



# Chapter 7

## Attorney's Fees

A look at the issues and caselaw regarding unconventional arrangements such as unbundling and bifurcation.

1



## Types of Arrangements

- Traditional Fee Agreements
- Non-Traditional Fee Agreements
  - Unbundling
  - Bifurcating fees
  - Bifurcating fees with Factoring
- Fee-Only Chapter 13

2

## Traditional Fee Agreements

- Proposed debtor pays counsel in full for services related to bankruptcy case before case is filed.
- Client either pays lump sum or is on a payment plan with the attorney until the fee is paid in full.
- *Lamie v. United States Trustee*, 124 S. Ct. 1023, 1032 (2004) ("It appears to be routine for debtors to pay reasonable fees for legal services before filing for bankruptcy to ensure compliance with statutory requirements.").

## Disclosure Requirements

- Section 329 requires attorneys to file with the court a statement of the compensation paid if the payment was made within one year of the filing and in contemplation of bankruptcy.
- Rule 2016(b) requires attorneys to file within 14 days after the order for relief the statement required by section 329, including whether the attorney has agreed to share the compensation with any other attorney.

## Other Governing Statutes

- Sections 526-528 of the Bankruptcy Code establish restrictions and requirements for debt relief agencies.
- Section 528(a)(1) requires a debt relief agency to execute a written contract with an assisted person
  - Within five business days after first provide service; and
  - Before the petition is filed.

## More on Traditional Fee Arrangements

- Any unpaid pre-petition fees are dischargeable. *Rittenhouse v. Eisen*, 404 F.3d 395, 397 (6th Cir. 2005); *Bethea v. Robert J. Adams & Assocs.*, 352 F.3d 1125, 1129 (7th Cir. 2003); *Hessinger and Assocs. v. U.S. Trustee (In re Biggar)*, 110 F.3d 685, 688 (9th Cir. 1997).
- While one circuit court has held that fees owed for services rendered post-petition, even when based on a pre-petition contract, may be collected without running afoul of the stay or discharge, the only other court of appeals that has addressed this question soundly rejected this approach. *Compare Gordon v. Hines (In re Hines)*, 147 F.3d 1185, 1191 (9th Cir. 1998) with *Bethea*, 352 F.3d 1125.

## Non-traditional Fee Agreements

- Unbundling – limiting services
- Bifurcating fees – distinguishing between pre-petition and post-petition services.
- Bifurcating with factoring - distinguishing between pre-petition and post-petition services, then using a third-party finance company

## What is Unbundling?

- Unbundling is limiting services provided to the client.

## Process of Unbundling

- The attorney prepares and files the petition for the debtor, but then does not agree to represent the debtor for all services post-petition.
- For example, the attorney might provide that it will not represent the debtor at the meeting of creditors or on motions for relief from stay or reaffirmation agreements.

## Cases Discussing Unbundling

- *Dignity Health v Seare (In re Seare)*, 493 B.R. 158 (Bankr. D. Nev. 2013)
- *In re Ortiz*, 496 B.R. 144 (Bankr. S.D.N.Y. 2013)
- *In re Ruiz*, 515 B.R. 362 (Bankr. M.D. Fla. 2014)



## *Dignity Health v Seare (In re Seare)*, 493 B.R. 158 (Bankr. D. Nev. 2013).

- This lengthy opinion examines all the issues regarding unbundling legal services to chapter 7 debtors. The 19 page retainer agreement provided that representation in any adversary proceedings would require an extra fee. When a creditor then filed a nondischargeability lawsuit against the debtors, counsel refused to represent them. The court found counsel's actions unreasonable given that the lawsuit was a "near certainty" under the facts of this case and defense of that action was necessary to achieve the debtors' goals in the case. Court found counsel failed his essential duty—to understand the clients' objective—and required disgorgement of all fees.

## *In re Ortiz*, 496 B.R. 144 (Bankr. S.D.N.Y. 2013)

- The Court found that chapter 7 debtor's counsel impermissibly excluded certain basic services in retention agreement, such as attendance at more than one 341 meeting.

## *In re Ruiz*, 515 B.R. 362 (Bankr. M.D. Fla. 2014)

- Attorney prepared bankruptcy petition, schedules, and statements, but did not sign the petition. Pursuant to the contract between the 82 year old debtor and the attorney, the attorney also agreed to assist the debtor post-petition with gathering documents for the trustee and with questions until the discharge was received but would not attend the meeting of creditors. The Court held that this limitation on representation which excluded attendance at the meeting of creditors and other fundamental duties was unreasonable under the circumstances and ordered all funds disgorged.

## What is bifurcation?

- When an attorney splits the work between pre-petition and post-petition services. Attorney representing the client in a chapter 7 bankruptcy case use two separate fee agreements.

