A GUIDE TO INTERPRETATION OF THE 2005 BANKRUPTCY LAW

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INTRODUCTION

In 2005, Congress enacted extensive revisions of the Bankruptcy Code in legislation named the "Bankruptcy Abuse Prevention and Consumer Protection Act" ("the 2005 law").[1] The title is a statement of two worthy purposes: abuse prevention and consumer protection. Legislative history supports finding these two purposes to be primary, along with a third purpose—fairness to creditors and debtors.[2] The legislation itself, however, is a defectively designed and poorly drafted mess.[3] It creates hundreds of difficult new issues that are now working their way up to and through the appellate system. Furthermore, the 2005 law has at least temporarily reduced access to bankruptcy because of increased costs due to new uncertainty, paperwork and hoop-jumping.[4] Even with the higher price tag, the numbers of personal bankruptcy filings have been gradually climbing, after an initial decline that largely reflected a pre-effective date spike in chapter 7 filings.[5] Litigation is booming.[6]

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1 Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 (codified at 11 U.S.C. § 101 et seq. (2006)).

2 H.R. REP. NO. 109-31, pt. 1, at 2–3, 10–18 (2005) (concerning abuse prevention and consumer protection purposes and objective to "ensure that the system is fair for both debtors and creditors"); *see* Megan A. Taylor, *Gag Me With a Rule of Ethics: BAPCPA's Gag Rule and the Debtor Attorney's Right to Free Speech*, 24 EMORY BANKR. DEV. J. 227, 261 (2008) ("The stated purpose of the BAPCPA was to protect the integrity and fairness of the bankruptcy system.").

3 *See* Hon. Thomas F. Waldron & Neil M. Berman, *Principled Principles of Statutory Interpretation: A Judicial Perspective After Two Years of BAPCPA*, 81 AM. BANKR. L.J. 195, 197 (2007) (referring to the "many poorly drafted provisions" of 2005 law and to the fact that it is "under-statement" to call the law "a mess"); Henry J. Sommer, *Trying to Make Sense Out of Nonsense: Representing Consumers Under the "Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*", 79 AM. BANKR. L.J. 191, 191 (2005) (discussing the numerous challenges 2005 law presents to attorneys who represent consumer debtors).

4 *See* Alexander Gordon, IV, *Changing Philosophy of Bankruptcy*, 40 MD. B. J. 12, 14 (May/June 2007) (discussing reduction in filings since 2005 law came into effect as caused by increased costs, including increased filing fees, credit counseling fees, education fees, and attorneys' fees); *see also infra* notes 24, 103-–06 and 192–94 and accompanying text (concerning these increased costs).

5 Charles J. Tabb, *Consumer Filings: Trends and Indicators, Part I*, 25 AM. BANKR. INST. J. 1, 1 (Nov. 2006) (noting spike in filings before general effective date of new law and decline thereafter, with both spike and decline being primarily in chapter 7 filings). For historical and recent statistics on filings, see American Bankruptcy Institute, *Quarterly U.S. Bankruptcy Statistics*, *available at* http://www.abiworld.org/am/template.cfm?section=Bankruptcy_Statistics1 (last visited Oct. 16, 2008) (in chart of "Annual Business and Non-business Filings by Year (1980–2007)," showing 2,039,214 cases in 2005, the year of the spike just before the effective date of the new law in October 2005, and 597,965 cases in 2006 and 822,590 cases in 2007); *see also* ADMINISTRATIVE OFFICE OF THE UNITED STATES COURTS,

As courts up and down the hierarchy wrestled with the new issues, the Supreme Court in 2007 decided *Marrama v. Citizens Bank of Massachusetts*,[7] sending a strong message to lower courts to keep purposes of bankruptcy law in the foreground as they interpret it. *Marrama*, an individual case, was decided under pre-2005 law[8] but there is no reason to think its methodology—a focus on broad purposes and efficiency in achieving results[9]—depends on the particular version of the Bankruptcy Code in effect. The Court's emphasis on purposes and policy as the primary basis of interpretation, and its de-emphasis of statutory language, could not have come at a more dramatically significant time in the history of bankruptcy law.[10]

Now more than ever, statutory interpretation is central in the day-to-day lives of bankruptcy practitioners and judges. Unfortunately, many are laboring under the misperception that the Supreme Court has issued clear instructions to treat interpretation of the Bankruptcy Code as a search for the plain meaning of its language. The first aim of this article is to correct this misconception, which has led to the embarrassingly common phenomenon of bankruptcy judges discovering multiple, conflicting plain meanings for the same language, when meaning is obviously debatable.[11] The Court varies its interpretive approach from case to case, but it consistently relies on purposes and policies and sometimes treats these

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2007 REPORT OF STATISTICS REQUIRED BY THE BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT OF 2005 (2005), http://www.uscourts.gov/bnkrpctystats/statistics.htm#calendar [hereinafter, AO, 2007 REPORT OF STATISTICS] (reporting 822,590 non-business cases were filed in calendar year 2007, 61 percent in chapter 7 and 39 percent in chapter 13).

[6] *See infra* Part II (concerning some of the major issues).

[7] Marrama v. Citizens Bank of Mass., 549 U.S. 365, 127 S. Ct. 1105 (2007).

[8] *Id*., 127 S. Ct. at 1108 (noting case was filed in 2003).

[9] *See infra* Part I; *see also* Rosson v. Fitzgerald (*In re* Rosson), No. 06-35724, slip op., at 13557 (9th Cir. 2008) (describing specific instance of bankruptcy court's broad power, supported by *Marrama*'s holding, "to take any action necessary to prevent bad-faith conduct or abuse of the bankruptcy process"); *In re* McKenzie-Gilyard, 388 B.R. 474, 480 (Bankr. E.D.N.Y. 2007) ("One of the fundamental principles of bankruptcy law is that a bankruptcy discharge enables a debtor to receive a 'fresh start.'" (citing *Marrama*, 127 S. Ct. at 1107)).

[10] For more recent evidence that the Supreme Court is turning away from strict textual analysis, see Fla. Dep't. of Revenue v. Piccadilly Cafeterias, Inc., 128 S. Ct. 2326, 2333, 2338 (2008) (declining to decide in chapter 11 case whether relevant section of Bankruptcy Code is ambiguous and treating as "decisive" substantive canon of interpretation favoring federalism); Waldron & Berman, *supra* note 3, at 204–06 (noting that "the differences between textualism and purposivism begin to fade" and that *Marrama* departs from a focus on purpose.).

[11] *See, e.g.*, Pearson v. Stewart (*In re* Pearson), 390 B.R. 706, 712–13, nn.3–4 (B.A.P. 10th Cir. 2008) (Thomas, J., concurring) (noting split among courts as to whether debtor may claim vehicle ownership deduction in absence of any loan or lease payments and providing string citations to cases on both sides of issue, which rely on dueling "plain meaning" arguments); *see also In re* Young, 392 B.R. 6, 16 (Bankr. D. Mass. 2008) (mentioning split in courts between those "allow[ing] the Debtor an ownership expense deduction on a vehicle owned outright and those that did not"). *See generally* Waldron & Berman, *supra* note 3, at 211, 213 (arguing "plain meaning" analysis can lead to "contrary results" and courts should go beyond "the fiction of finding plain meaning" because otherwise they are "likely to err and to bring on unintended consequences").

considerations, rather than statutory language, as primary.[12] The method of statutory interpretation called for by the Court's actions is to examine language, purposes and policies and attempt to reconcile all three, making sense of the law to the extent possible (sometimes a very tall order with the 2005 law).

Of course interpretation of the Bankruptcy Code calls for parsing its language and examining structural cues, but these steps will often not lead to definitive answers. Issues under the 2005 law frequently are not among Karl Llewellyn's six out of ten times where application of statutes to facts is easy.[13] The issues under this law tend to fall more in the difficult category, with multiple plausible possibilities for interpretation.[14] Investigating the purposes of the law can help solve some conundrums. However, in many cases the purposes of the 2005 law are stated at high levels of abstraction and as a balance between goals, with the result that purpose-based analysis will not produce confidence about "right" answers.[15] Thus, policy implications need to be explored, too. Bankruptcy practitioners and judges should be telling the appellate courts, including the Supreme Court, what is at stake as a practical matter in interpretive questions. At least bankruptcy litigation will then be about something real, rather than a search for phantom plain meaning.

This article does not seek to resolve the debates over methods of statutory interpretation, ranging from a plain meaning or textualist approach to "new" textualism or purposivism.[16] Suffice it to say that even an unreconstructed textualist frequently will be defeated by the 2005 law, which—in contrast to the 1978 law—

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[12] *See* discussion *infra* Part I (focusing on *Marrama* case and discussing its reliance on purposes and policies); Waldron & Berman, *supra* note 3, at 213 (explaining appropriateness of considering text as well as context, including legislative history, prior law and practice, and policy considerations); *see also* Sydney Foster, *Should Courts Give Stare Decisis Effect to Statutory Interpretation Methodology?*, 96 GEO. L.J. 1863, 1875 (2008) (noting that Supreme Court's actions show that it does not give stare decisis effect to methods of statutory interpretation)

[13] *See* Karl N. Llewellyn, *Remarks on the Theory of Appellate Decision and the Rules or Cannons About How Statutes Are To Be Construed*, 3 VAND. L. REV. 395, 397 (1950) (discussing importance of judges' "situation sense" and stating, "[i]n some six appealed cases out of ten the court feels this sense so clearly that lining up the authorities comes close to being an automatic job").

[14] *See id.* at 399, 401–06 (calling it "foolish pretense" that there is "only one single correct answer possible" in difficult cases and setting forth 28 sets of dueling canons of statutory construction); Thomas J. Miles & Cass R. Sunstein, *The New Legal Realism*, 75 U. CHI. L. REV. 831, 832 (2008) (stating Llewellyn "believed that, much of the time, existing law did not compel particular outcomes, in the sense that the available sources would not require a rational and fair-minded judge to reach only one result").

[15] *See* Llewellyn, *supra* note 13, at 396 (discussing necessity of judges selecting among available correct answers).

