will rise to $274. So that is a $65 increase.

Mr. WATT. Okay. Thank you, Mr. Chair.

Mr. CANNON. As long as we keep it under $210 and under $275, I guess that is okay, right?

I want to thank the panel for being here. This is an important area. We look forward to having input in the future on this matter. We will continue to oversee it carefully.

And I want to thank the Ranking Member and other members of the panel who have been here today, and with that, we're adjourned.

[Whereupon, at 3:36 p.m., the Subcommittee was adjourned.]

A P P E N D I X

Material Submitted for the Hearing Record

LETTER TO THE HONORABLE F. JAMES SENSENBRENNER, JR., HOUSE JUDICIARY COMMITTEE, FROM BRUCE LEONARD, CHAIR, AND JOHN A. BARRETT, CHAIR, BOARD OF GOVERNORS, INTERNATIONAL INSOLVENCY INSTITUTE

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July 25, 2005

BY FAX & COURIER

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Washington, D.C. 20515
U.S.A.
(Fax) 202.225.4299

Dear Chairman Sensenbrenner:

Re: Hearing on Tuesday, July 26, 2005 at 2:00 p.m.

On behalf of the International Insolvency Institute, I am writing to recommend that, when consideration is being given to procedures applicable to the new International Chapter 15 of the *Bankruptcy Code*, that serious consideration be given to utilizing or adapting the *Guidelines for Court-to-Court Communications in Cross-Border Cases* that were developed during the course of the American Law Institute's *Transnational Insolvency Project*. The *Transnational Insolvency Project* involved studies of the insolvency laws and procedures in the three NAFTA countries of the United States, Canada and Mexico to co-ordinate reorganizations and restructurings that involved more than one of the NAFTA countries.

The *Guidelines* were developed during the project on the acknowledged basis that enhanced communications between courts and between administrations in cases affecting more than one country would have the potential of saving

literally hundreds of millions of dollars in the aggregate that is currently being lost to stakeholders, employees, suppliers, local communities and public revenue authorities. The *Guidelines* were developed by the American Law Institute as a means of creating a structure that would promote cross-border communication and co-ordination in multinational cases. It is certainly the case that multinational cases have become more common than ever before and, in fact, it is unusual to find a large case that *does not* have international issues or ramifications.

In these circumstances, experience has consistently shown that it is essential for preserving the value of the enterprise that the two courts or the two insolvency administrations should be able to communicate with each other to coordinate the way in which the respective estates are managed so as to enhance the prospects of the rehabilitation of the reorganizing entity and the recovery for everyone involved in the case.

The *Guidelines* produced in the *Transnational Insolvency Project* were developed by distinguished domestic and international lawyers, academics and judges. The *Guidelines* have been unanimously approved by the membership of the American Law Institute and by the membership of the International Insolvency Institute and have been endorsed by leading judges from around the world. The *Guidelines* therefore are an internationally-accepted set of standards for the appropriate means by which courts and insolvency administrators can communicate with each other in international reorganizations. The *Guidelines* promote reorganizations and the "fresh start" concepts that originated in United States bankruptcy legislation. Consequently, the *Guidelines* are completely consistent with Chapter 15. Procedures in Chapter 15 based upon a formulation of the *Guidelines* would have a major positive effect on international reorganizations and would lead the world in facilitating transnational and multinational reorganizational cases.

The *Guidelines* have been translated into 12 different languages and the translations have been posted for public reference on the website of the International Insolvency Institute (www.iiiglobal.org/international/guidelines.html). In a sense, therefore, if the *Guidelines* were adapted under Chapter 15, the adapted text would actually be available all over the world in the domestic languages of the countries involved. This would establish and confirm a place of prominence and pre-eminence for Chapter 15 in the international insolvency area.

INTERNATIONAL INSOLVENCY INSTITUTE

A Non-Profit Corporation Dedicated to the Improvement of International Insolvency Systems and Procedures

We are forwarding for the Committee's reference copies of the *Guidelines* for its consideration and enclose a copy herewith for ease of reference. By way of background, the International Insolvency Institute is a non-profit voluntary association of leading insolvency professionals, judges, academics and regulators which is represented in over 50 countries. The III is dedicated to the improvement of international insolvency systems and procedures.

Thank you very much for your kind consideration of this suggestion. We would be very happy to work with the Committee's staff to answer any questions and to provide any assistance that would be helpful to the Committee. With very best regards,

Yours very truly,

THE INTERNATIONAL INSOLVENCY INSTITUTE

Bruce Leonard per D.W.

Bruce Leonard
Chair

John A. Barrett per D.W.

