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IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF OREGON

ERIC W. OLSEN,
KEVIN D. SWARTZ
JASON C. MCBRIDE

Case No. 05-6365-HO

Plaintiffs,

v.

ALBERTO GONZALES, in his official
capacity as Attorney General of the
United States of America, and

PLAINTIFFS' RESPONSE TO
DEFENDANTS' MOTION TO
DISMISS

ORAL ARGUMENT REQUESTED

ILENE LASHINSKY, in her official
capacity as United States Trustee

Defendant.

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Introduction

Congress passed the BAPCPA in 2005. Since the act took effect in October 2005 it has been criticized by bankruptcy judges and commentators alike¹. Congress did not consult bankruptcy judges or experts in the field. *See* fn 1.

While the issues before the Court are not how BAPCPA was drafted, the Court should be advised that Defendants' contentions that Congress heard evidence of specific problems is not entirely correct. Def. Memo. p.5. Rather, Congress heard evidence on prior drafts of the bill. However, BAPCPA was a Senate Bill and the Senate held no hearings and provided no legislative history for the 2005 act.

The issues that are before the Court are whether Congress can forbid and attorney from giving competent, ethical legal advice, forbid speech and compel speech (some of which is untrue) based on a client's wealth, and whether Congress specifically defined the parameters that govern 11 U.S.C. §§ 526-528.

Legal Standard

A claim will only be dismissed under F.R.C.P. 12(b)(6) motion if it appears beyond doubt that the pleader can prove no set of facts in support of the claim that would entitle the pleader to the relief. *Conley v. Gibson* 355 US 41, 45.

A. Section 526(a)(4) restricts speech in violation of the First Amendment and does not satisfy strict scrutiny or the “balancing test” under Gentile.

Defendants argue that Section 526(a)(4) of the Code is constitutional as a restriction on

¹ For an overview of criticism see:
<http://www.bankruptcylitigationblog.com/archives/cat-bapcpa.html>; and
<http://www.law.com/jsp/article.jsp?id=1139306710471>

speech because it satisfies the standard announced in *Gentile v. State Bar of Nevada*. 501 U.S. 1030 (1991). This analysis is incorrect under the facts of this case and the applicable law regarding restrictions on professional speech. Plaintiffs' ability to properly advise clients in the face of legitimate client concerns is restricted by Section 526(a)(4). The advice offered by plaintiffs offends neither the administration of justice nor the operation of the bankruptcy system. As such, Section 526(a)(4) is unconstitutional under either strict scrutiny or the *Gentile* standard.

1. Strict scrutiny, and not the standard in Gentile, is the proper test for evaluating the constitutionality of Section 526(a)(4).

Defendants maintain that Section 526(a)(4) is an "ethical rule" and is therefore entitled to a more lenient level of constitutional review. *See* Def. Memo at p.12. However, given the factual differences between the speech involved in *Gentile* and in the present case, the *Gentile* test is ill-suited to analyzing Section 526(a)(4). Moreover, professional speech, such as that restricted by Section 526(a)(4), is entitled to the highest level of constitutional protection.

As defendants set out in their memorandum, *Gentile* involved public statements made by an attorney, Gentile, in advance of a criminal trial. 501 U.S. at 1032-33. These statements were made during a press conference held shortly after Gentile's client was indicted. *Id.* The Court concluded that the State Bar of Nevada could legitimately regulate an attorney's speech where such speech posed a "substantial likelihood of material prejudice." *Id.* at 1075. In reaching this conclusion, the Court was sufficiently satisfied that certain extrajudicial statements made by attorneys could influence the outcome of a trial or prejudice the jury pool. *Id.* The Court recognized that such speech would interfere with the right to a fair trial, a fundamental interest under the Constitution. *Id.*

In contrast, the present case concerns the regulation of private, confidential speech between attorney and client. Plaintiffs seek to give lawful, ethical advice to their clients regarding incurring debt pre-petition. Section 526(a)(4) is not limited to “fraudulent” or “abusive” incursions of debts, but rather any debt incurred “in contemplation of” bankruptcy. On the other hand, *Gentile* involved not just any public statement, but only a public statement that was likely to result in material prejudice to the administration of justice.