[16] *See* William N. Eskridge Jr., *The New Textualism*, 37 UCLA L. REV. 621, 690–91 (1990) (applauding attention to text as important step, while also defending anti–formalist social construction as essence of statutory interpretation); Daniel A. Farber, *Do Theories of Statutory Interpretation Matter?: A Case Study*, 94 NW. U. L. REV. 1409, 1410–14 (2000) (describing textualism or formalism as opposed to dynamic interpretation or pragmatism and finding little connection between statutory interpretation method and outcomes in study of decisions of two judges on Court of Appeals for 7th Circuit: Richard Posner and Frank Easterbrook); Waldron & Berman, *supra* note 3, at 203 ("The Supreme Court's decisions involving bankruptcy issues have often been the battleground for the competing jurisprudential theories denominated purposivism and textualism.").

did not undergo expert vetting.[17] With a law this messy, a search for plain meaning will rarely be a sufficient judicial tool (leaving aside the theoretical question whether it ever is).[18] Not only is the language often sloppy, convoluted and obscure and the structure mangled,[19] but a more fundamental problem is that Congress acted on misinformation about underlying facts. It adopted approaches with effects different from announced objectives.[20] The law seems to be causing many unintended consequences, while in other ways it has much less effect than Congress apparently expected because of congressional misunderstanding about who files for bankruptcy.[21]

In particular, this article rejects the notion that a good strategy for dealing with the 2005 law, with all its drafting problems and empirically unsupported assumptions,[22] is to latch onto "plain meaning," catching Congress at its drafting

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[17] *See* Kenneth N. Klee, *Legislative History of the New Bankruptcy Law*, 54 AM. BANKR. L.J. 275, 277–94 (1980) (discussing expert process used to produce 1978 law); Justin Scheck, *Bankruptcy Rewrite Predicted to Bring a Flood of Appeals*, THE RECORDER, Feb. 8, 2006, *available at* http://www.law.com/jsp/article.jsp?id=1139306710471 (quoting Klee saying Republican congressional staff largely spurned efforts of National Bankruptcy Conference to deal with drafting mistakes, even typographical and grammatical errors); Waldron & Berman, *supra* note 3, at 217 (stating 2005 law's legislative history, "unlike the Bankruptcy Code of 1978, . . . [has] no floor statements from the floor managers that might be considered akin to a conference committee report or even consistent Senate and House committee reports to consult" and also noting that there is only a House committee report).

[18] *See In re* Donald, 343 B.R. 524, 529 (Bankr. E.D.N.C. 2006) (stating 2005 law's changes are "confusing, overlapping, and sometimes self-contradictory" and "introduce new and undefined terms that resemble, but are different from, established terms that are well understood"); Stanley Fish, *There Is No Textualist Position*, 42 SAN DIEGO L. REV. 629, 635, 649–50 (2005) (arguing human communication always depends on context).

[19] A favorite conundrum under the 2005 law is the "hanging paragraph" of section 1325(a), which entails a failure to provide ordinary structure. *See* Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, *supra* note 1; *In re* Cross, 376 B.R. 641, 644 (Bankr. S.D. Ohio 2007) ("The language added to § 1325(a), following § 1325(a)(9), has been referred to as the hanging paragraph because it follows numbered subsections, but has no numerical designation of its own."); *In re* Payne, 347 B.R. 278, 280 (Bankr. S.D. Ohio 2006) ("Given its awkward placement and lacking any identifying number or letter, the sentence has been termed by many as a 'hanging paragraph.'").

[20] *See infra* notes 89–107 and accompanying text; Lindsay E. Donn, Note, *The Best and Worst of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005: Its Effect on Bankruptcy Courts, the Reorganizing Business, and the American People*, 38 RUTGERS L.J. 573, 576–77 (2007) (observing 2005 law has not achieved its lofty goals and its shortcomings may have serious implications for the public).

[21] *See infra* notes 94–102 and accompanying text; *see also* Jean Braucher, *A Fresh Start for Personal Bankruptcy Reform: The Need for Simplification and a Single Portal*, 55 AM. U. L. REV. 1295, 1305–06 (2006) [hereinafter Braucher, *A Fresh Start*] (noting that 2005 law did not achieve its goals because it made bankruptcy "difficult for all while permitting relatively well-off persons who plan ahead to shelter both income and assets from their creditors"); A. Mechele Dickerson, *Consumer Over-Indebtedness: A U.S. Perspective*, 43 TEX. INT'L L.J. 135, 147 (2008) (discussing "unintended consequences" of 2005 law, such as decreased bankruptcy filings and additional administrative burdens and costs on consumers).

[22] *See In re* Trejos, 352 B.R. 249, 261 (Bankr. D. Nev. 2006) ("It is undisputed that the hanging paragraph is poorly drafted."); *In re* Donald, 343 B.R. 524, 529 (Bankr. E.D.N.C. 2006) (remarking that 2005 law is poorly drafted and "sometimes self-contradictory"); NAT'L BANKR. REVIEW COMM'N (U.S.), BANKRUPTCY: THE NEXT TWENTY YEARS: NATIONAL BANKRUPTCY REVIEW COMMISSION FINAL REPORT 84–85, 89–91 (1997) [hereinafter NBRC Report] (finding growth in supply of consumer credit, not increased abuse of

errors and using them to try to help hapless debtors. Rather, the better course is to focus on the announced purposes of the 2005 law and the assumptions about the problems to be addressed reflected in its provisions and to address only those problems, even though they are small. This approach will help to sustain the viability of bankruptcy relief and dull the negative impact on its affordability.

Thus, my second aim is more ambitious: to explain why interpretation of the 2005 law in light of purposes and policies is so frustrating but still the right approach for practitioners and judges to take. Congress set out to solve problems that were either minor or in tension with each other. In general, a mismatch between stated or apparent goals of law and actual impact is a common phenomenon, one that has given rise to the "law in action" school of thought,[23] but the 2005 bankruptcy law is an exquisite example of law unhinged from reality.

The effect of the new law is primarily to raise the price of access to bankruptcy,[24] thus deterring and delaying filing, perhaps particularly among the poorest debtors, not a purpose of the legislation. The unfortunate result is that more of the overindebted remain in the "sweat box of consumer credit" for longer, even when they lack the means to work their way out of debt without bankruptcy, leaving creditors able to collect in part in the meantime.[25] For those debtors who make it into bankruptcy despite the higher price, the system is left to cope with a lot of complexity that signifies fairly little. Congress adopted "consumer protection" and "abuse prevention" provisions that have little impact because reality was different from the assumptions behind the legislation.[26] It is not the job of the courts, however, to amend the law to make it have broader impact.

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bankruptcy process, accounted for growing use of bankruptcy and rejecting need for "means testing" because of lack of evidence that many debtors in bankruptcy could afford to repay their debts).

[23] *See* Stewart Macaulay, *The New Versus the Old Legal Realism: "Things Ain't What They Used to Be,"* 2005 WIS. L. REV. 365, 392–95 (2005) (discussing empiricism and legal realism).

[24] *See* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-08-697, DOLLAR COSTS ASSOCIATED WITH THE BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT OF 2005 21–27, 29–30 (2008) [hereinafter GAO, DOLLAR COSTS REPORT] (reporting increase in attorneys fees and filing fees); Ronald J. Mann, *Bankruptcy Reform and the "Sweat Box" of Credit Card Debt*, 2007 U. ILL. L. REV. 375, 377 (2007) (noting increase in costs of filings due to administrative hurdles related to credit counseling, debt relief agencies and attorney certifications).

[25] *See id.* at 384 (describing new law's principal impact as delaying bankruptcy filings by overindebted and allowing creditors to make larger partial collections as result); *see also* Oren Bar-Gill, *The Behavioral Economics of Consumer Contracts*, 92 MINN. L. REV. 749, 785–86 (2008) ("This does not mean, however, that the issuer did not collect substantial amounts of money before the consumer stopped paying. According to the sweat box model issuers extract most of their revenues at the pre-default stage.").

[26] *See* Braucher, *A Fresh Start*, *supra* note 21, at 1305–06 (noting perverse effects of new law in making bankruptcy more expensive for all, even those who are clearly not abusers, while leaving many loopholes for upper income debtors); Deanne Loonin & Elizabeth Renuart, *The Life and Debt Cycle: The Growing Debt Burdens of Older Consumers and Related Policy Recommendations*, 44 HARV. J. ON LEGIS. 167, 186 (2007) ("Congress passed comprehensive bankruptcy reform legislation in 2005. However, the changes to the bankruptcy laws actually make the system less accessible and less helpful for many consumers."); Katherine Porter & Deborah Thorne, *The Failure of Bankruptcy's Fresh Start*, 92 CORNELL L. REV. 67, 80 (2006) (observing 2005 law was produced in "a theoretical vacuum rather than informed by empirical reality").

Another problem is congressional failure to address explicitly the interaction between chapter 7 and chapter 13, particularly as this interaction arises both in "means testing" and debtors' efforts to retain collateral. Debtors, at least those with good lawyers, will gravitate to the option that meets their goals, and this could lead to counterintuitive results under the 2005 law unless the courts use remaining discretion wisely. The provisions on collateral in the two chapters pursue conflicting goals of warning debtors against impairing the fresh start while pushing them to pay more for collateral than it is worth.[27] The bankruptcy courts are uniquely positioned to consider interactions between the chapters and conflicts in congressional goals, ones that produce rampant ambiguity, and attempt to resolve them in sensible ways.

In sum, Congress designed a law that in many of its features addresses very small problems or deals with issues in contradictory ways. Rather than rewrite the law to expand its reach, the courts should apply the law to solve the rather small problems Congress identified as its targets (thinking these problems were bigger) and address the law's inconsistencies as best they can. The overall effect of such an approach would be to leave the bankruptcy system operating, even if burdened by largely peripheral new intricacies. New requirements, paperwork and complexity have increased the cost of bankruptcy,[28] but that was not an announced purpose of the new law. Congress gave no message that its purpose was a twisted or malevolent desire to reduce access to bankruptcy relief for the worst off. Courts appropriately should minimize this unintended consequence.

Costlier access is the biggest problem with the new bankruptcy law[29] and one the courts can ameliorate if not solve. Where new paperwork or other burdens do not serve a consumer protection or abuse prevention purpose, there is often enough leeway in the statute to allow interpretive approaches to minimize effects that were unintended, assuming—as the courts should—congressional good faith in seeking to protect consumer debtors and address abuse but not to make access more difficult for nonabusers.

After discussing in detail the interpretive methodology of *Marrama* in Part I, this article proceeds to discuss its implications for the bulge of bankruptcy litigation

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[27] *See infra* notes 290–96 and accompanying text (discussing retaining versus surrendering collateral in chapter 7 and chapter 13 bankruptcies). *Compare* 11 U.S.C. § 524(k)(3)(J)(i) (2006) (concerning new warning about reaffirmation in chapter 7), *with* 11 U.S.C. § 1325(a) (2006) (concerning repayment requirements under the "hanging paragraph" for certain secured loans in chapter 13).

[28] *See supra* note 4.

[29] *See* GAO, DOLLAR COSTS REPORT, *supra* note 24 (listing increases in bankruptcy fees); *see also* Elijah M. Alper, Note, *Opportunistic Informal Bankruptcy: How BAPCPA May Fail to Make Wealthy Debtors Pay Up*, 107 COLUM. L. REV. 1908, 1923 (2007) ("[T]hose with few assets may find the filing costs of bankruptcy prohibitive, even if they are rather insignificant when compared to other legal fees."); Michelle J. White, *Abuse or Protection? Economics of Bankruptcy Reform under BAPCPA*, 2007 U. ILL. L. REV. 275, 278 (2007) ("High costs would not discourage opportunistic debtors from filing because they can plan in advance by borrowing more to pay the fee. Nonopportunists, however, might be unable to file at all due to a lack of funds.").

working its way through the courts. Part II discusses examples of how a focus on consumer protection, abuse prevention and fairness purposes of the 2005 law can also produce reasonable results that do not unduly burden cases filed by the vast majority of debtors who are not abusing the system.[30]

I. THE SUPREME COURT'S USE OF PURPOSES TO INTERPRET BANKRUPTCY LAW

> *The principal purpose of the Bankruptcy Code is to grant a "'fresh start'" to the "'honest but unfortunate debtor.'"*[31]

So begins the 2007 Supreme Court opinion in *Marrama*, deciding a question of interpretation of provisions of the Bankruptcy Code[32] and pointedly *not* starting with the statutory language. Indeed, the Court quotes this purpose two more times,[33] while de-emphasizing the text of the statute itself, calling it merely "adequate authority" for its conclusion.[34] The Court, by how it proceeds, rejects even a hybrid of soft textualism and pragmatism—the idea that one should "begin with the text of the statute and interrogate its meaning in light of related provisions and the broader context of the statutory scheme as a whole," and "[o]nly then . . . proceed to other sources such as legislative history and policy."[35] Instead, the *Marrama* opinion is emphatically purposivist in its interpretive method.

