Consumer Bankruptcy: Is BAPCPA Working?

Hon. Gloria M. Burns – Moderator
U.S. Bankruptcy Judge (D. N.J.); Camden

Isabel C. Balboa
Chapter 13 Trustee; Cherry Hill, N.J.

Alane A. Becket
Becket & Lee, LLP; Malvern, Pa.

Erin Brignola
Cooper Levinson; Bear, Del.

Consumer Bankruptcy:
Is BAPCPA Working?

American Bankruptcy Institute
3rd Annual Mid-Atlantic Bankruptcy Workshop
August 9-11
Hyatt Regency Chesapeake Bay
Cambridge, Maryland

Presented by:

The Honorable Gloria M. Burns, D.N.J., Moderator
Isabel C. Balboa, Chapter 13 Trustee, Camden NJ
Erin Brignola, Bear, DE
Alane A. Becket, Malvern, PA

Erin Brignola

ABI Mid-Atlantic Bankruptcy Workshop

DOMESTIC SUPPORT OBLIGATIONS

1. Definition: Title 11 USC Section 101(14A)
2. Automatic Stay Changes: Title 11 USC Section 362 (b)(2)
3. Property of the Estate: Title 11 USC Section 541
4. Priorities: Title 11 USC Section 507 (a)(1)
5. Dischargeability: Title 11 USC Section 727; 1328
   Title 11 USC Section 523(a)(5) and (a)(15)
6. Exemption Changes: Title 11 USC Section 522(c)(1)
7. Preference Changes: Title 11 USC Section 547(c)(7)
8. Trustee Duties: Title 11 USC Section 704
9. Forms
10. Cases

I. Definition of Domestic Support Obligation
11 U.S.C. § 101(14A) (2007).

(14A) The term "domestic support obligation" means a debt that accrues before, on, or after the date of the order for relief in a case under this title, including interest that accrues on that debt as provided under applicable nonbankruptcy law notwithstanding any other provision of this title, that is--

(A) owed to or recoverable by--

(i) a spouse, former spouse, or child of the debtor or such child's parent, legal guardian, or responsible relative; or

(ii) a governmental unit;

(B) in the nature of alimony, maintenance, or support (including assistance provided by a governmental unit) of such spouse, former spouse, or child of the debtor or such child's parent, without regard to whether such debt is expressly so designated;

(C) established or subject to establishment before, on, or after the date of the order for relief in a case under this title, by reason of applicable provisions of--

(i) a separation agreement, divorce decree, or property settlement agreement;

(ii) an order of a court of record; or

(iii) a determination made in accordance with applicable nonbankruptcy law by a governmental unit; and

(D) not assigned to a nongovernmental entity, unless that obligation is assigned voluntarily by the spouse, former spouse, child of the debtor, or such child's parent, legal guardian, or responsible relative for the purpose of collecting the debt.

II. Automatic Stay

11 U.S.C. § 362(b)(2) (2007).

(b) The filing of a petition under section 301, 302, or 303 of this title, or of an application under section 5(a)(3) of the Securities Investor Protection Act of 1970, does not operate as a stay—

…

(2) under subsection (a)--

(A) of the commencement or continuation of a civil action or proceeding--

(i) for the establishment of paternity;

(ii) for the establishment or modification of an order for domestic support obligations;

(iii) concerning child custody or visitation;

(iv) for the dissolution of a marriage, except to the extent that such proceeding seeks to determine the division of property that is property of the estate; or

(v) regarding domestic violence;

(B) of the collection of a domestic support obligation from property that is not property of the estate;

(C) with respect to the withholding of income that is property of the estate or property of the debtor for payment of a domestic support obligation under a judicial or administrative order or a statute;

(D) of the withholding, suspension, or restriction of a driver's license, a professional or occupational license, or a recreational license, under State law, as specified in section 466(a)(16) of the Social Security Act;

(E) of the reporting of overdue support owed by a parent to any consumer reporting agency as specified in section 466(a)(7) of the Social Security Act;

(F) of the interception of a tax refund, as specified in sections 464 and 466(a)(3) of the Social Security Act or under an analogous State law; or

(G) of the enforcement of a medical obligation, as specified under title IV of the Social Security Act;

III. Property of the Estate
11 U.S.C. § 541(a) (2007).

(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

(2) All interests of the debtor and the debtor's spouse in community property as of the commencement of the case that is--

(A) under the sole, equal, or joint management and control of the debtor; or

(B) liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable.

(3) Any interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 of this title.

(4) Any interest in property preserved for the benefit of or ordered transferred to the estate under section 510(c) or 551 of this title.

(5) Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date--

(A) by bequest, devise, or inheritance;

(B) as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree; or

(C) as a beneficiary of a life insurance policy or of a death benefit plan.

(6) Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.

(7) Any interest in property that the estate acquires after the commencement of the case.

IV. Priorities
11 U.S.C. § 507(a)(1).

(a) The following expenses and claims have priority in the following order:

(1) First:

(A) Allowed unsecured claims for domestic support obligations that, as of the date of the filing of the petition in a case under this title, are owed to or recoverable by a spouse, former spouse, or child of the debtor, or such child's parent, legal guardian, or responsible relative, without regard to whether the claim is filed by such person or is filed by a governmental unit on behalf of such person, on the condition that funds received under this paragraph by a governmental unit under this title after the date of the filing of the petition shall be applied and distributed in accordance with applicable nonbankruptcy law.

(B) Subject to claims under subparagraph (A), allowed unsecured claims for domestic support obligations that, as of the date of the filing of the petition, are assigned

by a spouse, former spouse, child of the debtor, or such child's parent, legal guardian, or responsible relative to a governmental unit (unless such obligation is assigned voluntarily by the spouse, former spouse, child, parent, legal guardian, or responsible relative of the child for the purpose of collecting the debt) or are owed directly to or recoverable by a governmental unit under applicable nonbankruptcy law, on the condition that funds received under this paragraph by a governmental unit under this title after the date of the filing of the petition be applied and distributed in accordance with applicable nonbankruptcy law.

(C) If a trustee is appointed or elected under section 701, 702, 703, 1104, 1202, or 1302, the administrative expenses of the trustee allowed under paragraphs (1)(A), (2), and (6) of section 503(b) shall be paid before payment of claims under subparagraphs (A) and (B), to the extent that the trustee administers assets that are otherwise available for the payment of such claims.

V. Discharge and Dischargeability

11 U.S.C. § 1328(a) (2007).

(a) Subject to subsection (d), as soon as practicable after completion by the debtor of all payments under the plan, and in the case of a debtor who is required by a judicial or administrative order, or by statute, to pay a domestic support obligation, after such debtor certifies that all amounts payable under such order or such statute that are due on or before the date of the certification (including amounts due before the petition was filed, but only to the extent provided for by the plan) have been paid, unless the court approves a written waiver of discharge executed by the debtor after the order for relief under this chapter, the court shall grant the debtor a discharge of all debts provided for by the plan or disallowed under section 502 of this title, except any debt--

(1) provided for under section 1322(b)(5);

(2) of the kind specified in section 507(a)(8)(C) or in paragraph (1)(B), (1)(C), (2), (3), (4), (5), (8), or (9) of section 523(a);

(3) for restitution, or a criminal fine, included in a sentence on the debtor's conviction of a crime; or

(4) for restitution, or damages, awarded in a civil action against the debtor as a result of willful or malicious injury by the debtor that caused personal injury to an individual or the death of an individual.

