AND NOW, A WORD FROM OUR SPONSORS

BY GUEST WRITER PROF. NANCY B. RAPOPORT

You know that things in our economy are bad when you look back longingly at the stock market crash that Enron, WorldCom and other early-21st-century corporate fiascos caused. We may not be in a full-blown depression, but it's clear that things are very bad indeed.

And when things are bad, bankruptcy lawyers can be extremely useful. As of this writing, Herbst Gaming has filed a bankruptcy petition in Reno, and we're watching other businesses in Nevada file for bankruptcy protection as their clientele (and profit margins) all dry up. Consumer bankruptcy filings are also up, as people deal with everything from lost jobs to sudden medical issues to homes that are seriously underwater (worth less than the amounts owed on their mortgages).

Bankruptcy law is supposed to balance two very important, and competing, goals: giving the debtor a fresh start through the discharge of some debts, and giving creditors a central location where at least some portion of their debts can be paid fairly. Bankruptcy filings stop the "race to the courthouse," where the first creditor to win a case and collect takes everything – instead, some of what happens right before bankruptcy comes back into the debtor's estate for a more equitable distribution among all creditors.

Businesses have always had the option of deciding whether to liquidate and dissolve or to reorganize under bankruptcy protection. But after the 2005 bankruptcy amendments (known as BAPCPA – the Bankruptcy Abuse Prevention and Consumer Protection Act), the world got more difficult for many consumers.

Congress had spent years before BAPCPA hearing testimony about how many people filed for bankruptcy protection just to get out of debts that they'd incurred by profligacy and deviousness. Although several respected practitioners and academics argued that (1) bankruptcy abuse was a rare situation and (2) the Bankruptcy Code already had mechanisms for dealing with abusive debtors, Congress enacted new provisions designed to make it more difficult for many individuals to file Chapter 7 (liquidation) cases. D-Day was October 17, 2005 – bankruptcies filed after the amendments came into effect had to comply with all sorts of new rules.

Those rules included a requirement that debtors complete an educational program prior to filing, on the theory that if debtors knew about all sorts of options to repay their debts, they would decide that they might not need to file for bankruptcy after all. (There are, however, parts of the country in which getting the requisite debtor education training pre-petition is well-nigh impossible.) They also included the infamous "means test," which prevents people who have current monthly incomes at or above the median for their state from filing for protection under Chapter 7. Instead, people who have a reasonably good income must file for protection under Chapter 13 (assuming that they qualify under Chapter 13[1]), which requires them to pay their debts for several years before they may receive a discharge from some of their debts. Again, the theory was that too many debtors wanted to cheat the system – that these scofflaws wanted to ring up huge amounts of debt, file for bankruptcy protection, keep all of their "stuff" and discharge that debt. That theory, of course, was flawed from the start. I've never met someone for whom bankruptcy was a first-choice option.

Now, in a time of serious economic crisis, we're left with BAPCPA. For the middle class, bankruptcy is now more difficult to file, with fewer choices than before. When I go to conferences with bankruptcy judges and bankruptcy lawyers, many of them tell me how unlikely it is that most debtors who file Chapter 13 plans will be able to complete their plans successfully. The first mortgage on many people's home is the "killer," because it's usually undersecured – meaning that the mortgage amount is more than the house itself is worth. The Bankruptcy Code currently protects first mortgages (although it lets people stretch out the repayment of any arrearages). But without any ability to modify that first mortgage, many debtors cannot keep their homes, even in Chapter 13.

There is a proposal afoot to allow bankruptcy judges to modify first mortgages, and there are good arguments pro and con. Those who want judges to have the power to modify first mortgages point to the low success rate in Chapter 13 cases. Those who are against the proposal warn that the interest rate on mortgages in the future will be higher for the rest of us, if banks have to worry about the repayment of first mortgages.

Of course, there's always "jingle mail" – the out-of-bankruptcy solution to which some homeowners have resorted. In jingle mail, the homeowner just mails the keys back to the bank, saying in effect, "I don't have any equity in this home – you take it."

The sad thing is that, every time someone uses jingle mail, that person's neighbors all watch their own homes' values decline. Whether we're talking about consumer bankruptcies or business bankruptcies, all of these bankruptcies have a ripple effect on the rest of the economy.

What worries me more than anything is that the very same Congress that brought us the unnecessary BAPCPA is now bringing us a series of proposals to try to jump-start the economy. I worried – during Enron – when Congress passed Sarbanes-Oxley, because I thought then (and still think) that Congress rushed to find a solution to corporate governance problems before it actually had figured out what had caused those problems and how to solve them. Now I worry that Congress has rushed to enact a bailout (one that most folks in Congress have never even

read) without fully understanding what caused our current crisis.

A friend of mine who's a consumer-side debtor's lawyer recently told me how he answers people who ask him what he thinks of the bailout. He says, "Remember those people who gave you BAPCPA? They're the very same people who are giving you the bailout."

He's right, and I'm more than a little worried. I want us to recover from this economic crisis – and bankruptcy lawyers will be front and center in that recovery – but I also want us to learn from it. And learning from it is going to take time and a willingness to recognize the complex causes that brought us to this brink. Are we up to the challenge?

The Boyd School of Law is helping meet the challenge. We offer bankruptcy and related courses to our students. In addition, all students at the law school participate in our Community Service Program, in which students, under faculty supervision, provide basic legal information to Nevadans about a variety of legal topics. Thus far, the Community Service Program has helped over 27,000 Nevadans. Since spring 2002, bankruptcy has been one of the topics covered by the program. Thus far, nearly 4,500 Nevadans have received information about bankruptcy as part of the program. This includes nearly 1,100 in 2008, and more Nevadans are receiving bankruptcy information through the program thus far in 2009 than at a comparable time in 2008. I'm proud of our program, and I'm glad that we can be of significant help to our state. NL

NANCY RAPOPORT graduated summa cum laude from Rice University and graduated from Stanford Law School, where she was an editor of the Stanford Law Review. She was formerly Dean of the University of Nebraska College of Law and the University of Houston Law Center. Since 2007, she has been the Gordon Silver Professor of Law at the William S. Boyd School of Law. Her numerous publications include the 2009 edition of "Enron and Other Corporate Fiascos: The Corporate Scandal Reader" (co-edited with Jeffrey Van Neil and Bala Dharan). In 2009, she was named Public Service Counsel of the Year by the Association of Media and Entertainment Counsel.

---

1 If an individual's secured debt and unsecured debt are too high for Chapter 13, he or she would have to file for protection under Chapter 11.