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Can Software Be a Bankruptcy Petition Preparer?

Thomas Szaniawski, J.D. Candidate 2010

Recently, in *Reynoso v. United States (In re Reynoso)* — a case of first impression for the Ninth Circuit that addressed the intersection of cyberspace and bankruptcy — the court held that a provider of web-based bankruptcy software was a bankruptcy petition preparer (“BPP”) under 11 U.S.C. section 110 and that under California law, the features and functionality of the software went beyond mere typesetting and constituted the unauthorized practice of law. *Reynoso v. United States (In re Reynoso)*, 477 F.3d 1117 (9th Cir. 2007). *In re Reynoso* is significant because prior to this case, the Ninth Circuit had not considered whether the creator-provider of a software program could be deemed a BPP within the meaning of section 110. 477 F.3d at 1123.

This article will first explore the purpose and design of section 110 — the statutory backdrop for the *Reynoso* court’s analysis. Second, this article will discuss the facts and procedural posture surrounding the *Reynoso* litigation. Third, this article will discuss the court’s rationale in holding that (1) the defendant provider of software was indeed a BPP, and (2) the defendant provider of software had engaged in the unauthorized practice of law. Finally, this

article will conclude by discussing the significance and broader implications of the *Reynoso* decision.

11 U.S.C. § 110 — Background and Mechanics

When Congress adopted section 110 via the Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, section 308 (1994), its primary motivation was to protect consumer debtors filing for bankruptcy from the predatory practices of unscrupulous BPPs. *See* H.R. Rep. No. 835, § 308 (1994). As one court phrased it, “[section] 110 was enacted to remedy what was perceived to be widespread fraud and unauthorized practice of law in the BPP industry.” *Ferm v. United States (In re Crawford)*, 194 F.3d 954, 960 (9th Cir. 1999), *cert. denied*, *Ferm v. U.S. Trustee*, 528 U.S. 1189 (2000).

Although prior to the 1994 amendment, the Code already provided that it was “permissible for a petitioner preparer to provide services solely limited to typing,” the legislative history of section 110 articulates Congress’ concern that “far too many [BPPs] also attempt to provide legal advice and legal services to debtors.” H.R. Rep. No. 835 § 308. The legislative history of section 110 further reads: “These preparers often lack the necessary legal training and ethics regulation to provide such services in adequate and appropriate manner [sic]. These services may take unfair advantage of persons who are ignorant of their rights both inside and outside the bankruptcy system.” *Id.* Offering context to the type of fraud Congress sought to prevent, one commentator — referring to unscrupulous BPPs as “typing mills” — has noted: “Reports from the Justice Department have stated that typing mills were responsible for 30% of all bankruptcy filings in the Central District of California and that many of the filings in that district were by individuals who did not speak English or understand the bankruptcy system.”

NORTON BANKRUPTCY LAW AND PRACTICE 3D, section 18:1, at 18-2 (West 2008) (citing 140 Cong. Rec. H10772 (1994) (statement of Rep. Berman)).

Section 110 protects debtors filing for bankruptcy by imposing disclosure and filing requirements on BPPs as well as sanctions for their noncompliance. *See* 11 U.S.C. § 110; H.R. Rep. No. 835 § 308. Section 110 defines a BPP as “a person, other than an attorney or an employee of an attorney, who prepares for compensation a document for filing.” 11 U.S.C. § 110(a)(1) (2000).¹

The legislative history of section 110 elucidates BPP filing requirements and sanctions:

This section requires all bankruptcy preparation services to provide their relevant personal identifying information It requires copies of all bankruptcy documents to be given to the debtor and signed by the debtor. The section also provides that if the petition is dismissed as a result of fraud or incompetence on the preparer’s account, or if the preparer commits an inappropriate or deceptive act, the debtor is entitled to receive actual damages, plus statutory damages of \$2000 or twice the amount paid to the preparer, whichever is greater, plus reasonable attorney’s fees and costs The bankruptcy preparer is also subject to injunctive action preventing the preparer from further work in the bankruptcy preparation business.

H.R. Rep. No. 835 § 308. As one popular commentator has described it,

[s]ection 110 requires the filing of various disclosures based loosely on disclosures that are required of tax return preparers that, collectively, create a paper trail to identify nonattorneys who prepare documents to be filed by bankruptcy debtors It also prohibits some of the most prevalent abuses by petition preparers, such as the forging of debtors’ signatures on bankruptcy petitions.

3 COLLIER ON BANKRUPTCY, ¶ 110.01, at 110-7–100-8 (Alan N. Resnick et al. eds., 15th ed. rev. 2008) (internal citations omitted). For a more comprehensive overview of the background,

¹ Because this case arose prior to the ratification of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, all references in this memorandum are to the 2000 iteration of the Bankruptcy Code, which was in effect at the time of filing. 477 F.3d at 1120, n.1.

purpose, and function of section 110, see *Id.* at 110-7 and NORTON BANKRUPTCY LAW AND PRACTICE 3d, section 18:1, at 18-2.