The other cases cited by the defendants are similarly inapposite. The *Ohralik* case involved the solicitation of clients in person by an attorney. *Ohralik v. Ohio State Bar Ass’n*, 436 U.S. 447, 448 (1978). The Court analyzed the case under the standard used for commercial speech, a lesser test of constitutionality. *Id.* at 455-57. Plaintiffs do not read defendants’ memorandum to argue that advice of the kind regulated by Section 526(a)(4) is commercial speech. In any event, the Supreme Court has indicated that private attorney advice is not subject to the same test as expressly commercial speech. *See Board of Trustees of the State Univ. Of New York v. Fox*, 492 U.S. 469, 480, 486 (1989) (holding that legal advice is not speech that proposes a commercial transaction). Likewise, the *Cantella* case involved a restriction with a mechanism to limit enforcement to advice that is illegal or unjust. *Cantell v. Stovitz*, 263 F. Supp.2d 1064, 1076 (N.D. Cal 2005). As discussed above, Section 526(a)(4) contains no such limitation and requires a different standard for reviewing its application to plaintiffs.

Speech made in a professional capacity is entitled to strict scrutiny. Circumstances exist where speech made by attorneys should be entitled to the “strongest protection our Constitution has to offer.” *Florida Bar v. Went For It, Inc.*, 515 U.S. 618, 634 (1995). Providing perfectly legal advice and practical solutions to legal problems is just such a circumstance. Indeed, the

Court has stated that “[a]n informed, independent judiciary presumes an informed, independent bar.” *Legal Services Corp. v. Velazquez*, 531 U.S. 533, 545 (2001). Section 526(a)(4) impairs the independence of plaintiffs to fully and adequately advise their clients. As such, this section must be reviewed under strict scrutiny.

2. Section 526(a)(4) violates the First Amendment as it fails to pass strict scrutiny.

As stated above, claims involving non-commercial, professional speech are entitled to the highest level of constitutional protection and are only constitutional if they survive strict scrutiny review. To pass strict scrutiny, the regulation in question must support a compelling governmental interest and must restrict otherwise permissible speech in a way that is the least restrictive means to meet the particular interest. *See Sable Communications of Cal, Inc. v. Sable*, 492 U.S. 115, 126 (1988); *N.A.A.C.P. v. Button*, 371 U.S. 415, 439-44 (1963); *Conant v. Walters*, 309 F.3d 629, 637 (9th Cir. 2002), *cert. denied* 540 U.S. 946 (2003) (all applying strict scrutiny to professional speech). Defendants have failed to demonstrate any compelling government interest advanced by Section 526(a)(4) and, even assuming such an interest exists, have failed to show that Section 526(a)(4) utilizes the least restrictive means to meet such an interest.

a. Section 526(a)(4) does not implicate a compelling government interest.

Outside of Section 526(a)(4), no section of the Code specifically addresses the ills of incurring new debt in advance of filing a petition for relief. Instead, defendants would have this Court consider the potential maladies of non-dischargeability and possible “gaming” of the

bankruptcy system as compelling interests for restricting speech. *See* Def. Memo. at p. 14-15. Defendants further argue that advice from attorneys contributed to abuse of the bankruptcy system. *Id.* However, Section 526(a)(4) does little to advance such an interest. Moreover, many of the abusive practices cited by defendants violate ethical rules already in existence, thus diminishing the supposed interest furthered by additional legislation.

Defendants propose that Section 526(a)(4) promotes the integrity of the bankruptcy system. In actuality, many of the activities promoted by Section 526(a)(4) are impermissible under existing ethical rules. For example, the suggestion that incurring new debt to take advantage of the discharge or dilute the amount distributed to creditors would require that plaintiffs' advise debtors to commit fraud. Such activity is currently regulated under the Oregon Rules of Professional Conduct (herein "ORPC"). ORPC 3.3(b). Moreover, any injury to debtors as a result of unethical advice are also sufficiently safeguarded under the state rules. ORPC 1.1, 3.1, 3.3. As Section 526(a)(4) expressly does not limit or curtail these regulations, the interest in preventing abuse over and above these already-existing regulations is considerably diminished. 11 U.S.C. § 526(d)(2).

In addition, Congressional attempts to regulate speech may have legitimate objectives that are frustrated by the regulation itself. In *Velazquez*, Congress restricted the ability of attorneys to undertake constitutional challenges to existing welfare laws. 531 U.S. at 538. The government's asserted interest was to promote the efficiency and fairness of the welfare system. *Id.* at 547. The Court struck down the statutory provision as an unconstitutional regulation on speech in violation of the First Amendment. *Id.* at 549. The Court held the resulting impairment of the judicial function trumped the government's interest in maintaining the welfare system.