John A. Barrett
Chair, Board Of Governors.

BL/sb
Encl.

PREPARED STATEMENT OF THE INTERNATIONAL INSOLVENCY INSTITUTE

INTERNATIONAL INSOLVENCY INSTITUTE

A Non-Profit Corporation Dedicated to the Improvement of International Insolvency Systems and Procedures

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TESTIMONY

TUESDAY, JULY 26, 2005

OVERSIGHT HEARING ON THE IMPLEMENTATION OF THE BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT OF 2005

BEFORE THE SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW HOUSE JUDICIARY COMMITTEE

The International Insolvency Institute recommends that, when consideration is being given to procedures applicable to the new International Chapter 15 of the *Bankruptcy Code,* serious consideration be given to utilizing or adapting the *Guidelines for Court-to-Court Communication in Cross-Border Cases* that were developed during the course of the American Law Institute's *Transnational Insolvency Project.* The *Transnational Insolvency Project* involved studies of the insolvency laws and procedures in the three NAFTA countries of the United States, Canada and Mexico.

The *Guidelines* were developed during the project on the acknowledged basis that enhanced communications between courts and between administrations in cases affecting more than one country would have the potential of saving literally hundreds of millions of dollars in the aggregate which is currently being lost to stakeholders, employees, suppliers, local communities and public revenue authorities. The *Guidelines* were developed by the American Law Institute as a means of creating a structure that would promote cross-border communications in multinational cases. Multinational cases have become more common than ever before and, in fact, it is unusual to find a large case that *does not* have international issues or ramifications.

In those circumstances, the experience has shown that it is essential for preserving the value of the enterprise that the two courts or the two insolvency administrations should be able to communicate with each other to coordinate the way in which the respective estates are managed with a view

to enhancing the prospects of a successful financial rehabilitation of the business involved and enhancing the prospects of an improved recovery for everyone involved in the case.

The *Guidelines* in the *Transnational Insolvency Project* were developed by distinguished domestic and international lawyers, academics and judges. The *Guidelines* have been unanimously approved by the membership of the American Law Institute and the International Insolvency Institute and have been endorsed by leading judges from around the world. The *Guidelines* therefore are an internationally-accepted set of standards for the appropriate means by which courts and insolvency administrators can communicate with each other in international reorganizations. The *Guidelines* promote reorganizations and the "fresh start" concepts that originated in United States bankruptcy legislation. Consequently, the *Guidelines* are completely consistent with Chapter 15 and procedures in Chapter 15 based upon a formulation of the *Guidelines* would have a major positive effect on international reorganizations and would lead the world in facilitating transnational and multinational reorganizational cases.

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Copies of the *Guidelines* have been provided for the Committee's reference. The text of the *Guidelines*, as indicated above, is available on the website of the International Insolvency Institute. By way of background, the International Insolvency Institute is a non-profit voluntary association of leading insolvency professionals, judges, academics and regulators which is represented in over 50 countries. The III is dedicated to the improvement of international insolvency systems and procedures.

We appreciate the Committee's kind consideration of this suggestion. We would be very happy to work with the Committee's staff to answer any questions and to provide any assistance that would be helpful to the Committee.

THE AMERICAN LAW INSTITUTE

in association with

THE INTERNATIONAL INSOLVENCY INSTITUTE

Guidelines Applicable to Court-to-Court Communications in Cross-Border Cases

As Adopted and Promulgated in Transnational Insolvency: Principles of Cooperation Among the NAFTA Countries

BY

THE AMERICAN LAW INSTITUTE
At Washington, D.C., May, 2000

And as Adopted by

THE INTERNATIONAL INSOLVENCY INSTITUTE
At New York, June, 2001

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FOREWORD

In May of 2000 The American Law Institute gave its final approval to the work of the ALI's Transnational Insolvency Project. This consisted of the four volumes eventually published, after a period of delay required by the need to take into account a newly enacted Mexican Bankruptcy Code, in 2003 under the title of *Transnational Insolvency: Cooperation Among the NAFTA Countries.* These volumes included both the first phase of the project, separate Statements of the bankruptcy laws of Canada, Mexico, and the United States, and the project's culminating phase, a volume comprising *Principles of Cooperation Among the NAFTA Countries.* All reflected the joint input of teams of Reporters and Advisers from each of the three NAFTA countries and a fully transnational perspective. Published by Juris Publishing, Inc., they can be ordered on the ALI website (www.ali.org).

