09-BK-146

Via e-mail to Rules_Comments@ao.uscourts.gov

February 16, 2010

Mr. Peter G. McCabe
Secretary, Committee on Rules of Practice and Procedure
Thurgood Marshall Federal Judiciary Building
Washington, DC 20544

Re: Proposed Revisions to Bankruptcy Rule 3001

Dear Mr. McCabe:

In response to the August 12, 2009 notice issued by the Committee on Rules of Practice and Procedure (http://www.uscourts.gov/rules/proposed0809/Memo_Bench_BK_CR.pdf) the American Bankers Association[1], the Financial Services Roundtable[2] and the Mortgage Bankers Association[3] are pleased to submit these comments regarding proposed amendments to Rule 3001.

This letter shall supplement the oral statement of Mr. Phillip Corwin delivered at the February 5, 2010 hearing conducted in New York City by the Advisory Committee on Bankruptcy Rules as well as Mr. Corwin's Summary Statement submitted in advance of that hearing and available at http://www.uscourts.gov/rules/2009%20Comments%20Committee%20Folders/BK%20Comments%202009/09-BK-022-Testimony-Corwin.pdf .

Overview

[1] *The American Bankers Association brings together banks of all sizes and charters into one association. ABA works to enhance the competitiveness of the nation's banking industry and strengthen America's economy and communities. Its members – the majority of which are banks with less than $125 million in assets – represent over 95 percent of the industry's $13.3 trillion in assets and employ over 2 million men and women.*

[2] *The Financial Services Roundtable represents 100 of the largest integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the CEO. Roundtable member companies provide fuel for America's economic engine, accounting directly for $74.7 trillion in managed assets, $1.1 trillion in revenue, and 2.3 million jobs.*

[3] *The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,400 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field.*

The undersigned organizations believe that the proposed amendments to Rule 3001 constitute a "solution" in search of a problem. Notwithstanding unsubstantiated claims of "systematic abuse" from the debtor bar, we know of no substantial reporting of problems or statistical studies indicating that the current version of Rule 3001 in any way sanctions or encourages creditors to file proofs of claim that are suspect or that otherwise disadvantage debtors. In almost every case the proof of claim filed by a creditor corresponds to a debt or a line of credit that has already been listed by the debtor and thereby presumptively conceded by the debtor to be valid; if amendment of the Rule is to be considered, then we would suggest that a debtor's listing of a debt on Schedule F should constitute prima facie evidence of the obligation's existence. Moreover, in almost every Chapter 7 case, the unsecured creditor will not receive a distribution from the estate because there will be no unencumbered assets.

Yet, despite the failure of the Advisory Committee to articulate a compelling need for amendment of the Rule, the proposed amendments will, at a minimum, significantly increase the cost and administrative burden on creditors and debt buyers filing a proof of claim and will often discourage the pursuit of legitimate claims. It will also undoubtedly diminish the amount that third parties are willing to pay original creditors for such debts. This will ultimately result in less credit availability and higher borrowing costs at a time of substantial economic distress, and into the future. Requiring additional documentation for its own sake, rather than to address a demonstrated and well documented problem, is proceeding down an incorrect path that will inevitably lead to the denial of legitimate claims. We must question why the Committee consulted with only two groups – a small number of bankruptcy judges, and the National Association of Chapter 13 Trustees -- during its preparation of these proposed amendments, but never sought input from unsecured creditors or the trade groups that represent them.

Our organizations are also concerned that the proposed amendments exceed the grant of statutory authority to establish bankruptcy rules provided to the Judicial Conference under the Rules Enabling Act ("REA"). *See* 28 U.S.C. 2075. Section 2075 of the REA specifically and unequivocally states that the power granted to the Judicial Conference to "prescribe by general rules...the practice and procedures in cases under title 11...shall not abridge, enlarge, or modify any substantive right." In our view, Congress created a detailed and specific scheme for addressing proofs of claim (and objections to proof of claim) by enacting 11 U.S.C. 502. Under Section 502(a), a proof of claim timely filed "is *deemed allowed*, unless a party in interest...objects." (*Emphasis added*) Further, Section 502(b) provides that a claim shall be allowed "except to the extent that" it falls within nine stated grounds – and failure to include documentation is not one of them. The plain language of Section 502 is clear -- all timely filed proofs of claim are presumptively valid, and shall be allowed except if they fall within statutorily stated grounds. Thus, creditors have a statutorily guaranteed, substantive right to rely on this presumption and, under the REA, any rules of bankruptcy procedure must respect this statutory right.