Id. at 547-48. Similarly, Section 526(a)(4) limits debtors' access to advice from plaintiffs in frustration of the judicial function. Legitimate pre-bankruptcy planning may result in incurring new debt. However, Section 526(a)(4) removes the independence of plaintiffs to engage in such planning. As such, the independence of the judiciary to review a debtor's petition for relief and afford a "fresh start" is equally reduced. As such, the government interest in promoting the fairness of the bankruptcy system is outweighed by the interests of an independent judiciary.

b. Even assuming Section 526(a)(4) advances a compelling interest, it does not use the least restrictive means to do so.

As noted above, Section 526(a)(4) does not contain restrictive language such as "fraudulent" or "abusive" to limit the application of the speech restriction. Rather, Section 526(a)(4) limits any advice to incur debt "in contemplation of" a bankruptcy filing. Such a blanket limitation squelches any legitimate pre-bankruptcy debt planning advice provided by plaintiffs. The examples of such advice are numerous; however, two examples will be provided by way of illustration.

First, many debtors are in such financial difficulty that they cannot afford to pay for plaintiffs' services and the court fee for filing a bankruptcy petition. Oftentimes, a close friend or relative may be willing to loan the potential debtor the funds needed to engage plaintiffs' services. If plaintiffs were to advise the debtor to take advantage of the loan, they would violate Section 526(a)(4) as they advised a client to incur debt because of the bankruptcy to pay the attorney fees. While the friend or relative would have the debt discharged and the debtor may risk a non-dischargeability problem, this situation is a far cry from abuse of the bankruptcy system. Practically speaking, the creditor and debtor in this scenario care very little about the

machinations of the bankruptcy process. But for Section 526(a)(4), plaintiffs could and would advise clients to seek such loans in order to facilitate the clients' needs.

Second, some clients may have assets with values that clearly exceed the allowed exemptions under Oregon law. Before the effective date of Section 526(a)(4), the Code allowed a debtor to use secured debt to protect the asset and convert the funds from the loan into an exempt asset. *See e.g. In re Cook*, Adv. Proc. No. 04-03261-tmb (Bankr. Or. Dec. 14, 2004) (stating that debtor was not to be denied discharge under Section 727 because of a pre-petition debt taken against otherwise non-exempt automobile where funds from loan used to pay down debtor's mortgage to increase homestead exemption). Even under the revised Code, the conversion of non-exempt assets to exempt assets continues to be a permitted practice. *See* 11 U.S.C. § 727. However, plaintiffs would not be permitted to advise a client about the possibility of using pre-petition debt to protect certain asset, despite the legality of such activity. Again, but for Section 526(a)(4), plaintiff could and would provide such advice to clients.

These examples illustrate that plaintiffs' ability to fully advise their clients is curtailed by Section 526(a)(4). Each of the examples provides a plausible fact situation in which plaintiffs would provide advice to incur debt because of the planned bankruptcy filing. In one case, the reason is to file the case itself; in the other, the reason is to avoid liquidation of an asset and to take full advantage of the debtor's exemptions under state law. Defendants' reasoning that the language of the statute itself limits application of Section 526(a)(4) is unavailing. Even adopting defendants' reading of the statute, there exist a number of legitimate reasons to incur debt because of a planned bankruptcy filing. As such, Section 526(a)(4) does not represent the least restrictive means to advance the purported government interests.

For the reasons stated above, Section 526(a)(4) does not pass strict scrutiny and is unconstitutional as it infringes on plaintiffs' rights under the First Amendment.

3. Even under the test in Gentile, Section 526(a)(4) is unconstitutional.

Assuming, *arguendo*, that the Court were to apply the test in the *Gentile* case, Section 526(a)(4) still lacks the necessary narrow tailoring to pass constitutional muster. Under the *Gentile* test, the Court must balance plaintiffs' First Amendment interests against the government's interest in regulating the activity in question. *Gentile*, 501 U.S. at 1075. In addition, should the government's interest prevail, the challenged legislation must be narrowly tailored to the proffered interests. *Id.* at 1076.