A byproduct of our work on the Principles volume, these *Guidelines Applicable to Court-to-Court Communications in Cross-Border Cases* appeared originally as Appendix B of that volume and were approved by the ALI in 2000 along with the rest of the volume. But the *Guidelines* have played a vital and influential role apart from the *Principles*, having been widely translated and distributed, cited and applied by courts, and independently approved by both the International Insolvency Institute and the Insolvency Institute of Canada. Although they were initially developed in the context of a project arrived at improving cooperation among bankruptcy courts within the NAFTA countries, their acceptance by the III, whose members include leaders of the insolvency bar from more than 40 countries, suggests a pertinence and applicability that extends far beyond the ambit of NAFTA. Indeed, there appears to be no reason to restrict the *Guidelines* to insolvency cases; they should prove useful whenever sensible and coherent standards for cooperation among courts involved in overlapping litigation are called for. See, e.g., American Law Institute, International Jurisdiction and Judgments Project §12(e) (Tentative Draft, 2003).

The American Law Institute expresses its gratitude to the International Insolvency Institute for its continuing efforts to publicize the *Guidelines* and to make them more widely known to judges and lawyers around the world; to III Chair E. Bruce Leonard of Toronto, who as Canadian Co-Reporter for the Transnational Insolvency Project was the principal drafter of the Guidelines in English and has been primarily responsible for arranging and overseeing their translation into the various other languages in which they now appear; and to the translators themselves, whose work will make the *Guidelines* much more universally accessible. We hope that this greater availability, in these new English and bilingual editions, will help to foster better communication, and thus better understanding, among the diverse courts and legal systems throughout our increasingly globalized world.

LANCE LIEBMAN
Director
The American Law Institute

January 30, 2004

International Insolvency Institute

Introduction

The International Insolvency Institute, a world-wide association of leading insolvency professionals, judges, academics and regulators, is pleased to recommend the adoption and the application in cross-border and multinational cases of The American Law Institute's *Guidelines for Court-to-Court Communications in Cross-Border Cases*. The *Guidelines* were reviewed and studied by a Committee of the III and were unanimously approved by its membership at the III's Annual General Meeting and Conference in New York in June 2001.

Since their approval by the III, the *Guidelines* have been applied in several cross-border cases with considerable success in achieving the coordination that is so necessary to preserve values for all of the creditors that are involved in international cases. The III recommends without qualification that insolvency professionals and judges adopt the *Guidelines* at the earliest possible stage of a cross-border case so that they will be in place whenever there is a need for the courts involved to communicate with each other, e.g., wherever the actions of one court could impact on issues that are before the other court.

Although the *Guidelines* were developed in an insolvency context, it has been noted by litigation professionals and judges that the *Guidelines* would be equally valuable and constructive in any international case where two or more courts are involved. In fact, in multijurisdictional litigation, the positive effect of the *Guidelines* would be even greater in cases where several courts are involved. It is important to appreciate that the *Guidelines* require that all domestic practices and procedures be complied with and that the *Guidelines* do not alter or affect the substantive rights of the parties or give any advantage to any party over any other party.

The International Insolvency Institute expresses appreciation to its members who have arranged for the translation of the *Guidelines* into French, German, Italian, Korean, Japanese, Chinese, Portuguese, Russian and Swedish and extends its appreciation to The American Law Institute for the translation into Spanish. The III also expresses its appreciation to The American Law Institute, the American College of Bankruptcy, and the Ontario Superior Court of Justice Commercial List Committee for their kind and generous financial support in enabling the publication and dissemination of the *Guidelines* in bilingual versions in major countries around the world.

Readers who become aware of cases in which the *Guidelines* have been applied are highly encouraged to provide the details of those cases to the III (fax: 416-360-8877; email: *info@iiiglobal.org*.) so that everyone can benefit from the experience and positive

results that flow from the adoption and application of the *Guidelines*. The continuing progress of the *Guidelines* and the cases in which the *Guidelines* have been applied will be maintained on the III 's website at *www.iiiglobal.org*.

The III and all of its members are very pleased to have been a part of the development and success of the *Guidelines* and commend The American Law Institute for its vision in developing the *Guidelines* and in supporting their worldwide circulation to insolvency professionals, judges, academics, and regulators. The use of the *Guidelines* in international cases will change international insolvencies and reorganizations for the better forever and the insolvency community owes a considerable debt to The American Law Institute for the inspiration and vision that has made this possible.