11 U.S.C. §§ 523(a)(5), (15) (2007).

(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt—

…

(5) for a domestic support obligation;

…

(15) to a spouse, former spouse, or child of the debtor and not of the kind described in paragraph (5) that is incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court of record, or a determination made in accordance with State or territorial law by a governmental unit;

VI. Exemptions

(c) Unless the case is dismissed, property exempted under this section is not liable during or after the case for any debt of the debtor that arose, or that is determined under section 502 of this title as if such debt had arisen, before the commencement of the case, except--

(1) a debt of a kind specified in paragraph (1) or (5) of section 523(a) (in which case, notwithstanding any provision of applicable nonbankruptcy law to the contrary, such property shall be liable for a debt of a kind specified in section 523(a)(5));

11 U.S.C. § 522(c)(1) (2007).

VII. Preferences

(c) The trustee may not avoid under this section a transfer—

…

(7) to the extent such transfer was a bona fide payment of a debt for a domestic support obligation;

11 U.S.C. § 547(c)(7) (2007).

VIII. Trustee Duties

(a) The trustee shall—

…

(10) if with respect to the debtor there is a claim for a domestic support obligation, provide the applicable notice specified in subsection (c);

…

(c) (1) In a case described in subsection (a)(10) to which subsection (a)(10) applies, the trustee shall--

(A) (i) provide written notice to the holder of the claim described in subsection (a)(10) of such claim and of the right of such holder to use the services of the State child support enforcement agency established under sections 464 and 466 of the Social Security Act for the State in which such holder resides, for assistance in collecting child support during and after the case under this title;

(ii) include in the notice provided under clause (iii) the address and telephone number of such State child support enforcement agency; and

(iii) include in the notice provided under clause (i) an explanation of the rights of such holder to payment of such claim under this chapter;

(B) (i) provide written notice to such State child support enforcement agency of such claim; and

(ii) include in the notice provided under clause (i) the name, address, and telephone number of such holder; and

(C) at such time as the debtor is granted a discharge under section 727, provide written notice to such holder and to such State child support enforcement agency of--

(i) the granting of the discharge;

(ii) the last recent known address of the debtor;

(iii) the last recent known name and address of the debtor's employer; and

(iv) the name of each creditor that holds a claim that--

(I) is not discharged under paragraph (2), (4), or (14A) of section 523(a); or

(II) was reaffirmed by the debtor under section 524(c).

(2) (A) The holder of a claim described in subsection (a)(10) or the State child support enforcement agency of the State in which such holder resides may request from a creditor described in paragraph (1)(C)(iv) the last known address of the debtor.

(B) Notwithstanding any other provision of law, a creditor that makes a disclosure of a last known address of a debtor in connection with a request made under subparagraph (A) shall not be liable by reason of making such disclosure.

11 U.S.C. §§ 704(a)(10), (c) (2007).

"HIT THE ROAD JACK", IS IT EASIER TO EVICT A RESIDENTIAL TENANT AFTER BAPCPA?

Prepared by: Isabel C. Balboa, Chapter 13 Standing Trustee

INTRODUCTION

Almost two years after the implementation of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) it would appear that some of its provisions are meeting their objectives better than others. In the case of residential tenancy issues, the number of new disclosure requirements coupled with submissions required to overcome the exceptions to the automatic stay have had their intended effect. In reviewing this particular area of BAPCPA the number of reported cases is scant, reflecting the limited issues subject to challenge.

With regard to the treatment accorded residential tenancy issues where a judgment for possession has **not** been entered pre-petition, the state of the law remains unchanged. With regard to cases where the judgment for possession in debtor's residence has been entered pre-petition, the amendments and modifications brought about by BAPCPA have had a marked impact on the number of cases filed with the principal goal of retaining an interest in a residential lease. BAPCPA also amended a number of provisions pertaining to the assumption and rejection of nonresidential leases. However, these are not addressed here.

RESIDENTIAL TENANCY - INTERPLAY BETWEEN BAPCPA AND STATE LAW

It is generally accepted that the automatic stay applies to a debtor's possesory interest in a tenancy. Whether a debtor has an interest in real property is determined by state law. Courts have examined the outer bounds of such interest and have held that mere physical possession without more is insufficient to trigger the automatic stay. See, Culver v. Boozer, 285 B.R. 163, 167 (D. Md. 2002) Likewise, ". . . mere possesory interest (for instance, a 'squatter' or tenant at sufferance) in an expired lease at the time of filing has been held insufficient to sustain the protections of the automatic stay." In re Turner, 326 B.R. 563, 573 (Bankr. W. D. Pa. 2005). Under many states' laws the tenant whose lease has expired retains no property interest in the tenancy that could ever become property of the estate. It follows that if the tenancy is not property of the estate the automatic stay does not apply. However, it seems clear that in all jurisdictions a Debtor/Lessee's belongings are "property of the estate". See Alan M. Ahart, "The Inefficiency of the New Eviction Exceptions to the Automatic Stay", 80 Am. Bankr. L.J. 125, 140 (2006). See also, United States v. Whiting Pools, Inc., 103 S. Ct. 2309, 2313 (1983); In re: Atlantic Business Community Corporation, 901 F. 2d. 325, 328 (3d. Cir. 1990).

RESIDENTIAL LEASES – THE STATE OF THE LAW - NO JUDGMENT IN PLACE

The automatic stay will protect debtors from a lessor's quest for possession, eviction or unlawful detainer once a case has been filed if no judgment for possession has been entered. Moreover, attempts to collect rent, notice a default or non-renewal of a

lease could be construed as violations of the stay. See, In re Lansaw, 358 B. R. 666 (Bankr. W. D. Pa. 2006) (as to a non-residential lease). Relief from the stay is required to evict a debtor based on a post-petition default. In light of the existing provisions of the law, debtors may still propose to cure residential pre-petition rent arrears and assume residential leases in a Chapter 13 plan.

RESIDENTIAL LEASES – THE NEW EXCEPTIONS TO THE STAY

Substantive changes arose in the area of residential tenancy issues with the enactment of BAPCPA. Provisions in 11 U.S.C. § 362(b)(22) and 11 U.S.C. § 362(b)(23) have created two notable exceptions to the automatic stay. Other provisions under 11 U.S.C. § 362 (l)(5)(A) require the debtor disclose the judgment of possession in the petition together with the landlord's name and address (referred to as "lessor" in §362(d)(5)(A) and as "landlord" in the Official Voluntary Petition form). The debtor must also file a certification with the petition, in effect setting forth why the exception to the stay should not apply.

The exception set out in § 362(b)(22) applies only where the lessor has obtained a judgment for possession pre-petition in a property in which debtor resides under a lease or rental agreement. The legislative history indicates the exception extends to manufactured housing communities where the debtor pays rent for the lot. This exception to the stay takes effect 30 days after the commencement of a Chapter 13 case, provided debtor meets the conditions set out in 11 U.S.C. § 362 (l). To salvage the tenancy for at least 30 days: 1. The debtor must file a certification with the petition

asserting non-bankruptcy law permits a cure of the entire monetary default that gave rise to the judgment; and 2. The debtor or his dependent deposits (pre-pays) one month's rent with the clerk of the court. BAPCPA does not address lessor's right to object to debtor's initial certification and presumably a lessor is not precluded from doing so (i.e. to challenge the truthfulness asserted in debtor's certification). Debtor may extend the stay beyond 30 days under § 362 (l)(2) by filing an additional certification attesting that the pre-petition default that gave rise to the judgment has been cured in its entirety. If the lessor objects to this second certification a hearing is set down within ten days to consider the merits. If the court rules in favor of the lessor, pursuant to § 362(b)(22) the exception to the automatic stay applies.

