Reading Packet for Law, 199: Best of American Case Law
Consumer Finance
July 21, 2020
Professor Robert M. Lawless

I. General Comments

Americans owe $15.4 trillion in household debt, including $11.2 trillion in home mortgages and $1.7 trillion in student loans. These are staggering sums. To gain some sense of just how staggering, consider that 15.4 trillion seconds is over 487,000 years, longer than human beings have been on the planet. There is $60,245 of debt for every adult in the United States, meaning both persons with debt and without. The median household income is $68,703, such that the debt per person is about one year of household income. We are a deeply indebted society.

Today's reading discusses three important cases in the area of consumer finance. Because of the amount of money involved and complexity of the regulation, there is a strong demand for legal services in the consumer financial industry. A poll on the popular *Brian Leiter's Law School Reports* named consumer law as the number-one topic that deserves more attention in the legal academy (http://leiterlawschool.typepad.com/leiter/2013/04/so-which-areas-of-law-deserve-more-attention-in-the-legal-academy.html). The College of Law offers a class in Consumer Finance plus many other courses that touch upon the topic such as Contracts, Bankruptcy, Real Estate Finance, and Secured Transactions.

Students interested in public-interest work often overlook the financial courses, but that is a mistake. One of the most valuable things lawyers can do in the public interest is help people have the financial security that makes sure they have a roof over their head and food on the table. By itself, debt is neither good or bad. The $15.4 trillion that Americans owe has purchased homes, automobiles, vacations, and even college educations. Lenders deserve to be repaid and receive reasonable compensation for the capital they have made available. But, any industry attracts its share of problems. The household lending industry seems to attract more than its share, probably because of the nature of household lending where relatively unsophisticated consumers must navigate often complex financial decisions.

The first case in our readings, *Marquette National Bank*, is one of the most consequential Supreme Court cases of the last fifty years. Although revolving around a seemingly nonconsequential issue in an obscure statute, *Marquette National Bank* set the stage for the explosion of consumer credit that occurred in the 1980s. Today, it may be hard to imagine a world where the ability to incur massive amounts of consumer debt was not sitting in your wallet. The so-called "democratization" of credit that occurred in the 1980s changed the way we consume and spend. Right after *Marquette National Bank* is some Senate testimony I once gave about the decision. The testimony and the graph after it will provide some context about the growth in consumer debt.

Marquette National Bank also is a statutory case. That is, it involves the interpretation of what the words in a federal statute mean. Most of what lawyers do revolves around statutes. To have a sense of what it means to practice law today requires understanding how to read and use statutes.

The second case, *Commonwealth v. Fremont Investment & Loan*, is an application of a statute unfair deceptive acts & practices law or "UDAP law" as they are called. UDAP laws are an important tool for consumers and state regulators to use. *Fremont Investment* gives us an opportunity not only to see how UDAP laws operate but also a window into the mortgage lending practices that led to the Great Recession of 2008. Some of these practices remain as traps for the unwary.

The third case, *United States v. Kras*, is a more traditional constitutional analysis. The question is whether there is a constitutional right of access to the bankruptcy courts. After discussing the easy consumer credit created by *Marquette,* the *Kras* opinion will allow us to discuss what society should do, if anything, to those who amass too much debt. We also can use *Kras* as a jumping-off point to discuss access to courts, which in turn requires us to think about what courts are and what they do. Before *Kras*, I have included a brief explanation about some basic points about bankruptcy law.

In editing the cases, I have followed the conventions I use in my co-authored casebooks. The cases have been edited heavily for readability, which is why you are reading 21 pages that also include explanatory text instead of about 40 pages of Supreme Court opinions. Note that omissions from the originals are NOT shown by ellipses or otherwise indicated. Also, most citations have been removed. Where I have added language, it is in brackets. This is not the way the cases would appear in the official reporter, but it is typical of how they might appear in a casebook. The editing also allows us to focus on the parts of the cases that are of most relevance to our discussion.

II. Creating the Consumer-Credit Economy

Marquette National Bank v. First of Omaha Service Corp.

439 U.S. 299 (1978)

JUSTICE BRENNAN delivered the opinion of the Court.

The question for decision is whether the National Bank Act, 12 U.S.C. § 85, authorizes a national bank based in one State to charge its out-of-state credit-card customers an interest rate on unpaid balances allowed by its home State, when that rate is greater than that permitted by the State of the bank's nonresident customers.

I

The First National Bank of Omaha (Omaha Bank) is a national banking association with its charter address in Omaha, Nebraska. Omaha Bank is a card-issuing member in the BankAmericard plan. This plan enables cardholders to purchase goods and services from participating merchants and to obtain cash advances from participating banks throughout the United States and the world. Omaha Bank has systematically sought to enroll in its BankAmericard program the residents, merchants, and banks of the nearby State of Minnesota. The solicitation of Minnesota merchants and banks is carried on by respondent First of Omaha Service Corp. (Omaha Service Corp.), a wholly owned subsidiary of Omaha Bank.

Minnesota residents are obligated to pay Omaha Bank interest on the outstanding balances of their BankAmericards. Nebraska law permits Omaha Bank to charge interest on the unpaid balances of cardholder accounts at a rate of 18% per year on the first $999.99, and 12% per year on amounts of $1,000 and over. Minnesota law, however, fixes the permissible annual interest on such accounts at 12%. To compensate for the reduced interest, Minnesota law permits banks to charge annual fees of up to $15 for the privilege of using a bank credit card.

The instant case began when petitioner Marquette National Bank of Minneapolis (Marquette) itself a national banking association enrolled in the BankAmericard plan, brought suit to enjoin Omaha Bank and Omaha Service Corp. from soliciting in Minnesota for Omaha Bank's BankAmericard program until such time as that program complied with Minnesota law. Marquette claimed to be losing customers to Omaha Bank because, unlike the Nebraska bank, Marquette was forced by the low rate of interest permissible under Minnesota law to charge a $10 annual fee for the use of its credit cards.