E. Bruce Leonard
Chairman
The International Insolvency Institute

Toronto, Ontario
March, 2004

Judicial Preface

We believe that the advantages of co-operation and co-ordination between Courts is clearly advantageous to all of the stakeholders who are involved in insolvency and reorganization cases that extend beyond the boundaries of one country. The benefit of communications between Courts in international proceedings has been recognized by the United Nations through the *Model Law on Cross-Border Insolvency* developed by the United Nations Commission on International Trade Law and approved by the General Assembly of the United Nations in 1997. The advantages of communications have also been recognized in the European Union Regulation on Insolvency Proceedings which became effective for the Member States of the European Union in 2002.

The *Guidelines for Court-to-Court Communications in Cross-Border Cases* were developed in the American Law Institute's Transnational Insolvency Project involving the NAFTA countries of Mexico, the United States and Canada. The *Guidelines* have been approved by the membership of the ALI and by the International Insolvency Institute whose membership covers over 40 countries from around the world. We appreciate that every country is unique and distinctive and that every country has its own proud legal traditions and concepts. The *Guidelines* are not intended to alter or change the domestic rules or procedures that are applicable in any country and are not intended to affect or curtail the substantive rights of any party in proceedings before the Courts. The *Guidelines* are intended to encourage and facilitate co-operation in international cases while observing all applicable rules and procedures of the Courts that are respectively involved.

The *Guidelines* may be modified to meet either the procedural law of the jurisdiction in question or the particular circumstances in individual cases so as to achieve the greatest level of co-operation possible between the Courts in dealing with a multinational insolvency or liquidation. The *Guidelines*, however, are not restricted to insolvency cases and may be of assistance in dealing with non-insolvency cases that involve more than one country. Several of us have already used the *Guidelines* in cross-border cases and would encourage stakeholders and counsel in international cases to consider the advantages that could be achieved in their cases from the application and implementation of the *Guidelines*.

Mr. Justice David Baragwanath
High Court of New Zealand
Auckland, New Zealand

Chief Justice Donald I. Brenner
Supreme Court of British Columbia
Vancouver

Hon. Sidney B. Brooks
United States Bankruptcy Court
District of Colorado
Denver

Hon. Charles G. Case, II
United States Bankruptcy Court
District of Arizona
Phoenix

Mr. Justice Miodrag Dordević
Supreme Court of Slovenia
Ljubljana

Mr. Justice J.M. Farley
Ontario Superior Court of Justice
Toronto

Hon. James L. Garrity, Jr.
United States Bankruptcy Court
Southern District of New York (Ret'd)
Shearman & Sterling
New York

Hon. Allan L. Gropper
Southern District of New York
United States Bankruptcy Court
New York

Mr. Justice Paul R. Heath
High Court of New Zealand
Auckland, New Zealand

Hon. Hyungdu Kim
Supreme Court of Korea
Seoul

Chief Judge Burton R. Lifland
United States Bankruptcy Appellate
Panel for the Second Circuit
New York

Mr. Justice Gavin Lightman
Royal Courts of Justice
London

Hon. George Paine II
United States Bankruptcy Court
District of Tennessee
Nashville

Hon. Chiyong Rim
District Court
Western District of Seoul
Seoul, Korea

Mr. Justice Adolfo A.N. Rouillon
Court of Appeal
Rosario, Argentina

Hon. Shinjiro Takagi
Supreme Court of Japan (Ret'd)
Industrial Revitalization Corporation of Japan
Tokyo

Mr. Justice Wisit Wisitsora – At
Business Reorganization Office
Government of Thailand
Bangkok

Mr. Justice R.H. Zulman
Supreme Court of Appeal of South Africa
Parklands

Guidelines
Applicable to Court-to-Court Communications
in Cross-Border Cases

Introduction:

One of the most essential elements of cooperation in cross-border cases is communication among the administrating authorities of the countries involved. Because of the importance of the courts in insolvency and reorganization proceedings, it is even more essential that the supervising courts be able to coordinate their activities to assure the maximum available benefit for the stakeholders of financially troubled enterprises.

These Guidelines are intended to enhance coordination and harmonization of insolvency proceedings that involve more than one country through communications among the jurisdictions involved. Communications by judges directly with judges or administrators in a foreign country, however, raise issues of credibility and proper procedures. The context alone is likely to create concern in litigants unless the process is transparent and clearly fair. Thus, communication among courts in cross-border cases is both more important and more sensitive than in domestic cases. These Guidelines encourage such communications while channeling them through transparent procedures. The Guidelines are meant to permit rapid cooperation in a developing insolvency case while ensuring due process to all concerned.

A Court intending to employ the Guidelines — in whole or part, with or without modifications — should adopt them formally before applying them. A Court may wish to make its adoption of the Guidelines contingent upon, or temporary until, their adoption by other courts concerned in the matter. The adopting Court may want to make adoption or continuance conditional upon adoption of the Guidelines by the other Court in a substantially similar form, to ensure that judges, counsel, and parties are not subject to different standards of conduct.