RECENT REPORTED OPINIONS

Few cases addressing residential tenancies have been published since the enactment of BAPCPA. The most colorful being, In re Baird out of the Eastern District of Tennessee. This case with some egregious facts and unsavory characters serves as a good analysis of the applicability of § 362(b)(22). In this case, debtors filed for Chapter 7 protection after the lessor obtained a judgment for possession. The debtors failed to comply with the provisions of § 362(l). As a consequence, the court found that § 362(b)(22) excepted the *judgment* from the automatic stay. In this case, however, the debtors sought the Bankruptcy court's assistance in retrieving their personal property from the residential property. The court held the lessor had an affirmative duty to turn over the property pursuant to 11 U.S.C. § 542(a) . The court also found that the lessor

had willfully violated the automatic stay in denying debtors access to their personal property and awarded damages to debtor. In re Baird, 2006 WL 3922527 (Bankr. E.D. Tenn. 2006).

ARE THERE EXCEPTIONS TO THE §362(b)(22) EXCEPTION TO THE STAY

Judge Alan M. Ahart, a United States Bankruptcy Judge in the Central District of California, contends that if "…a lessor has a pre-petition judgment against the debtor for possession [he] would be barred from taking any further acts to obtain possession of the property (or from disposing of the debtor's personal belongings) by both § 362(a)(1) and § 362(a)(2)." See Alan M. Ahart, "The Inefficacy of the New Eviction Exceptions to the Automatic Stay", 80 Am. Bankr. L. J. 125, 142 (2006). Since the enactment of BAPCPA Bankruptcy courts have held that the § 362(b)(22) exception may not apply in the case of a public housing tenant as the tenant is entitled to remain in the premises under 11 U.S.C. § 525 (a) even if debtor discharges rather than cures the pre-petition rent default. In re Kelly, 356 B.R. 899 (Bankr. S. D. Fl. 2006). Additionally, a bankruptcy court in the District of Columbia held that § 362(b)(22) did not apply where the foreclosure purchaser sought the eviction of a serial filer. There the purchaser at foreclosure failed to assert that the debtor was a lessee or had a lease or rental agreement consequently § 362(b)(22) did not apply. In re McCray, 342 B.R.668 (Bankr. D.C. 2006). The court vacated the stay on other grounds.

As a practical matter the 11 U.S.C. §362(b)(22) exception to the stay has plugged

the dike in Chapter 13 cases seeking to salvage a tenancy where the lessor obtained a judgment for possession pre-petition. Most debtors who would have the financial ability to cure pre-petition rent arrears within 30 days of filing would not be motivated to file for bankruptcy for the principal purpose of salvaging the tenancy.

BAPCPA does not direct that a lease or contract is rejected or ceases to be property of the estate if a judgment for possession has been entered pre-petition. Judge Lundin in his treatise on Chapter 13 practice presumes that a Bankruptcy court order allowing the assumption of a residential lease and specifying how a debtor will cure rental default would be a complete defense to the lessor's action for possession. The provisions of § 362(b)(22) will accelerate the assumption process but do not denigrate a Chapter 13 debtor's rights under § 365 and § 1322(b)(7). See Lundin, Keith , Chapter 13 Practice, 3d. Ed. Vol. 5 § 382.1 (2006).

The second exception to the stay impacting residential tenancies is found in 11 U.S.C. § 362(b)(23). This section provides that the automatic stay under § 362(a)(3) (which applies exclusively to property of the estate) subject to the provisions of § 362(m) will not apply to the eviction or similar proceeding involving residential property in which the debtor resides, under the circumstances described below. The exception acts to terminate the automatic stay upon the filing of a certification by lessor, that during the 30 days preceding the filing of the certification, the debtor endangered the property or used or allowed to be used a controlled substance on the property. § 362(m)(1) provides for the application of the exception within 15 days of the filing of the certification. Unlike

the provisions under § 362(b)(22) , this section does not prevent the automatic stay from taking effect upon filing. Additionally, § 362(a)(1) would seem to enjoin a lessor from continuing any judicial action that was filed or served pre-petition against the debtor.

The debtor may file and serve an objection to lessor's certification. If the debtor objects, the court must hold a hearing within ten days to determine the merits of the objection. The objection keeps the automatic stay in place until the court enters its ruling. At the hearing the debtor may argue that the lessor's certification is inaccurate or demonstrate that the situation set forth in the certification has been remedied. §362(m)(2)(C) does not specify a time frame for the cure of the situation that gave rise to the certification. Thus, it is possible for the debtor to remedy the improper activity at any time before the hearing. If the court rules against the debtor or the debtor fails to object in a timely manner, the lessor may proceed with eviction. Since the exception is limited to § 362(a)(3), the lessor may not proceed with enforcement against the debtor for pre-petition claims pertaining to such things as damages to the property, without first moving for stay relief under § 362(a)(1) and (a)(6).

CONCLUSION

Case law remains to be developed with respect to residential tenancy issues which will arise as a result of BAPCPA. At present the changes which have been enacted coupled with the rulings that have come down suggest that the new residential tenancy provisions have been of greatest benefit to lessors. Until further decisions are published, it would be prudent for lessors to proceed with caution as it pertains to the limits of the

automatic stay and for debtor/tenants as it pertains to the cumbersome mandates required for compliance and ensuring protections.

June 1, 2007

Emerging Issues In Applying The Provisions Of 707(b)(2) In Chapters 7 And 13

ABI Mid-Atlantic Meeting
August 9-11, 2007
Cambridge, MD

Alane A. Becket
Becket & Lee LLP
Malvern, PA
610-644-7800
abecket@becket-lee.com

1. Means Test Statistics:

Information from the United States Trustee as reported at the ABI Annual Spring Meeting and in the June 2007 ABI Journal:

Of chapter 7 debtors, 7.9% are above median.

9.5% of above median debtors had "presumed abuse."

Of the 10% of filers who Chapter 7 filers who are above median, UST motions filed in about 20% of cases where there was presumed abuse. The number of motions filed are approximately twice the pre-BAPCPA rate.

2. Calculation of Household Size:

Affects the "median income"
Affects deductions: National and Local standards are based on household size

UST guidelines:

Household size is debtor, debtor's spouse and any dependents debtor could claim under IRS dependency tests. The UST departs from IRS standards in cases justifying reasonable exceptions, e.g. a longstanding economic unit of unmarried persons and their children.

In re Pampas, 2007 Bankr. Lexis 1741 (Bankr. M.D. La. 2007):

Debtor can not claim an unborn child as a household member. Based on *In re Singletary*, 354 BR 455 (Bankr. S.D. Tx. 2006). Presentation of facts not present in the means test requires use of the "special circumstances" provision of 707(b)(2)(B).

In re Loper, 2007 Bankr. LEXIS 1386, at *17 n. 7 (Bankr. D. Colo. 2007):

> For purposes of this discussion [regarding above or below the state's median family income for a family of the same size], the Court must conclude that the Loper's family size is two, instead of three. Their son is beyond the age of majority, and they do not contribute to his living or educational expenses.