II

Omaha Bank is a national bank; it is an "instrumentalit[y] of the federal government, created for a public purpose, and as such necessarily subject to the paramount authority of the United States." *Davis v. Elmira Savings Bank*, 161 U.S. 275, 283 (1896). The interest rate that Omaha Bank may charge in its BankAmericard program is thus governed by federal law. The provision of § 85 called into question states:

> Any association may take, receive, reserve, and charge on any loan or discount made, or upon any notes, bills of exchange, or other evidences of debt, interest at the rate allowed by the laws of the State, Territory, or District *where the bank is located*, . . . and no more, except that where by the laws of any State a different rate is limited for banks organized under State laws, the rate so limited shall be allowed for associations organized or existing in any such State under this chapter. (Emphasis supplied.)

Section 85 thus plainly provides that a national bank may charge interest "on any loan" at the rate allowed by the laws of the State in which the bank is "located." The question before us is therefore narrowed to whether Omaha Bank and its BankAmericard program are "located" in Nebraska and for that reason entitled to charge its Minnesota customers the rate of interest authorized by Nebraska law.

There is no question but that Omaha Bank itself is located in Nebraska. The National Bank Act requires a national bank to state in its organization certificate "[t]he place where its operations of discount and deposit are to be carried on, designating the State, Territory, or district, and the particular county and city, town, or village." The charter address of Omaha Bank is in Omaha, Nebraska.

The State of Minnesota, however, contends that this conclusion must be altered if Omaha Bank's BankAmericard program is considered: "In the context of a national bank which systematically solicits Minnesota residents for credit cards to be used in transactions with Minnesota merchants the bank must be deemed to be 'located' in Minnesota for purposes of this credit card program." Reply Brief for Petitioner at p. 7.

We disagree. Section 85 was originally enacted as § 30 of the National Bank Act of 1864. The congressional debates surrounding the enactment of § 30 were conducted on the assumption that a national bank was "located" for purposes of the section in the State named in its organization certificate. Although the convenience of modern mail permits Minnesota residents holding Omaha Bank's BankAmericards to receive loans without visiting Nebraska, credit on the use of their cards is nevertheless similarly extended by Omaha Bank in Nebraska by the bank's honoring of the sales drafts of participating Minnesota merchants and banks. Finance charges on the unpaid balances of cardholders are assessed by the bank in Omaha, and all payments on unpaid balances are remitted to the bank in Omaha. Furthermore, the bank issues its BankAmericards in Omaha, after credit assessments made by the bank in that city.

III

At the time Congress enacted the National Bank Act of 1864, so petitioners' argument runs, it intended "to insure competitive equality between state and national banks in the charging of interest." Brief for Petitioner at p. 24. This policy could best be effectuated by limiting national banks to the rate of interest allowed by the States in which the banks were located. Since Congress in 1864 was addressing a financial system in which incorporated banks were "local institutions," it did not "contemplate a national bank soliciting customers and entering loan agreements outside of the state in which it was established."

Close examination of the National Bank Act of 1864, its legislative history, and its historical context makes clear that, contrary to the suggestion of petitioners, Congress intended to facilitate a national banking system.

Although in the debates surrounding the enactment of § 30 there is no specific discussion of the impact of interstate loans, these debates occurred in the context of a developed interstate loan market.

We find it implausible to conclude, therefore, that Congress meant through its silence to exempt interstate loans from the reach of § 30. We would certainly be exceedingly reluctant to read such a hiatus into the regulatory scheme of § 30 in the absence of evidence of specific congressional intent. Petitioners have adduced no such evidence.

Petitioners' final argument is that the "exportation" of interest rates, such as occurred in this case, will significantly impair the ability of States to enact effective usury laws. This impairment may in fact be accentuated by the ease with which interstate credit is available by mail through the use of modern credit cards. But the protection of state usury laws is an issue of legislative policy, and any plea to alter § 85 to further that end is better addressed to the wisdom of Congress than to the judgment of this Court.

Senate Committee on the Judiciary
Hearings on Supreme Court Decisions on Health, Safety, and Employment
Statement of Professor Robert M. Lawless

June 11, 2008

Very technical and dry regulatory issues that only a lawyer could love can end up as Supreme Court cases that dig into the pocketbooks of consumers. These cases are litigated outside the blare of the media spotlight, followed closely only by experts and obscure to the millions of consumers who will bear the brunt of the decisions. The committee is to be commended for convening this hearing and casting some light on the importance of these underappreciated cases.

This is not a partisan issue, not a matter of the justices or some subset of the justices sitting in a room and deciding to be "pro-business" or "anti-consumer." Instead, it is a simple fact of our political system that cases are going to end up in the Supreme Court where business interests will have systematic advantages. The good news is that there are measures Congress could take to restore some of the balance.

In his comments to the Federal Reserve's proposed regulations to prohibit unfair credit card practices, Mr. Michael Rosado of Elkton, Maryland, writes about how a credit card company's mistake resulted in penalty rates that rose into the "high 20's." As a citizen of Maryland, Mr. Rosado is protected by a usury law that prohibits a creditor from charging more than 24% interest. How is it possible, then, for Mr. Rosado to be charged interest over 24%? Because of the Supreme Court's decision in *Marquette National Bank v. First of Omaha Serv. Corp.*, the Maryland usury statute is virtually worthless to Mr. Rosado and every other

Marylander. National consumer lenders operate in an environment that is free of usury restrictions because of the *Marquette* decision.

In *Marquette*, the issue revolved around the interpretation of five words in section 85 of the National Bank Act. Other than experts in the banking industry, few people would have any idea of what section 85 provides or, for that matter, what the National Bank Act provides. Passed in 1864, the National Bank Act created a national banking system and was intended to help create a stable national currency amidst the financial chaos of the Civil War. Section 85 of that law allows a national bank to charge an interest rate allowed by the state 'where the bank is located.' By enacting section 85, Congress wanted to protect nationally chartered banks from predatory state legislation designed to drive the nationally chartered banks out of business to the benefit of state-chartered. In 1864, bank lending was primarily a local business. Banks lent on the strength of personal relationships with members of the local community. The idea that a bank in one state would seek out lending business with citizens in another state was simply not something an 1864 Congress would have considered.