The Guidelines should be adopted following such notice to the parties and counsel as would be given under local procedures with regard to any important procedural decision under similar circumstances. If communication with other courts is urgently needed, the local procedures, including notice requirements, that are used in urgent or emergency situations should be employed, including, if appropriate, an initial period of effectiveness, followed by further

consideration of the Guidelines at a later time. Questions about the parties entitled to such notice (for example, all parties or representative parties or representative counsel) and the nature of the court's consideration of any objections (for example, with or without a hearing) are governed by the Rules of Procedure in each jurisdiction and are not addressed in the Guidelines.

The Guidelines are not meant to be static, but are meant to be adapted and modified to fit the circumstances of individual cases and to change and evolve as the international insolvency community gains experience from working with them. They are to apply only in a manner that is consistent with local procedures and local ethical requirements. They do not address the details of notice and procedure that depend upon the law and practice in each jurisdiction. However, the Guidelines represent approaches that are likely to be highly useful in achieving efficient and just resolutions of cross-border insolvency issues. Their use, with such modifications and under such circumstances as may be appropriate in a particular case, is therefore recommended.

Guideline 1

Except in circumstances of urgency, prior to a communication with another Court, the Court should be satisfied that such a communication is consistent with all applicable Rules of Procedure in its country. Where a Court intends to apply these Guidelines (in whole or in part and with or without modifications), the Guidelines to be employed should, wherever possible, be formally adopted before they are applied. Coordination of Guidelines between courts is desirable and officials of both courts may communicate in accordance with Guideline 8(d) with regard to the application and implementation of the Guidelines.

Guideline 2

A Court may communicate with another Court in connection with matters relating to proceedings before it for the purposes of coordinating and harmonizing proceedings before it with those in the other jurisdiction.

Guideline 3

A Court may communicate with an Insolvency Administrator in another jurisdiction or an authorized Representative of the Court in that jurisdiction in connection with the coordination and harmonization of the proceedings before it with the proceedings in the other jurisdiction.

Guideline 4

A Court may permit a duly authorized Insolvency Administrator to communicate with a foreign Court directly, subject to the approval of the foreign Court, or through an Insolvency Administrator in the other jurisdiction or through an authorized Representative of the foreign Court on such terms as the Court considers appropriate.

Guideline 5

A Court may receive communications from a foreign Court or from an authorized Representative of the foreign Court or from a foreign Insolvency Administrator and should respond directly if the communication is from a foreign Court (subject to Guideline 7 in the case of two-way communications) and may respond directly or through an authorized Representative of the Court or through a duly authorized Insolvency Administrator if the communication is from a foreign Insolvency Administrator, subject to local rules concerning ex parte communications.

Guideline 6

Communications from a Court to another Court may take place by or through the Court:

(a) Sending or transmitting copies of formal orders, judgments, opinions, reasons for decision, endorsements, transcripts of proceedings, or other documents directly to the other Court and providing advance notice to counsel for affected parties in such manner as the Court considers appropriate;

(b) Directing counsel or a foreign or domestic Insolvency Administrator to transmit or deliver copies of documents, pleadings, affidavits, factums, briefs, or other documents that are filed or to be filed with the Court to the other Court in such fashion as may be appropriate and providing advance notice to counsel for affected parties in such manner as the Court considers appropriate;

(c) Participating in two-way communications with the other Court by telephone or video conference call or other electronic means, in which case Guideline 7 should apply.

Guideline 7

In the event of communications between the Courts in accordance with Guidelines 2 and 5 by means of telephone or video conference call or other electronic means, unless otherwise directed by either of the two Courts:

(a) Counsel for all affected parties should be entitled to participate in person during the communication and advance notice of the communication should be given to all parties in accordance with the Rules of Procedure applicable in each Court;

(b) The communication between the Courts should be recorded and may be transcribed. A written transcript may be prepared from a recording of the communication which, with the approval of both Courts, should be treated as an official transcript of the communication;

(c) Copies of any recording of the communication, of any transcript of the communication prepared pursuant to any Direction of either Court, and of any official transcript prepared from a recording should be filed as part of the record in the proceedings and made available to counsel for all parties in both Courts subject to such Directions as to confidentiality as the Courts may consider appropriate; and

(d) The time and place for communications between the Courts should be to the satisfaction of both Courts. Personnel other than Judges in each Court may communicate fully with each other to establish appropriate arrangements for the communication without the necessity for participation by counsel unless otherwise ordered by either of the Courts.

