

## **Did the 2005 change to the bankruptcy code have its desired effect?**

In 2005 Congress passed a sweeping reform of the US Bankruptcy Code that was allegedly intended to reduce the number of people filing bankruptcy by making it more difficult to discharge your debts.

In their infinite wisdom, Congress intentionally kept the entire bankruptcy bar, judiciary, and educators out of the loop; after all, they were the fox guarding the hen house. The system was badly broken, and those inside it couldn't be trusted to have any real input on reform. Right?

Actually, the system (at least in the three Federal Districts where I have practiced) was not broken. Credit card companies complained that they needed to have high interest rates and charges because so many people were filing bankruptcy, and Congress listened. Sort of.

Let me give a side note here – have credit card companies reduced their interest rates and fees since 2005 because fewer people were filing bankruptcy? Yeah right.

Well Congress rewrote the book on bankruptcy, but all they really accomplished was to make it more expensive to go bankrupt and create a lot more busy work for a lot of people in the legal field who could now charge more to help out those going bankrupt. The new law required the debtor's attorney to fill out forms to see whether a person qualified for a Chapter 7 bankruptcy (liquidation) or a Chapter 13 bankruptcy (reorganization) using national IRS standards for the basis of calculating expenses.

The old way of dealing with this was for the debtors to file their bankruptcy Schedules, and for those involved to look at the amount of expenses claimed, and excess income left to pay debts each month, and determine which chapter best fit the bill. While changing the rules didn't really change the outcome (there are a few exceptions where it does, but that's another blog), it did make a lot more paperwork for attorneys (who get paid to do it).

The new bankruptcy code also made things complex enough that while people are still allowed to represent themselves, it is highly recommended they don't attempt it, as a mistake in procedure can result in the complete dismissal of a case (and the new Code gives the judges no gray areas to give credit for the best compliance that an individual can accomplish).

In addition the new bankruptcy code is poorly written. Here's an example. Congress wanted to stop people from filing back to back to back bankruptcies, so they wrote rules limiting the protection from creditors if there had been a case dismissed within one calendar year prior to the current filing, and rules if there had been 2 or more cases dismissed in that time period.

The rules for one prior case clearly state that if the debtor does not request and have a hearing to show the court why their creditor protection (the automatic stay) should continue, it will end 30 days after the 2nd case is filed. What Congress intended was for creditor protection to end after 30 days. What they wrote, however was that the automatic stay ends as to the debtor after 30

days. To a layman, that may not seem like a problem. The legal result, however, is that while the creditor protection terminates in 30 days (assuming no hearing, or no order from a hearing extending the automatic stay) it only terminates as to the person themselves, and NOT as to their property. This means the property they own remains under the trustee's control, and their creditors can't touch it. That section, being poorly written, gave the creditors nothing.

Of course Congress worded the section regarding 2 or more prior dismissed bankruptcy cases within a calendar year differently, and the automatic stay protection there will end as to the person and as to their property (what Congress wanted for both sections).

Another example is a paragraph that was not given a number or letter in drafting the rules (all laws have a number and/or letter for each paragraph like an outline, making it possible to find the exact paragraph being used by an attorney). It's been 5 years, and Congress hasn't seen fit to go back and amend to either number or letter that one paragraph they missed.

This might not seem like much to most people, but the legal effect is that there is a split of opinions between courts as to whether the paragraph modifies ONLY the immediate preceding paragraph, or whether it modifies the ENTIRE preceding section – very different results.

In the long run, the bankruptcy code rewrite of 2005 did reduce the number of bankruptcies filed, but it is my opinion that much of that is due to several reasons.

The immediate drop in filings after the 2005 code went into effect was due to the press it received in advance. Bankruptcy attorneys nationwide filed record numbers of cases in the month immediately preceding the effective date of the 2005 change, and then no cases for months after.

The next drop in filings was also due in part to the press the revision received in the bankruptcy community. We had all seen the sweeping changes that were to go into effect, had seen all the additional work required, had seen possible problems from multiple poorly written sections, and many of the bankruptcy attorneys just gave up. Some retired, some just moved to doing other types of work. Most of those have never come back to filing bankruptcies.

Another drop has had to do with the increased cost to go bankrupt. Filing fees changed, as well as the amount that an attorney was going to charge you. The new procedures were so complex the average layman can't follow them in order to file on their own. So effectively, the broke among us can't afford to go bankrupt.

Did the 2005 change help the credit card industry? No way. At least not in any way you have seen. Did the code change make rates go down? No. Did charges go down? No. Has the code made it harder to file bankruptcy on your credit cards? Not really. Did the code stabilize the credit industry? I'll let the present economy speak to that.

I would love to hear your thoughts on this. Isn't this just more of Congress wasting everyone's time and money to fix something that wasn't broken?

See my poll on Linded in on this topic.

<http://polls.linkedin.com/p/101272/ydgyp>