As stated above, the regulations reviewed in *Gentile* and *Cantella* each contained a restrictive provision that limited the application of the regulation to specific types of speech. In *Gentile* itself, the regulation only limited speech of a kind that would have a "substantial likelihood of material prejudice" on a pending case. 501 U.S. at 1034. The speech restriction in Section 526(a)(4) contains no such restriction. It is a blanket restriction on any advice on incurring debt because of a planned bankruptcy. Defendants' reasoning that the language of the statute itself is limiting enough is simply wrong. *See* Def. Memo. at p. 10-11. There exist plausible, legal reasons for incurring debt in contemplation of bankruptcy, and the restriction of plaintiffs' ability to provide legal advice on this matter offends the First Amendment.

Plaintiffs submit for this reason, and the reasons stated above, the restriction on speech imposed by Section 526(a)(4) is unconstitutional.

B. Section 526(a)(1) unconstitutionally chills speech by subjecting Plaintiffs to sanctions for failing to perform services which later become unethical or ill advised.

Section 526(a)(1) punishes Plaintiffs for “fail[ing] to perform any service that [Plaintiffs] informed an assisted person or prospective assisted person it would provide in connection with a case or proceeding under this title.” The Code does not make exceptions.

Husbands and wives are entitled to file a joint petition for bankruptcy relief. 11 U.S.C. § 302. This allows joint debtors to file one petition, pay one filing fee, and usually half the attorney fees that would be required in the event married debtors were to file separate petitions. However, occasionally joint debtors divorce. Commonly one divorcing debtor will become the creditor of the other through spousal support. As such, Plaintiffs will then have a conflict of interest between clients who divorce. To the extent Plaintiffs have promised services that have yet to be completed, Plaintiffs then run the risk of not performing the services and be subject to sanctions, or performing the services and run the risk of discipline for violation of ORPC 1.7². Plaintiffs only recourse is to not promise services, which is an abridgment of Plaintiffs’ speech.

These risks are not limited to ethical matters. If a debtor becomes disabled and their income diminishes while the debtor is in a reorganization under chapter 13 to keep his home, what are an attorneys requirements when the debtor chooses to forgo life-extending medicine to make his chapter 13 payment to preserve his home?

ORPC 2.1 states, “ In representing a client, a lawyer shall exercise independent professional judgment and render candid advice. In rendering advice, a lawyer may refer not only to law but to other considerations such as moral, economic, social and political factors, that may be relevant to the client's situation.”

²Oregon Rules of Professional Conduct available at http://www.osbar.org/_docs/rulesregs/orpc.pdf

Should an attorney not wish to represent a client who is placing his life in danger rather than protect his property, he is subject to sanctions under § 526(a)(1). Again, Plaintiffs other option is to not promise services. This is an abridgement of Plaintiffs' First Amendment rights.

Defendant argues that, "Congress's purpose in enacting the BAPCPA was to reduce the amount of unethical conduct by attorneys." Def. Memo. at p.17. This is a protection of the debtor, not the attorney. As such, the Congressional purpose was to require attorneys to do those things their clients' request. If the object is to curb attorneys failing to perform promised services to debtors, then the statute must be read as opposing Defendants' position.

"Statutory language should be interpreted consonant with the provisions of the whole law, and . . . its object and policy." *Holloway v. United States*, 526 U.S. 1, 9 (1999) internal citations omitted.

Plaintiffs are less able to advise their clients because their advice may later become unethical or ill advised. However, the client may benefit from Plaintiffs' services because it will help the debtors avoid the costs of obtaining another attorney when Plaintiffs are conflicted, or because the client can accomplish their ill advised plans. As such, Plaintiffs cannot rely on the Congressional intent to save them from § 526(a)(1).

C. Section 527 is unconstitutional because it compels attorneys to state that a client has a right to hire a petition preparer.

Section 527 requires Plaintiffs to provide a document entitled by the United States Trustee's Office as a "Bankruptcy Information Sheet."³ At the time plaintiffs filed their

³This information is available at http://www.usdoj.gov/ust/eo/ust_org/bky-info/index.htm.

complaint the sheet was factually inaccurate. However, the information has been corrected and Plaintiffs no longer assert a claim for violation of their First Amendment Rights for requiring its dissemination.