Guideline 8

In the event of communications between the Court and an authorized Representative of the foreign Court or a foreign Insolvency Administrator in accordance with Guidelines 3 and 5 by means of telephone or video conference call or other electronic means, unless otherwise directed by the Court:

(a) Counsel for all affected parties should be entitled to participate in person during the communication and advance notice of the

communication should be given to all parties in accordance with the Rules of Procedure applicable in each Court;

(b) The communication should be recorded and may be transcribed. A written transcript may be prepared from a recording of the communication which, with the approval of the Court, can be treated as an official transcript of the communication;

(c) Copies of any recording of the communication, of any transcript of the communication prepared pursuant to any Direction of the Court, and of any official transcript prepared from a recording should be filed as part of the record in the proceedings and made available to the other Court and to counsel for all parties in both Courts subject to such Directions as to confidentiality as the Court may consider appropriate; and

(d) The time and place for the communication should be to the satisfaction of the Court. Personnel of the Court other than Judges may communicate fully with the authorized Representative of the foreign Court or the foreign Insolvency Administrator to establish appropriate arrangements for the communication without the necessity for participation by counsel unless otherwise ordered by the Court.

Guideline 9

A Court may conduct a joint hearing with another Court. In connection with any such joint hearing, the following should apply, unless otherwise ordered or unless otherwise provided in any previously approved Protocol applicable to such joint hearing:

(a) Each Court should be able to simultaneously hear the proceedings in the other Court.

(b) Evidentiary or written materials filed or to be filed in one Court should, in accordance with the Directions of that Court, be transmitted to the other Court or made available electronically in a publicly accessible system in advance of the hearing. Transmittal of such material to the other Court or its public availability in an electronic system should not subject the party filing the material in one Court to the jurisdiction of the other Court.

(c) Submissions or applications by the representative of any party should be made only to the Court in which the representative making the submissions is appearing unless the representative is specifically given permission by the other Court to make submissions to it.

(d) Subject to Guideline 7(b), the Court should be entitled to communicate with the other Court in advance of a joint hearing, with or without counsel being present, to establish Guidelines for the orderly making of submissions and rendering of decisions by the Courts, and to coordinate and resolve any procedural, administrative, or preliminary matters relating to the joint hearing.

(e) Subject to Guideline 7(b), the Court, subsequent to the joint hearing, should be entitled to communicate with the other Court, with or without counsel present, for the purpose of determining whether coordinated orders could be made by both Courts and to coordinate and resolve any procedural or nonsubstantive matters relating to the joint hearing.

Guideline 10

The Court should, except upon proper objection on valid grounds and then only to the extent of such objection, recognize and accept as authentic the provisions of statutes, statutory or administrative regulations, and rules of court of general application applicable to the proceedings in the other jurisdiction without the need for further proof or exemplification thereof.

Guideline 11

The Court should, except upon proper objection on valid grounds and then only to the extent of such objection, accept that Orders made in the proceedings in the other jurisdiction were duly and properly made or entered on or about their respective dates and accept that such Orders require no further proof or exemplification for purposes of the proceedings before it, subject to all such proper reservations as in the opinion of the Court are appropriate regarding proceedings by way of appeal or review that are actually pending in respect of any such Orders.

Guideline 12

The Court may coordinate proceedings before it with proceedings in another jurisdiction by establishing a Service List that may include parties that are entitled to receive notice of proceedings before the Court in the other jurisdiction ("Non-Resident Parties"). All notices, applications, motions, and other materials served for purposes of the proceedings before the Court may be ordered to also be provided to or served on the Non-Resident Parties by making such materials available electronically in a publicly accessible system or by facsimile transmission, certified or registered mail or delivery by courier, or in such other manner as may be directed by the Court in accordance with the procedures applicable in the Court.

Guideline 13

The Court may issue an Order or issue Directions permitting the foreign Insolvency Administrator or a representative of creditors in the proceedings in the other jurisdiction or an authorized Representative of the Court in the other jurisdiction to appear and be heard by the Court without thereby becoming subject to the jurisdiction of the Court.

Guideline 14

The Court may direct that any stay of proceedings affecting the parties before it shall, subject to further order of the Court, not apply to applications or motions brought by such parties before the other Court or that relief be granted to permit such parties to bring such applications or motions before the other Court on such terms and conditions as it considers appropriate. Court-to-Court communications in accordance with Guidelines 6 and 7 hereof may take place if an application or motion brought before the Court affects or might affect issues or proceedings in the Court in the other jurisdiction.