In re Napier, 2006 Bankr. LEXIS 2248, at **2, 4 (Bankr. D.S.C. 2006) :

> Debtors allow the daughter of a close family friend and her fiancé to live in their residence without rent or other payment…. Debtors seek to include these individuals as members of their household for purposes of determining their allowed deductions under the National and Local Standard deductions allowed by the means test…. Debtors acknowledge that the boarders are not their dependents…. Furthermore, in this Court's view, additional expenses incurred in boarding non-dependents are not "reasonable" or "necessary," as required by § 1325(b)(3). While the Debtors' acts are admirable, Debtors should not be allowed to voluntarily put the needs of these non-dependents above their obligation in this bankruptcy to their unsecured creditors, as this would appear to contradict § 1325(b)(1)(B) and indicate a lack of good faith in proposing their plan. To the extent that Official Form B22C indicates that Debtors may include the boarders in the means test calculation, it must yield to the plain language of § 707(b)(2), which only allows Debtors to include dependents.

This Court specifically terms these boarders as "non-dependents". Also, it applies the disposable income test as well as a good faith scrutiny.

In re Jewell, 2007 Bankr. LEXIS 811, at **10-12 (Bankr. D. Ohio 2007):

> The key to resolution of this matter lies in the interpretation of the term "household." The UST points to the Internal Revenue Manual ("IRM") which states that the number of household members allowed for purposes of determining the applicable National Standards should generally be the same as those allowed as dependents on the taxpayer's tax returns. … The Debtors counter that, since median family income is defined by Bankruptcy Code § 101 (39A) as "the median family income both calculated and reported by the Bureau of the Census," n6 the Court should look to the Bureau of the Census definition of household: "all the people who occupy a housing unit." Alternatively, Debtors suggest that the Court should use the ordinary meaning of the term "household" as defined by Black's Law Dictionary: "A family living together . . . . Those who dwell under the same roof and compose a family. . . ." Both definitions are simply a "heads on beds" approach without regard to financial contribution of the household member, relationship to the debtor, or dependency.
>
> The Bankruptcy Code does not define the terms "household," "family," or "dependents." Given the purpose of Official Form 22A, that being a "means test" or determination of disposable income, the Court is unwilling to accept the broad definitions of that term suggested by the Debtors of "heads on beds." Such a definition is inconsistent with the methodology and purpose of Official Form 22A for calculating a debtors' disposable income in that it does not include the element of a debtor's support of the person who puts the head on the bed. If a person lives in the home with the debtor but the debtor does not support that person, then inclusion of that person for purposes of calculating the applicable median family income and disposable income would give rise to a faulty calculation and would result in an inaccurate figure for both. Additionally, the purpose for which the Bureau of the Census determines a household is radically different (i.e., determining the number and demographics of those residing in particular areas of the United States) and bears no relationship to the purpose of the Official Form B22A.
>
> The Court is also unwilling to accept the UST's narrow definition inasmuch as it fails to recognize those instances when a debtor may be actually providing support for a household member, but the circumstances do not fall neatly within the parameters envisioned by the UST (i.e., a group of people living together for a year and pooling income). While the IRM indeed states that, for IRS collection purposes, the number of household members allowed should generally be the same as those claimed as dependents on the taxpayer's tax returns, the IRS also recognizes that there may be reasonable exceptions. IRM at § 5.15.1.7.

(footnotes omitted)

The Court held that the debtors' adult daughter and her 3 children were household members for purposes of calculating median income. Debtors supported them daughter, providing a home, food and other necessities for the family, as well as providing funds to their daughter for gas and medical expenses. No evidence was provided that the living arrangements were only temporary, or that the group did not function as an economic unit. On the other hand, the evidence showed that Chris was, in fact, merely a head on a bed. The Debtors did not show that they supported their son in the form of meals, clothing, and the like, or that he was claimed as a dependent on their recent tax returns. Although he had never left home, he was employed full time and paid most of his own expenses. (The court also ruled on whether their children's income was required to be included in the Debtors' calculation of CMI.)

3. Application of the IRS allowances

Information from the United States Trustee as reported at the ABI Annual Spring Meeting and in the June 2007 ABI Journal:

> For above median debtors, use of the IRS standards were favorable. For the lower income above median debtors, the IRS standards provided more than $400 in expenses above what was claimed on Schedule J. This differential decreased as the debtors' incomes increased.

In re Pampas, 2007 Bankr. Lexis 1741, at *12-*13 (M.D. La.) notes the split of authority:

The *Slusher* Line of Cases

> Several reported opinions considering this issue have concluded that a debtor may claim a transportation ownership cost only for vehicles he finances or leases. *See Slusher,* 359 B.R. 290, 2007 WL 118009; *In re Hardacre,* 338 B.R. 718 (Bankr. N.D. Tex. 2006); *In re McGuire,* 342 B.R. 608 (Bankr. W.D. Mo. 2006) (chapter 13 debtor not entitled to deduct cost for vehicle owned free and clear of any liens); *In re Barraza,* 346 B.R. 724, 727-29 (Bankr. N.D. Tex. 2006) (chapter 7 debtor not entitled to take standard ownership cost for 18-year old pickup truck that was not financed or leased). These courts reason that because Congress incorporated the IRS standards into the Bankruptcy Code, bankruptcy courts must apply the standards as the IRS would have. *See e.g., Slusher,* 359 B.R. 290, 2007 WL 118009 at *14 ("Congress' decision to use the IRS standards within the Bankruptcy Code strongly suggests that courts should look to how the IRS determined those standards; that is, as to how the IRS would have applied them in similar circumstances.")

The *Fowler* Line of Cases

> Other courts have concluded that a debtor may claim the transportation ownership cost even if the debtor's vehicle is unencumbered. *See, e.g., In re Fowler,* 349 B.R. 414 (Bankr. D. Del. 2006) and *In re Wilson,* 356 B.R. 114 (Bankr. D. Del. 2006). These courts emphasize the plain language of 11 U.S.C. § 707(b)(2)(A)(ii) in concluding that Congress used the words *actual* in connection with Other Necessary Expenses and *applicable* with respect to the National and Local Standards because it intended two different things. *Fowler,* 349 B.R. at 418, citing *Duncan v. Walker,* 533 U.S. 167, 173, 121 S. Ct. 2120, 150 L. Ed. 2d 251 (2001) ("where Congress includes particular language in one section of an act but omits it in another section of the same legislation, Congress generally is presumed to have acted intentionally and purposely in disparate inclusion or exclusion.").
> (footnotes omitted)

"Applicable vs. Actual":

In re Grunert, 353 B.R. 591, 592-593 (Bankr. E.D. Wis. 2006):

> The issue boils down to the meaning of the phrase "applicable . . . amounts specified under the Local Standards." One argument is that "applicable" means applicable to a particular debtor who owns a vehicle subject to a lien. On the other side are those who argue that "applicable" means the region where the debtor lives or the number of vehicles owned by the debtor (the standards allow deductions for up to two). …
>
> Congress drew a distinction in the statute between "applicable" expenses on the one hand and "actual" expenses on the other. "Other Necessary Expenses" must be the debtor's "actual" expenses. Expenses under the "Local Standards," in contrast, need only be those "applicable" to the debtor -- because of where he lives and how large his household is. It makes no difference whether he "actually" has them.

***In re Crews*,** 2007 Bankr. LEXIS 729, at *14 (Bankr. D. Ohio 2007):

> The Internal Revenue Manual does indicate that the transportation ownership standards are caps in the context of analyzing a taxpayer's ability to pay. Taxpayers will be allowed the local standard or the amount actually paid, whichever is less. Int. Rev. Manual 5.8.5.5.2. Nevertheless, 11 U.S.C.S. § 707(b)(2)(A) only incorporates, for purposes of determining "disposable income" under 11 U.S.C.S. § 1325(b)(2), the "Local Standards" contained in the Internal Revenue Manual, not all of the detailed collection procedures contained in the Internal Revenue Manual. *Accord In re Farrar-Johnson,* 353 B.R. at 231: Section 707(b)(2)(A)(ii)(I), however, deems the debtor's expenses to be the "amounts specified" in the Local Standards. . . . It nowhere incorporates wholesale all the IRS criteria for collection matters.