***In re Reynoso* — Facts and Procedural Posture**

Defendant Frankfort Digital Services (“Frankfort”), which was owned and operated by Henry Ihejirika — who was not an attorney — sold licenses to websites that allowed customers to access (1) browser-based software for preparing bankruptcy petitions and schedules and (2) informational guides that promised advice on relevant aspects of bankruptcy law. *Reynoso v. United States (In re Reynoso)*, 477 F.3d 1117, 1120 (9th Cir. 2007). In preparing to file for bankruptcy, debtor Jayson Reynoso accessed one of Frankfort’s websites, the “Ziinet Bankruptcy Engine,” which represented itself as offering expertise in the field of bankruptcy law. *Id.* The website’s description claimed, *inter alia*:

Ziinet is an expert system and knows the law. Unlike most bankruptcy programs which are little more than customized word processors the Ziinet engine is an *expert system*. It knows bankruptcy laws right down to the applicable state in which you live. Now you no longer need to spend weeks studying bankruptcy laws.

Id. The website further promised that the program would select exemptions for the user and eliminate the need for the user herself to choose which schedule to use for a given piece of information. 477 F.3d at 1120–21. The site also offered access to its “Bankruptcy Vault,” a body of information on “loopholes” and “stealth techniques,” such as how to hide a bankruptcy filing from credit bureaus and how to retain certain types of property through the filing. *Id.* at 1121.

Debtor Reynoso purchased a sixty-day license for access to the Ziinet Engine and the Bankruptcy Vault for \$219, and the software performed as advertised. *Reynoso v. United States*

(*In re Reynoso*), 477 F.3d 1117, 1121 (9th Cir. 2007). The software prompted Reynoso to enter personal information, debts, and income into dialog boxes; the program then generated a completed set of bankruptcy forms. *Id.* As promised, the software selected schedules and exemptions for Reynoso — he himself did not choose any of the exemptions that appeared on the completed forms. *Id.*

However, where the completed bankruptcy forms provided space for any non-attorney petitioner preparer's signature and social security number — as required by section 110 — the software simply generated the response, “not applicable.” *Id.* Furthermore, question number nine on the “Statement of Financial Affairs” section of the petition read in part: “[l]ist all payments made [by] . . . debtor to any persons, including attorneys, for consultation concerning debt consolidation, relief under the bankruptcy law, or preparation of a petition in bankruptcy within one year immediately preceding the commencement of this case.” *Id.* The software generated the following response:

Realizing that this document is signed under penalty of perjury, I declare that I prepared my own bankruptcy by myself using a computer and that I was not assisted by an attorney, paralegal, or bankruptcy preparer. I downloaded the software into my computer's browser as a web page, typed in my bankruptcy information and printed my bankruptcy documents on my printer in the privacy of my own home without any human intervention other than mine. The software printed the official Federal bankruptcy forms with the information I typed in within a few seconds of my pressing the print button and no one other than myself inputted, edited or reviewed my bankruptcy information or handled my bankruptcy documents at any point in the process. The contents of my documents are based entirely upon my own research and no one gave me legal advice or told me to include or omit any information from my documents.

Id.

The fact that Reynoso had paid for and utilized Frankfort's online bankruptcy engine came to light during Reynoso's first meeting with creditors, when the chapter 7 trustee noticed

errors on the petition and queried Reynoso about them. *Reynoso v. United States (In re Reynoso)*, 477 F.3d 1117, 1121 (9th Cir. 2007). After subsequent investigation, the trustee commenced an adversary proceeding against Frankfort alleging, *inter alia*, violations of 11 U.S.C. section 110. *Id.* Based upon an analysis of the features and functionality of the petition preparation software, the Bankruptcy Court for the Northern District of California held that Frankfort had acted as a BPP within the meaning of 11 U.S.C. section 110. *Id.* at 1120. The Bankruptcy Court further held that Frankfort had committed fraudulent, unfair, or deceptive conduct, and additionally had engaged in the unauthorized practice of law. *Id.* Accordingly, the court ordered Frankfort to pay fines and disgorge fees, enjoined it from acting as a BPP, and certified the facts to the district court for entry of an order for damages pursuant to 11 U.S.C. section 110(i). *Frankfort Digital Servs., Ltd. v. Neary (In re Reynoso)*, 315 B.R. 544, 547 (B.A.P. 9th Cir. 2004) (amended op.), *aff'd*, 477 F.3d 1117 (9th Cir. 2007). Frankfort appealed the decision to the Bankruptcy Appellate Panel (“BAP”) of the Ninth Circuit, which affirmed the lower court’s decision, including the relief granted. *Id.* After Frankfort appealed the BAP decision, the case came before the Court of Appeals for the Ninth Circuit, which likewise affirmed in all regards. *Reynoso v. United States (In re Reynoso)*, 477 F.3d 1117, 1126 (9th Cir. 2007).