Further, based upon any reasonable reading, the proposed sanctions scheme for Rule 3001 runs afoul of the REA by "modifying" and "diminishing" a creditor's or debt buyer's statutory right to rely on a presumption of validity for timely-filed proofs of claim. This is most evident in proposed Rule 3001(c)(1)(D), which would impose

sanctions on a mortgage servicer and/or prevent a mortgage servicer from using certain documentary evidence of the validity of a claim "in any form" if there is a later objection to that claim. In fact, under Rule 3001(c)(1)(D) as presently drafted, it appears the court may award attorney's fees and other "relief" even if there has been no objection filed by a debtor.

The proposed sanctions structure for Rule 3001 clearly undermines and conflicts with Section 502, which unambiguously establishes a different claims process, because all proofs of claim are effectively no longer presumed valid unless accompanied by extraneous materials. The threat of sanctions for not providing, in advance of any objection, detailed information to support a proof of claim renders the statutory presumption of validity moot. These proposed sanctions for non-compliance with Rule 3001 should be eliminated to avoid undermining the Congressionally-created claims process established under Section 502. At a minimum, if the sanctions scheme in Rule 3001 is not eliminated -- as we believe it must be absent a clear grant of authority under new law -- we suggest that the Committee narrow the circumstances in which sanctions are permitted to actions by a creditor that intentionally and willfully violate the new proof of claim requirements. However, as failure to provide the proposed documentation would result in the creditor or debt buyer not having a valid claim, we see no need or justification for any additional sanctions beyond that harsh and unjust result. This is especially true given that creditors and debt buyers are already subject to a fine of up to $500,000 or imprisonment of up to five years for the filing of a fraudulent claim, and that debtors have the opportunity to object to any claim.

Finally, we note that the proposed amendments would impose documentation requirements that are far more burdensome than those enacted by Congress governing the collection of debts outside the bankruptcy process in the Fair Debt Collection Practices Act. This further buttresses our view that the proposed amendments intrude upon the policymaking prerogative of the legislative branch and are inconsistent with existing law.

Comments on Specific Proposed Amendments

Last Account Statement Requirement - The inclusion of the last open-end or revolving credit account statement would likely confuse rather than assist the debtor, as the creditor's or debt purchaser's claim is for the amount due on the date of the filing of the bankruptcy petition, not as of the last statement date. In many instances creditor practices regarding charged off accounts as well as state law considerations will result in a very substantial time gap between the transmittal of the last statement and the filing of the associated bankruptcy. Such statements would also be difficult to produce where a bank merger has occurred. Moreover, a debt purchaser could find it difficult or even impossible to obtain such a statement if the debt is old. The inability to supply the required statement, whatever its cause, would have the unjust result of negating an otherwise valid proof of claim that is entitled to a statutory presumption of validity. Testimony submitted to the Committee suggests that less than one percent of all proofs of claim for unsecured consumer debt are ever subject to an objection, and that only a miniscule portion of those objections are upheld. Yet this proposal would require

creditors to file statements for 100 percent of all such claims, inundating the bankruptcy courts with tens of millions of additional pages of documents annually. Further, privacy concerns as well as the existence of medical and other sensitive information on these statements could well result in the necessity for manual redaction of information by creditors, placing a nearly impossible burden on them given the volume of consumer bankruptcy cases.

Itemized Statement of Interest, Fees, Expenses, or Other Charges Requirement - The requirement for an itemized statement of interest, fees, expenses or charges would be very difficult or impossible to comply with unless a standardized calculation formula is adopted. Devising such a formula is a complex technical matter that we believe is beyond the authority and likely the competence of the Judiciary, as can be readily seen upon review of Regulation Z promulgated by the Federal Reserve Board to implement the Truth in Lending Act. For example, what is the "principal amount", and how should a creditor treat an account that includes a balance transfer from another lender? It is also inconsistent with the National Bank Act, which permits creditors to treat all interest and other charges as principal once they have accrued. It is unclear what benefit this difficult and burdensome requirement is intended to provide to the debtor, nor is there any clear statutory authority for the Committee to take this action.