3. Does a Debtor really get to expense payments on any secured debt?

See: Attached article: William A. McNeal and Alane A. Becket, Secured Debt Service – A *Carte Blanche* in Chapter 13? NACTT Quarterly, Vol. 19, No. 3 (April/May/June 2007), reprinted with permission from the National Association of Chapter 13 Trustees (www.nactt.com).

4. What constitutes "special circumstances" for rebutting a finding of abuse?

***In re Delbecq*,** 2007 Bankr. LEXIS 1542, at **8, 11-14 (Bankr. S.D. Ind. Apr. 26, 2007):

> [T]he Court finds the term 'special circumstances' to be ambiguous and, therefore, turns to § 707(b)'s legislative history for additional guidance…. [Legislative history] strongly suggests to the Court that the term 'special circumstances' requires a fact-specific, case-by-case inquiry into whether the debtor has a 'meaningful ability' to pay his or her debts in light of an additional expense or adjustment to income not otherwise reflected in the means test calculation…. [T]he legislative history does not indicate that the explicit examples included in § 707(b)(2)(B) were

> intended to define, qualify or otherwise limit the meaning of 'special circumstances'…. Section 707(b)(2)(B) requires the Court to find that there is 'no *reasonable* alternative' to the claimed expense. (Italics added).

In this case involving a student loan, the court, finding ambiguity in the "special circumstances" language, applied, instead, the "no reasonable alternative test" because it could do so, unambiguously, based on the facts of the matter before it. The debtor was successful.

In re Haman, 2007 Bankr. LEXIS 1335, at *13-18 (Bankr. D. Del. Apr. 20, 2007):

> [T]his Court concludes that section 707 (b)(2)(B) does not require a debtor to demonstrate special circumstances of an involuntary nature…. Second … the legislative history of BAPCPA indicates that the examples of special circumstances set forth in subsection (i) were meant to be expansive - not limiting…. In general, 'special circumstances' are 'circumstances beyond a debtor's reasonable control, such as [the examples given in § 707 (b)(2)(B)(i)]'… [T]he plain language of the statute, along with the applicable case law, require [the debtor] to demonstrate that her student loan obligation leaves her with no reasonable alternative….

This court also found no ambiguity in the statutory language about lack of a reasonable alternative as applied to a student loan. It also found the statute's list of examples as unexhaustive. The court cited with approval other examples of not involuntary, acceptable, special circumstances: "Those special circumstances include: (1) mandatory 401(k) loan repayment obligations, see Lenton, 358 B.R. 651, 2006 WL 3850011 at *7; Thompson, 350 B.R. at 777-78; (2) unusually high transportation costs, see In re Batzkiel, 349 B.R. 581, 586 (Bankr. N.D. Iowa 2006); and (3) failure to find suitable employment, despite diligent search, along with the inability to relocate due to a divorce settlement, see Graham, 2007 Bankr. LEXIS 720, 2007 WL 685945 at *4. See also 6 COLLIER ON BANKRUPTCY P 707.05 [2] [d] (Alan N. Resnick et al. eds., 15th ed. rev. 2006) (providing examples of special circumstances, such as 'high commuting costs, the increased price of gas, security costs in dangerous neighborhoods, or the cost of infant formula and diapers' and noting: 'Indeed, any legitimate expense that is out of the ordinary for an average family, or that may have increased since the IRS guidelines were calculated, could be considered.')."

In re Herbert, 2007 Bankr. LEXIS 1726, at *7 (Bankr. D. Neb. May 21, 2007):

> "[T]he Bankruptcy Code specifically delineates two special circumstances: (1) a serious medical condition; or (2) active duty in the Armed Forces. Certainly, those two items are not an exhaustive list, but are examples of what Congress intended to constitute special circumstances. Thus, rebutting the presumption of abuse requires circumstances that are truly special."

For this court, the test is "truly special". It determined that "the post-petition reduction in Debtors' overtime income in this case is not a sufficient 'special circumstance' to rebut the presumption of abuse." *Id*. at **8-9. The same court earlier found that income fluctuation due to its commission basis is not truly special, and does not qualify as a special circumstance. *In re Ferando*, NO. BK06-81855, 2007 Bankr. LEXIS 607, at **5-6 (Bankr. D. Neb. Mar. 1, 2007).

In re Graham, 2007 Bankr. LEXIS 720, at **11-12 (Bankr. S.D. Ohio Mar. 6, 2007).
A court found that a debtor successfully showed special circumstances as those being beyond his control, as the U.S. Trustee urged. However, the court specifically rejected this test for special circumstances, based on the language of the statute, but provided no alternative.

5. Does "passing" the Means Test insulate a debtor from dismissal based on ability to pay?

NO:

See, e.g., Eugene Wedoff, Judicial Discretion to Find Abuse under §707(b)(3), ABI Journal, Vol. XXV, No. 3, p. 1 (April 2006)

> The key to understanding the proper role of the means test in chapter 7 is to recognize that it is simply a mechanism for generating a presumption; it does not result in any final determination. …
>
> The status of the means test as a presumption has one final–and critical–feature. A presumption is merely one method of establishing a fact necessary to obtain relief. Where a presumption does not arise, the party seeking relief may prove the necessary fact directly, using the same kind of evidence that could be used to establish the fact in connection with a rebuttal of the presumption. A party asserting abuse under §707(b)(1) may seek to prove that the debtor's actual disposable income is at or above the abuse threshold, even if the means-test presumption does not arise, using the same type of evidence that would be presented if the debtor sought to show that the means-test presumption was inaccurate. …
>
> There is no provision in §707(b) stating that the means test is the only method through which the debtor's disposable income can be established. To the contrary, §707(b)(3) explicitly states that, in the absence of the means-test presumption, "the court shall consider...whether...the totality of the circumstances...of the debtor's financial situation demonstrates abuse." Given that the means test is directed at measuring debt-paying ability as a presumption, this direction confirms that where the presumption does not arise, the debtor's actual debt-paying ability must be assessed in ruling on a motion under §707(b)(1).
>
> … [T]he means test itself failed to accomplish the goal of its sponsors. And situations like the hypothetical will arise not infrequently, since the means test is inefficient in identifying likely abuse of chapter 7. However, BAPCPA did not exacerbate this flaw by making the absence of a means-test presumption conclusive of debt-paying ability. Section 707(b)(3) requires judges, when an abuse motion is raised, to determine the debtor's actual financial condition, including debt-paying ability. Ultimately, even when the means test does not presume abuse, genuinely wealthy debtors may be denied chapter 7 relief.

Cases agreeing with Judge Wedoff include:

In re Lenton, 358 B.R. 651, 663 (Bankr. E.D. Pa. 2006):

> By its terms, § 707(b)(3) "explicitly mandates that the totality of the circumstances of the Debtor's financial situation be considered in determining whether there is an abuse when the presumption of abuse under paragraph (b)(2) does not arise or is rebutted." Paret, 347 B.R. at 15. The broad language "totality of circumstances" and "financial situation" clearly encompasses a debtor's ability to pay. Pak, 343 B.R. at 243 (finding "instructive . . . the use of the phrase 'totality of the circumstances'"); Wedoff Article at 236 ("'passing' the means test does not preclude a discretionary finding of abuse . . . if a debtor's overall financial circumstances would easily allow the debtor to repay debts . . . the court may find abuse").
>
> …
>
> Had Congress wished to eliminate consideration of a debtor's ability to pay, as Debtor asserts, it would have done so expressly or by explicit reference to § 707(b)(2)(A). See 11 U.S.C. § 1325(b)(3) (expressly incorporating § 707(b)(2)(A) and (B) into disposable income test). "'[W]here Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion.'" Russello v. United States, 464 U.S. 16, 23, 104 S.Ct. 296, 300, 78 L. Ed. 2d 17 (1983) (citation omitted). Congress did not do so here. Instead it instructs the Court in broad language to examine the: "totality of the circumstances of the debtor's financial situation." Logically, this must include Debtor's ability to pay his debts.