***In re Reynoso* — BPP Analysis**

While the *Reynoso* court’s narrow holding imputing BPP status to a provider of software was indeed unprecedented, the court was able to rely on parallels to cases deeming individuals or corporations BPPs.

In *Ferm v. U.S. Trustee (In re Crowe)*, the Bankruptcy Appellate Panel for the Ninth Circuit held that mere equivocation or semantic legerdemain is not enough to exempt one from BPP status — one who acts as the functional equivalent of the traditional BPP and provides assistance in petition preparation falls squarely within the ambit of section 110. 243 B.R. 43, 49–50 (B.A.P. 9th Cir. 2000), *aff'd*, 246 F.3d 673 (9th Cir. 2000). There, the court held that the author of an instructional book on bankruptcy petitions was a BPP because he made the guarantee that he would complete his customers' petitions for free if they were unable to do so themselves using the information provided in the book. *Id.* The court held that under the circumstances, the act of selling the book was tantamount to serving as a BPP. *Id.* at 50. Further, the court characterized as disingenuous the defendant's attempt to shield himself from BPP status by claiming he was merely an author, rebuking that argument as a thinly-veiled attempt to sidestep the "for compensation" element of a BPP under section 110. *See Id.* Ultimately, the court stated that "the book is a mere front for [defendant author's] services. Because what [defendant author] really sells are his services, [defendant author] is subject to the court's jurisdiction for violations of § 110." *Id.* at 50 (emphasis added).

Similarly, in *Doser v. U.S. Trustee (In re Doser)*, the Ninth Circuit held that an agent who prepared petitions was a BPP despite the fact that the agent never personally met its customers. 281 B.R. 292, 303–04 (Bankr. D. Idaho 2002), *aff'd*, 292 B.R. 652 (D. Idaho 2003), *aff'd*, 412 F.3d 1056 (9th Cir. 2005). In that case, customers had met and consulted with a remote franchisee, who in turn transmitted the relevant information to the agent preparer. *Id.* The agent then completed the petition and returned it electronically to the franchisee, who printed copies and delivered them to the customers; the agent and the remote franchisee shared the fees for the transaction. *Id.* In its analysis of section 110 liability, the *Doser* court — like the *Ferm* court —

focused on the fact that the defendant agent performed the *function* of the traditional BPP: “preparing documents for filing for a fee.” *See Id.*

Returning to *In re Reynoso*, defendant Frankfort’s argument was simply that “the creation and ownership of a software program used by a licensee to prepare his or her bankruptcy forms is not preparation of a document for filing under the statute.” *Reynoso v. United States (In re Reynoso)*, 477 F.3d 1117, 1123 (9th Cir. 2007). Frankfort attempted to color its conduct not as “preparation” within the meaning of the statute, but rather as merely having “created a computer software program which is used by the licensee to create his or her own forms, no more.” Appellant’s Br. at *10, available on Westlaw at 2005 WL 627332. Frankfort argued that “[t]he software used by the prospective debtor makes no decisions of any kind. . . . The software does not explain anything except how to enter information and how to print.” *Id.* at *11. Additionally, Frankfort argued that the fact it had never communicated with Reynoso precluded the court from imputing BPP status. *Id.* at *10.

The *Reynoso* court found defendant Frankfort’s arguments unavailing and pointed approvingly to the B.A.P. opinion:

Frankfort charged fees to permit customers to access web-based software. Frankfort’s software solicited information from the customers. Critically, it then translated that information into responses to questions on the bankruptcy forms, and prepared the bankruptcy forms for filing using those responses. As the BAP noted, “The software did not simply place the debtors’ answers, unedited and unmediated into official forms where the debtors had typed them on a screen; rather, it took debtors’ responses to questions, restated them, and determined where to place the revised text into official forms.”

In re Reynoso, 477 F.3d at 1123 (quoting *Frankfort Digital Servs., Ltd. v. Neary (In re Reynoso)*, 315 B.R. 544, 552 (B.A.P. 9th Cir. 2004) (amended op.)).