Plaintiffs do assert a claim for the Code's requirement that Plaintiffs to state that a client has a right to hire a bankruptcy petition preparer. Debtors in bankruptcy can receive little benefit from a non-attorney petition preparer. One Court commenting on what a petition preparer can do is, "not much." *In re Gutierrez*, 248 B.R. at 297-98. Bankruptcy petition preparers cannot give legal advice⁴.

Most debtors who come to bankruptcy attorneys are near or are in desperate financial problems. Requiring Plaintiffs to inform debtors of their right to hire a non-attorney requires Plaintiffs to give ill-advised advice in violation of the First Amendment. Defendants cite as authority *Casey* which requires doctors to advise patients of the risks of abortion. *Planned Parenthood of Southeast Pennsylvania v. Casey*, 505 U.S. 833, 884 (1992). The Plaintiffs' situation is factually different than the doctors in *Casey*. Plaintiffs are not required to inform clients of the risk of filing bankruptcy. Rather, Plaintiffs are required to tell their clients essentially, "you can go somewhere else that is cheaper." Given debtors financial concerns and the fact that petition preparers operate in "shadowy grey areas" of bankruptcy representation it would be ill advised for debtors to seek the help of bankruptcy petition preparers. See *In Re Attorneys at Law and Debt Relief Agencies*, 332 B.R. 66 (Bankr. S.D. Ga. 2005).

⁴ For an in depth discussion of what petition preparers may not do see *In re Bush*, 275 B.R. 69 (Bankr. Idaho 2002).

The Code requires Plaintiffs to make these statements at Plaintiffs' own expense and while Plaintiffs are consulting their clients. Rather than under *Casey* this Court should analyze the case at hand under the standard delineated in *PG&E v. PUC. Pacific Gas & Elec. Co. v. Public Util. Comm'n*, 475 U.S. 1 (1986). In *PG&E* the Supreme Court held a law unconstitutional a regulation that required a utility to disclose the viewpoint of its opponents.

“Appellant does not, of course, have the right to be free from vigorous debate. But it does have the right to be free from government restrictions that abridge its own rights in order to “enhance the relative voice” of its opponents. *Buckley v. Valeo*, 424 U.S. 1, 49, and n. 55 (1976). The Commission's order requires appellant to assist in disseminating TURN's views; it does not equally constrain both sides of the debate about utility regulation.” *Id* at 14.

D. Section 528 Is unconstitutional because it compels untrue speech.

Section 528 requires “debt relief agencies” to “clearly and conspicuously use the following statement in such advertisement: ‘We are a debt relief agency. We help people file for bankruptcy relief under the Bankruptcy Code.’ or a substantially similar statement.”

Mr. McBride is the only plaintiff to assert a claim under this provision. Mr. McBride advises his clients to file bankruptcy, and advises his clients about the dischargeability of spousal and child support. Complaint ¶ 18. Mr. McBride is a “debt relief agency” and provides “bankruptcy assistance” by virtue of the advice he gives his clients⁵. However, Mr. McBride

⁵Mr. McBride further advertises his willingness to help consumers under the Fair Debt Collection Practices Act. His advertisement reads “Debt and Collection Issues—Harassment, abuse and clearly illegal tactics appear to be the norm for many debt collectors. It’s important to remember that the vast majority of those who do owe money aren’t “deadbeats” – just people who’ve hit a bad patch due to unforeseen circumstances, who have every intention of paying when they can. If you have issues regarding debts and harassment by creditors, I can help stop the harassing calls and help you get your financial life back on

does not represent clients in bankruptcy matters nor does he file petitions for relief under the Bankruptcy Code. Complaint ¶ 12.

Mr. McBride is now precluded from advertising or relaying any information relating to the Bankruptcy Code unless he makes the disclosures required by § 528. Mr. McBride currently has information on his website about help for those who are being contacted by debt collectors, as well as information about the collectability of child support and spousal support. These are all people who can benefit from bankruptcy information. Mr. McBride can benefit from advertising information about the effects of bankruptcy on his website. However, he cannot address issues of a person filing bankruptcy without making untrue disclosures.

The Supreme Court has ruled that “...because disclosure requirements trench much more narrowly on an advertiser's interests than do flat prohibitions on speech, “warning[s] or disclaimer[s] might be appropriately required . . . in order to dissipate the possibility of consumer confusion or deception.”” *Zauderer v. Office of Disciplinary Counsel*, 471 U.S. 626, 651 (1985) (internal citations omitted).