In re Fries, 2007 Bankr. LEXIS 1803 at *7 (W.D. Mo. May 18, 2007)

> Although some courts have held that the ability to repay factor must be coupled with other factors in order to find abuse under § 707(b)(3)'s totality of circumstances test, this Court believes that a debtor's ability to pay may, in some circumstances, be dispositive of the Debtors' abuse. Here, a finding of abuse is warranted based on the significant amount of money and percentage of unsecured debt the Debtors would have the ability to pay in a chapter 13 bankruptcy case. (footnotes omitted)

See also:

> *In re Zaporski*, 2007 Bankr. LEXIS 1449, *33-*35 (Bankr. E.D. Mi. 2007); In re Pak, 343 B.R. 239, 241-44 (Bankr. N.D. Cal. 2006); *In re Mestemaker*, 2007 Bankr. LEXIS 78 (Bankr. N.D. Ohio Jan. 10, 2007); *In re Simmons*, 357 B.R. 480, 487-89 (Bankr. N.D. Ohio 2006); *In re Richie*, B.R. , 353 B.R. 569, 2006 Bankr. LEXIS 2886, 2006 WL 3019209 (Bankr. E.D. Wis. Oct. 3, 2006); *In re Paret*, 347 B.R. 12 (Bankr. D. Del. 2006);

YES:

See. e.g. Marianne B. Culhane & Michaela M. White, **Catching Can-Pay Debtors: Is the Means Test the Only Way**?, 13 Am. Bankr. Inst. L. Rev. 665 (2005).

> This paper will respectfully disagree with Judge Wedoff, and argue that Congress intended the means test to be the only test of ability to pay under the revised Code. With the detailed statutory means test in place, "filed in bad faith" and "totality of the circumstances" no longer authorize judges to define ability to pay. Instead, these phrases must be read as limited to serious debtor misconduct. (at 666)
>
> Legislative history shows Congress was clearly dissatisfied with inconsistent, unpredictable outcomes under former section 707(b), where the "inherently vague" substantial abuse standard "led to disparate interpretation . . . by the bankruptcy bench." Use of judicial can-pay tests, in addition to the means test, would prolong the prior decisional disarray and lead to big increases in section 707(b) litigation, imposing extra expense on all parties.
>
> Further, ad hoc judicial tests would contravene the Congressional policy choices reflected in the means test; decisions to promote important interests such as free exercise of religion, secured consumer credit, retirement savings and broader health insurance coverage.
>
> Of course, the "filed in bad faith" and "totality of the circumstances" standards of section 707(b)(3) have roles to play, but they are limited roles. Bad-faith filing covers such debtor offenses as serial filings and pervasive non-cooperation aimed at frustrating creditors, rather than seeking a discharge. Totality of the circumstances has a broader scope, including unjustified debtor attempts to "cheat" on the means test. However, judicial tests of ability to pay are no longer a primary component.
>
> We disagree, however, with Judge Wedoff's second point: that a judge who thinks the means test is not mean enough may "fix it" by substituting his or her own more stringent standards of ability to pay and idiosyncratic views of appropriate debts and expenses. In our view, the language of the revised Code, the interaction among its sections, its legislative history, and the need for uniformity in consumer bankruptcy law all support the view that the means test is now the exclusive ability to pay test. It may not perform as advertised, but it is the only ability to pay test Congress intended to impose.

6. Does the amount of the Debtor's payment reflect a debtor's good (or bad) faith?

William A. McNeal, Does BAPCPA Take Good Faith on Faith?, ABI Journal, Vol. XXV, No. 10, p. 14 (December/January 2007). Selected portions reprinted with permission from the American Bankruptcy Institute (www.abiworld.org):

Some courts maintain the position that BAPCPA retains the 1984 Act's removal of ability to pay or amount of payment from the consideration of a debtor's good faith. They include the *Barr* court,[1] with the *Alexander* court agreeing;[2] the *Johnson* court, at least to a degree;[3] the court in *In re*

[1] 341 B.R. at 184.

Farrar-Johnson, which opined that disposable income is simple arithmetic based on 11 U.S.C. § (b)(2)(A) and (B) and that a debtor's good faith in claiming them cannot be relevant;[4] and the *Rotunda* court, which found that the enactment of BAPCPA limited its discretion to review a plan's reasonableness based on the totality of the circumstances even if it meant confirmation of a zero percent plan.[5]

Other courts found sufficiency of payment to unsecured creditors to continue in its role as a factor in assessing a debtor's good faith. In *Lewis*, the court opined that, in the absence of any amendment to § 1325(a)(3) of the Code by BAPCPA, the Tenth Circuit's *Flygare* factors remained determinative of a plan's good faith.[6] The court found that debtors' "cramdown" treatment of debt secured by a vehicle lacked good faith because it denied money that would otherwise go to their unsecured creditors.[7] The United States Bankruptcy Court for the Northern District of Georgia, in *In re Grady*, opined that a debtor's payment into her plan of her projected disposable income (exemplifying the risk of unintended consequences, the court coined the term "actual" disposable income, perhaps, inadvertently adding semantic confusion to an already confusing topic), as required by 11 U.S.C. § 1325(b)(1)(B), harmonized with the good faith requirement of § 1325(a)(3).[8] *In re Edmunds*, decided by the United States Bankruptcy Court in the District of South Carolina, concluded that the so-called *Deans* factors[9] remain relevant under BAPCPA, and opined that nothing in BAPCPA's legislative history indicated that Congress intended to abandon, as elements of good faith, consideration of a debtor's actual financial situation at the time of his petition or the percentage of his proposed plan's repayment to unsecured creditors.[10] Elsewhere, in a thorough and thoughtful review of the issues and facts before it in *In re LaSota*, the United States Bankruptcy Court for the Western District of New York sustained a chapter 13 trustee's objection to confirmation of a plan that, according to the trustee, understated the amount the debtors had the ability to pay.[11] Pointing out that BAPCPA did not repeal, though it could have done so, the good faith requirement, the court opined, "Contrary to some other authority, this writer finds that BAPCPA does not command that there be no inquiry into such matters."[12] Rather colloquially but, nevertheless, with an undeniably viscerally appealing rationality, the court quoted itself, "'Give up the Harley Davidson and increase your payment to your credit card debts and to your old rent defaults to your previous landlady and then you can have a Plan confirmed that will discharge the rest.'"[13]

---

[2] 344 B.R. at 752.
[3] 346 B.R. at 261-62.
[4] 2006 Bankr. LEXIS 2214, at *20.
[5] 2006 Bankr. LEXIS 2346, at *24.
[6] 347 B.R. at 774*13.
[7] *Id*. at *14.
[8] 343 B.R. 747, 751 (Bankr. N.D. Ga. 2006).
[9] *See Deans v. O'Connell*, 692 F.2d 968, 972 (4th Cir. 1982).
[10] No. 06-01602-JW, 2006 Bankr. LEXIS 2255, at **30-32 (Bankr. D.S.C. Sept. 18, 2006).
[11] No. 05-70085, 2006 Bankr. LEXIS 2345, at **18-19 (Bankr. W.D.N.Y. Sept. 19, 2006).
[12] *Id*. at *15.
[13] *Id*. at *5.