In concluding on the point, the court found that Frankfort's bankruptcy engine was analogous to the BPPs in *In re Doser* and *In re Crowe*: "In sum, for a fee, [defendant] provided customers with completed bankruptcy petitions. Customers merely provided the data requested . . . and printed the finished forms. . . . This is materially indistinguishable from other cases in which individuals or corporations have been deemed bankruptcy petition preparers." *In re Reynoso*, 477 F.3d at 1123 (internal citations omitted). The *Reynoso* court pointed to *In re Doser* and *In re Ferm* in handily repudiating Frankfort's argument that a paucity of contact between an entity and its customer militated against BPP status. *Id.*

***In re Reynoso* — Unauthorized Practice of Law Analysis**

In framing the question whether defendant Frankfort had engaged in the unauthorized practice of law, the *Reynoso* court noted that "the practice of law . . . includes legal advice and counsel and the preparation of legal instruments and contracts[,]" but further commented that "ascertaining whether a particular activity falls within this general definition may be a formidable endeavor." *Reynoso v. United States (In re Reynoso)*, 477 F.3d 1117, 1125 (9th Cir. 2007) (citing *Baron v. City of L.A.*, 469 P.2d 353, 357–58 (Sup. Ct. Cal. 1970)). In defining the contours of this "formidable" issue, the *Reynoso* court looked to *California v. Landlords Professional Services* for the proposition that mere clerical assistance does not constitute the practice of law. *In re Reynoso*, 477 F.3d at 1125 (citing *California v. Landlords Prof'l Servs.*, 264 Cal. Rptr. 548 (Cal. Ct. App. 1990)). However, the *Reynoso* court also noted that *People v. Sipper* established that any activity beyond pure clerical assistance — even merely suggesting what type of document is appropriate — does constitute practice of law. *In re Reynoso*, 477 F.3d at 1125 (citing *People v. Sipper*, 142 P.2d 960 (Cal. App. Dep't Super. Ct. 1943)).

With respect to the scope of advice a BPP could properly provide, the *Reynoso* court looked to several cases in crafting its analysis. The *Reynoso* court looked to *In re Kaitangian* for the proposition that providing *personalized guidance* in how to prepare a bankruptcy petition constitutes the practice of law. *In re Reynoso*, 477 F.3d at 1125–26 (citing *In re Kaitangian*, 218 B.R. 102, 110 (Bankr. S.D. Cal. 1998)). The *Reynoso* court looked to *Hastings v. U.S. Trustee (In re Agyekum)* for the proposition that BPPs are prohibited from advising debtors on the selection of exemptions. *In re Reynoso*, 477 F.3d at 1126 (citing *Hastings v. U.S. Trustee (In re Agyekum)*, 225 B.R. 695 (B.A.P. 9th Cir. 1998)). The *Reynoso* court additionally looked to *In re Anderson* for the proposition that advising a client on the consequences of bankruptcy or selecting exemptions for the client constitutes a rendering of legal services. *In re Reynoso*, 477 F.3d at 1126 (citing *In re Anderson*, 79 B.R. 482, 484–85 (Bankr. S.D. Cal. 1987)).

In holding that defendant Frankfort had engaged in the unauthorized practice of law, the *Reynoso* court stated that by providing software that held itself out as offering legal advice, projected an aura of expertise, and provided specific — albeit automated — advice tailored to each customer’s unique situation, the defendant’s had overstepped the boundaries of permissible BPP conduct and engaged in the unauthorized practice of law. *In re Reynoso*, 477 F.3d at 1126.

Conclusion

In re Reynoso is significant because it established two novel propositions. First, the mere act of providing software may qualify an individual as a BPP; in that situation, the software provider is subject to the strictures of section 110. Failure to disclose the identity of the BPP or the fees tendered for the service, e.g., will expose the software provider to sanctions pursuant to section 110(i). Second, a provider of automated petition preparation services that does qualify as

a BPP must obey the strict limitations on the scope of permissible BPP conduct. Any conduct that goes beyond mere typesetting — counseling on the selection of exemptions or advising on consequences of filing, e.g. — can result in liability for the unauthorized practice of law. The fact that such conduct occurs by way of an automated system and not traditional interpersonal interaction is not a defense.

In re Reynoso has established a precedent that courts will no doubt draw upon as the intersection of technology, transactional automation, and law continues to evolve. Several courts — both within the Ninth Circuit and beyond — have already looked favorably upon *In re Reynoso*'s analysis for guidance adjudicating similar issues. *See, e.g., In re Newman*, No. 07-10706, 2007 WL 2261384, at *1 (Bankr. N.D. Cal. Aug. 6, 2007) (citing *In re Reynoso* for proposition that soliciting information later translated into a completed petition constitutes unauthorized practice of law); *In re Spence*, Bankr. No. 05-90478PM, 2009 WL 122760, at *10 (Bankr. D. Md. Jan. 14, 2009) (citing *In re Reynoso* for proposition that courts apply section 110 broadly in deeming a person a BPP).

With the widespread utilization of software like Turbo Tax in the tax field, e.g., it is not difficult to envision similar automation of predominantly transactional legal services. *In re Reynoso* stands for the proposition that putative providers of such software must consider carefully the contours of permissible conduct and remain mindful of the controlling legislation and case law to avoid adverse legal consequences.