Delaware Consumer Bankruptcy Program 2019

January 22, 2019

"Views from the Bench: Ethical Considerations in Consumer Bankruptcy"

Moderator: Michael B. Joseph, Chapter 13 Trustee

Panelists:

Hon. Brendan Linehan Shannon

Hon. Laurie Selber Silverstein

Hon. Keith M. Lundin

1. Judicial Recusal:
   a. Claim of Personal Bias or Prejudice:

28 USC Sec. 455:

(a) Any justice, judge, or magistrate judge of the United States shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned.

(b) He shall also disqualify himself in the following circumstances:
(1) Where he has a personal bias or prejudice concerning a party, or personal knowledge of disputed evidentiary facts concerning the proceeding;

i. **Debtor perceives every ruling by the Bankruptcy Court is adverse to him, and favors the creditors. Debtor files for recusal of the Judge or in the alternative for the Court to transfer venue to the Middle District of Florida where the warm weather and the Florida Court will definitely be more pleasant**.

See: Liteky v United States 510 U.S. 540 (1994):

"First, judicial rulings alone almost never constitute a valid basis for a bias or partiality motion. See *United States* v.*Grinnell Corp.,* 384 U. S., at 583. In and of themselves (*i. e.,* apart from surrounding comments or accompanying opinion), they cannot possibly show reliance upon an extrajudicial source; and can only in the rarest circumstances evidence the degree of favoritism or antagonism required (as discussed below) when no

extrajudicial source is involved. Almost invariably, they are proper grounds for appeal, not for recusal. Second, opinions formed by the judge on the basis of facts introduced or events occurring in the course of the current proceedings, or of prior proceedings, do not constitute a basis for a bias or partiality motion unless they display a deep-seated favoritism or antagonism that would make fair judgment impossible." p. 555

ii. Party files a Motion for Recusal of Judge based upon recent publicity from a prior proceeding. The Motion states that the Judge has a personal bias or prejudice against the party in favor of the adversary. It is asserted the personal bias arises from extra judicial sources, in this case the prior proceeding and the publicity.

"…it is equally clear that a claim of bias or prejudice based on judicial knowledge gained from prior hearings or other cases is not sufficient grounds for disqualification of a judge whether it be from prior judicial exposure to the defendant or prior judicial rulings adverse to the defendant in the same or different cases…" See United States v Sinclair 424 F.Supp. 715 (D. Del 1976) J. Latchum.

b. Judge's Comments and Impartiality Questioned:

iii. Statements and comments during proceedings in open Court appear to show bias by a Judge. The Judge remarks that the defendants complained included stating the defendants have a long history of masterminding schemes and illusory contracts, creating smoke screens, and other unsavory business practices.

See In Re: Allegro Law LLC 545 B.R. 765 (Bankr. MD Ala 2016)

The Supreme Court held in *Liteky* that the extrajudicial source factor applies to § 455(a), *see* 510 U.S. at 554, 114 S.Ct. 1147, and, as noted above, all of the bases the Defendants assert as grounds for recusal are remarks made in the course of judicial proceedings — either this adversary proceeding or the Allegro bankruptcy. Thus, the Defendants' recusal motion cannot succeed under § 455(a) unless the undersigned's remarks would display a deep-seated favoritism

or antagonism that would lead an objective, fully informed lay observer to question the Court's impartiality. A lay observer who was fully informed of the nature of the Allegro business model, the ruinous effect Allegro had on its clients, Allegro's relationship with AmeriCorp and McCallan, and McCallan's (and his lawyers') conduct in this litigation would not reasonably question the Court's impartiality based on the remarks the Defendants complain of. A lay observer with even a modest understanding of finance and credit would conclude that Allegro's activities with AmeriCorp and McCallan were predatory and fraudulent. Moreover, a fully informed lay observer would not reasonably expect a court to disregard a litigant's or lawyer's misbehavior in front of it, or ignore when a litigant violates its orders or intentionally provokes it. All of the statements the Defendants complain of have been made by the Court in response to what either Allegro or the Defendants have done in conducting their businesses and this litigation. That is not a sufficient reason to question the Court's impartiality. P. 707

iv. **Pro se litigant files over several years files over five dozen lawsuits in federal district courts including over 30 complaints in the District Court for the District of Delaware. After dismissal of the cases rather than filing an appeal the litigant files new lawsuits and demands further review. After one such case the Court issues an Order barring further actions from being filed without first obtaining the Court's approval. Instead of appealing the Order the litigant instead files a new action and among other things names the Judge as a defendant, and then seeks recusal of the Judge.**