Secured Debt Service – A *Carte Blanche* in Chapter 13?

William A. McNeal, Esq.,
Malvern, PA

Alane A. Becket, Esq.,
Malvern, PA

Contributing Editors:
Gilbert B. Weisman, Esq. and Emily Abbott, Esq.
Becket & Lee, LLP,
Malvern PA

Of the changes to the Bankruptcy Code wrought by BAPCPA of 2005, one of the most important is the complex formula used to determine a Chapter 13 debtor's permissible monthly expenses, *i.e.*, "budget," which is determined, in part, by a debtor's income. For those whose income stands below the median income for their domiciles, BAPCPA retains intact the earlier case law approach, which focused on whether a particular budgetary item was reasonably necessary. Contrastingly, for those whose income exceeds the median for their states, BAPCPA imposes a fairly prescriptive blueprint for reasonably necessary expenses. Specifically, the drafters of the Act, rather than detail the allowable expenses for an "above-median" debtor, imported and imposed by reference, wholesale, the "means test" of 11 U.S.C. § 707(b)(2) as determinative of what expenses are reasonably necessary.

Much has been written about the application of the expense regime found in 11 U.S.C. § 707(b)(2) to an "above-median" Chapter 13 debtor. Although the drafters presumably intended to make the statutory language in the Code clear and precise, language meant to cover all contingencies often contains ambiguities. This has resulted in a variety of opinions interpreting the language of the Code and that of the Internal Revenue Service standards which are incorporated by reference in this statutory section.[1] Thus, in the frequent disputes over what amounts a debtor may expense for the commonplace needs for housing, transportation, and other household requirements, the law is emerging, district by district, across the country.

However, one category of expense, secured debt service, seems to have been left almost unchallenged despite extremely consequential changes in the language of the Code. This may be because Form B22C merely inventories, without challenge, future payments on secured claims (line 47), and because other allowable expenses are specified by the "imported" Internal Revenue Service standards, apparently vitiating the role of judicial discretion. But it seems unlikely that Congress intended that an "above-median" Chapter 13 debtor be required to carefully compile his budget for providing for his and his family's needs for shelter, transportation, and other household expenses, but remain free to service, without constraint, other debts, even those for luxury items, merely because they happen to be collateralized. This article discusses possible alternative approaches to interpreting 11 U.S.C. § 707(b)(2)(A)(ii) and concludes that the statute does not allow a debtor to service secured debt but rather allows the expensing of certain costs to house, transport and otherwise provide for his and his family's needs.

1. Secured Debt Payments Must Be Reasonable And Necessary.

One argument, relying on the straightforward meaning of statutory language, is that the Code requires that every expense proposed by a Chapter 13 debtor must, as a threshold matter, be reasonably necessary.[2] Proponents argue that ignoring this test violates the tenets that unambiguous statutory language is accorded its plain meaning,[3] and that a statute be construed holistically[4] such than one statutory provision, *e.g.*, 11 U.S.C. § 707(b)(2), should be interpreted together with another , *viz.*, 11 U.S.C. § 1325(b). Thus, this position would deny a debtor secured debt expenses not considered reasonable and necessary.

However, it may be argued that this construction in fact overlooks the plain language of the statute that requires only the **amounts** be reasonably necessary, rather than the expense type or category.[5] Thus, an objection based on unreasonableness of the **expense** is assailable by resort to the plain language of the statute. For example, a modest payment for a luxury item may survive objection, even though the item may not be a necessity, because the plain language of the statute supports an objection only to the amount of the expense, rather than the expense itself.

2. Guidance From The IRS.

Another approach forces a debtor's expenses to run the arguably more demanding gauntlet of the "necessary" expense test found in the Internal Revenue Manual 5.15.1, Financial Analysis Handbook.[6] This test preambles the expenses regime utilized by the IRS for its purposes, and is imported, so argue proponents of this position, by 11 U.S.C. § 707(b)(2)(A)(ii) for plan confirmation pursuant to 11 U.S.C. § 1325(b). It requires that an expense, to be allowable, be necessary for a taxpayer's and his or her family's health and welfare, or for the production of income. Thus, payments for secured debts would be allowed only to the extent that the expense is shown to be necessary.

A critic of this approach argues, *inter alia*, that Congress intended for bankruptcy to adopt the Internal

CONTINUED NEXT PAGE

Revenue Service's allowances only, particularly those in the National and Local Standards, and not the analysis found in the Internal Revenue Manual's Financial Analysis Handbook.[7] This position is supported by the fact that an earlier version of BAPCPA contained language that specifically invoked the "Internal Revenue Service financial analysis for expenses".[8] This language did not survive to the 2005 enactment, arguably demonstrating Congress' intent that a debtor be limited by the Service's expense amounts only, and not by other requirements used in taxpayer matters.

3. *Lex Sola* – The Statute Alone Provides The Solution.

A simple, elegant and thus far overlooked construction presents itself from the plain language of the statute itself, which by its precise terms prohibits a debtor from expensing debt service. 11 U.S.C. § 707(b) (2)(A)(ii)(I) states, "Notwithstanding any other provision of this clause, the monthly expenses of the debtor shall not include any payments for debts." Such clear statutory language is determinative, unless ambiguous,[9] contraindicated by legislative intent,[10] or inconsistent with its policy objectives[11]

Of the greatest import is "notwithstanding". This word signals an exception to the allowable expense protocol in the two sentences that precede it. In the interpretation of "Notwithstanding the provisions of section 405(b)" found in section 318 of the then-new Immigration and Nationality Act of 1952, the United States Supreme Court found that the word connoted congressional intent to preserve a specific exception to the relevant savings clause in section 405(b) of the Act.[12] The use of the word showed that "[t[he congressional purpose must have been to have § 318 supersede rights stemming from [pre-Act] petitions [for naturalization, under section 405]."[13] Indeed, "the use of such a 'notwithstanding' clause clearly signals the drafter's intention that the provisions of the 'notwithstanding' section override conflicting provisions of any other section."[14]

Thus, it appears that regardless of, and in supersedure of any other provisions of 11 U.S.C. § 707(b) (2)(A)(ii)(I), a debtor's allowable monthly expenses shall not include any debt payments.

When a debt is not a "debt", or, The importance of a word.

There arises an apparent difficulty of reconciling the "notwithstanding" sentence's disallowance of expenses of debt service with the previous two sentences' specification of allowable expenses, some of which may require payment of debt service, *e.g.*, home mortgage and automobile purchase loans. This is overcome, however, by recognizing that the statutory language refers to the **expense** amounts specified under Internal Revenue Service standards, which are entitled, "Allowable Living Expenses". The word "debt" does not appear in "National Standards" or "Local Standards". Thus, the statute, while denying the payment of debt service, preserves a debtor's right to expense the costs to house, feed, clothe, transport, and otherwise provide for the needs of himself and his family.