## Process of bifurcation

Under the first “pre-petition” agreement, the debtor pays a nominal or no fee for work performed on the case prior to filing (i.e. Skeletal or barebones petition)

After filing, the debtor and attorney enter into a second, “postpetition” agreement, which covers preparation and filing of the schedules, statement of financial affairs, required documents and other post-petition services.

## *Recent Cases Discussing Bifurcation*

- *In re Grimmett*, 2017 Bankr. Lexis 1492 (Bankr. D. Idaho, June 15, 2017).
- *In re Hazlett*, 2019 WL 1567751 (Bankr. D. Utah April 10, 2019).
- *In Re Carr*, 613 B.R. 427 (Bankr. E.D. Ky 2020).



## *In re Grimmett*, 2017 Bankr. Lexis 1492 (Bankr. D. Idaho, June 15, 2017).

- Chapter 7 debtor's attorney entered into an agreement that provided the debtor would pay \$500 pre-petition for pre-petition services and \$1,500 post-petition for post-petition services, including preparing schedules and appearing at the meeting of creditors. The agreement provided that failure to pay could result in dismissal of the case, withdrawal of counsel, and a collection action. Post-petition, counsel informed client of "drastic actions" that would result from failure to pay. On a motion by the U.S. Trustee, the court ordered counsel to disgorge all fees, finding that counsel engaged in "a variety of inappropriate conduct and actions." Among other things, counsel improperly attempted to unbundle services and created a conflict of interest with the client through threats to terminate representation and coercive collection procedures.

## *In re Hazlett*, 2019 WL 1567751 (Bankr. D. Utah April 10, 2019).

The court held that bifurcated fee agreements (no-money down chapter 7s) can be acceptable with appropriate disclosure to the client. Post-petition fees may not include amounts for work done pre-petition. The court held that bifurcated agreements are only permissible where they are in the client's best interests, as opposed to the lawyer's financial interests. All fee arrangements must be fully revealed in the Rule 2016 Disclosure of Compensation. The disclosures must include the details of the pre-petition and post-petition fee agreements, any payment plan, and any interest charge on installment payments.

## *In Re Carr*, 613 B.R. 427 (Bankr. E.D. Ky 2020).

Counsel received \$300 pre-petition and entered into a \$1,185 post-petition contract with the debtor. The court expressed concern with the level of disclosure of the two contracts to the court, but found that the attorneys made full disclosures to the client, so the client could make an informed decision. While noting that “[n]ot all multiple fee arrangements will pass muster,” the court found the payment arrangements in this case were reasonable.

## Issues with Bifurcation

- Are bifurcated amounts accurate or just a fiction to do a no-money or little-money down bankruptcy case?
- Is the client receiving full advice if pre-petition analysis and consultation is limited? If the attorney does little work before filing the chapter 7, could issues arise under Section 707(b)(4) or Rule 11 if later disclosures reveal information that would have impacted decision to file chapter 7?
- Is the decision to enter into post-petition contract really completely independent?
- Does the attorney disclose all the payment options and their terms?

## What is Factoring?

- In another feature of bifurcating fees, the attorney has the client execute an agreement authorizing a third-party finance company to make automatic periodic debits for the fees due under the post-petition contract.

## Process of Factoring

- Attorney bifurcates fees
- The client executes the post-petition agreement along with an agreement authorizing a third-party finance company to make automatic periodic debits for the fees due under the post-petition contract.
- The attorney then assigns the right to collect from the debtor under the post-petition agreement to the third-party finance company in exchange for a lump sum discounted payment.

## *In re Wright*, 591 B.R. 68 (Bankr. N.D. Okla. 2018)

The court found serious deficiencies in the attorney's conduct, notably that the attorney charged a higher fee to clients using the factoring model than charged to his "conventional" clients. The attorney admitted that in several cases he designated fees for pre-petition services as post-petition, which the court described as "a fraud both on the debtor and the Court." And the court found that the attorney's fee disclosures were "grossly misleading and indicative of a wanton disregard—to the point of negligence—for the level of candor required under § 329." (emphasis in original). The court ordered the attorney to disgorge all fees, voided the "postpetition" agreements, and barred the attorney and the factoring company from collecting any additional fees, in 17 cases.

## Problems with Factoring

- The finance company has the right to collect payments from the debtor and to take collection action, including to sue and garnish, should the debtor default.



## Other Non-traditional Approaches

- *Allen v. Fitzgerald*, 2019 WL 6742996 (W.D. Va. Dec. 11, 2019).
  - A law firm engaged in a practice of referring clients to a towing company, which paid the clients' bankruptcy attorney's fees in exchange for taking possession of and in some cases selling the clients' vehicles by priming the lenders' secured claims. The Bankruptcy Court found the program was implemented in bad faith and the District Court affirmed that finding.

## Fee-Only Chapter 13

- The Attorney files a chapter 13 for the client only to pay the attorneys' fees, because the client could not pay the lump sum to file a chapter 7 under the Traditional Fee Agreement.