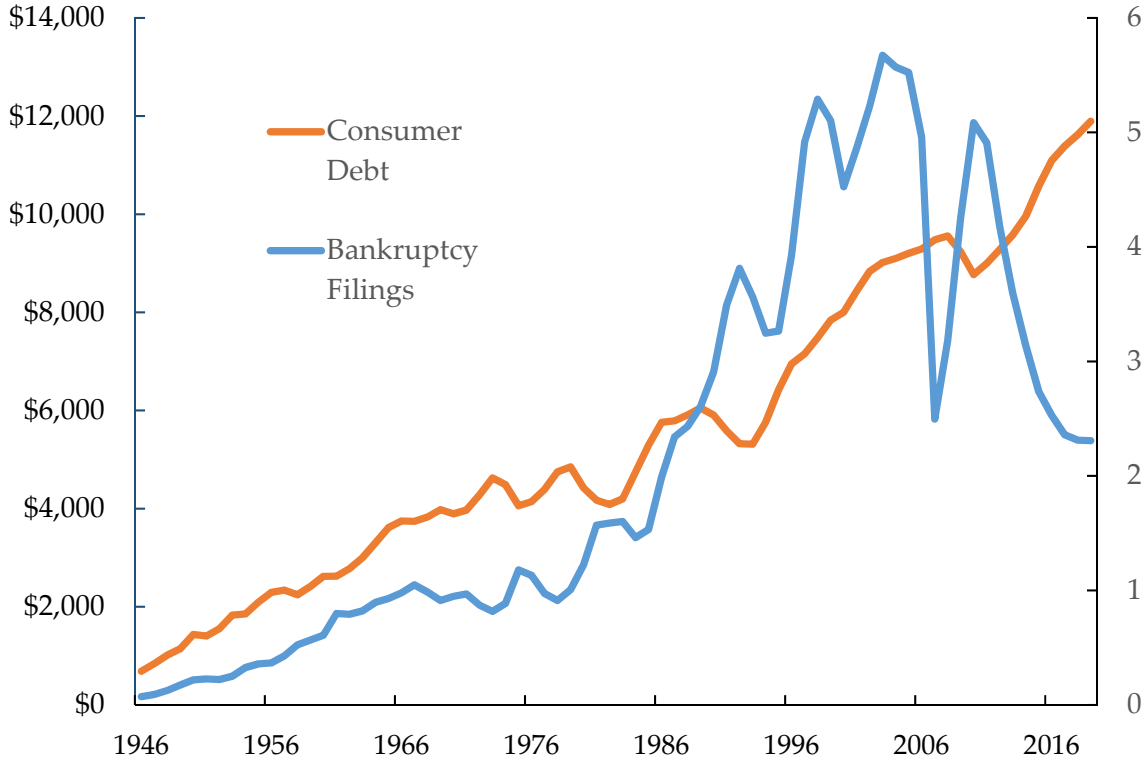
By 1978, information technology had dramatically changed the potential meaning of section 85. The *Marquette* case had its genesis in the decision of a Nebraska bank to expand its operations and lend to Minnesota citizens at an interest rate greater than allowed under Minnesota law but less than the amount allowed under Nebraska law. First of Omaha Bank argued that section 85 allowed it to charge the interest rate allowed by Nebraska law, the interest rate allowed by the state where First of Omaha was physically located. Although Congress had intended section 85 as a shield for national banks, First National Bank of Omaha now wanted to use section 85 as a sword to export Nebraska's interest rate into Minnesota. Ignoring the purpose of the National Bank Act and Congress' original intentions, the Supreme Court agreed with First National Bank.

The effect of the *Marquette* decision cannot be understated. Because a national bank now could charge whatever interest rate its own state allowed, some states simply repealed their interest rate caps. The national banks flocked to these states, set up operating subsidiaries, and began issuing credit cards at interest rates that would have been illegal under the state law where consumers were using these credit cards. Whichever states were willing to race to the bottom and offer the fewest consumer protections would win all of the consumer credit business. When consumers wonder how it can possibly be legal to get charged an interest rate that would have been considered usurious a generation ago, they can look to the *Marquette* decision.

With banks able to charge whatever interest rate they could get customers to pay, household debt exploded, and this increase in household debt is one of the greatest changes of our generation. We have come from a society where consumer debt was unusual to a society where consumer debt is ubiquitous. Where our parents would have been shocked to hear a neighbor owed a great deal of money, we now have conversations where permanent indebtedness is discussed a way of life. All of these effects can be traced to a decision of the United States Supreme Court.

U.S. Consumer Credit & Bankruptcy Filings, 1946 – 2018

The solid orange line shows total U.S. consumer credit per capita and inflation-adjusted to 2015 dollars. "Consumer credit" credit-card borrowing, auto loans, and other major forms of consumer debt. It does not include home mortgages. Bankruptcy filings are the annual number of filings per 1,000 U.S. population. All data are from U.S. government sources (Administrative Office of U.S. Courts, Census Bureau, Bureau of Economic Analysis, and the Federal Reserve).



III. State UDAP Laws & Mortgage Lending

Shifting topics, the next case is about the Massachusetts unfair and deceptive acts and practices law or UDAP law. Most every state has a UDAP law. Although there is significant variation, broadly speaking a state UDAP prohibits acts that are "unfair" or "deceptive" or, in some states, "unlawful." The statutes generally do not define these terms and leave it to the courts to fill out the meaning. In the following case, the state attorney general sought an injunction against foreclosure by a mortgage lender that the attorney general argued had made unfair loans. The mortgage lender responded that no law prohibited the loans and that it had fully disclosed all of the loan terms. The mortgage lender argued that the attorney general was trying to retroactively deem loans as "unfair" simply because they did not work out in hindsight. The court was not buying it.

Commonwealth v. Fremont Investment & Loan
897 N.E.2d 548 (Mass. 2008)

Botsford, J.

The Commonwealth, acting through the Attorney General, commenced this consumer protection enforcement action against the defendant Fremont Investment & Loan and its parent company, Fremont General Corporation (collectively, Fremont), claiming that Fremont, in originating and servicing certain "subprime" mortgage loans between 2004 and 2007 in Massachusetts, acted unfairly and deceptively in violation of G.L. c. 93A, § 2. All of the loans at issue are secured by mortgages on the borrowers' homes.

1. *Background.* Fremont is an industrial bank chartered by the State of California. Between January, 2004, and March, 2007, Fremont originated 14,578 loans to Massachusetts residents secured by mortgages on owner-occupied homes. Of the loans originated during that time period, roughly 3,000 remain active and roughly 2,500 continue to be owned or serviced by Fremont. An estimated fifty to sixty per cent of Fremont's loans in Massachusetts were subprime. Because subprime borrowers present a greater risk to the lender, the interest rate charged for a subprime loan is typically higher than the rate charged for conventional or prime mortgages.[8] After funding the loan, Fremont generally sold it on the secondary market, which largely insulated Fremont from losses arising from borrower default.