Guideline 15

A Court may communicate with a Court in another jurisdiction or with an authorized Representative of such Court in the manner prescribed by these Guidelines for purposes of coordinating and harmonizing proceedings before it with proceedings in the other jurisdiction regardless of the form of the proceedings before it or before the other Court wherever there is commonality among the issues and/or the parties in the proceedings. The Court should, absent

compelling reasons to the contrary, so communicate with the Court in the other jurisdiction where the interests of justice so require.

Guideline 16

Directions issued by the Court under these Guidelines are subject to such amendments, modifications, and extensions as may be considered appropriate by the Court for the purposes described above and to reflect the changes and developments from time to time in the proceedings before it and before the other Court. Any Directions may be supplemented, modified, and restated from time to time and such modifications, amendments, and restatements should become effective upon being accepted by both Courts. If either Court intends to supplement, change, or abrogate Directions issued under these Guidelines in the absence of joint approval by both Courts, the Court should give the other Courts involved reasonable notice of its intention to do so.

Guideline 17

Arrangements contemplated under these Guidelines do not constitute a compromise or waiver by the Court of any powers, responsibilities, or authority and do not constitute a substantive determination of any matter in controversy before the Court or before the other Court nor a waiver by any of the parties of any of their substantive rights and claims or a diminution of the effect of any of the Orders made by the Court or the other Court.

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The text of the *Guidelines Court-to-Court Communications in Cross-Border Cases* is available in English and several other languages including Chinese, French, German, Italian, Japanese, Korean, Portuguese, Russian, Spanish and Swedish on the website of the International Insolvency Institute at http://www.iiiglobal.org/international/guidelines.html.

Insert A

This translation has been made, published and distributed with the authorization of The American Law Institute. The American Law Institute and the International Insolvency Institute express their appreciation to ____________ [Please insert name of translator] for creating and providing this translation.

PREPARED STATEMENT OF SAMUEL K. CROCKER, ON BEHALF OF THE NATIONAL ASSOCIATION OF BANKRUPTCY TRUSTEES, SUBMITTED BY THE HONORABLE MARK GREEN, A REPRESENTATIVE IN CONGRESS, FROM THE STATE OF UTAH

On behalf of the National Association of Bankruptcy Trustees (NABT), I would like to thank the Subcommittee for the opportunity to comment on the implementation of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (the "ACT"). NABT represents the interests of over 1,200 private panel Trustees who administer cases filed under Chapter 7. Panel Trustees will have an important role in the administration of the new provisions of the Act and we are committed to making the Act work. Our comments today are focused on issues relating to the implementation of the Act.

First let me say that Chapter 7 panel Trustees are committed to implementing the changes to the Code which have been proscribed by Congress. As the "gatekeepers" of the bankruptcy system, we will always utilize the tools provided us to help honest but unfortunate Debtors get the relief intended them, while being ever vigilant for fraudulent and abusive filings. The NABT is committed to maintaining the effectiveness of the system, and to that end we believe there are several areas of the law that Congress may want to look at with an eye toward implementation, which may effectively allow us to do what was intended.

1. Notification of Child Support Claimants

NABT is at work developing methods to implement the new § 704(a)(10), through which child support claimants will be notified of their rights as creditors in Chapter 7 cases of Debtors from whom a support obligation is due. We envision that this provision will, with the cooperation of the EODST, be effectively implemented through a series of procedures and notices provided by the panel Trustee throughout the case. We believe that, through this process, claimants owed domestic support obligations can and will be made aware of the options available to them to enforce Court-ordered support.

2. Additional Information Required of Debtors

NABT believes that the additional information which is required to be furnished to the Trustee (and others), prior to the first meeting of creditors, will aid in the identification and liquidation of assets for the benefit of creditors. We are actively working on methods of delivery which will allow us to effectively utilize the volume of information which will be provided to us by each Debtor. Additionally, we will attempt to insure that this information will remain confidential, and be used solely for the purposes intended by the statute.

Review of this required information will serve to insure that all assets are disclosed and, where appropriate, applied to the payment of creditors' claims. It will also, in many cases, more adequately define the Debtors' circumstances, which will allow the panel Trustee to perform the job more effectively.

3. Waiver of Filing Fee

Amended 28 U.S.C. § 1930(f)(1) provides for the waiver of Chapter 7 case filing fees for individuals with "income less than 150 percent of the income official poverty line" if the Court determines the individual is unable to pay the fee in installments.