Inconsistency with Rule 3001(f) – Both of the above referenced proposed new documentation requirements would contravene the implied presumption of validity accorded to a creditor's claim under Rule 3001(f), "Evidentiary Effect", which states "A proof of claim executed and filed in accordance with these rules *shall constitute prima facie evidence* of the validity and amount of the claim." *(Emphasis added.)* Requiring additional documentation is at complete odds with this prima facie presumption of validity, yet the proposed amendments contain no explicit waiver of Rule 3001f. Please note that we do not advocate the addition of such a waiver – in fact, we would strongly oppose it.

Statement of Cure Amount Requirement -- The proposed requirement to include a statement of the amount necessary to cure any default for debts secured by property requires significant further refinement. For example, if the claim is based upon a judgment lien then the cure amount would be the entire debt. We also question whether this proposal serves any worthwhile purpose, as the holder of a secured claim is already required to list the amount of pre-petition arrearage in Box 4 on Official Form B-10.

Escrow Account Statement Requirement -- The proposed requirement for an escrow account statement for debts secured by a principal residence is already the local rule in many jurisdictions. But there is no uniform national form for providing such information, and the Committee should withdraw this proposed amendment and develop such a form before proceeding further on this aspect of the proposal.

Proposed Additional Sanctions -- The additional sanctions proposed for creditors who fail to provide the proposed documentation required by the amendments are outside the proper role of the Judiciary. We do not believe that Congress has provided adequate

statutory authority for this portion of the proposed amendments. Further, the proposed "exclusionary rule" that bars a creditor or other claim holder from presenting any omitted information or document in any contested matter or adversary proceeding, except with leave of the court under narrowly circumscribed grounds, changes existing law and will encourage debtors to file objections based on omitted documents – even if they can be provided to counter the objection – rather than bona fide disputes. Finally, we do not believe that a failure to provide any of the information or documentation required by Rule 3001 rises to the level of conduct subject to sanction, as that generally requires proof of a knowing or willful action.

In our view, Section 105(a) of the Code -- which provides the Bankruptcy Court with general authority to issue any order, process, or judgment necessary or appropriate to carry out the provisions of Title 11, and to take any action necessary or appropriate to enforce or implement court orders **or rules**, or to prevent an abuse of process – does not constitute sufficient statutory basis for these proposed additional sanctions. The authority provided in Section 105 is limited and does not authorize actions foreclosed by other provisions of the Code or Rules. At best, Section 105 is a limited grant of authority to bankruptcy judges to take action on a discretionary case-by-case basis and cannot be the basis for the promulgation of general Rules, which is governed by the REA.

Beyond the lack of an adequate statutory basis, the granting of such general authority for additional sanctions seems unduly excessive, given that failure to comply with the proposed documentation requirements would result in an invalid proof of claim. Further, providing general authority for the awarding of debtor attorney fees will almost surely encourage dilatory litigation and thereby place an unnecessary and unjustifiable burden upon the court system.

Conclusion

We share the Committee's belief that assuring accuracy of proofs of claim is very important for all parties in interest and the integrity of the bankruptcy court system. But the proposed amendments would place an unreasonable burden upon consumer lenders and debt purchasers that in many cases will be impossible to satisfy. Overall, the proposed amendments would fundamentally alter the balance between debtors and creditors in bankruptcy. By requiring additional information and penalizing the omission of this information, the proposed amended Rule would impose additional costs on creditors and encourage debtors to dispute otherwise undisputed claims and encourage unnecessary litigation. It would likely result in a further diminution of consumer credit availability and greater losses for financial institutions as a result of its detrimental impact upon the purchased debt market. We do not know of any serious problems in regard to proofs of claim for unsecured consumer debt that justify this negative economic impact.

Further, the proposed amendments raise serious issues as to consistency with the statutory authority of the Bankruptcy Code and the Rules Enabling Act. And, as set forth in this letter, portions of the proposal raise credit market policy issues that should be

properly addressed by the legislative branch, rather than the judiciary. We therefore strongly urge the Committee to withdraw the proposed amendments in their entirety.

To the extent that we have suggested refinements of, or national forms related to, secondary aspects of the proposed amendments they can be addressed in a revised and far narrower proposal. But, for all the reasons stated above, we are strongly opposed to the two major provisions of the proposed amended Rule – the new documentation requirements and the authorization of additional judicial sanctions for the failure to provide those documents.

We appreciate the opportunity to comment upon the proposed amendments and hope that the Committee finds our views to be helpful and informative.

Sincerely,

American Bankers Association
Financial Services Roundtable
Mortgage Bankers Association