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Via e-mail only

Administrative Office of the United States Courts

Re: Proposed Amendments to Bankruptcy Rules

Dear sir or madam:

I have been practicing consumer bankruptcy law in the District of South Carolina since 1984. I primarily represent debtors but occasionally represent individual or small-business creditors. I am grateful for the opportunity to comment on the proposed amendments to the Federal Rules of Bankruptcy Procedure and would like to focus on the 3000-series rules relating to proofs of claim and mortgage notices.

In general terms, the proposed amendments to Rule 3001 seek to bring transparency to proofs of claim that are frequently quite opaque and obscure to debtors, their counsel, and trustees. They require creditors filing claims to give information necessary to the prudent review of their claims – usually information particularly within the knowledge of the creditors. They contribute to judicial economy by aiming to eliminate claim litigation that frequently arises out of lack of information. And for the most part, they require creditors to provide only those types of information than many currently give and that honest creditors would find it in their interest to disclose openly.

Proposed Amendment to Fed. R. Bank. P. 3001(c)(1)

The proposed amendment would require a creditor holding a revolving consumer credit claim to file the last pre-petition account statement with its proof of claim. This requirement would have a definite salutary effect. In this age of rampant, casual assignment of bad debts, it is frequently impossible to determine which of several possible unsecured claims the putative creditor is asserting. For example, the debtor's Citgo gas credit card may be serviced by Chase Bank, and Chase may have assigned it to Resurgent Capital Acquisitions without notice to the debtor. The debtor cannot relate the claim Resurgent files with any debt he owes. This uncertainty can lead to an unnecessary claim objection and can prevent the debtor or the trustee from making a well-founded one.

The amended rule would allow the debtor and the trustee to identify the claim filed by Resurgent as the one scheduled as Citgo or Chase and thus allow either to determine whether the claim is valid. In this way, the new provision would prevent unnecessary effort by debtor's counsel, creditor's counsel, and the court.

Proposed Fed. R. Bank. P. 3001(c)(2)(A)

This proposed new subsection would require a creditor to itemize the interest and other charges included in its proof of claim. This provision is important because the amount stated in a proof of claim frequently exceeds the balance shown on the debtor's last account statement. Without an explanation of the difference, the debtor and trustee cannot determine whether the amount of the claim is accurate or decide intelligently whether to object. For this reason, most conscientious creditors already include such information in their claims under the current rules.

In addition to fostering judicial economy, the ability of a debtor or trustee to assess intelligently whether to object to a claim contributes to the accuracy of the claims allowance process. This is important in a number of different situations. In Chapter 7 asset cases (the only Chapter 7 cases in which creditors file claims), the trustee almost always has a fixed amount of funds, bearing no relationship to the total claims filed, for distribution to creditors. An excessive or dishonest claim reduces the funds available for honest creditors. In Chapter 13 cases, an inaccurate secured claim being paid through the debtor's plan will likely result in the debtor having to pay a larger plan payment and may thereby endanger the feasibility of the reorganization. And in Chapter 13, an inaccurate claim of any classification cheats the honest creditors, especially under the "pot" plans used in many districts.

Proofs of claim when properly documented carry a presumption of validity – a rule that reverses the usual burden of proof and sharply tips the playing field in claim disputes in favor of creditors. *See* Fed. R. Bank. P. 3001(f). In exchange for this advantage, requiring a creditor to explain how it arrived at the presumptively valid claim amount seems a modest demand.

Proposed Fed. R. Bank. P. 3001(c)(2)(B)

This proposed new subsection would require a secured creditor to state the amount necessary to cure a pre-petition default. This requirement is absolutely necessary in one situation and extremely beneficial in another.

11 U.S.C. § 1322(b)(5) permits the debtor to cure a default on a long-term debt through his Chapter 13 plan while maintaining post-petition payments, either through or outside the plan. This is the typical treatment of a mortgage claim in Chapter 13, and mortgage defaults are the most common reason debtors elect Chapter 13. In order to effectuate this cure-and-maintain treatment, the parties, trustee, and court must be able to determine the arrearage. The logical starting point for this determination is the creditor's version of the arrearage.

Where the debtor proposes to pay a secured debt outside any plan of reorganization, either because he has filed an asset Chapter 7 case or because his Chapter 13 proposes payments directly to the creditor on a specified claim, the proposed requirement notifies the debtor what amount the creditor contends is necessary to cure any pre-petition default. This helps the debtor determine whether he can retain the collateral and, if applicable, reaffirm the debt or whether he must surrender the collateral. Because the collateral is most often a necessity such as a home or car, an informed decision on these questions contributes to the rehabilitative effect of the fresh start.

The current proof of claim form requires each secured creditor to state the amount of arrearage or other charges included in its claim. *See* Official Form 10. The proposed subsection primarily just codifies this requirement.