The dissenting opinion underscores the methodological significance of the 5–4 decision by describing the issue as involving "clear terms"[36] of the Bankruptcy Code that "unambiguously"[37] direct a contrary conclusion to that of the "strained reading"[38] by the majority, and the dissent even backs up its textualism with a purpose-based analysis of its own, interjecting a note of pragmatism.[39] Students of the Court will find the lineups for the majority and dissenting sides predictable but nonetheless telling. Justice Stevens writes gleefully for a majority consisting of

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[30] *See* Marrama v. Citizens Bank of Mass., 549 U.S. 365, 127 S. Ct. 1105, 1111 (2007) (concerning Supreme Court's recognition that "vast majority" of debtors are honest but unfortunate non-abusers).

[31] *Marrama*, 127 S. Ct. at 1107 (quoting Grogan v. Garner, 498 U.S. 279, 286–87 (1991)). The odd double quotes in the quotation from *Marrama* result from the fact that the Supreme Court is quoting itself quoting itself.

[32] *See infra* notes 50–77 and accompanying text for detailed analysis of the provisions in issue.

[33] *Marrama*, 127 S. Ct. at 1111.

[34] *Id.*

[35] *See* Marjorie O. Rendell, *2003—A Year of Discovery: Cybergenics and Plain Meaning in Bankruptcy Cases*, 49 VILL. L. REV. 887, 888–89 (2004) (describing this approach as "prevailing trend" in federal courts and noting references to "extratextual aids are legion"); *see also* Fish, *supra* note 18, at 635 (supplying sophisticated explanation of what is wrong with very idea of "plain meaning" of a text, independent of search for drafter's intent).

[36] Marrama v. Citizens Bank of Mass., 549 U.S. 365, 127 S. Ct. 1105, 1112 (2007).

[37] *Id.*; *see infra* notes 82–86 and accompanying text (concerning the purpose and policy analysis of the dissent).

[38] *Marrama*, 127 S. Ct. at 1114.

[39] *See id.* at 1115 (noting that compliance with roundabout procedure of the statute would provide structure to process of identifying "bad faith" debtors).

himself and Justices Kennedy, Souter, Ginsburg, and Breyer, while Justice Alito writes with considerable chagrin about method (but not necessarily about the result), joined by Chief Justice Roberts and Justices Scalia and Thomas.[40]

Rather than focus on the particular issue in *Marrama* and its immediate ramifications, which have already been fully and lucidly discussed by John Rao in an earlier issue of this journal,[41] this part revisits the broader question of methods of statutory interpretation as applied to the Bankruptcy Code. Although *Marrama* arguably is of significance to statutory interpretation in general, the scope of this Article is limited to its bankruptcy implications. To the frequent consternation of bankruptcy experts, Supreme Court decisions on bankruptcy issues have often been more about the methodology of statutory interpretation than about bankruptcy policy and in particular have often showcased textualist interpretation.[42] *Marrama* is in the Supreme Court tradition of using bankruptcy cases to work out theories of interpretation, albeit this time to pitch textualism to the side. The opinion is not result-oriented in the ordinary sense; the "liberal" majority sides with the principal creditor against the debtor. The majority seems to want to make a point about interpretive method, specifically that purposes are supreme. On the other hand, the "conservative" dissenters suggest that debtors have more rights than the majority recognizes and that there are other ways to deal with the majority's policy concerns, while hewing more closely to the text of the statute.[43]

The opinions in *Marrama* show rather than tell lower courts and litigants that the Supreme Court, to a greater or lesser extent, is nearly always likely to take a purposive approach to bankruptcy law interpretation; even the dissenters in *Marrama* consider purposes. It is an old story that the Court is unpredictable in its interpretive methodology. As Professor Daniel J. Bussel put it in an article published in 2000, "[T]extualism (at least in the bankruptcy caselaw) appears to be a method only of convenience for the Court majority and abandoned at will . . . ."[44] That reality persists to this day. Justice Kennedy, part of the *Marrama* majority, wrote the Court's 2004 opinion in *Lamie v. U.S. Trustee*.[45] The *Lamie* opinion insists that there is a "plain meaning"[46] to a bankruptcy provision with a clear

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[40] *See id.* at 1107, 1112 (citing majority and dissenting justices).

[41] John Rao, *Impact of* Marrama *on Case Conversions: Addressing the Unanswered Questions*, 15 AM. BANKR. INST. L. REV. 585 (2007).

[42] *See* Daniel J. Bussel, *Textualism's Failures: A Study of Overruled Bankruptcy Decisions*, 53 VAND. L. REV. 887, 900–01 (2000) (concerning bankruptcy cases as "proving ground for textualist interpretation," leading to frequent congressional reversal of judicial rulings); Walter A. Effross, *Grammarians at the Gate: The Rehnquist Court's Evolving "Plain Meaning" Approach to Bankruptcy Jurisprudence*, 23 SETON HALL L. REV. 1636, 1640–1746 (1993) (analyzing numerous Supreme Court decisions that focused on method of statutory interpretation); John Hennigan, Rousey *and the New Retirement Funds Exemption*, 13 AM. BANKR. INST. L. REV. 777, 786 (2005) ("Several scholarly surveys of the Court's approach to the Code in particular have identified textualism or 'plain meaning' as its primary (but not exclusive) analytical technique.").

[43] *See also infra* notes 80–86 and accompanying text.

[44] Bussel, *supra* note 42, at 893.

[45] 540 U.S. 526 (2004).

[46] *Id.* at 536.

drafting error[47] as well as language that the majority concedes "may well be surplusage"[48] under the Court's reading. The opinion takes the position, however, that when there is a choice between an interpretation of a statute that treats part of it as surplusage and a reading that the statute is ambiguous, it is preferable to find surplusage in order to conclude that there is a plain meaning![49]

The Supreme Court does not treat what it says about statutory interpretation in various cases as in any sense a "holding" that binds the Court in the future, absent overruling. In the face of the Court's methodological polymorphism, the lesson for the lower courts, from the bankruptcy courts to the U.S. Courts of Appeals, as well as for bankruptcy lawyers, is that apparent "plain meaning" should be checked against congressional purposes and policy effects on the bankruptcy system, and not just when there is facial ambiguity in the text.[50] This is not a surprising or a new lesson, but it needs to be learned. Bankruptcy courts in particular should resist facile use of the phrase "plain meaning," to which too many bankruptcy judges have become wedded.[51] Rather, they should probably eschew the phrase entirely, because it so often leads them astray—that is, into making the error of thinking that they can stop their analysis once they have considered the relevant statutory language and its context in the Bankruptcy Code as a whole.[52] To satisfy the Supreme Court in purposive mode, litigants and lower courts must go on to consider stated purposes of Congress, history of bankruptcy law and decisions, legislative history of the current version, and policy implications of alternative plausible interpretations.

To analyze the methodology of statutory interpretation in *Marrama*, it is necessary to understand the particular issue in the case, but the emphasis here will be on interpretive technique. The question presented in *Marrama* is whether a

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[47] *Lamie*, 540 U.S. at 534–35 (holding provision in question, which left out an "or" necessary to make it grammatical, should still be read for its plain meaning).

[48] *Id.* at 536.

[49] *Lamie*, 540 U.S. at 536

> Where there are two ways to read the text—either attorney is surplusage, in which case the text is plain; or attorney is nonsurplusage (*i.e.*, it refers to an ambiguous component in § 330(a)(1)), in which case the text is ambiguous—applying the rule against surplusage is, absent other indications, inappropriate. We should prefer the plain meaning since that approach respects the words of Congress. In this manner we avoid the pitfalls that plague too quick a turn to the more controversial realm of legislative history.

[50] It is an old point that ambiguity can be revealed by investigation of context; the nature of human communication is contextual. *See* Fish, *supra* note 18, at 635, 649–50.

[51] For an example of a judge resisting this type of analysis, see Pearson v. Stewart (*In re* Pearson), 390 B.R. 706, 714 (B.A.P. 10th Cir. 2008) (Thurman, J., concurring) (objecting to labeling one interpretation of certain provisions as based on "plain meaning" because alternative analysis "is supported by a host of thoughtful and considered decisions").

[52] For an egregious example of the use of plain meaning in service of a position the judge found nonsensical, and which he suggested Congress should change, see *In re* McNabb, 326 B.R. 785, 791 (Bankr. D. Ariz. 2005) (recommending Congress fix "technical glitches" in statute, but until such changes are made, applying "unambiguous statute as written").

chapter 7 debtor may convert to chapter 13 despite bad faith behavior prior to the attempted conversion.[53] The Court concludes that the answer is no. The particular bad behavior in the case was lying about transfer of assets and their value.[54]

Probably few debtors lie, under penalty of perjury, about major assets in the way Marrama did (as opposed to making minor and mostly inadvertent errors).[55] On the other hand, policing of outlier behavior is necessary to maintain the legitimacy of debt relief in bankruptcy. Denying a right of chapter 13 conversion to chapter 7 debtors who lie about significant nonexempt assets leaves the chapter 7 trustee in control of these assets and better equipped to protect against their dissipation.[56] The *Marrama* majority's approach is also a check on debtors who attempt to hide assets in chapter 7—rather than surrendering them to the trustee for liquidation and distribution to creditors—and if caught, quickly convert to chapter 13 and pay the assets' value to keep them.[57]

As noted above, the *Marrama* opinion begins with a statement of the Bankruptcy Code's purpose to grant a discharge to the "honest but unfortunate" debtor.[58] Nearly three pages and five footnotes after this opening, the Court finally quotes two of the relevant statutory provisions to be interpreted, but not before also quoting with approval the reasoning of the Court of Appeals that, "[w]e can discern neither a theoretical nor a practical reason" for the textualist interpretation asserted by the debtor.[59]

The debtor's argument, based on the language of subsections (a) and (d) of section 706, was that he had an absolute right to convert to chapter 13 because he had not already converted from another chapter and met the eligibility requirements

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[53] Marrama v. Citizens Bank of Mass., 549 U.S. 365, 127 S. Ct. 1105, 1107–08 (2007).

[54] *Id*. at 1108 (noting debtor made statements about his principal asset that were misleading or inaccurate).