Admittedly, the IRS' schedule of "Other Necessary Expenses", also given operation by 11 U.S.C. § 707(b)(2)(A)(ii)(I), includes two categories of debt, *i.e.*, secured and unsecured.[15] According to the Internal Revenue Manual,[16] however, the service of these debts must meet the necessary expenses test, *i.e.*, necessary for the health and welfare of the debtor or his or her family, or necessary for the production of income. Then, they are allowable "other necessary **expenses**", thus avoiding offense to the plain language of the prohibition of payments for **debts**.[17]

The argot of financial accounting clarifies the importance of the distinction between "debt" and "expense". An income statement summarizes revenues (or, for a consumer debtor, income) and expenses. A balance sheet summarizes assets and liabilities (or, for a consumer debtor, debts). The language of the Code, incorporating IRS standards, specifies a debtor's allowable **expenses**, essentially his permissible "budget" of income and expenses. Payment for debts, which are balance sheet liabilities, seems to be prohibited by the plain meaning of the statutory language.

Legislative history and intent, and public policy goals

Legislative history and intent appear to support such a precise reading of the Code's wording. "[T]he debtor's monthly expenses - exclusive of any payments for debts (unless otherwise permitted) - must be the applicable monthly amounts set forth in the Internal Revenue Service Financial Analysis Handbook as Necessary Expenses under the National and Local Standards categories and the debtor's actual monthly expenditures for items categorized as Other Necessary Expenses."[18] Regarding the intent of the legislature, BAPCPA sponsor Sen. Charles Grassley and cosponsor Sen. Jeff Sessions wrote thus: "In calculating repayment ability, PL 109-8 permits a debtor to deduct the allowances provided in the applicable IRS local standards for housing. Importantly, PL 109-8 also provides that the debtor's expenses in this category may not include any payment for secured debts, such as mortgage payments."[19]

Such a construction of the statute accords with the attendant public policy goals of "ensur[ing] that debtors make a good-faith effort to repay as much as they can afford" while affording "those who need it most …… a fresh start."[20] A debtor is denied a *carte blanche* to expense any and all debt service to the detriment of unse-

cured creditors, but also is assured that his plan will not leave him without an expense budget that is reasonably necessary for his and his family's support, and that fulfills his domestic support obligations, addresses his charitable giving desires,[21] and maintains the continuity of his business if he operates one.[22]

What about 11 U.S.C. § 707(b)(2)(A)(iii)?

There remains a reconciliation of the "notwithstanding" sentence with 11 U.S.C. § 707(b)(2)(A)(iii),[23] which provides a formula for calculating secured debt payments. One commentator posits that this statutory provision serves to "set out" the deduction for secured debt.[24] The result is that "debt secured even by such items as luxury vehicles, pleasure boats, and vacation homes would be deductible."[25]

Such a result seems inconsistent with the already discussed plain meaning of 11 U.S.C. § 707(b)(2)(A)(ii)(I), legislative history and intent, and the policy goals of the Code. That writer's remedy for such a viscerally unappealing construction is to look to the totality of the circumstances test for abuse found in 11 U.S.C. § 707(b)(3).[26] Unfortunately, this remedy is unavailable to an objector to a Chapter 13 plan, which needs to conform to 11 U.S.C. § 707(b)(2)(A) and (B) only.[27] Moreover, even in a Chapter 7 filing, this construction incorrectly shifts evidentiary burdens from the debtor, who bears the burden to overcome a presumption of abuse,[28] to the creditor.[29]

Likewise, such a result is, according to one court, bizarre.[30] The *Alexander* court, somewhat counter intuitively, seems prepared to confirm a plan that "has huge secured debt for luxury items that, bizarrely, may be deducted in full as a reasonable and necessary expense".[31] No explanation is provided that reconciles a "bizarre" deduction with reasonableness and necessity. Contrast this approach with that of the court in *In re LaSota*,[32] which found that a calculation of a debtor's projected disposable income that accommodated luxury boat payments would yield an absurd result.[33] (Despite the striking synonymy, it is important to note that the *LaSota* court explained that "absurd" is not a pejorative but rather an "elusive legal standard that permits departure" from statutory plain language,[34] though, as shown above, none is necessary.)

Rather than contradicting the language of the "notwithstanding" sentence, 11 U.S.C. § 707(b)(2) (A)(iii) serves only to prescribe the method of computing expenses for secured debt service, assuming such secured debt is properly classified as an allowable expense under the National or Local Standards or as an Other Necessary Expense.[35]

Conclusion

The U.S. Bankruptcy Court for the Western District of New York sustained a Chapter 13 trustee's objection to confirmation of a plan that, according to the trustee, understated the debtors' projected disposable income.36

The court opined that BAPCPA left unchanged a finding that a debtor could not reduce the payout to unsecured creditors in order to support the debt on a nice $10,000 sailboat that the debtor enjoys racing in a fleet on summer evenings ?…."[37] " To comply with the statutory requirement to devote all "projected disposable income", a plan "often requires surrender of those luxuries to repossession or foreclosure, if confirmation of a less-than-100% Plan is to be won."[38]

Many observers have decried, as resulting in confusion and inconsistency, the drafters' attempts to reduce discretion by their formulaic approach. This criticism seems misplaced, at least in an analysis of the treatment of debts of an "above-median" Chapter 13 debtor. A careful textual analysis, illuminated by legislative history and intent, and tested by public policy, clears away the confusion. Debtors may not expense, without limit or question, any and all secured debt service to the detriment of unsecured creditors. ◉

FOOTNOTES:

[1] "The debtor's monthly expenses shall be the debtor's applicable monthly expense amounts specified under the National Standards and Local Standards, and the debtor's actual monthly expenses for the categories specified as Other Necessary Expenses issue by the Internal Revenue Service ……." 11 U.S.C. § 707(b)(2)(A)(ii)(I).

[2] 11 U.S.C. §§ 1325(b)(2) and (3).

[3] *BedRoc Ltd., LLC v. United States*, 541 U.S. 176, 183 (2004).

[4] *United States Nat'l Bank of Oregon v. Indep. Ins. Agents of Am., Inc.*, 508 U.S. 439, 455 (1993).

[5] 11 U.S.C. §§ 1325(b)(2) and (3).

[6] *See* especially section 5.15.1.7, item 1

[7] *In re Fowler*, 349 B.R. 414, 419 (Bankr. D. Del. 2006).

8 *Id.*, quoting H. R. 3150, February 5, 1998 — Version 1, 105th Congress.

[9] *BedRoc Ltd., LLC*, 541 U.S. at 183; s*ee also United States v. Fisher*, 6 U.S. 358, 399 (1805) (Washington, J., dissenting).

[10] *U.S. v. Ron Pair Enters., Inc.*, 489 U.S. 235, 241-42 (1989).

[11] *United States v. Heirs of Boisdore*, 49 U.S. 113, 122 (1849).

[12] *Shomberg v. United States*, 348 U.S. 540, 546 (1955).

[13] *Id.* at 545.

[14] *Cisneros v. Alpine Ridge Group*, 508 U.S. 10, 18 (1993).

[15] Internal Revenue Manual 5.15.1.10.

[16] *Id.*

[17] Expenses set forth in 11 U.S.C. § 707(b)(2)(a)(iv) would thus also be allowed.

[18] H.R. Rep. No. 109-31(I), at 13-14 (2005), *reprinted* in 2005 U.S.C.C.A.N. 88, 99-100.

[19] Letter from United States Senators Charles Grassley and Jeff Sessions to The Hon. Chief Justice John Roberts (March 13, 2006).

[20] Presidential Signing Statement for BAPCPA of 2005, found at. *See also* Senate Floor Statement of Senator Jeff Sessions (R. Ala.) "People who need a fresh start under this bill will get one. The people who can pay some of their debts back will have to do that." (March 10, 2005).

CONTINUED ON PAGE 29