Proposed Fed. R. Bank. P. 3001(c)(2)(C)

This proposed new subsection would require a residential mortgage creditor to include an escrow statement as of the petition date with its proof of claim. The necessity for this information arises primarily in Chapter 13 cases where the debtor proposes section 1322(b)(5) cure-and-maintain treatment of such a mortgage. Concomitantly, a mortgage creditor rarely needs to file a proof of claim in any other situation.

When a mortgage is in default, an escrow shortage is typically one component of the arrearage. Debtors rarely understand the mathematical formula that RESPA requires mortgage holders to use in determining how to recoup escrow shortages and setting the escrow component of future mortgage payments. The proposed escrow statement will explain this analysis so that the debtor can accurately assess, and in case of dispute the court can accurately determine, whether the claimed shortage component is accurate.

In addition to facilitating the "cure" aspect of 1322(b)(5) treatment, an escrow statement would assist the debtor in maintaining post-petition payments by informing him whether he should expect the escrow component of the payment to change in the future.

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Proposed new rule 3002.1 represents an intelligent response to a set of common problems that are caused by lack of information concerning home mortgages and that frequently subvert the debtor's fresh start.

Proposed Fed. R. Bank. P. 3002.1(a)

This proposed new subsection would require residential mortgage creditors to keep debtors, their counsel, and trustees informed about changes in post-petition payments. This information is essential to permit debtors to maintain such payments during the pendency of a case – primarily Chapter 13 debtors implementing cure-and-maintain plan provisions.

RESPA does not require that a mortgage creditor provide annual escrow reconciliation statements to a debtor who is in bankruptcy. Additionally, mortgage holders frequently contend that the automatic stay precludes them from communicating with the debtor about changes in payments. The resulting breach in communication means the debtor remains in the dark about ARM resets, escrow adjustments, and other factors that can affect the payment required to remain current with post-petition payments. When this occurs, the debtor inevitably finds himself in default of his contractual obligation as to post-petition payments, even though he has performed those obligations according to the best available information. Such defaults are extremely damaging to both debtor and creditor.

Many bankruptcy judges currently approve or even propose plan language requiring notices of the kind this rule would require uniformly. The uniformity the rule would bring would be beneficial to all: to creditors who would face a consistent requirement countrywide, and to debtors who virtually all need the information to carry out their Chapter 13 plans. And it would avoid the costly litigation over such requirements that has tended to occur when they are embedded in debtors' plans.

Proposed Fed. R. Bank. P. 3002.1(c)

The remaining provisions of proposed rule 3002.1 are aimed at ensuring that a debtor who fully performs a Chapter 13 plan designed to cure a residential mortgage default, including making all required post-petition payments on a residential mortgage, emerges from bankruptcy with any pre-petition default fully cured. That is, they implement the promise of 11 U.S.C. § 1322(b)(5) that leads most Chapter 13 debtors to file bankruptcy in the first place. Of these provisions, subsection 3002.1(c) is the most important.

One of the most common ways in which a debtor may be frustrated in the attempt to bring a home mortgage current is by the mortgage holder's assessment of fees and charges during the pendency of the bankruptcy. The debtor may have made all plan payments and may believe he has made all post-petition mortgage payments, but upon discharge he learns that the mortgage holder contends he still owes charges that accrued during the case. The holder typically has not notified the debtor of these charges, usually contending the automatic stay prohibits such notice.

Such charges may be entirely proper. For example, if a debtor makes a post-petition payment outside any contractual grace period, the mortgage holder may usually assess a late fee. And there may be occasions, such as serious post-petition payment defaults, that would justify the mortgage holder in retaining counsel and assessing the resulting fees to the debtor.

On the other hand, we frequently see mortgage holders assess improper or excessive post–petition charges ("junk fees"). The mortgage holder may not use the necessary method of accounting separately for trustee vs. direct payments, so that every post-petition payment results in unjustified late fees and other default charges. A payment may simply be misapplied to another account or held in suspense, with similar result. The mortgagee may charge the debtor for unjustified attorney's fees including fees for an improvident motion for stay relief or (according to some courts) for preparation of a proof of claim.

The propriety of such charges should be determined in bankruptcy court while the case is pending, not in state court thereafter. Bankruptcy judges understand how Chapter 13 requires mortgage holders to apply payments; state court judges do not. State courts are likewise ill-equipped to determine whether it was necessary for the mortgagee's attorney to take a given step in a bankruptcy case or whether the associated fees are reasonable.

In short, this subsection facilitates the fresh start promised by Chapter 13 by bringing these charges to the debtor's attention during the bankruptcy case and affording an opportunity to challenge them before the court best prepared to resolve the issue.

I appreciate your consideration of these comments as well as the thoughtful work that went into the proposed amendments.

Sincerely,

Lex A. Rogerson, Jr.
Attorney at Law

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