In originating loans, Fremont did not interact directly with the borrowers; rather, mortgage brokers acting as independent contractors would help a borrower select a mortgage product, and communicate with a Fremont account executive to request a selected product and provide the borrower's loan application and credit report. If approved by Fremont's underwriting department, the loan would proceed to closing and the broker would receive a broker's fee.

Fremont's subprime loan products offered a number of different features to cater to borrowers with low income. A large majority of Fremont's subprime loans were adjustable rate mortgage (ARM) loans, which bore a fixed interest rate for the first two or three years, and then adjusted every six months to a considerably higher variable rate for the remaining period of what was generally a thirty-year loan. Thus, borrowers' monthly mortgage payments would start out lower and then increase substantially after the introductory two-year or three-year period. To determine loan qualification, Fremont generally required that borrowers have a debt-to-income ratio of less than or equal to fifty per cent—that is, that the borrowers' monthly debt obligations, including the applied-for mortgage, not exceed one-half their income. However, in calculating the debt-to-income ratio, Fremont considered only the monthly payment required for the introductory rate period of the mortgage loan, not the

[8] In 51.4 per cent of Fremont's loans generally, and seventy-three per cent of a sample of delinquent Fremont loans analyzed by the Attorney General, Fremont paid a "yield spread premium" to the broker as compensation for placing the borrower into a higher interest rate bracket than the one for which he or she would otherwise qualify.

payment that would ultimately be required at the substantially higher "fully indexed" interest rate. As an additional feature to attract subprime borrowers, who typically had little or no savings, Fremont offered loans with no down payment. Instead of a down payment, Fremont would finance the full value of the property, resulting in a "loan-to-value ratio" approaching one hundred per cent. Most such financing was accomplished through the provision of a first mortgage providing eighty per cent financing and an additional "piggy-back loan" providing twenty per cent.

As of the time the Attorney General initiated this case in 2007, a significant number of Fremont's loans were in default.

The [trial court] granted a preliminary injunction in a memorandum of decision dated February 25, 2008. In his decision, the judge found no evidence in the preliminary injunction record that Fremont encouraged or condoned misrepresentation of borrowers' incomes on stated income loans, or that Fremont deceived borrowers by concealing or misrepresenting the terms of its loans. However, the judge determined that the Attorney General was likely to prevail on the claim that Fremont's loans featuring a combination of the following four characteristics qualified as "unfair" under G.L. c. 93A, § 2: (1) the loans were ARM loans with an introductory rate period of three years or less; (2) they featured an introductory rate for the initial period that was at least three per cent below the fully indexed rate; (3) they were made to borrowers for whom the debt-to-income ratio would have exceeded fifty per cent had Fremont measured the borrower's debt by the monthly payments that would be due at the fully indexed rate rather than under the introductory rate; and (4) the loan-to-value ratio was one hundred per cent, or the loan featured a substantial prepayment penalty (defined by the judge as greater than the "conventional prepayment penalty" defined in G.L. c 183C, § 2 or a prepayment penalty that extended beyond the introductory rate period.

The judge reasoned that Fremont as a lender should have recognized that loans with the first three characteristics just described were "doomed to foreclosure" unless the borrower could refinance the loan at or near the end of the introductory rate period, and obtain in the process a new and low introductory rate.[14] The fourth factor, however, would make it essentially impossible for subprime borrowers to refinance unless housing prices increased, because if housing prices remained steady or declined, a borrower with a mortgage loan having a loan-to-value ratio of one hundred per cent or a substantial prepayment penalty was not likely to have the necessary equity or financial capacity to obtain a new loan.

3. *Discussion.*

a. *Retroactive application of unfairness standards.* Fremont's basic contention is that, while the terms of its subprime loans may arguably seem "unfair" within the meaning of G.L. c. 93A, § 2, if judged by current standards applicable to the mortgage lending industry, they did

[14] The judge's prognosis of doom followed from the fact that the interest payments required when the introductory rate period ended and the fully indexed rate came into play would be significantly greater than the payments called for under the introductory rate (so-called "payment shock"). As a result, the borrower's debt-to-income ratio would necessarily increase, probably and foreseeably beyond the borrower's breaking point.

not violate any established concept of unfairness at the time they were originated; the judge, in Fremont's view, applied new rules or standards for defining what is "unfair" in a retroactive or ex post facto fashion and also represents "bad policy," because (among other reasons) lenders cannot know what rules govern their conduct, which will reduce their willingness to extend credit, hurting Massachusetts consumers. We do not agree that the judge applied a new standard retroactively.

General Laws c. 93A, § 2(a) makes unlawful any "unfair or deceptive acts or practices in the conduct of any trade or commerce." Chapter 93A creates new substantive rights and, in particular cases, makes conduct unlawful which was not unlawful under the common law or any prior statute. The statute does not define unfairness, recognizing that there is no limit to human inventiveness in this field. What is significant is the particular circumstances and context in which the term is applied. It is well established that a practice may be deemed unfair if it is within at least the penumbra of some common-law, statutory, or other established concept of unfairness.

Fremont correctly points out that as a bank in the business of mortgage lending, it is subject to State and Federal regulation by a variety of agencies. Well before 2004, State and Federal regulatory guidance explicitly warned lending institutions making subprime loans that, even if they were in compliance with banking-specific laws and regulations and were "underwrit[ing] loans on a safe and sound basis, [their] policies could still be considered unfair and deceptive practices" under G.L. c. 93A. More particularly, the principle had been clearly stated before 2004 that loans made to borrowers on terms that showed they would be unable to pay and therefore were likely to lead to default were unsafe and unsound, and probably unfair. Thus, an interagency Federal guidance published January 31, 2001, jointly by the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System, the FDIC, and the Office of Thrift Supervision, stated: "Loans to borrowers who do not demonstrate the capacity to repay the loan, *as structured*, from sources other than the collateral pledged are generally considered unsafe and unsound" (emphasis supplied). Expanded Guidance for Subprime Lending Programs at 11 (Jan. 31, 2001). On February 21, 2003, one year before the first of Fremont's loans at issue, the OCC warned that certain loans could be unfair to consumers:

> When a loan has been made based on the foreclosure value of the collateral, rather than on a determination that the borrower has the capacity to make the scheduled payments under the terms of the loan, based on the borrower's current and expected income, current obligations, employment status, and other relevant financial resources, the lender is effectively counting on its ability to seize the borrower's equity in the collateral to satisfy the obligation and to recover the typically high fees associated with such credit. Not surprisingly, such credits experience foreclosure rates higher than the norm.
>
> [S]uch disregard of basic principles of loan underwriting lies at the heart of predatory lending . . . .