[55] Schedules, including a schedule of assets, are filed under penalty of perjury. *See* Bankruptcy Official Form 6, Schedules, including, "Declaration Concerning Debtor's Schedules—Declaration Under Penalty of Perjury By Individual Debtor." *See generally* 11 U.S.C. § 727(a)(4)(B) (2006) (providing courts shall grant debtor discharge unless debtor commits fraud); Taylor v. Freeland & Kronz, 503 U.S. 638, 644 (1992) (stating "[d]ebtors and their attorneys face penalties under various provisions for engaging in improper conduct in bankruptcy proceedings").

[56] *See Marrama*, 127 S. Ct. at 1107 (noting chapter 13 debtor retains possession of assets, as opposed to trustee control of nonexempt assets in chapter 7); *see also id.* at 1112, n.13 (pointing out that debtor could put assets at risk in interval between allowance of motion to convert and granting of motion to dismiss chapter 13 case).

[57] *See id.* at 1116 (Alito, J., dissenting) (acknowledging "[a] debtor who is convinced that he or she can successfully conceal assets has a significant incentive to pursue Chapter 7 liquidation in lieu of a Chapter 13 restructuring"); *see also* 11 U.S.C. § 1325(a)(4) (2006) (providing chapter 13 debtor can keep nonexempt assets in chapter 13 by paying their value); Condon v. Brady (*In re* Condon), 358 B.R. 317, 327 (B.A.P. 6th Cir. 2007) (denying conversion to chapter 13 because it would take authority away from trustee to act on behalf of estate and would have given this power to debtor who attempted to fraudulently conceal assets).

[58] *Marrama*, 127 S. Ct. at 1107.

[59] Marrama v. Citizens Bank of Mass., 549 U.S. 365, 127 S. Ct. 1105, 1109–10 (2007) (quoting Marrama v. Citizens Bank of Mass. (*In re* Marrama), 430 F.3d 474, 479 (1st Cir. 2005) and 11 U.S.C. § 706(a)–(d) (2006)).

for that chapter.[60] The relevant provisions of section 706, relied on by the debtor and ultimately quoted by the Court, are these:

> (a) The debtor may convert a case under this chapter to a case under chapter 11, 12, or 13 of this title at any time, if the case has not been converted under section 1112, 1208, or 1307 of this title. Any waiver of the right to convert a case under this subsection is unenforceable.
>
> . . .
>
> (d) Notwithstanding any other provision of this section, a case may not be converted to a case under another chapter of this title unless the debtor may be a debtor under such chapter.[61]

Quoting the statutory language, albeit belatedly, shows some attention to text, but instead of then proceeding directly to analyze the applicable provisions, the Court again heads away from the text, quoting and analyzing relevant passages of the committee reports dealing with the issue.[62] The committee reports contained some language troubling to the Court's analysis, such as the Senate Report statement that section 706(a) "gives the debtor the one-time absolute right of conversion of a liquidation case to a reorganization or individual repayment plan case."[63] The Court responds that the report's reference to an "absolute right" of conversion is overstated because the right is qualified in two ways—it is "only a one-time right that does not survive a previous conversion" and, in addition, the debtor must under section 706(d) be someone who "may be a debtor under such chapter."[64]

The Court finally turns to the central question, the meaning of the section 706(d) reference to who may be a debtor in chapter 13, acknowledging that section 109(e) sets forth exclusions (debtors are ineligible for chapter 13 if they are not individuals, lack regular income to fund a plan or exceed specified debt limits).[65]

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[60] *Marrama*, 127 S. Ct. at 1109–10 (noting defendant's claim that because he became employed since time he originally filed under chapter 7, he was now entitled to file under chapter 13).

[61] 11 U.S.C. § 706(a)–(d).

[62] *Marrama*, 127 S. Ct. at 1110 (citing S. REP. NO. 95-989, at 94 (1978) and H.R. REP. NO. 95-595, at 380 (1977)).

[63] *Marrama*, 127 S. Ct. at 1110 (quoting S. REP. NO. 95-989, at 94 (1978)).

[64] *See Marrama*, 127 S. Ct. at 1110 (stating debtor does not always have right to conversion because right does not survive previous conversion to chapter 13 and debtor must "be a debtor under such chapter"); *see also* Bobroff v. Cont'l Bank (*In re* Bobroff), 766 F.2d 797, 803 (3d Cir. 1985) (stressing conversion is prohibited when debtor does not qualify as debtor under chapter to which debtor wants to convert); *In re* Muth, 378 B.R. 302, 303 (Bankr. D. Colo. 2007) (remarking right to convert is only available once and does not survive previous conversion).

[65] Marrama v. Citizens Bank of Mass., 549 U.S. 365, 127 S. Ct. 1105, 1114 n.2 (2007). *See* 11 U.S.C. § 109(e) (2006) (listing requirements needed to qualify as debtor under chapter 13: being "an individual with regular income" and having debts within specific dollar ranges); *see also* Branigan v. Bateman (*In re* Bateman), 515 F.3d 272, 281 (4th Cir. 2008) (noting court must look to section 109(e) to determine

The Court maintains that another meaning of who "may be a debtor" under chapter 13 is to incorporate section 1307(c), which provides that a chapter 13 case may be dismissed or converted "for cause," a phrase that has been interpreted to include bad faith.[66] The Court does not engage with two telling textual points made by the dissenters: that section 109 carries the caption, "Who may be a debtor"[67] and that section 1307(c) is about ending a case that is already in chapter 13, not a test for conversion from chapter 7 to chapter 13, so that "the Court's holding in this case finds no support in the terms of the Bankruptcy Code."[68]

Instead of dealing with these textual points, the Court again quotes the purpose of protecting the "honest but unfortunate debtor"[69] and concludes that section 706(d) is "adequate authority" for the court's interpretation based on purpose.[70] Language need only be "adequate," while purpose is treated as the linchpin in the analysis. Here is the key reasoning:

> In practical effect, a ruling that an individual's Chapter 13 case should be dismissed or converted to Chapter 7 because of

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eligibility for chapter 13); *In re* Lewis, 339 B.R. 814, 816 (Bankr. S.D. Ga. 2006) ("Whether an individual is eligible to be a debtor under chapter 13 is established under 11 U.S.C. § 109(e).").

[66] *Marrama*, 127 S. Ct. at 1110–11 (noting although section 1307(c) does not include bad faith in its list of 10 causes justifying dismissal or conversion of chapter 13 proceeding, "Bankruptcy courts nevertheless routinely treat dismissal for prepetition bad faith conduct as implicitly authorized by the word 'for cause'"); *see* 11 U.S.C. § 1307(c) (2006) (providing chapter 13 case may be converted or dismissed for cause, such as, "unreasonable delay by the debtor that is prejudicial to creditors" and "material default by the debtor with respect to a term of a confirmed plan"); *see also* Rosson v. Fitzgerald (*In re* Rosson), No. 06-35724, 2008 WL 4330558, at *6 (9th Cir. 2008) (holding debtor does not have absolute right to dismiss, and bankruptcy court may deny dismissal to prevent abuse of process due to debtor's bad faith conduct).

[67] *See Marrama*, 127 S. Ct. at 1114 (Alito, J., dissenting) (indicating debtor must meet specific requirements in section 109(e) to qualify as debtor under chapter 13); *see also* 11 U.S.C § 109(e) (requiring debtor under chapter 13 be "an individual with regular income" who owes debts within specified dollar ranges); *In re Lewis*, 339 B.R. at 816 (stating section 109(e) determines whether debtor qualifies as debtor under chapter 13).

[68] *Marrama*, 127 S. Ct. at 1115 (Alito, J., dissenting) (observing section 1307(c) does not set forth requirements to qualify as debtor under chapter 13, but it presents standard to be used in determining whether chapter 13 case should be dismissed or converted to chapter 7 case); *see* 11 U.S.C. § 1307(c)

> [O]n request of a party in interest or the United States trustee and after notice and a hearing, the court may convert a case under this chapter to a case under chapter 7 of this title, or may dismiss a case under this chapter, whichever is in the best interests of creditors and the estate, for cause . . . .

[69] *Marrama*, 127 S. Ct. at 1111 (explaining "honest but unfortunate" debtors make up "vast majority" of those filing under chapter 7).

[70] *Id*. at 1110–11 (citing 11 U.S.C. § 706(d) (2006)) (stating section 706(d) provides adequate authority to deny debtor's conversion to chapter 13 because it only allows debtor to convert if he qualifies as debtor under chapter 13); *see* 11 U.S.C. § 706(d) ("Notwithstanding any other provision of this section, a case may not be converted to a case under another chapter of this title unless the debtor may be a debtor under such chapter."); Bobroff v. Cont'l Bank (*In re* Bobroff), 766 F.2d 797, 803 (3d Cir. 1985) (finding since debtor was never eligible for chapter 13 relief, he did not meet requirements under section 706(d) and was prevented from converting to chapter 13).

> prepetition bad-faith conduct, including fraudulent acts committed in an earlier Chapter 7 proceeding, is tantamount to a ruling that the individual does not qualify as a debtor under Chapter 13. That individual, in other words, is not a member of the class of "'honest but unfortunate debtor[s]'" that the bankruptcy laws were enacted to protect. See *Grogan v. Garner*, 498 U.S., at 287, 111 S.Ct. 654. The text of § 706(d) therefore provides adequate authority for the denial of his motion to convert.[71]

The Court thus solves the "procedural anomaly"[72] that it believes would exist if a chapter 7 debtor could convert to chapter 13, only to have his case dismissed or reconverted to chapter 7 for bad faith. Lest the reader have any doubt as to the primary emphasis on broad statutory purpose as the basis of interpretation, the Court states again—a third time!—the aim of protecting only "[t]he class of honest but unfortunate" debtors.[73]

At the end of the opinion, the Court also discusses two highly discretionary—and thus relatively textually unbound—possible alternative rationales. First, it states that the broad authority of bankruptcy courts under section 105(a) to prevent an abuse of process "is surely adequate"[74] to support the Court's conclusion. Second, it notes that the inherent power of federal courts to sanction abusive litigation practices "might well provide an adequate justification for a prompt, rather than a delayed, ruling on an unmeritorious attempt to qualify as a debtor under Chapter 13."[75]

Another aspect of the methodology bears examination; it supports interpretations of the Bankruptcy Code that preserve access to legitimate debt relief. The Court twice refers to the "the class"[76] of honest but unfortunate debtors, thus dividing debtors into two classes, those worthy of debt relief and those who are not. In particular, it emphasizes that better treatment is due to the honest but unfortunate debtors, who are "the vast majority" of filers, stating that they "do possess an absolute right to convert their cases from Chapter 7 to Chapter 13 . . . ."[77]

A question acknowledged but not addressed by the Court is how some debtors can have an absolute right to convert while others do not. The Court suggests that a way to accomplish something close to this feat is to have a very high substantive bar for denying a motion to convert. It leaves for another day "to articulate with

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[71] Marrama v. Citizens Bank of Mass., 549 U.S. 365, 127 S. Ct. 1105, 1111 (2007).