However, § 528 creates the kind of consumer confusion that the Supreme Court states should be prohibited. Because Mr. McBride does not represent clients in bankruptcy matters it is misleading for him to advertise that he does.

The First Amendment protects commercial speech. *Zauderer*, 471 U.S. at 651. “[U]njustified or unduly burdensome disclosure requirements might offend the First Amendment by chilling protected commercial speech.” *Id.* Here, Mr. McBride’s speech is chilled because

track.” http://www.jasonmbridelaw.com/CustomPage_3.shtml

if he advertises without making the disclaimer required by § 528 he is subject to sanction. If he advertises with the disclaimers required by § 528 he runs the risk of being inundated with clients that he has no interest in representing.

E. Sections 526-28 Are unconstitutionally vague.

Sections 526-528 are unconstitutionally vague because Plaintiffs cannot tell who is an assisted person because “nonexempt property” is not defined by the bankruptcy code. Therefore, Plaintiffs cannot know how to value assets or what exemptions, if any, to apply. Furthermore, Plaintiffs cannot know what the value of the assets are.

“A statute can be impermissibly vague for either of two independent reasons. First, if it fails to provide people of ordinary intelligence a reasonable opportunity to understand what conduct it prohibits. Second, if it authorizes or even encourages arbitrary and discriminatory enforcement.” *Hill v. Colorado*, 530 U.S. 703, 732 (2000) citing *Chicago v. Morales*, 527 U.S. 41, 56-57 (1999).

In the case at hand, a person of ordinary intelligence cannot understand what is prohibited because he cannot understand who is an “assisted person.” He cannot tell because the code does not inform him which exemptions to apply, the “value” of an asset is indeterminable, and § 522 of the code does not define the word “exempt.” As such, Plaintiffs must guess who is an assisted person.

Because the Code forbids certain speech and compels other speech to assisted persons §§ 526-528 fail the standard set out in *Hoffman Estates* which states, “...the most important factor affecting the clarity that the Constitution demands of a law is whether it threatens to inhibit the exercise of constitutionally protected rights. If, for example, the law interferes with

the right of free speech or of association, a more stringent vagueness test should apply.” *Hoffman Estates v. Flipside Hoffman Estates, Inc.*, 455 U.S. 489, 499 (1982).

1. The Bankruptcy Code does not inform Plaintiffs which exemptions to apply when calculating nonexempt property.

Defendants’ analysis that Plaintiffs can simply refer to § 522 is wanting. For instance, Mr. Swartz, practices before both the Washington and Oregon Bankruptcy Courts. Washington has opted to allow debtors to choose federal or state exemptions. No section of the code tells Mr. Swartz which exemptions apply when one set of exemptions produces more than \$150,000 in nonexempt assets and the other produces less than \$150,000 in nonexempt assets. However, Mr. Swartz is subject to sanctions if he guesses incorrectly.

2. The Bankruptcy Code does not inform plaintiffs how to value assets.

Section 522 defines “value” as fair market value. 11 U.S.C. § 522(a)(2). However, the code does not inform Plaintiffs which market to use to value the assets. The Supreme Court has acknowledged that there are several ways to value assets. *Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997).

When valuing vehicles Kelly Blue Book and the National Automobile Dealers Association (NADA) guides list several values for the same asset, namely 1) wholesale, 2) retail and 3) private party. Further, Kelly Blue Book and NADA do not agree on the value of the same asset. See *in re Gray*, 285 B.R. 379, 382-384 (N.D. Tex. 2002). Since *Rash* Bankruptcy Courts still have different ways of valuing a vehicle⁶. The code does not state which method to choose,

⁶See eg *In re McElroy*, 210 B.R. 833 (Bankr. D. Or. 1997); *In re Getz*, 242 B.R. 916 (B.A.P. 6th Cir. 2000); *In re Lyles*, 226 B.R. 854 (Bankr. W.D. Tenn. 1998); *In re Williams*, 224 B.R. 873 (Bankr. S.D. Ohio 1998); *In re Franklin*, 213 B.R. 781 (Bankr. N. D. Fla.

which guide to use, which market within a guide, leaving Plaintiffs to guess which will not have them sanctioned for failing to make disclosures, or for advising their client to incur new debt in contemplation of filing bankruptcy.