Trustees are paid compensation of $60.00 for administering cases in which no assets are available for liquidation. The funding for these fees is derived from the Chapter 7 case filing fee [see 11 U.S.C. § 330(b)(I)] and Miscellaneous Bankruptcy Court Fees prescribed by the Judicial Conference of the United States [see 11 U.S.C. § 330(b)(2)].

The Act makes no provision for payments to Trustees in those cases where the filing fees are waived. Some have even suggested that the statutory language as drafted may prevent Trustees from being paid for services in such cases. This apparent oversight needs to be corrected, and a system established to provide adequate funding for payment of Trustee fees in these cases.

4. Protecting Patient Records

The Act adds a new § 351 to the Code that provides a procedure for notification and disposal of patient records in cases where the Trustee does not have sufficient funds to pay for the storage of records in the manner required under applicable federal or state laws. The Act fails to take into account that in some cir-

cumstances Trustees will lack sufficient funds to comply with the procedure established under § 351. For example, under § 351 Trustees are required to undertake various costly actions including: storing records for one year; publishing a notice in one or more appropriate newspapers; notifying every patient and appropriate insurance carrier by mail; communicating by certified mail with each appropriate federal agency; and destroying the records. It is estimated that these costs could range anywhere from $3,500.00 in smaller cases (500 or fewer patients) to $35,000.00 in medium cases (10,000 patients) and higher in large cases (up to 100,000 patients and more). If Trustees do not have the funds to pay for the storage and notices required in § 351, patient records may not be administered properly and could be lost.

The problem can be corrected by allowing a court in no asset or limited asset cases, upon motion of the Trustee, to direct the person or persons responsible for maintaining, storing or disposing of patient records under state law, prior to the appointment of the trustee, to resume the responsibility of preserving the records. In such circumstances, the responsible party would be directed, by court order, to perform the functions required under § 351.

5. Payment in Converted Cases

The Act was intended to provide a mechanism and payment schedule for Chapter 7 Trustees to receive compensation in cases converted or dismissed pursuant to 707(b). The Act included changes to § 1326(b) of the Code specifying the payment schedule to be applied if Trustees are allowed compensation due to the conversion or dismissal of case under § 707(b). These changes are inadvertently ineffective, however, unless § 326 of the Code is also modified to provide for Trustee compensation in converted or dismissed cases. Under current judicial interpretations of § 326, Trustees have been denied compensation in cases converted or dismissed under § 707(b) because Trustees have not actually disbursed or turned over moneys to parties in interest in such cases (which that statute requires as a prerequisite).

The problem can be corrected by adding a new subsection (e) to § 326 to provide that the Court may allow reasonable compensation for services rendered by the Trustee, if the Trustee in a Chapter 7 case commences a motion to dismiss or convert under § 707(b) and such motion is granted, or if the case is converted from Chapter 7 to another chapter, and the actions or positions of the Chapter 7 Trustee were a factor in the conversion of the case. Since cases are most often converted from Chapter 7 to 13 without the processing of a formal § 707(b) motion (a threat of a motion is often sufficient), Trustees should be allowed compensation if their actions or positions were a factor in the conversion of the case.

Trustees have and will continue to drive those Debtors who have an ability to repay some or all of their debts into a Chapter 13 repayment plan. It was the intent of Congress to reward us for these efforts, and encourage the continued vigilance.

6. Avoiding Automatic Dismissal in Asset Cases

The Act modifies § 521 of the Code to compel an automatic dismissal of cases where certain information is not timely provided. If a Debtor does not reaffirm or surrender collateral within 45 days after the first meeting of creditors, the automatic stay under § 362(a) is terminated and the property "shall no longer be property of the estate", even if there is equity in that property for the benefit of the estate.

The automatic dismissal language raises concerns insofar as it renders valuable property "no longer property of the estate" and places it beyond the reach of the trustee or the court. Trustees may not be able to determine whether there are unencumbered non-exempt assets to administer by the deadlines imposed under § 521, in part, because debtors who are dilatory in reaffirming/surrendering are often unresponsive to trustees. Although trustees may ask for extensions of the § 521 deadlines, circumstances may prevent the trustee from having sufficient information to support a motion for an extension of time.

Terminating the stay under § 326(a) is adequate to allow a creditor to take action with respect to property as permitted under applicable law. This would also serve to avoid decreeing that the property is "no longer property of the estate" and ensure that valuable property will not be lost to the estate and its creditors in some cases.

7. Increase in "No Asset Fee"

Under the present law, Trustees receive $60.00 for administering Chapter 7 cases in which no assets are liquidated. The last increase in this Trustee compensation occurred in 1996, when the fee was raised from $45.00 to $60.00.