[72] *See id.* at 1108.

[73] *Id.* at 1111.

[74] *Id.* at 1112 (noting broad authority given to Bankruptcy Courts is "adequate to authorize an immediate denial of a motion to convert"); *see* 11 U.S.C. § 105(a) (2006) (enabling court to "issue any order, process, or judgment that is necessary or appropriate").

[75] *Marrama*, 127 S. Ct. at 1112.

[76] *Id.* at 1111.

[77] Marrama v. Citizens Bank of Mass., 549 U.S. 365, 127 S. Ct. 1105, 1111 (2007).

precision what conduct qualifies as 'bad faith'" but states that the debtor's conduct must be at least "atypical," perhaps even "extraordinary."[78] Procedural subtlety is also needed to avoid burdening honest debtors, for example those whose incomes go up after filing and who seek to make legitimate use of chapter 13 to pay creditors and retain assets. John Rao has painstakingly explained procedural and substantive means to implement the Court's decision, dividing the dishonest from the honest while minimizing burdens on the latter, much larger group.[79] *Marrama s*upports and calls for this type of analysis, which is greatly needed on a host of new issues under the 2005 law to achieve efficient sorting of abusers from the much larger class of honest debtors who have no means to repay.

It is notable that even the dissent in *Marrama* is only textualist to a point, underscoring the majority's desire to serve purpose first and as directly as possible, without being much troubled by textual analysis. The dissenting opinion begins with the text and the broader context of the Bankruptcy Code as a whole, considering the particular provisions to be interpreted in comparison to[80] and in light of others.[81] The dissent then itself turns to purposes and finds that allowing conversion to chapter 13, followed by a hearing on dismissal or reconversion, is not as pointless as the majority suggests, because bankruptcy rules provide a structure for notice and a hearing if that procedure is used.[82] More substantively, waiting until the case is converted before deciding whether there are grounds to dismiss or reconvert it for cause makes it possible for the bankruptcy court to consider whether

[78] *Id*. at 1112 n.11.

[79] Rao, *supra* note 41, at 588–601 (discussing procedural steps of not automatically treating motion to convert as contested matter, requiring pleading with particularity of legal and factual basis for raising issue of bad faith in objection, and putting burden of proof of bad faith on party resisting conversion); *see id.* at 605–08 (arguing substantive test of bad faith should require more than mistake or excusable neglect but rather attempts to intentionally manipulate court system—as *Marrama* did—by making numerous misrepresentations about assets during bankruptcy case).

[80] *Marrama*, 127 S. Ct. at 1113 (Alito, J., dissenting) (noting contrast between section 706 and other sections explicitly giving bankruptcy judges discretion to deny conversion requests).

[81] *Id*. (discussing explicit consequence of denial of discharge under section 727(a)(3) for specific conduct such as concealing records and making false accounts).

[82] *See id.* at 1115 (Alito, J., dissenting) ("It is by no means clear, however, that conversion under § 706(a) followed by a reconversion proceeding under § 1307(c) would be an empty exercise."); *see also* Pequeno v. Schmidt, 307 B.R. 568, 580 (S.D. Tex. 2004) (noting "convert[ing] only to reconvert . . . allows one to comply with both the Congressional mandate of Section 706(a) and the duty to protect the bankruptcy process from abuse"). *See generally* Lynne F. Riley & Maria C. Furlong, *The Supreme Court Restores Discretion and Enhances Jurisdiction of the Bankruptcy Courts*, 2008 NORTON ANN. SURV. BANKR. L., pt. I § 4 (commenting on *Marrama* dissent's reasoning that debtor who files chapter 7 petition has absolute statutory right to convert to another chapter). Although Rao, *supra* note 41, at 588–90, analyzes how existing bankruptcy rules can accommodate the *Marrama* decision, the procedure of conversion from chapter 7 to chapter 13, followed by consideration of dismissal or reconversion under section 1306(c), more obviously already fits with bankruptcy rules. *See Marrama*, 127 S. Ct. at 1115 (discussing Federal Rules of Bankruptcy Procedure 1017(f) and 9014).

the chapter 13 plan, if already filed, indicates good faith (for example by treating creditors better than they would be treated in chapter 7).[83]

Considering the alternative grounds of decision discussed by the majority, the dissent expresses the reservation that neither a bankruptcy court's general powers under section 105(a) nor its inherent equitable powers "authorizes a bankruptcy court to contravene the Code."[84] The dissenting opinion takes the position that importing a test for dismissal or reconversion of a chapter 13 case into the question whether the debtor can convert from chapter 7 to chapter 13 does contravene the statute. The dissent, however, acknowledges that the majority identifies a real problem,[85] but it suggests an alternative solution to deal with bad faith: the bankruptcy courts could use their statutory and equitable authority to craft remedies, such as enjoining alienation of property of the estate and penalizing counsel,[86] rather than contravening the Code's direction to allow a one-time right of conversion to chapter 13 for eligible debtors. The dissent's interpretation is both faithful to the text and attuned to practical problems. The majority, however, opts for a more direct route to policing extraordinary or at least atypical bad faith behavior. *Marrama* thus stands in favor of a principle of efficiency in achieving policy objectives.[87] *Marrama*'s method is to separate debtors into two classes, abusers, on the one hand, and honest but unfortunate debtors, on the other, and to interpret the Code so as to deny relief to the former without burdening the latter, who are "the vast majority of the hundreds of thousands of individuals who file

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[83] *See* Marrama v. Citizens Bank of Mass., 549 U.S. 365, 127 S. Ct. 1105, 1116 (2007) (Alito, J., dissenting); Gier v. Farmers State Bank of Lucas, Kan. (*In re* Gier), 986 F.2d 1326, 1328 (10th Cir. 1993) (setting forth non-exhaustive list of factors guiding good faith determination). *See generally* Avi Goldenberg, *Supreme Court Rules That a Debtor Has No Absolute Right to Convert From Chapter 7 to Chapter 13*, 125 BANKING L.J. 84, 87 (2008) (discussing dissent's reasoning).

[84] *See Marrama*, 127 S. Ct. at 1116 (Alito, J., dissenting) ("[A] bankruptcy court's general and equitable powers 'must and can only be exercised within the confines of the Bankruptcy Code.'" (quoting Norwest Bank Worthington v. Ahlers, 485 U.S. 197, 206 (1988))). *See generally* SEC v. U.S. Realty & Improvement Co., 310 U.S. 434, 455 (1940) ("A bankruptcy court . . . is guided by equitable doctrines and principles except in so far as they are inconsistent with the [statutory framework]."); Adelphia Bus. Solutions, Inc. v. Abnos, 482 F.3d 602, 609 (2d Cir. 2007) ("Section 105(a) grants broad equitable power to the bankruptcy courts to carry out the provisions of the Bankruptcy Code so long as that power is exercised within the confines of the Bankruptcy Code.").

[85] *Marrama*, 127 S. Ct. at 1116 (Alito, J., dissenting). *See generally* Lindsay Sherp, Comment, *To Strike Or Dismiss, That Is the Question: How Courts Should Dispose of Bankruptcy Cases Filed by Debtors Who Failed to Obtain Credit Counseling*, 60 BAYLOR L. REV. 317, 328–31 (2008) (discussing mechanics of bad-faith conversion from chapter 7 to chapter 13 involved in *Marrama*).

[86] *Marrama* at 1116–17; *see* Everly v. 4745 Second Ave., Ltd. (*In re* Everly), 346 B.R. 791, 797 (B.A.P. 8th Cir. 2006) (describing sanctions against counsel to prevent abuse of bankruptcy processes); *In re* Bartmann, 320 B.R. 725, 732 (Bankr. N.D. Okla. 2004) (describing injunction against alienation of property of estate to deter bad faith behavior).

[87] *See Marrama*, 127 S. Ct. at 1112 (describing efficiency—"prompt, rather than . . . delayed, ruling on an unmeritorious attempt to qualify as a debtor under Chapter 13"—as desirable); Kowal v. Malkemus (*In re* Thompson), 965 F.2d 1136, 1145 (1st Cir. 1992) (noting "important policy favoring efficient bankruptcy administration . . . ."); *see also* Riley & Furlong, *supra* note 82, at 12 (describing *Marrama* as contributing to trend of regarding bankruptcy courts as courts of equity with broad discretion to hear and decide issues requiring capable and efficient adjudication).

Chapter 7 petitions each year."[88] Indeed, the methodology of *Marrama* could be interpreted as designed to promote this approach going forward.

II. INTERPRETATION BASED ON PURPOSES AND POLICIES IN THE FACE OF LEGISLATIVE MISUNDERSTANDING

As discussed in Part I, the Supreme Court's actions call for interpretations of bankruptcy law that take into account legislative purposes as well as policy implications for operation of the bankruptcy system. Bankruptcy courts have understandably resisted this conclusion because the detailed prescriptions of the 2005 law often are based on faulty factual assumptions or lack of understanding about policy implications. This section uses examples of this sort of congressional error to illustrate how interpretation based on congressional purposes and policies can still work reasonably well in many instances, if not all. Rather than exhaustive analysis of each issue used as an example, the purpose of this section is to outline an approach that can be used not only for the particular issues discussed, but also for many others. In the 2005 law, Congress had goals that did not match the problems on the ground. Part II argues that the courts should fix the problems Congress identified but not attempt to rewrite the law to have other, more consequential effects.

A. Provisions with Consumer Protection Purposes

Congress gave consumer protection as its rationale for several new features of the 2005 law: among others, the required briefing on available credit counseling, the required short course on financial management, and the "debt relief agency" provisions apparently regulating debtors' attorneys and petition preparers.[89] Under the heading "Consumer Debtor Bankruptcy Protections," the House Report states that the credit counseling provisions "are intended to give consumers in financial distress an opportunity to learn about the consequences of bankruptcy—such as the potentially devastating effect it can have on their credit rating."[90] More generally, according to the same report, the counseling is supposed to enable debtors to "make

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[88] *Marrama*, 127 S. Ct. at 1111. *See generally* Goldenberg, *supra* note 83, at 86–87 (analyzing *Marrama*'s methodology in differentiating between chapter 7 and chapter 13).

[89] 11 U.S.C. § 101(12A) (2006) (concerning debt relief agencies); 11 U.S.C. § 109(h) (2006) (concerning credit counseling requirement); 11 U.S.C. §§ 526–28 (2006) (concerning debt relief agencies); 11 U.S.C. §§ 727(a)(11), 1141(d)(3)(C), 1328(b) (2006) (describing debtor education requirement).