3. Some assets defy valuation.

Vehicles are one of the more straightforward assets to value given the fact that there are guides published listing values. Plaintiffs cannot know how to value a life estate in real property, the equitable interest in married debtor's assets who is filing a petition as an individual, a redemption right in an asset that expires in 20 days, or what amount of money is "reasonably necessary" for a debtor.

Further, some assets simply have an unknown value. When Plaintiffs interview a debtor who has been in a car accident, how do Plaintiffs value the cause of action against the other drivers? Plaintiffs would have to make a determination of who was at fault, how great the injury was, when the injured debtor will stop treating, what are the extent of the medical bills at the end of the treatment, what the insurance company or jury would give as an award, and what the debtor would accept to settle the case. Plaintiffs are left to guess nearly all of this information.

Another asset that has an unknown value is a contingent remainder in a trust. To determine the value of a debtor's contingent remainder in a trust the attorney would have to know when the existing beneficiaries will die, how much of the assets of the trust the prior beneficiaries will consume, what is the rate of appreciation of trust assets, and what a willing

1997); *In re Renzelman*, 227 B.R. 740 (Bankr. W.D. Mo. 1998); *In re Russell*, 211 B.R. 12 (Banr. E.D.N.C. 1997).

buyer would pay for the debtor for the present value of the trust, if it is assignable. Plaintiffs attorneys cannot know this.

Bankruptcy Courts as well as other courts litigate for years the value of assets. However, Plaintiffs must make this determination at least within 3 days of the initial consultation pursuant to 11 U.S.C. § 527(a)(2). If Plaintiffs make the incorrect determination they are subject to forfeiture of fees and other sanctions.

4. Some exemption statutes allow “reasonably necessary” amounts as exempt.

ORS 18.345(1)(i) exempts, “[s]pousal support, child support, or separate maintenance *to the extent reasonably necessary* for the support of the debtor and any dependent of the debtor.” ORS 18.345(1)(L) exempts, “[t]he debtor’s right to receive, or property that is traceable to, a payment in compensation of loss of future earnings of the debtor or an individual of whom the debtor is or was a dependent, *to the extent reasonably necessary* for the support of the debtor and any dependent of the debtor.”

Section 522 of the Bankruptcy Code also exempts “reasonably necessary” amounts. Section 522(d)(10)(D) exempts, “alimony, support, or separate maintenance, *to the extent reasonably necessary* for the support of the debtor and any dependent of the debtor.” Section 522(d)(10)(E) exempts, “a payment under a stock bonus, pension, profitsharing, annuity, or similar plan or contract on account of illness, disability, death, age, or length of service, *to the extent reasonably necessary* for the support of the debtor and any dependent of the debtor...” (emphasis added to all above citations).

Plaintiffs cannot know what amount is “reasonably necessary” to calculate an exemption. In fact, in the case *Rousey v. Jacoway*, the Bankruptcy Court and intermediate appellate courts

all stated that the debtors' retirements were not exempt. However, the United States Supreme Court disagreed. *Rousey v. Jacoway* 544 U.S. 320 (2005). If the Courts cannot agree what is exempt, Plaintiffs cannot know what is exempt within the short time that Plaintiffs are required to make disclosures or advise their clients.

5. Definition of exempt and property of the estate

The code leaves Plaintiffs to guess the answer to "exempt from what?" Section 522(b)(1) exempts some of debtor's property. However, it does not address what, if anything, to do with encumbered property. Section 522(f) instructs that debtors may avoid liens to the extent that the lien impairs an exemption after consensual liens are factored. However, the remainder of § 522 is silent on consensual liens. Therefore, an attorney is forced to guess when dealing with a client who has a home worth \$200,000 that the debtor has given trust deeds to secure \$150,000 in loans, does the person have nonexempt assets worth more than \$150,000? The Oregon homestead exempts \$39,600. ORS 18.395. While an unsecured creditor may not levy on the home, the secured creditors may conduct a judicial or nonjudicial foreclosure. The Bankruptcy Trustee may not sell the home for the benefit of creditors. However, is it exempt if the secured creditor or the county tax assessor can execute on the property?