OCC Advisory Letter, Guidelines for National Banks to Guard Against Predatory and Abusive Lending Practices, AL 2003–2 at 2 (Feb. 21, 2003).

The record here suggests that Fremont made no effort to determine whether borrowers could "make the scheduled payments under the terms of the loan." Rather, as the judge determined, loans were made in the understanding that they would have to be refinanced before the end of the introductory period. Fremont suggested in oral argument that the loans were underwritten in the expectation, reasonable at the time, that housing prices would improve during the introductory loan term, and thus could be refinanced before the higher payments began. However, it was unreasonable, and unfair to the borrower, for Fremont to structure its loans on such unsupportable optimism.

b. *General Laws c. 183C.* The Massachusetts Predatory Home Loan Practices Act, effective November 7, 2004, prohibits a lender from making a "high-cost home mortgage loan" unless the lender reasonably believes at the time the loan is made that the borrower "will be able to make the scheduled payments to repay the home loan based upon a consideration of the [borrower's] current and expected income, current and expected obligations, employment status, and other financial resources other than the borrower's equity in the dwelling which secures repayment of the loan." G.L. c. 183C, § 4. Chapter 183C expressly provides that a violation of the statute constitutes a violation of G.L. c. 93A.

Fremont's mortgage loans were not "high cost home mortgage loans" governed by G.L. c. 183C. Fremont contends, however, that the judge improperly interpreted c. 183C to reach Fremont's loans, and thereby violated basic rules of statutory construction that prohibit inferring a legislative intent to reach conduct that the statute's unambiguous language clearly does not cover.

Fremont's argument lacks merit. Even though the loans have different terms from Fremont's, the conduct the act prohibits, and deems a violation of G.L. c. 93A, is similar to the central element of unfairness the judge found in Fremont's lending practices: the origination of a home mortgage loan that the lender should recognize at the outset the borrower is not likely to be able to repay. That the Legislature chose in the act to focus specifically on home loan mortgages with different terms and features from Fremont's is not dispositive; the question is whether the act may be read to establish a concept of unfairness that may apply in similar contexts.

c. *General Laws c. 93A, § 3.* Fremont argues that the Commonwealth's claim is barred by G.L. c. 93A, § 3, because Fremont's actions were permitted by the law as it existed at the time it originated the loans. We disagree.

General Laws c. 93A, § 3, provides:

> Nothing in this chapter shall apply to transactions or actions otherwise permitted under laws as administered by any regulatory board or officer acting under statutory authority of the commonwealth or of the United States.

> For the purpose of this section, the burden of proving exemptions from the provisions of this chapter shall be upon the person claiming the exemptions.

This provision must be read together with G.L. c. 93A, § 2. That section created new substantive rights, and thus the fact that particular conduct is permitted by statute or by common law principles should be considered, but it is not conclusive on the question of unfairness. A defendant's burden in claiming the exemption is a difficult one to meet. To sustain it, a defendant must show more than the mere existence of a related or even overlapping regulatory scheme that covers the transaction. Rather, a defendant must show that such scheme affirmatively *permits* the practice which is alleged to be unfair or deceptive.

To carry its burden under G.L. c. 93A, § 3, of demonstrating that a regulatory scheme affirmatively *permits* the practice which is alleged to be unfair, Fremont must show that some regulatory scheme affirmatively permitted the practice of combining all of those features. Fremont has not done so. Rather, it cites authority demonstrating, it asserts, that each of the four features was permitted by statute and regulatory authorities. Assuming, without deciding, that Fremont is correct that every feature was affirmatively permitted separately, it was Fremont's choice to combine them into a package that it should have known was doomed to foreclosure; the relevant question is whether some State or Federal authority permitted that combination. No authority did.

d. *Public interest.* Because the Attorney General, in the name of the Commonwealth, brings this case to carry out her statutory mandate to enforce the Consumer Protection Act, it is necessary to consider whether the preliminary injunction order promotes the public interest. Fremont argues that it does not, primarily because in Fremont's view, the order imposes new standards on lending practices that were considered permissible and acceptable when the loans were made. The result, Fremont claims, will be an unwillingness on the part of lenders to extend credit to Massachusetts consumers because they will be unwilling to risk doing business in an environment where standards are uncertain and the rules may change after the fact.

Our previous discussion, and rejection, of Fremont's claim that the judge retroactively applied new unfairness standards disposes of Fremont's public interest argument; we do not accept the premise that, in concluding that Fremont is likely to be found to have violated established concepts of unfairness, the judge's order has created an environment of uncertainty that lenders will shun. The injunction order crafted by the judge strikes a balance between the interests of borrowers who face foreclosure and loss of their homes under home loan mortgage terms that are at least presumptively unfair, on the one hand; and the interest of the lender in recovering the value of its loans to borrowers who received the benefit of those loaned funds and continue to have a contractual obligation to repay, on the other. The order does not bar foreclosure as a remedy for the lender, nor does it relieve borrowers of their obligations ultimately to repay the loans. Rather, it requires, where the mortgage loan terms include all four features deemed presumptively unfair, that Fremont explore alternatives to foreclosure in the first instance (a step that Fremont has indicated its desire to take in any event), and then

seek approval of the court. If the court does not approve the foreclosure, that decision merely leaves the preliminary injunction in place until the Commonwealth has an opportunity to try to prove that the particular loan at issue actually violated c. 93A—a burden that is never shifted to Fremont. We conclude the order serves the public interest.

4. *Conclusion.* A judgment is to be entered affirming the grant of the preliminary injunction and remanding the case to the Superior Court for further proceedings.

