

Change Is on the Horizon

Practitioners and Debtors Wait for Bankruptcy Changes to Take Effect

By MICHAEL J. GRILLI

With all the provisions of the new Bankruptcy law set to be implemented in October of 2005, it is time to look at how the new legislation has affected debtors since it was signed in April, as well as the likely future impact upon full implementation. This law will directly impact any individual who falls upon hard financial times and considers bankruptcy in the future.

Very rarely has there been such diverse reaction to new legislation as there was on April 20, 2005, when President Bush signed the new Bankruptcy law. The legislation was lauded by the credit card companies as a necessity to fight back against reckless and free-spending consumers who sought to run up their credit card bills and then skip out without paying.

At the same time, consumer advocates, a majority of bankruptcy judges, and bankruptcy attorneys nationwide painted the new law as legislation bought and paid for by the credit card companies in an effort to increase their own profit margins and to protect themselves from consumers who should never have been granted credit by the companies in the first place.

If the intent behind the new law, whose official title is "The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005" was to limit the number of Bankruptcy filings, then the result in the months leading up to the impending change has had the opposite result. As reported by the American Bankruptcy Institute, bankruptcy filings nationwide for the months of April, May and June were up by 12% over the same period last year. The mindset of debtors (those who are filing the bankruptcy) seems to be that if they do

not act now, they will not be able to act later.

This frenzy to file may indeed cause many people to file, although with careful planning and budgeting, they may not need to.

In their push for passage of the new bankruptcy laws, its propo-

and in fear of losing the house and cars, in addition to using up their modest savings, John begins to use credit cards to pay some of the household expenses. As the situation worsens, he begins to take cash advances and draw further on the credit card accounts to

income will most likely exceed the median income in Massachusetts for a family of four, John and Jean would have to file a Chapter 13 bankruptcy. Their living expenses would be analyzed to determine if they exceeded necessary expenses and a determination would be made as to how much of their debt they would have to repay. In a situation such as this, any amount is too much because, as previously stated, given their expenses, they have no money to pay toward these bills. In addition, their living expenses are not judged based on how much they actually spend, but on a formula which sets forth what reasonable and necessary expenses are. No deference is given to things such as extraordinary medical expenses.

John and Jean would be forced into what would be a five-year repayment plan for a portion of their debts. If by chance something unforeseen should happen and they can't make the plan payments, their repayment plan would fail, their bankruptcy would be dismissed and they would still face a mountain of debt without any reasonable likelihood of being able to repay, facing likely foreclosure on their home.

This situation is the essence of what is unfair about the new bankruptcy legislation: the law does not differentiate between those who incur their debts as a result of their own doing and those whose situation is the result of unforeseen and/or tragic circumstances.

In addition, the new bankruptcy law also contains other important changes:

- The need to wait eight years before filing another bankruptcy as opposed to the current wait of six years
- Mandatory credit counseling

nents zeroed in on the concept of the reckless spender, who ran up his or her credit card bills and tried to get out of paying by filing for bankruptcy. It was this caricature that was used to drum up support for legislative change. However, it is important to look at how bankruptcy reform will affect someone who does not fit into this mold.

John and Jean have lived an upper-middle class lifestyle. John is an executive with a local company and Jean stays home with their two young children. John earns \$100,000 per year and they have recently purchased a new \$400,000 home for which they took out a \$350,000 mortgage. While they live a comfortable lifestyle, after monthly payments of mortgage, automobiles, living expenses and a small amount of credit card debt, John and Jean do not have a lot of excess income at the end of the month.

One day Jean falls sick and is admitted to a hospital for two months, with a period of rehabilitation at home for an additional four months. In order to care for her and the children, John is forced to take an unpaid leave of absence from his employer. During this period of no income,

make the mortgage and car payments, as well as to pay for Jean's medical care and prescriptions.

Once Jean is well and John is able to return to work, their credit card debt has gone from \$2,000 to more than \$25,000 in a period of six months. After payment of their living expenses and Jean's ongoing medical treatment, there is no money left over at the end of the month to pay any of the credit card bills.

This situation is not unreasonable, nor would John and Jean be characterized as reckless spenders. More accurately, they would be described, as are most people, as those who live within their means but are one unforeseen event away from disaster.

Under the pre-reform bankruptcy laws, this couple would be able to get relief. Because of the limited equity in their home (and the fact that they kept their mortgage current) and the fact that they have little to no excess income, they would have most likely be able to file a Chapter 7 bankruptcy and relieve themselves completely of their credit card bills and keep their house and the remainder of their assets.

The same cannot be said after October. Given the fact that their

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prior to filing, at the debtor's expense; and

- An increase in filing fees.

The increase in the complexity of the bankruptcy law, coupled with the requirement that more debtors file Chapter 13 bankruptcy, will likely cause an increase in the fees that attorneys have to charge, thus further limiting some debtors' ability to file.

As October approaches and the change in the bankruptcy laws take effect, consumers will have to deal with the realization

that the tide has been turned against them. They will no longer be judged on their own circumstances but on the government's determination of 'reasonable' expenses and what 'too much income' is.

In the few weeks remaining, attorneys expect to continue to be bombarded by those attempting to file before the deadline without any real thought as to the necessity of filing bankruptcy. In addition, in the weeks after October, practitioners will have to counsel numerous individuals who would

have been much better off filing before the change and are now left to make due with the laws as reformed.

No one would argue that some debtors have taken advantage of the law as a way to walk away from debts that they knew they could never afford to pay. However, the new bankruptcy law is so heavy-handed in its approach that it will serve no purpose but to rob deserving debtors of the fresh start that the bankruptcy laws were originally enacted to provide.

The bottom line is that anybody thinking about filing bankruptcy had better do so soon, or they may lose their opportunity to truly relieve their debts.❖

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