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Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@portfoliomedia.com

The High Court Stance In *Milavetz V. US*

Law360, New York (March 17, 2010) -- In 2005, Congress enacted substantial revisions to the Bankruptcy Code through the Bankruptcy Abuse and Consumer Protection Act (BAPCPA). One provision that attracted relatively little attention at the time imposed various communication and disclosure rules on a class of bankruptcy professionals termed “debt relief agencies.”

These rules took on new importance for bankruptcy lawyers when the U.S. Supreme Court handed down its recent decision in *Milavetz Gallop & Milavetz PA, et al. v. United States*.

The threshold issue in *Milavetz* was whether attorneys qualify as “debt relief agencies” when they counsel and represent clients in bankruptcy. The question is significant because debt relief agencies are subject to a number of special rules under the Bankruptcy Code.

For example, debt relief agencies are forbidden from advising clients to incur any additional debt before filing for bankruptcy. 11 U.S.C. § 526(a)(4). Debt relief agencies are also subject to mandatory disclosure requirements with respect to advertisements and other solicitation materials, as well as engagement letters. 11 U.S.C. §§ 527, 528.

The Supreme Court, in a unanimous opinion authored by Justice Sonia Sotomayor, held that attorneys are indeed “debt relief agencies” subject to the rules described above. The court went on to consider whether the disclosure rules applicable to debt relief agencies ran afoul of the First Amendment when applied to attorneys.

Section 528 of the Code requires that, in any bankruptcy-related advertisements, a “debt relief agency” must include a clear and conspicuous statement that it is a debt relief agency and that it assists its clients to file for relief under the Bankruptcy Code.

The court found that Section 528 is directed only at misleading commercial speech and that it imposes only “a disclosure requirement rather than an affirmative limitation on speech.” Accordingly, the court held that attorneys could constitutionally be made subject to the disclosure requirements of Section 528.

The court added an important caveat, however, regarding the rule in Section 526(a)(4) forbidding attorneys to advise their clients to take on more debt. Reading the provision narrowly, the court held that attorneys are prohibited only from advising a debtor to incur more debt because the debtor is filing for bankruptcy, rather than for some other valid purpose.

The court’s opinion states that that the advice restriction “is best understood to provide an additional safeguard against the practice of loading up on debt prior to filing.” The court suggested that this narrow reading ensures that attorneys will not “unknowingly run afoul” of the prohibition.

For example, the court suggested that an attorney could permissibly advise a client contemplating bankruptcy “to refinance a mortgage or purchase a reliable car” in advance of filing, so long as the advice is intended to improve the client’s financial prospects and ability to repay creditors rather than to take unfair advantage of a discharge of debts.

The scope of the Milavetz holding is narrow, since it applies only to attorneys representing “assisted persons.” The Bankruptcy Code defines “assisted persons” to include any person whose debts are primarily consumer debts and whose nonexempt property is valued at less than \$164,250. 11 U.S.C. § 101(3).

Many corporate bankruptcy attorneys do not represent “assisted persons” and thus are not subject to the rules discussed in Milavetz. However, even attorneys who normally do not counsel consumer debtors may find themselves drawn in to the Milavets minefield in the context of pro bono work.

In the wake of the court’s decision, any attorney who advises consumer debtors, even rarely, would be well advised to review the standard engagement letters used for such representations to ensure compliance with the terms of the Bankruptcy Code.

Although the Milavetz decision did not address the issue, Section 527 of the Code requires debt relief agencies to provide clients and prospective clients with a written notice discussing their options for obtaining bankruptcy-assistance services. In the wake of Milavetz, bankruptcy attorneys must take care to comply with this provision of the Code.

--By Adam J. Wiener, Foley & Lardner LLP

Adam Wiener is an associate with Foley & Lardner in the firm's Detroit office and a member of the firm's bankruptcy & business reorganizations and general commercial litigation practices. He can be reached at awienner@foley.com. Foley partner Salvatore A. Barbatano assisted in the preparation of this article.

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