See In re: Noble No 16-2915 (3rd Cir 2016) The Court in denying the recusal request states: " His only argument for relief is that he named Judge Robinson as a defendant in the severed civil rights action, but that alone is not sufficient to require her recusal under Sec. 455…"

2. Bankruptcy Court Initiated Attorney Sanctions:

    a. Debtor's Attorneys

        i. **Attorney's practice consists of primarily representing debtors in consumer Chapter 7 and 13 bankruptcy cases. Attorney has a legal assistant who has no formal legal education and has learned some of the requirements while working in the attorney's office. The cases are commenced under the attorney's name by the legal assistant. Every case filed in the past year were deficient, notices issued by the Court, and 90% of the chapter 13 cases were dismissed and 70% of the chapter 7 cases were dismissed. When questioned about the individual cases the attorney relies upon the legal assistant for answers.**

See In Re Fahey case 09-00501 (Bankr S.D. Tex 2009): Court sanctions attorney and enjoins him from providing Bankruptcy Assistance to Assisted Persons.

The Court opened a miscellaneous case against Edward Fahey ("Counsel"):

Upon finding that he .." has demonstrated a clear and consistent pattern of (1) failure to file information required by Bankruptcy Code § 521 when he files petitions commencing cases under the Bankruptcy Code, (ii) inadequate representation of clients, (iii) lack of expertise in bankruptcy law, (iv) unreasonable delegation of authority and responsibility to a contract paralegal that resulted in substantial harm to bankruptcy debtors, (iv) filing pleadings containing false statements, and (v) failure to comply with the Bankruptcy Code, Federal Rules of Bankruptcy Procedure (FRBP), and local rules. The pattern is clear and egregious. Counsel has failed to respond to prior admonitions. The Court concludes that the defalcations were either intentional or represented contemptuous indifference for the Bankruptcy Code, FRBP, local rules, and interests of clients."

"Counsel has displayed, and continues to display, incompetence and disregard of the statutes and rules that govern bankruptcy practice. While some of the blame for these failures perhaps rests on counsel's paralegal, unreasonable delegation is itself a violation of the rules and of the statute."

ii. **Debtors meet with legal assistants and paralegals in attorney's law office, fill out bankruptcy forms, complete the credit counseling at office computer, and sign after preparation by the assistants. The attorney meets the debtors for the first time at the Section 341 meeting**

See Clark v LaBarge 223 F.3rd 859 (8th Cir. 2000:

"The bankruptcy court also rendered findings of fact specific to each debtor's case, reciting a litany of problems that included: inconsistencies in Walton's filings about payments and in response to the Trustee's objections; execution of blank forms; unauthorized or forged signatures of both Walton and debtors; and Walton's ignorance of the cases for which he was responsible. The court concluded that Walton had failed to properly represent the debtors or perform the legal services contemplated by the fee, and that he had done so in bad faith

b. Creditor's Attorneys

i. **Debtors in a bankruptcy case had 3 houses, and bank/servicer held liens on all of the houses. The debtors agreed to stay relief on one of the houses in which they were not living. Although both sides, the debtor's lawyer and the bank's lawyer thought that the house that was the subject of the stipulation was the house the debtors were voluntarily surrendering, the legal description was actually the house the debtors did not want to surrender. When the mistake was pointed out, the bank's attorney acknowledged the error but refused to agree to a consent order vacating the mistaken stipulation stating the client had not given him authority to do so.**

See In Re: Martinez 393 B.R. 27 (Bankr. D. Nev 2008)