IV. Bankruptcy Relief for the Overindebted

When things go wrong for borrowers, the U.S. bankruptcy system is supposed to offer a fresh start for the "honest but unfortunate debtor." Local Loan Co. v. Hunt, 292 U.S. 234 (1934). What sort of fresh start a bankruptcy system offers says a lot about who society sees as a deserving debtor. In *United States v. Kras*, Mr. Kras wanted access to the fresh start, but he could not afford it. The Supreme Court declined to give him the access unless he could pay the filing fee. Before reading *Kras*, it would be useful to have a basic understanding of the U.S. bankruptcy system. What follows is a document intended for pro se litigants that the U.S. Courts put together to describe the bankruptcy system.

Administrative Office of U.S. Courts
Bankruptcy Basics
(2011)

Process

Article I, Section 8, of the United States Constitution authorizes Congress to enact "uniform Laws on the subject of Bankruptcies." Under this grant of authority, Congress enacted the "Bankruptcy Code" in 1978. The Bankruptcy Code, which is codified as title 11 of the United States Code, has been amended several times since its enactment. It is the uniform federal law that governs all bankruptcy cases.

There is a bankruptcy court for each judicial district in the country. Each state has one or more districts. There are 90 bankruptcy districts across the country. The bankruptcy courts generally have their own clerk's offices.

The court official with decision-making power over federal bankruptcy cases is the United States bankruptcy judge, a judicial officer of the United States district court. The bankruptcy judge may decide any matter connected with a bankruptcy case, such as eligibility to file or whether a debtor should receive a discharge of debts. Much of the bankruptcy process is administrative, however, and is conducted away from the courthouse.

A debtor's involvement with the bankruptcy judge is usually very limited. A typical chapter 7 debtor will not appear in court and will not see the bankruptcy judge unless an objection is raised in the case. A chapter 13 debtor may only have to appear before the bankruptcy judge at a plan confirmation hearing. Usually, the only formal proceeding at which

a debtor must appear is the meeting of creditors, which is usually held at the offices of the U.S. trustee. This meeting is informally called a "341 meeting" because section 341 of the Bankruptcy Code requires that the debtor attend this meeting so that creditors can question the debtor about debts and property.

A fundamental goal of the federal bankruptcy laws enacted by Congress is to give debtors a financial "fresh start" from burdensome debts. The Supreme Court made this point about the purpose of the bankruptcy law in a 1934 decision:

> [I]t gives to the honest but unfortunate debtor…a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt.

Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934). This goal is accomplished through the bankruptcy discharge, which releases debtors from personal liability from specific debts and prohibits creditors from ever taking any action against the debtor to collect those debts. This publication describes the bankruptcy discharge in a question and answer format, discussing the timing of the discharge, the scope of the discharge (what debts are discharged and what debts are not discharged), objections to discharge, and revocation of the discharge. It also describes what a debtor can do if a creditor attempts to collect a discharged debt after the bankruptcy case is concluded.

Discharge in Bankruptcy

What is a discharge in bankruptcy?

A bankruptcy discharge releases the debtor from personal liability for certain specified types of debts. In other words, the debtor is no longer legally required to pay any debts that are discharged. The discharge is a permanent order prohibiting the creditors of the debtor from taking any form of collection action on discharged debts, including legal action and communications with the debtor, such as telephone calls, letters, and personal contacts.

Although a debtor is not personally liable for discharged debts, a valid lien (i.e., a charge upon specific property to secure payment of a debt) that has not been avoided (i.e., made unenforceable) in the bankruptcy case will remain after the bankruptcy case. Therefore, a secured creditor may enforce the lien to recover the property secured by the lien.

How does the debtor get a discharge?

Unless there is litigation involving objections to the discharge, the debtor will usually automatically receive a discharge. The Federal Rules of Bankruptcy Procedure provide for the clerk of the bankruptcy court to mail a copy of the order of discharge to all creditors, the U.S. trustee, the trustee in the case, and the trustee's attorney, if any. The notice informs creditors generally that the debts owed to them have been discharged and that they should not attempt any further collection. They are cautioned in the notice that continuing collection efforts could subject them to punishment for contempt.

Are all of the debtor's debts discharged or only some?

Not all debts are discharged. The debts discharged vary under each chapter of the Bankruptcy Code. Section 523(a) of the Code specifically excepts various categories of debts from the discharge granted to individual debtors.

The most common types of nondischargeable debts are certain types of tax claims, debts not set forth by the debtor on the lists and schedules the debtor must file with the court, debts for spousal or child support or alimony, debts for willful and malicious injuries to person or property, debts to governmental units for fines and penalties, debts for most government funded or guaranteed educational loans or benefit overpayments, debts for personal injury caused by the debtor's operation of a motor vehicle while intoxicated, debts owed to certain tax-advantaged retirement plans, and debts for certain condominium or cooperative housing fees.

In reading the *Kras* opinion that follows, it is useful to keep in mind that the effect of inflation. One dollar in 1973 is worth about the same as $6.27 in 2021. Thus, the $50 filing fee at issue is the equivalent of $313 in 2021. The filing fee for a chapter 7 bankruptcy is currently $338 such that the filing is about the same amount as it was in 1973, inflation adjusted. You can multiply the other dollar figures by six to get a sense of their equivalent spending power today. The Court decides Mr. Kras does not have a constitutionally protected right to file bankruptcy. The dissent from Justice Marshall remains a powerful statement about what it means to be overindebted.

United States v. Kras
409 U.S. 434 (1973)

JUSTICE BLACKMUN delivered the opinion of the Court.

The Bankruptcy Act imposes fees and makes the payment of those fees a condition to a discharge in voluntary bankruptcy.

Kras, an indigent petitioner in bankruptcy, challenged the fees on Fifth Amendment grounds.

I

Section 14(b)(2) of the Bankruptcy Act provides that "the court shall discharge the bankrupt if no objection has been filed and if the filing fees required to be paid by this title have been paid in full." Section 14(c) similarly provides that the court "shall grant the discharge unless satisfied that the bankrupt . . . (8) has failed to pay the filing fees required to be paid by this title in full." Section 59(g) relates to the dismissal of a petition in bankruptcy

and states that "in the case of a dismissal for failure to pay the costs," notice to creditors shall not be required. Three separate sections of the Act thus contemplate the imposition of fees and condition a discharge upon payment of those fees.