Oregon law establishes property rights of Oregon debtors. Section 541 of the Bankruptcy Code relies on state law to determine what is property of the estate. A debtors interest in property is not a self evident matter. The Oregon Court of Appeals has cited with approval a 1934 Oregon Supreme Court opinion which casts a great cloud over Plaintiffs' ability to determine what is property of the debtor when the property is encumbered. "[W]hile Oregon generally subscribes to the lien theory of chattel mortgages, a chattel mortgagee, upon default,

acquires a "qualified ownership" interest in the collateral and "may maintain an action in replevin for possession of the property or in trover for its conversion". *McKinley v. State Dept. of Motor Vehicles*, 179 Or. App. 350 fn. 5 (2002) citing *Commercial Securities, Inc. v. Mast*, 145 Or. 394, 400-02, 28 P.2d 635 (1934).

Defendants rely on *Owen v. Owen* to answer this question. 500 U.S. 305 (1991). However, *Owen* is marginally helpful. *Owen* relies on Florida law to determine what is exempt. In the case at hand Florida law does not apply. Therefore, the Supreme Court's reliance on § 541(d) will apply only if Oregon and Florida have similar laws regarding the case interpreted by the Court.

As noted by the *Owen* Court, when a debtor has only bare title to property, that is the property is subject to a mortgage for the full value, the property does not become property of the estate. *Id* at 308-309. This is different than Oregon law. See ORS 86.010.

Further, the *Owen* Court does not address property that is encumbered up to the point of the homestead exemption. Does the home then become property of the estate? or does part of the home become property of the estate? or does none of the home become property of the estate?

Owen has limited value because, if read as Defendants suggest, *Owen* does away with § 362 of the Code for fully encumbered property. If Defendants' reading of *Owen* is accurate and a fully encumbered property is not property of the estate then the automatic stay, which applies to property of the estate, does not apply to such property and a creditor could foreclose despite a bankruptcy filing. However, a creditor may not so much as obtain a Forcible Entry and

Detainer Judgment against a debt who has had their legal interest terminated. See *In re Lowrey*, 25 B.R. 52 (Bankr. E.D. Mo. 1982).

There are numerous cases interpreting the broad effect of the automatic stay and what is property of the estate. To accept Defendants' reading of *Owen* to make fully encumbered property exempt, and not property of the estate, eliminates the automatic stay. Therefore, *Owen* must mean something different than what Defendant suggests.

6. Valuation of nonexempt property has not previously been held unconstitutionally vague.

Defendants suggest that because no court has previously held the exemption scheme is unconstitutionally vague and because courts have given rulings on exemptions in the past, the exemption scheme must not be unconstitutionally vague. However, prior to the BAPCPA amendments to the code, an evaluation of exempt property was a practical one. The only issue that arose out of exemptions were 1) can the trustee sell the asset and 2) can we avoid a lien under § 522(f) because the lien impairs an exemption.

Now, Plaintiffs are required to know as a matter of law what is exempt or not. With no relation to the practicality of the code, Plaintiffs are now required to know what is exempt so Plaintiffs know to whom disclosures must be made and who they can advise to incur more debt.

This is particularly troubling for Mr. McBride who does not represent debtors in bankruptcy and therefore would have to learn the minutia of the Bankruptcy Code just to tell his clients that their child support is nondischargeable in bankruptcy.

7. Sections 526-528 are unconstitutional because they allow arbitrary and discriminatory treatment.

“A law is unconstitutionally vague if it fails to provide a reasonable opportunity to know what conduct is prohibited, *id.* (citing *Giaccio v. Pennsylvania*, 382 U.S. 399, 402-03, 86 S.Ct. 518, 15 L.Ed.2d 447 (1966)), or is so indefinite as to allow arbitrary and discriminatory enforcement, *id.* (citing *City of Chicago v. Morales*, 527 U.S. 41, 52, 119 S.Ct. 1849, 144 L.Ed.2d 67 (1999)).” *Tucson Woman’s Clinic v. Eden*, 379 F.3d 531 (9th Cir. 2004).

Here, Plaintiffs are subject to arbitrary and discriminatory enforcement of § 526-528 because the value of an asset is entirely undefined. If an attorney does not make disclosures or advises a client believing that §§ 526-528 do not apply, the government may bring a complaint against Plaintiffs claiming Plaintiffs undervalued the debtor’s assets.

Therefore, §§ 526-528 are unconstitutionally vague.

WHEREFORE, Plaintiffs respectfully request that this Court deny Defendants’ motion.

DATED April 3, 2006.

Olsen, Olsen & Daines

/s/ Keith D. Karnes
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