[90] H.R. REP. NO. 109-31, *supra* note 2, at 17–18; *see In re* Tulper, 345 B.R. 322, 327 (Bankr. D. Colo. 2006) (discussing legislature's intention to give consumers opportunity to learn about consequences of declaring bankruptcy prior to doing so); *In re* Rios, 336 B.R. 177, 179–80 (Bankr. S.D.N.Y. 2005) (finding Congress, by requiring credit counseling, clearly sought to provide debtors with opportunity to make informed choices about financial alternatives available to them before declaring bankruptcy).

an informed choice about bankruptcy, its alternatives, and consequences."[91] The House Report also states that the financial management training required before debtors can get a discharge "will provide them with guidance about how to manage their finances, so that they can avoid future financial difficulties."[92] The debt relief agency provisions are described under the same consumer protection heading as having the goal of "strengthening professionalism standards for attorneys and others who assist consumer debtors with their bankruptcy cases."[93]

This ambitious set of consumer protection goals reflects a combination of ignorance about the facts and wishful thinking about likely effects of the measures adopted. In other contexts, consumer protections are put through a cost-benefit analysis.[94] Congress apparently acted on an erroneous assumption that many people were filing for bankruptcy at a time when credit counseling could solve their problems and leave their credit ratings in better shape. In fact, as the General Accounting Office determined in a 2007 study, a wide range of observers question the value of the credit counseling requirement.[95] Credit counseling might work for more debtors if they could get it earlier, before their debt loads become unmanageable, but the required briefing comes too late, typically after a debtor visits a bankruptcy lawyer or petition preparer and learns of the requirement.[96] By

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[91] H. R. REP. NO. 109-31, *supra* note 2, at 2; *see In re* Tomco, 339 B.R. 145, 152 (Bankr. W.D. Pa. 2006) (discussing how requirement of credit counseling forces debtors to "obtain education and counseling regarding both the economic consequences of filing . . . and the non-bankruptcy alternatives available" to rebuild financial health).

[92] H. R. REP. NO. 109-31, *supra* note 2, at 18; *see also* Karen Gross & Susan Block-Lieb, *Empty Mandate or Opportunity for Innovation? Pre-Petition Credit Counseling and Post-Petition Financial Management Education*, 13 AM. BANKR. INST. L. REV. 549, 549 (2005) (discussing how goal of financial management training was to help debtors make "better choices in the consumer financial markets after their cases were closed"); Vanessa A. Lantin, *Don't Be Cruel: Did Congress Really Intend to Deny an Individual "Emergency Debtor," Acting in Good Faith, the Opportunity to Be a Debtor Under the Bankruptcy Code?*, 15 NORTON J. BANKR. L. & PRAC. 3 Art. 4, 323, 331 (2006) (remarking legislative goal of post-petition financial counseling is "a means to guide and educate individual debtors how to avoid, in the future, the financial pitfalls that brought them to the bankruptcy court in the first place").

[93] H. R. REP. NO. 109-31, *supra* note 2, at 17; *see* Zelotes v. Martini, 352 B.R. 17, 22 (D. Conn. 2006) (discussing how legislative intention behind enacting 2005 law was partially to improve standards of assistance to consumers).

[94] *See generally* Jean Braucher, *Defining Unfairness: Empathy and Economic Analysis at the Federal Trade Comm*ission, 68 B.U. L. REV. 349, 417–29 (1988) (discussing FTC's use of cost-benefit analysis in rule-making).

[95] U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-07-203, VALUE OF CREDIT COUNSELING REQUIREMENT IS NOT CLEAR 19 (2007) [hereinafter, GAO, CREDIT COUNSELING REPORT]; *see also* Dickerson, *supra* note 21, at 148 (stating credit counseling requirement is "an administrative obstacle to debtors, rather than a financially beneficial exercise").

[96] GAO, CREDIT COUNSELING REPORT, *supra* note 95, at 19 (noting "anecdotal evidence suggests that by the time most consumers receive the counseling, their financial problems are dire and they have few viable alternatives to bankruptcy"); *see In re* Wilson, 346 B.R. 59, 62 (Bankr. N.D.N.Y. 2006) (finding credit counseling occurs too late to have beneficial result); Dickerson, *supra* note 21, at 148 ("[C]ommentators uniformly have concluded that pre-filing credit counseling is of little value to most consumers because, by the time most people are contemplating a bankruptcy filing, their financial situation is so dire that they have no realistic alternative but to file for bankruptcy.").

this time, most debtors already are in deep debt trouble and have terrible credit ratings, so that they may actually improve access to new credit by filing in bankruptcy.[97] The GAO quoted estimates that only two to three percent of debtors who get the pre-bankruptcy counseling enter into debt management plans.[98] Furthermore, the success rate of those plans would have to be studied to see whether they turn out to be a viable alternative; in general, debt management plans fail at a high rate.[99] The GAO concluded that the value of the counseling requirement (which does not require actual counseling but rather a briefing about available counseling and a budget analysis) has not been shown.[100] The GAO also noted that effective oversight and decision-making require better data, particularly tracking of results of the counseling requirement.[101] The agency expressed fewer reservations about the financial management education requirement, based on reports from participants in the bankruptcy process that the education is beneficial. The GAO had no statistical data to back up that conclusion, however, and other studies have not shown long-term or concrete benefit from financial education courses, which may even cause harm by creating over-confidence rather than greater financial literacy.[102]

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[97] *See* Katherine Porter, *Bankrupt Profits: The Credit Industry's Business Model for Postbankruptcy Lending*, 93 IOWA L. REV. 1369, 1373 (2008) (reporting key finding in study of debtors after bankruptcy is that creditors "repeatedly solicit debtors to borrow after bankruptcy" beginning right after debtors get discharge); *see also* Timothy Egan, *Newly Bankrupt Raking in Piles of Credit Offers*, N.Y. TIMES, Dec. 11, 2005, at 1 (reporting how individuals, even after declaring bankruptcy, receive numerous credit card offers); Caroline Mayer, *Bankrupt and Swamped With Credit Offers: When Chapter 7 Filers Wipe Out Their Debts, Card Firms Jump*, WASH. POST, Apr. 15, 2005, at A1 (discussing how 96 percent of recent debtors who responded to survey received offers for credit cards, car loans, mortgages and other credit in year after debts discharged).

[98] GAO, CREDIT COUNSELING REPORT, *supra* note 95, at 22.

[99] *See* Dickerson, *supra* note 21, at 149 (stating most consumers facing decision to declare bankruptcy cannot afford to pay their debts under debt management plan); *see also* David A. Lander, Essay: *A Snapshot of Two Systems That Are Trying to Help People in Financial Trouble*, 7 AM. BANKR. INST. L. REV. 161, 180 (1999) (noting study by National Foundation for Consumer Credit found 48 percent of debtors in debt management programs stopped making payments within first six months); Loonin & Renuart, *supra* note 26, at 189 (discussing how credit counseling agencies often place consumers on debt management plans they cannot afford).

[100] GAO, CREDIT COUNSELING REPORT, *supra* note 95, at 39 ("[T]he value of the prefiling credit counseling requirement is not clear . . . [i]t is therefore uncertain whether the requirement is achieving its key goal of helping consumers determine whether or not to file for bankruptcy."). *See generally* Robert J. Landry, III & Amy K. Yarbrough, *An Empirical Examination of the Direct Access Costs to Chapter 7 Consumer Bankruptcy: A Pilot Study in the Northern District of Alabama*, 82 AM. BANKR. L.J. 331, 337 (2008) (discussing evidence suggesting that additional cost of credit counseling does not render any benefit to consumers).

[101] GAO, CREDIT COUNSELING REPORT, *supra* note 95, at 25–26, 39 ("Without reliable data on the outcomes of the prefiling credit counseling sessions, policymakers and program managers lack information that would allow them to determine how well the statutory requirement is truly serving to inform consumers about their options."); *see* Clifford J. White III, *Making Bankruptcy Reform Work: A Progress Report in Year 2*, 16 AM. BANKR. INST. J. 16, 51 (June 2007) [hereinafter White, *Year 2*] (discussing need for further research "to determine the overall effectiveness of credit counseling").

[102] *See* GAO, CREDIT COUNSELING REPORT, *supra* note 95, at 28 & n.45 (noting belief by bankruptcy professionals that debtor education courses will help improve financial literacy); *see also* Jean Braucher, *An*

Balanced against questionable benefit of these new counseling and education features, there is quite specific evidence of costs. Debtors are typically paying $50 for the required credit counseling briefing and another $50 for a short course in financial management.[103] In addition, in part due to the administrative costs of regulating providers of the counseling briefing and financial management course (along with other new features of the 2005 law, particularly the means testing discussed below), filing fees have gone up by $90 for chapter 7 and $80 for chapter 13.[104] The government is also absorbing some of the new administrative costs, meaning taxpayers are paying for them.[105] The cost of both the credit counseling and financial management education requirements is also paid in debtors' time and inconvenience. Overall, the GAO concluded that "a wide range of stakeholders view the prefiling counseling requirement as an administrative obstacle rather than a useful exercise."[106]

Empirical Study of Debtor Education in Bankruptcy: Impact on Chapter 13 Completion Not Shown, 9 AM. BANKR. INST. L. REV. 557, 578–79 (2001) [hereinafter Braucher, *Debtor Education*] (finding lack of impact on plan completion from education when multiple regression analysis is used to control for influence of other factors and finding that use of wage orders to have employers directly pay chapter 13 trustee is practice most likely to increase plan completion); Lauren Willis, *Against Financial Literacy Education*, 94 IOWA L. REV. (forthcoming 2008), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1105384 (discussing empirical evidence that financial literacy education in general does not work and may actually produce worse financial outcomes because of increase in over-confidence rather than in financial literacy).

[103] *See* GAO, DOLLAR COSTS REPORT, *supra* note 24, at 21 (observing increased costs to bankruptcy filers due to new credit counseling and debtor education requirements). *See generally* Gary Neustadter, *2005: A Consumer Bankruptcy Odyssey*, 39 CREIGHTON L. REV. 225, 265–66 (2006) ("Without knowing how well the mandatory instruction under the Act may achieve some unstated objective, it is troubling that debtors will be burdened with the expense of this instruction in addition to fees, if applicable, for pre-petition credit counseling . . . ."). Approved agencies must provide some debtors counseling and education without charge, based on need, but there are no clear guidelines defining need. *See* GAO, DOLLAR COSTS REPORT, *supra* note 24, at 33 (observing need for formal guidance on what constitutes client's "ability to pay" due to varying policies for waiving fees); *see also* GAO, CREDIT COUNSELING REPORT, *supra* note 95, at 29–32 (concerning varying policies of providers on fee waivers and lack of agency guidance on determining ability to pay); John Fitzgerald & Mark Neal, *USTP Addresses New Issues in Approving Credit Counseling and Debtor-Education Providers*, 24 AM. BANKR. INST. J. 14, 54 (Oct. 2005) (stating "[c]redit counseling agencies must use their expertise to evaluate clients' 'ability to pay' on a case-by-case basis").

[104] GAO, DOLLAR COSTS REPORT, *supra* note 24, at 29 (indicating chapter 7 filing fees rose from $209 to $299 and chapter 13 fees rose from $194 to $274 as result of 2005 law). The increased costs of the trustee program were related to, first, the implementation of the means test and, in addition, credit counseling and debtor education requirements, debtor audits, studies and reporting, information technology, and facilities expansion. *Id.* at 12. There were also substantial new costs to the federal judiciary. *Id.* at 14–16 (noting "new docketing, noticing, and hearing requirements [made] addressing bankruptcy cases more complex and time-consuming").