Three charges are imposed: $37 for the referee's salary and expense fund, $10 for compensation of the trustee, and $3 for the clerk's services. These total $50. The fees are payable upon the filing of the petition. Section 40(c)(1), however, contains a proviso that in cases of voluntary bankruptcy, all the fees "may be paid in installments, if so authorized by General Order of the Supreme Court of the United States." The Court's General Order in Bankruptcy No. 35(4) provides that, upon a proper showing by the bankrupt, the fees may be paid in installments within a six-month period, which may be extended not to exceed three months.

II

Robert William Kras presented his voluntary petition in bankruptcy to the United States District Court for the Eastern District of New York on May 28, 1971. [In an affidavit, Kras stated:]

1. Kras resides in a 2½-room apartment with his wife, two children, ages 5 years and 8 months, his mother, and his mother's 6-year-old daughter. His younger child suffers from cystic fibrosis and is undergoing treatment in a medical center.

2. Kras has been unemployed since May 1969 except for odd jobs producing about $300 in 1969 and a like amount in 1970. His last steady job was as an insurance agent with Metropolitan Life Insurance Company. He was discharged by Metropolitan in 1969 when premiums he had collected were stolen from his home and he was unable to make up the amount to his employer. Metropolitan's claim against him has increased to over $1,000 and is one of the debts listed in his bankruptcy petition. He has diligently sought steady employment in New York City, but, because of unfavorable references from Metropolitan, he has been unsuccessful. Mrs. Kras was employed until March 1970, when she was forced to stop because of pregnancy. All her attention now will be devoted to caring for the younger child who is coming out of the hospital soon.

3. The Kras household subsists entirely on $210 per month public assistance received for Kras' own family and $156 per month public assistance received for his mother and her daughter. These benefits are all expended for rent and day-to-day necessities. The rent is $102 per month. Kras owns no automobile. He receives no unemployment or disability benefit. His sole assets are wearing apparel and $50 worth of essential household goods. He has a couch of negligible value in storage on which a $6 payment is due monthly.

4. Because of his poverty, Kras is wholly unable to pay or promise to pay the bankruptcy fees, even in small installments. He has been unable to borrow money. The New York City Department of Social Services refuses to allot money for payment of the fees. He has no prospect of immediate employment.

5. Kras seeks a discharge in bankruptcy of $6,428.69 in total indebtedness in order to relieve himself and his family of the distress of financial insolvency and creditor harassment and in order to make a new start in life. It is especially important that he obtain a discharge of his debt to Metropolitan soon "because until that is cleared up Metropolitan will continue to falsely charge me with fraud and give me bad references which prevent my getting employment."

III

In the District Court Kras first presented a statutory argument that he was entitled to relief from payment of the bankruptcy charges because of the provisions of 28 U.S.C. § 1915(a).[1]

The District Court rejected the argument. It reached this result by noting that § 51(2) of the Bankruptcy Act had provided for a waiver of fees upon the filing of an affidavit of inability to pay. [In the Referees' Salary Bill in 1946, Congress repealed this provision.] The 1946 statute, being later and having a positive and specific provision for postponement of fees in cases of indigency, overrode the earlier general provisions of § 1915(a).

The District Court went on to hold, however, that the prescribed fees, payment of which served to deny Kras his Fifth Amendment right of due process, including equal protection. The court rested its decision primarily upon *Boddie v. Connecticut*, 401 U.S. 371 (1971).

IV

Boddie was a challenge by welfare recipients to certain Connecticut procedures, including the payment of court fees and costs, that allegedly restricted their access to the courts for divorce. The plaintiffs, simply by reason of their indigency, were unable to bring their actions. Justice Harlan, writing for the Court, stressed state monopolization of the means for legally dissolving marriage and identified the would-be indigent divorce plaintiff with any other action's impoverished defendant forced into court by the institution of a lawsuit against him. He declared that a meaningful opportunity to be heard was firmly imbedded in our due process jurisprudence and that this was to be protected against denial by laws that operate to jeopardize it for particular individuals. The Court then concluded that Connecticut's refusal to admit these good-faith divorce plaintiffs to its courts equated with the denial of an opportunity to be heard and, in the absence of a sufficient countervailing justification for the State's action, a denial of due process.

[1] "Any court of the United States may authorize the commencement, prosecution or defense of any suit, action or proceeding, civil or criminal, or appeal therein, without prepayment of fees and costs or security therefor, by a person who makes affidavit that he is unable to pay such costs or give security therefor."

But the Court emphasized that "we go no further than necessary to dispose of the case before us." *Id.*, at 382.

"We do not decide that access for all individuals to the courts is a right that is, in all circumstances, guaranteed by the Due Process Clause of the Fourteenth Amendment so that its exercise may not be placed beyond the reach of any individual, for, as we have already noted, in the case before us this right is the exclusive precondition to the adjustment of a fundamental human relationship. The requirement that these appellants resort to the judicial process is entirely a state-created matter. Thus we hold only that a State may not, consistent with the obligations imposed on it by the Due Process Clause of the Fourteenth Amendment, pre-empt the right to dissolve this legal relationship without affording all citizens access to the means it has prescribed for doing so." *Id.*, at 382-83.

V

B. The appellants in *Boddie*, on the one hand, and Robert Kras, on the other, stand in materially different postures. The denial of access to the judicial forum in *Boddie* touched directly on the marital relationship and on the associational interests that surround the establishment and dissolution of that relationship. On many occasions we have recognized the fundamental importance of these interests under our Constitution. The *Boddie* appellants' inability to dissolve their marriages seriously impaired their freedom to pursue other protected associational activities. Kras' alleged interest in the elimination of his debt burden, and in obtaining his desired new start in life, although important and so recognized by the enactment of the Bankruptcy Act, does not rise to the same constitutional level. If Kras is not discharged in bankruptcy, his position will not be materially altered in any constitutional sense. Gaining or not gaining a discharge will effect no change with respect to basic necessities. We see no fundamental interest that is gained or lost depending on the availability of a discharge in bankruptcy.

E. There is no constitutional right to obtain a discharge of one's debts in bankruptcy. The Constitution, Art. I, § 8, cl. 4, merely authorizes the Congress to "establish . . . uniform Laws on the subject of Bankruptcies throughout the United States." Although the first bankruptcy law in England was enacted in 1542 and a discharge provision first appeared in 1705, primarily as a reward for cooperating debtors, voluntary bankruptcy was not known in this country at the adoption of the Constitution. Indeed, for the entire period prior to the present Act of 1898, the Nation was without a federal bankruptcy law except for three short periods aggregating about 15 1/2 years.