"As a result, the attempted refuge to client instructions is unavailing. Clients may not demand unethical or unlawful conduct from their lawyers and expect compliance. As established

above, Cooper Castle and its lawyers knew, or should have known, that Wells Fargo had no reasonable or nonfrivolous basis to oppose setting aside the stipulation. At a minimum, they had a duty to tell this to Wells Fargo, NEV. RPC 1.4(a)(5), and to withdraw from the representation or take some other action if Wells Fargo insisted on opposing. *Id.* 1.16(a)(1) ("a lawyer shall not represent a client or, where representation has commenced, shall withdraw from the representation of a client if: [¶] (1) The representation will result in violation of the Rules of Professional Conduct or other law"). They neither withdrew nor did they offer any evidence of compliance with Rule 1.4"

ii. **Stay Relief Motion prepared by non-attorney employees of law firm relying on computer generated information. The Motion alleges that the debtors have failed to pay current monthly mortgage payments since the commencement of the bankruptcy. The Motion also states the debtors have little or no equity in the real estate. The attorney for the creditor does nothing to verify or review the Motion. In fact there was a pending dispute by the debtors for the Bank's charging them forced place insurance. Further the debtors had been making their regular monthly mortgage payments except for the force place insurance charges. Creditor's attorney advises the Court, after questioning of inability to obtain an accounting from the client after repeated requests.**

See In Re: Taylor 655 F.3rd 274 (3rd Cir 2011)

"In this opinion, we focus on several statements by appellees: (1) in the motion for relief from stay, the statements suggesting that the Taylors had failed to make payments on their mortgage since the filing of their bankruptcy petition and the identification of the months in which and the amount by which they were supposedly delinquent; (2) in the motion for relief from stay, the statement that the Taylors had no or inconsequential equity in the property; (3) in the response to the claim objection, the statement that the figures in the proof of claim were accurate; and, (4) at the first hearing, the attempt to have the requests for admission concerning the lack of mortgage payments deemed admitted. As discussed above, all of these statements involved false or misleading representations to the court"

"We appreciate that the use of technology can save both litigants and attorneys time and money, and we do not, of course, mean to suggest that the use of databases or even certain automated

communications between counsel and client are presumptively unreasonable. However, Rule 11 requires more than a rubber-stamping of the results of an automated process by a person who happens to be a lawyer. Where a lawyer systematically fails to take any responsibility for seeking adequate information from her client, makes representations without any factual basis because they are included in a "form pleading" she has been trained to fill out, and ignores obvious indications that her information may be incorrect, she cannot be said to have made reasonable inquiry. Therefore, we find that the bankruptcy court did not abuse its discretion in imposing sanctions on Doyle or the Udren Firm itself. However, it did abuse its discretion in imposing sanctions on Udren individually."

3. Judicial "Sewer Sponte" (sua sponte) in General

   Interpreting United Student Aid Funds, Inc. v Espinosa 599 U.S. 260 (2010) and to what extent the Supreme Court held Judges have an independent duty to raise issues and objections sua sponte?

   See In Re: Briggs 570 B.R. 730 (Bankr. W.D LA 2017) (reversed)

   Briggs v Johns 591 B.R. 664 (D. W.D. LA 2018)

4. Duty of Reasonable Inquiry:

   11 USC Sec 707(b) (4) (C) & (D):

(C) The signature of an attorney on a petition, pleading, or written motion shall constitute a certification that the attorney has—
(i) performed a reasonable investigation into the circumstances that gave rise to the petition, pleading, or written motion; and
(ii) determined that the petition, pleading, or written motion—
(I) is well grounded in fact; and
(II) is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law and does not constitute an abuse under paragraph (1).

(D) The signature of an attorney on the petition shall constitute a certification that the attorney has no knowledge after an inquiry that the information in the schedules filed with such petition is incorrect

BR 9011(b)

(b) REPRESENTATIONS TO THE COURT. By presenting to the court (whether by signing, filing, submitting, or later advocating) a petition, pleading, written motion, or other paper, an

attorney or unrepresented party is certifying that to the best of the person's knowledge, information, and belief, formed after an inquiry reasonable under the circumstances,—
(1) it is not being presented for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation;
(2) the claims, defenses, and other legal contentions therein are warranted by existing law or by a nonfrivolous argument for the extension, modification, or reversal of existing law or the establishment of new law;
(3) the allegations and other factual contentions have evidentiary support or, if specifically so identified, are likely to have evidentiary support after a reasonable opportunity for further investigation or discovery; and
(4) the denials of factual contentions are warranted on the evidence or, if specifically so identified, are reasonably based on a lack of information or belief.

Debtor lists a claim owed to the Debtor on a promissory note in the Statement of Financial Affairs but not on the Schedules nor is it listed as exempt. At the Section 341 meeting under questioning by the Trustee, the attorney responds to why it is not listed in the Schedules as the attorney was under the impression that it was essentially uncollectible. Acting under that representation, the Trustee administered the case as a no asset Chapter 7 and debtor received a discharge. A month later the Trustee was contacted by an attorney who informed the Trustee that the true payoff of the note was $61,000 and monthly payments had been made to the Debtor.