[105] As a result of the new law, initially filings went down substantially, and thus so did revenues from fees; reduction in bankruptcy fee revenues was offset by increases in appropriated funds. *Id.* at 17–20.

[106] GAO, CREDIT COUNSELING REPORT, *supra* note 95, at 39. *See generally* Dickerson, *supra* note 21, at 148 (concluding pre-filing credit counseling requirement has not had its intended results and "is of little value to most consumers"). *Cf.* Katherine A. Jeter-Boldt, Note, *Good in Theory, Bad in Practice: The Unintended Consequences of BAPCPA's Credit Counseling Requirement*, 71 MO. L. REV. 1101, 1114–16 (2006) (suggesting credit counseling requirement may be of no benefit to certain debtors, such as those facing foreclosure and victims of natural disasters). Perhaps the best news in the GAO report is that a feared problem of a massive consumer protection problem from credit counseling agencies steering debtors away

A debtor is supposed to receive a briefing on available counseling before filing, subject to a few narrow exceptions,[107] but the law is silent about what is supposed to happen if a debtor files without having had it. Debtors' lawyers are well aware of the requirement, and counseling is available on line and on the telephone around the clock, so those who fail to get counseling are usually pro se filers.[108] In contrast to the silence about remedy for ineligibility for filing before getting the counseling briefing, the law is quite specific that an individual debtor, absent an applicable exception,[109] is not entitled to a discharge unless the debtor attends the required short course on financial management.[110] Obviously, the courts cannot repeal these two requirements and save debtors $100 and the time and trouble necessary to comply with them. The courts do, however, have room to interpret the law, particularly to fill in the gap about remedy for not getting a briefing on credit counseling, to minimize the negative impact on debtors in light of the congressional purpose to protect them.[111]

In the face of statutory silence about the remedy for neglecting to get a prefiling briefing on available credit counseling, it is particularly appropriate to take into

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from bankruptcy and into unsustainable debt management problems did not materialize. *See* GAO, CREDIT COUNSELING REPORT, *supra* note 95, at 8–9 (discussing congressional hearings and federal and state investigations concerning abusive practices in industry, including Internal Revenue Service examinations of agencies' tax exempt status, including revoking or terminating text-exempt status); *id.* at 14–16 (noting limited complaints about counseling provided in connection with bankruptcy requirement, although there were some complaints of providers giving legal advice, discouraging bankruptcy filing, or not informing clients of possibility of fee waiver based on need).

[107] *See* 11 U.S.C. §109(h)(2)–(4) (2006) (providing specific circumstances when credit counseling briefing requirement does not apply). Lack of availability of counseling in a district, dealt with in section 109(h)(2), has not been a problem because of telephone and Internet services, although there have been problems accessing useful services among some populations such as non-English speakers and persons with limited literacy. GAO, CREDIT COUNSELING REPORT, *supra* note 95, at 32–36 (highlighting actions taken to address potential challenges faced by consumers in fulfilling requirements, such as offering credit counseling and debtor education services in Spanish and other languages). The exceptions of section 109(h)(3)–(4) do not cover debtors who simply did not know about the counseling requirement. *See* Jean Braucher, *The Challenge to the Bench and Bar Presented by the 2005 Bankruptcy Act: Resistance Need Not Be Futile*, 2007 U. ILL. L. REV. 93, 101 (2007) [hereinafter Braucher, *Bench and Bar*] ("The only broad exception to getting a prefiling briefing is in cases of exigent circumstances . . . .").

[108] GAO, CREDIT COUNSELING REPORT, *supra* note 95, at 21–22, 32–34, 36–37 (concerning availability on telephone and Internet, options favored by most debtors, and noting debtors filing without attorney occasionally are unaware of counseling requirement).

[109] *See* 11 U.S.C. §§ 727(a)(11), 1141(d)(3)(C), 1328(g) (2006) (concerning relevant exceptions to debtor education requirement). These provisions incorporate the exceptions for credit counseling, set forth in section 109(h)(4).

[110] *See id.* (relating to personal finanancial management course as requirement for discharge). To the extent debtors' failure to take the course leads to dismissal of cases, the requirement has considerable negative impact—the debtor may have paid attorneys' fees, a filing fee, and a counseling fee, and even have completed a chapter 13 plan, yet fail to get a discharge. *See also infra* notes 120–22 and accompanying text (concerning impact of dismissals on later cases filed within a year).

[111] *See* H.R. REP. NO. 109-31, *supra* note 2, at 2, 17–18 (noting legislative purpose to allow consumers to make informed decisions about whether to file in bankruptcy by providing information about alternatives to bankruptcy); *In re* Manalad, 360 B.R. 288, 296 (Bankr. C.D. Cal. 2007) (concluding Congress did not intend to mandate dismissal when debtors do not comply with the counseling requirement).

account the consumer protection purpose of Congress. The silence about remedy does not have a plain meaning. Congress stated that the counseling briefing was intended to protect debtors from unnecessary bankruptcy that would hurt their credit ratings and to help them make informed decisions in light of alternatives to bankruptcy,[112] not to punish them for failing to punch a ticket. Therefore, the best remedy is to allow a debtor who has already filed to get the counseling and then allow the debtor to make a fresh decision about whether bankruptcy is the best choice.[113] If the debtor learns that a debt management plan or some other solution might work and wants to try it, the case should be stricken so that there is no record of it (among other reasons, to minimize impact on credit rating, as Congress stated was its intent).[114] If the debtor learns—as most debtors do—that bankruptcy is the only workable way to get out of debt,[115] the debtor should be permitted to file an amended petition and proceed in bankruptcy. Bankruptcy Rule 1009 provides for amending petitions,[116] and the 2005 law contains a new reference to doing so.[117] Relying on legislative history stating a consumer protection purpose for the counseling requirement, at least one bankruptcy court has adopted the approach of allowing an amended petition to cure the temporary ineligibility caused by filing the

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[112] *See* H.R. REP. NO. 109-31, *supra* note 2, at 17–18 ("The legislation's credit counseling provisions are intended to give consumers in financial distress an opportunity to learn about the consequences of bankruptcy—such as the potentially devastating effect it can have on their credit rating—before they decide to file for bankruptcy relief."); *see also In re* Enloe, 373 B.R. 123, 126 (Bankr. D. Colo. 2007) (explaining intent behind counseling requirement to evaluate debtor's financial condition and determine if bankruptcy is best option); *In re* Bricksin, 346 B.R. 497, 502 (Bankr. N.D. Cal. 2006) (suggesting purpose behind counseling requirement is to encourage alternatives to bankruptcy and to promote debtor awareness of effects of bankruptcy).

[113] *See* H.R. REP. NO. 109-31, *supra* note 2, at 17–18 (discussing choice of bankruptcy relief and its consequences); *In re Manalad*, 360 B.R. at 310 ("It makes more sense to minimize the negative consequences on a credit report by allowing debtors who do not obtain credit counseling prior to filing their bankruptcy petition to continue with their bankruptcy case rather than suffer a dismissal."); *In re Enloe*, 373 B.R. at 131 (likening credit counseling requirement to section 109(g) where dismissal was considered discretionary, and consequently refusing to dismiss debtor's case for failing to comply with section 109(h) due to debtor's counsel's oversight).

[114] *See supra* note 112 and accompanying text. *See generally In re* Dyer, 381 B.R. 200 (Bankr. W.D.N.C. 2007) (explaining congressional purpose behind section 109(h) to inform debtors about consequences of bankruptcy); *In re* Ginsberg, 354 B.R. 644, 646 (Bankr. E.D.N.Y. 2006) (noting "'potentially devestating effect'" bankruptcy can have on credit rating) (citation omitted).

[115] *See supra* notes 95–97 and accompanying text; *see also In re Manalad*, 360 B.R. at 308 (reviewing debtor's lack of better payment alternative other than bankruptcy); Mendez v. Salven (*In re* Mendez), 367 B.R. 109, 114 n.4 (B.A.P. 9th Cir. 2007) (noting "[e]xperience with the credit counseling requirement has been disappointing" and "[a] National Association of Consumer Bankruptcy Attorneys study found that only 3.3% of all consumers seen by the credit counseling firms as the required first stop under the new bankruptcy law were able to utilize the debt management plans contemplated by the new law" (quoting *In re* Parker, 351 B.R. 790, 799 n.8 (Bankr. N.D. Ga 2006))).

[116] FED. R. BANKR. P. 1009(a) ("A voluntary petition, list, schedule, or statement may be amended by the debtor as a matter of course at any time before the case is closed.").

[117] *See* 11 U.S.C. § 362(c)(3)(C)(i)(II)(aa) (2006).

original petition without prior counseling.[118] That court's opinion notes that allowing an amended petition saves the debtor a new filing fee ($299 in chapter 7 and $274 in chapter 13).[119]

Striking cases where the debtor does not wish to proceed and allowing an amended petition, rather than dismissal and refilling where the debtor wants to go forward, are the best remedies for other reasons. The 2005 law provides for the automatic stay to lift after 30 days if the debtor filed a previous case in the last year that was dismissed, unless the debtor shows by clear and convincing evidence that the second filing is in good faith.[120] If the debtor filed two previous cases in the past year that were dismissed, the debtor does not get the benefit of an automatic stay and only gets a stay by requesting one within 30 days of filing and demonstrating good faith by clear and convincing evidence.[121] These consequences for the automatic stay of dismissed cases make it inappropriate to dismiss a case due to an oversight of not meeting the counseling requirement. The effect would not be to protect consumer debtors but rather to burden them with extra costs in a new case. Dismissal and refiling could add significantly to the cost of a case if an attorney must appear to show by clear and convincing evidence that the second case was filed in good faith in order to keep or get a stay in place.[122]

The debt relief agency provisions were also intended as consumer protections.[123] There has been some doubt about whether these provisions apply to

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[118] *See In re* Anderson, 391 B.R. 758, 759–60 (Bankr. S.D. Tex. 2008) (allowing amended petition after debtor received credit counseling (citing H.R. REP. NO. 109-31, pt. 1, at 104 (2005)). *Anderson* follows an earlier case from that district stating that there is no case when an ineligible debtor files a petition. *See In re* Salazar, 339 B.R. 622 (Bankr. S.D. Tex. 2006). This could mean no automatic stay is in place, but this would only matter if the creditor took actions that would violate a stay before the debtor can cure ineligibility. It might be preferable to view the case as filed, with an automatic stay in place, until stricken, if that is what the debtor wants after getting counseling.

[119] *See In re Anderson*, 391 B.R. at 760 ("[The debtors] seek for the Court to recognize the amended petition in order to avoid the necessity of paying an additional filing fee."). *See generally* GAO, DOLLAR COSTS REPORT, *supra* note 24, at 5 (noting cost of filing fees for chapter 13 and chapter 7 filers after Deficit Reduction Act of 2005); Braucher, *Bench and Bar, supra* note 107, at 107 (noting that a lack of credit counseling is "a curable defect").