G. If the $50 filing fees are paid in installments over six months as General Order No. 35 (4) permits on a proper showing, the required average weekly payment is $1.92. If the payment period is extended for the additional three months as the Order permits, the average weekly payment is lowered to $1.28. This is a sum less than the payments Kras makes on his couch of negligible value in storage, and less than the price of a movie and little more than the

cost of a pack or two of cigarettes. If, as Kras alleges in his affidavit, a discharge in bankruptcy will afford him that new start he so desires, and the Metropolitan then no longer will charge him with fraud and give him bad references, and if he really needs and desires that discharge, this much available revenue should be within his able-bodied reach when the adjudication in bankruptcy has stayed collection and has brought to a halt whatever harassment, if any, he may have sustained from creditors.

VI

We decline to extend the principle of *Boddie* to the no-asset bankruptcy proceeding. That relief, if it is to be forthcoming, should originate with Congress.

Reversed.

Justice STEWART, with whom Justice DOUGLAS, Justice BRENNAN, and Justice MARSHALL join, dissenting.

The debtor, like the married plaintiffs in *Boddie*, originally entered into his contract freely and voluntarily. But it is the Government nevertheless that continues to enforce that obligation, and under our legal system that debt is effective only because the judicial machinery is there to collect it. The bankrupt is bankrupt precisely for the reason that the State stands ready to exact all of his debts through garnishment, attachment, and the panoply of other creditor remedies. The appellee can be pursued and harassed by his creditors since they hold his legally enforceable debts.

And in the unique situation of the indigent bankrupt, the Government provides the only effective means of his ever being free of these Government-imposed obligations. As in *Boddie*, there are no recognized, effective alternatives. While the creditors of a bankrupt with assets might well desire to reach a compromise settlement, that possibility is foreclosed to the truly indigent bankrupt. With no funds and not even a sufficient prospect of income to be able to promise the payment of a $50 fee in weekly installments of $1.28, the assetless bankrupt has absolutely nothing to offer his creditors. And his creditors have nothing to gain by allowing him to escape or reduce his debts; their only hope is that eventually he might make enough income for them to attach. Unless the Government provides him access to the bankruptcy court, Kras will remain in the totally hopeless situation he now finds himself. The Government has thus truly pre-empted the only means for the indigent bankrupt to get out from under a lifetime burden of debt.

In my view, this case, like *Boddie*, does not require us to decide "that access for all individuals to the courts is a right that is, in all circumstances, guaranteed by the Due Process Clause . . . so that its exercise may not be placed beyond the reach of any individual . . . ." 401 U.S., at 382-83. It is sufficient to hold, as *Boddie* did, that 'a State may not, consistent with the obligations imposed on it by the Due Process Clause . . ., pre-empt the right to dissolve this

legal relationship without affording all citizens access to the means it has prescribed for doing so.' *Id.*, at 383.

The Bankruptcy Act relieves the honest debtor from the weight of oppressive indebtedness, and (permits) him to start afresh free from the obligations and responsibilities consequent upon business misfortunes. It holds out a promise to the debtor of "a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt." *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934). Yet the Court today denies that promise to those who need it most, to those who every day must live face-to-face with abject poverty—who cannot spare even $1.28 a week.

The Court today holds that Congress may say that some of the poor are too poor even to go bankrupt. I cannot agree.

Justice MARSHALL, dissenting.

A. The majority notes that the minimum amount that appellee Kras must pay each week if he is permitted to pay the filing fees in installments is only $1.28. It says that "this much available revenue should be within his able-bodied reach."

I cannot agree with the majority that it is so easy for the desperately poor to save $1.92 each week over the course of six months. The 1970 Census found that over 800,000 families in the Nation had annual incomes of less than $1,000 or $19.23 a week. I see no reason to require that families in such straits sacrifice over 5% of their annual income as a prerequisite to getting a discharge in bankruptcy.

It may be easy for some people to think that weekly savings of less than $2 are no burden. But no one who has had close contact with poor people can fail to understand how close to the margin of survival many of them are. A sudden illness, for example, may destroy whatever savings they may have accumulated, and by eliminating a sense of security may destroy the incentive to save in the future. A pack or two of cigarettes may be, for them, not a routine purchase but a luxury indulged in only rarely. The desperately poor almost never go to see a movie, which the majority seems to believe is an almost weekly activity. They have more important things to do with what little money they have—like attempting to provide some comforts for a gravely ill child, as Kras must do.

It is perfectly proper for judges to disagree about what the Constitution requires. But it is disgraceful for an interpretation of the Constitution to be premised upon unfounded assumptions about how people live.

C. The majority says that "(t)he denial of access to the judicial forum in *Boddie* touched directly . . . on the marital relationship." It sees "no fundamental interest that is gained or lost depending on the availability of a discharge in bankruptcy." If the case is to turn on distinctions between the role of courts in divorce cases and their role in bankruptcy cases, I agree with. Justice Stewart that this case and *Boddie* cannot be distinguished; the role of the Government in standing ready to enforce an otherwise continuing obligation is the same.

However, I would go further than Mr. Justice Stewart. I view the case as involving the right of access to the courts, the opportunity to be heard when one claims a legal right, and not just the right to a discharge in bankruptcy. When a person raises a claim of right or entitlement under the laws, the only forum in our legal system empowered to determine that claim is a court. Kras, for example, claims that he has a right under the Bankruptcy Act to be free of any duty to pay his creditors. There is no way to determine whether he has such a right except by adjudicating his claim. Failure to do so denies him access to the courts.

Congress has since provided by statute the relief the Supreme Court did not find in the Constitution. First, a person may pay the bankruptcy filing fee through no more than four installment payments over 120 days. *See* 28 U.S.C. § 1930(a); FED. R. BANKR. PROC. 1006(b). For a person who income is within 150 percent of the official federal poverty line and in a chapter 7 only, the court may waive the filing fee. 28 U.S.C. § 1930(f). The poverty line varies by household size. In 2021, 150 percent of the poverty line for a household of two would be just under $26,000. The court has complete discretion to waive the filing fee, and there is substantial variation around the country in the willingness of the courts to grant a fee waiver. In a case where the fee is waived, the chapter 7 trustee does not get paid.