See In re: Kayne 453 BR 372 (9th Cir.BAP 2011)

“By his own admissions, Orton confesses to a failure to conduct a reasonable investigation into the facts presented in the schedules and thus concedes that he violated Rule 9011(b) and § 707(b)(4)(D). Our inquiry could, therefore, stop here and we could confidently conclude that the bankruptcy court did not err in ruling that Orton "violated Rule 9011(b) of the Federal Rules of Bankruptcy Procedure and § 707(b)(4)(D) of the Bankruptcy Code." Memorandum at 2.

But the bankruptcy court went beyond the basic finding and ruled that Orton's conduct was "egregious." *Id.* at 3. Orton not only did not conduct a reasonable inquiry into whether the schedules were well grounded in fact, but he had "knowledge... that the information in the schedules filed with such petition [was] incorrect." § 707(b)(4)(D). “

5. Appearance Only Counsel; Limited Services Agreements; Unbundling

11 USC Section 101(4) & (4A)

(4) The term "attorney" means attorney, professional law association, corporation, or partnership, authorized under applicable law to practice law.
(4A) The term "bankruptcy assistance" means any goods or services sold or otherwise provided to an assisted person with the express or implied purpose of providing information, advice, counsel, document preparation, or filing, or attendance at a creditors' meeting or appearing in a case or proceeding on behalf of another or providing legal representation with respect to a case or proceeding under this title.

Delaware Local Rule:

Rule 9010-1

(f) Standards for Professional Conduct. Subject to such modifications as may be required or permitted by federal statute, court rule or decision, all attorneys admitted or authorized to practice before this Court, including attorneys admitted on motion or otherwise, shall also be governed by the Model Rules of Professional Conduct of the American Bar Association, as may be amended from time to time.

a. Delaware attorney for creditor enters appearance and relies on outside counsel for preparation and accuracy of all documents.

The Delaware Court of Chancery has addressed "local counsel" issues:

The Practice Guidelines published by the Court of Chancery are entitled: "Guidelines to Help Lawyers Practicing in the Court of Chancery

"II. GUIDELINES ON BEST PRACTICES FOR LITIGATING CASES BEFORE THE COURT OF CHANCERY

1. Role of Delaware Counsel

a. The concept of "local counsel" whose role is limited to administrative or ministerial matters has no place in the Court of Chancery. The Delaware lawyers who appear in a case are responsible to the Court for the case and its presentation.

b. If a Delaware lawyer signs a pleading, submits a brief, or signs a discovery request or response, it is the Delaware lawyer who is taking the positions set forth therein and making the representations to the Court. It does not matter whether the paper was initially or substantially drafted by a firm serving as "Of Counsel."

c. The members of the Court recognize that Delaware counsel and forwarding counsel frequently allocate responsibility for work and that, in some cases, the allocation will be heavily weighted to forwarding counsel. The members of the Court recognize that forwarding counsel may have primary responsibility for a matter from the client's perspective. This does not alter the Delaware lawyer's responsibility for the positions taken and the presentation of the case.

d. Non-Delaware counsel shall not directly make filings or initiate contact with the Court, absent extraordinary circumstances. Such contact must be conducted by Delaware counsel.

e. It is not acceptable for a Delaware lawyer to submit a letter from forwarding counsel under a cover letter saying, in substance, "Here is a letter from my forwarding counsel."

b. Attorney A consistently does not appear for Section 341 meetings or court hearings for clients. Instead attorney contracts with Attorney B who appears and who states that this is only a limited appearance. Attorney B receives a nominal payment for each appearance. Proper? What further may be required for informed consent of the debtor? Is disclosure necessary in the initial retention?

See: In re: D'Arata 587 BR 819 (S.D N.Y. 2018) : Debtor attends 2 Section 341 meetings with appearance only counsel whom he had never met, and each appearance counsel were unaware of the debtor's Chapter 7 Petition, information in the Schedules, Statement of Financial Affairs and inaccuracies needing correction. Prior to the meeting, debtor was unaware he would be represented by an attorney he never met. The Court concluded the Debtor's lawyer violated several of New York's Rules of Professional Responsibility including failing to obtain Debtor's informed consent when using appearance counsel at two Section 341 meetings.