[120] 11 U.S.C. § 362(c)(3) (2006). *Compare In re* Rumbough, No. 6:07-bk-02298-ABB, 2007 WL 4348071, at *1 (Bankr. M.D. Fla. July, 25, 2007) (confirming termination of automatic stay 30 days after second filing), *with In re* Corbin, No. 05-90280-SD, 2006 WL 5737842, at *3 (Bankr. D. Md. Jan. 19, 2006) (extending automatic stay due to debtor's showing by clear and convincing evidence that second filing was in good faith).

[121] 11 U.S.C. § 362(c)(4)(D) (2006) ("[A] case is presumptively filed not in good faith (but such presumption may be rebutted by clear and convincing evidence to the contrary)."). *Compare In re* Schroeder, 356 B.R. 812, 813 (Bankr. M.D. Fla. 2006) (granting automatic stay motion to debtors who showed good faith in their third filing), *with In re* Thornes, 386 B.R. 903, 910–11 (Bankr. S.D. Ga. 2007) (denying automatic stay to debtor for failure to show good faith in third filing by clear and convincing evidence).

[122] *See* Braucher, *Bench and Bar, supra* note 107, at 109 (noting "the advantage of allowing an amended petition, rather than requiring the filing of a new case, is that the debtor can avoid a new filing fee" and that "[f]iling fees have gone up and are not cheap").

[123] *See* H.R. REP. NO. 109-31, *supra* note 2, at 17 (describing how debt relief agency provisions "strengthen[] professionalism standards for attorneys and others who assist consumer debtors with their bankruptcy cases").

lawyers, with a split in the authority.[124] Assuming that they do, as more cases have been holding, some of those provisions represent practices that attorneys would be well advised to follow anyway (such as offering clients written contracts specifying the services to be provided),[125] while others are quite problematic or even unconstitutional.[126]

The DRA provisions, together with many other new complexities of the new law, discouraged some lawyers from continuing in this field. The definition of "debt relief agency" seems to say that providing "bankruptcy assistance" in one case could make a lawyer into a DRA, with no time limit[127] and attendant disclosure and substantive requirements applicable. It is a common observation in the bankruptcy world that this aspect of the new law helped to drive out lawyers who only did an occasional case;[128] it just was not worth their while to undertake the cost of compliance (along with the cost of figuring out how to practice in general under the much changed new law). Furthermore, as we will see, the obvious defects in the disclosure scheme tended to tip the balance for lawyers considering whether to continue in the field.[129]

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[124] *Compare* Milavetz, Gallop & Milavetz, P.A. v. United States, 541 F.3d 785, 797 (8th Cir. 2008) (finding attorneys providing bankruptcy assistance to "assisted persons" are debt relief agencies), *and* Conn. Bar Ass'n v. United States, 394 B.R. 274, 280 (D. Conn. 2008) (reading statute for its "plain meaning" that attorneys are debt relief agencies), *with In re* Attorneys at Law and Debt Relief Agencies, 332 B.R. 66, 71 (Bankr. S.D. Ga. 2005) (finding attorneys are not debt relief agencies "so long as their activities fall within the scope of the practice of law and do not constitute a separate commercial enterprise"), *and In re* Reyes, 361 B.R. 276, 281 (Bankr. S.D. Fla. 2007) (finding debtor's counsel provided service pro bono and thus did not fall within debt relief agency category).

[125] *See* 11 U.S.C. § 528(a)(1) (2006) (setting forth requirement of written contract); *see also* Braucher, *Bench and Bar*, *supra* note 107, at 137 (discussing limitations on advice attorneys can offer prior to signing contract along with other ramifications of contract requirement). *See generally In re* Robinson, 368 B.R. 492, 500 n.7 (Bankr. E.D. Va. 2007) ("[T]here can be little doubt that the requirement for a written contract applies to attorneys representing consumer debtors and is constitutional.").

[126] *See Conn. Bar*, 394 B.R. at 284 (holding unconstitutional 11 U.S.C. § 526(a)(4) "gag rule" on attorneys advising clients to incur debt in contemplation of bankruptcy); *see also Milavetz*, 541 F.3d at 797 (finding 11 U.S.C § 526(a)(4) unconstitutional when applied to attorneys as debt relief agencies); Erwin Chemerinsky, *Constitutional Issues Posed in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 79 AM. BANKR. L.J. 571, 579 (2005) (noting section 526(a)(4) prohibits such advice even when "completely legal and even desirable for the client").

[127] *See* 11 U.S.C. § 101(12A) (2006) (neglecting to set any minimum number of cases handled in order to be debt relief agency); Sommer, *supra* note 3, at 207 (stating lack of time limit implies that representing one assisted person could make firm DRA forever); *see also* Catherine E. Vance & Corinne Cooper, *Nine Traps and One Slap: Attorney Liability under the New Bankruptcy Law*, 79 AM. BANKR. L.J. 283, 294 (2005) (questioning whether attorney volunteering to look over debtor's papers turns attorney into DRA).

[128] *See In re Attorneys at Law*, 332 B.R. at 68–70 (noting state regulation of practice of law and that preemption should not be lightly presumed, especially under the ambiguous provisions of 2005 bankruptcy law).

[129] *See* Braucher, *Bench and Bar*, *supra* note 107, at 134–35 (concerning how discouraging it is to attorneys to be required to give misleading disclosures); *see also* Claude R. Bowles, *Expecting the Unexpected: Unusual Domestic Relations Law Issues that May Arise Under the BAPCPA*, 41 FAM. L.Q. 343, 361 (2007) (discussing difficulty of disclosure compliance and impact it has on domestic relations attorneys deemed DRAs); David G. Epstein, *A Few Lines*, 55 AM. U. L. REV. 1291, 1310–11 (2006) (stating result of changes will be fewer attorneys willing to provide bankruptcy assistance to debtors).

The use of the label "debt relief agency," apparently for both attorneys and non-attorney petition preparers, could confuse the public about the difference.[130] A long standard form disclosure set forth in the statute[131] is poorly formatted and tends to give the impression that filing without a lawyer could be a good choice; most bankruptcy experts would strongly disagree; the 2005 law is very complex and full of traps for the unwary, so that filing pro se—while permitted—is an almost guaranteed recipe for making a mess of a case. Assuming applicability to lawyers and considering the consumer protection purpose of the required disclosures, courts should clarify that debtors' lawyers may improve on the communication in required disclosures, both in form and in substance. Improvements could include changes in wording or providing supplementary information.

Changed wording to clarify the message should be allowed under the statutory language permitting a "substantially similar" statement for several disclosures.[132] For example, the statute sets forth the requirement of the following disclosure or "a substantially similar statement":

> We are a debt relief agency. We help people file for bankruptcy relief under the Bankruptcy Code.[133]

Attorneys should be able to improve this statement to this:

> We are attorneys who help people file for bankruptcy relief under the Bankruptcy Code.

Petition preparers should be able to state:

> We are petition preparers who help people fill out forms to file for bankruptcy relief under the Bankruptcy Code. We are not attorneys and cannot provide legal advice.[134]

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[130] Congress seems to have been concerned about lawyers who tried to obscure the fact that chapter 13 is a form of bankruptcy, which has been a problem. *See* Jean Braucher, *Lawyers and Consumer Bankruptcy: One Code, Many Cultures*, 67 AM. BANKR. L.J. 501, 552 (1993) [hereinafter Braucher, *Lawyers and Consumer Bankruptcy*] (reviewing advertisements of bankruptcy lawyers and noting avoidance of word "bankruptcy"). However, the label "debt relief agency" is not an effective tool to accomplish this goal and may get in the way of the rest of the disclosure; some lawyers have advertised that they provide "debt relief" to avoid the negative connotations associated with the word "bankruptcy." *See id*. *See generally* David Hahn, *Velvet Bankruptcy*, 7 THEORETICAL INQUIRIES L. 523, 525 (2006) (discussing "connotation[s] of failure" and "stigma" of personal bankruptcy).

[131] 11 U.S.C. § 527(b) (2006).

[132] 11 U.S.C. §§ 527(b) & 528(a)(4) (2006); *see* Conn. Bar Ass'n. v. United States, 394 B.R. 274, 284–87 (D. Conn. 2008) (finding constitutional statutory disclosure or one "substantially similar"). *See generally* Marisa Terranova, Note, *Attorneys as Debt Relief Agencies: Constitutional Considerations*, 13 FORDHAM J. CORP. & FIN. L. 443, 462–64 (2008) (discussing constitutionality of 11 U.S.C. § 527(b)).

[133] 11 U.S.C. § 528(a)(4) (2006); *see* Olsen v. Gonzales, 350 B.R. 906, 920 (D. Or. 2006) (noting determination whether disclosure is "substantially similar" requires case-by-case determination).

The specific phrase "debt relief agency" should not be required because it is not clear (and may sound like a government agency, but at any rate certainly does not immediately make a reader think that the "agency" might be a bankruptcy lawyer in private practice).

A long model disclosure set forth in the statute states:

> IMPORTANT INFORMATION ABOUT BANKRUPTCY ASSISTANCE SERVICES FROM AN ATTORNEY OR BANKRUPTCY PETITION PREPARER.
>
> If you decide to seek bankruptcy relief, you can represent yourself, you can hire an attorney to represent you, or you can get help in some localities from a bankruptcy petition preparer who is not an attorney. THE LAW REQUIRES AN ATTORNEY OR BANKRUPTCY PETITION PREPARER TO GIVE YOU A WRITTEN CONTRACT SPECIFYING WHAT THE ATTORNEY OR BANKRUPTCY PETITION PREPARER WILL DO FOR YOU AND HOW MUCH IT WILL COST. Ask to see the contract before you hire anyone.
>
> The following information helps you understand what must be done in a routine bankruptcy case to help you evaluate how much service you need. Although bankruptcy can be complex, many cases are routine.
>
> Before filing a bankruptcy case, either you or your attorney should analyze your eligibility for different forms of debt relief available under the Bankruptcy Code and which form of relief is most likely to be beneficial for you. Be sure you understand the relief you can obtain and its limitations. To file a bankruptcy case, documents called a Petition, Schedules and Statement of Financial Affairs, as well as in some cases a Statement of Intention need to be prepared correctly and filed with the bankruptcy court. You will have to pay a filing fee to the bankruptcy court. Once your case starts, you will have to attend the required first meeting of creditors where you may be questioned by a court official called a 'trustee' and by creditors.
>
> If you choose to file a chapter 7 case, you may be asked by a creditor to reaffirm a debt. You may want help deciding whether to

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[134] One of the problems with petition preparers is that it may be impossible to fill out bankruptcy forms without providing legal advice. The forms raise many legal issues. *See In re* Hennerman, 351 B.R. 143, 151 (Bankr. D. Colo. 2006) (stating preparing forms is "inherently 'legal advice'") (citation omitted); *see also In re* Lazarus, No. 05-80274C-7D, 2005 WL 1287634, at *4 (Bankr. M.D.N.C. Mar. 14, 2005) (discussing role and limitations of petition preparers); Vance & Cooper, *supra* note 127, at 295–98 (discussing how blurred "legal advice" line is in analysis of document preparer "We The People").

> do so. A creditor is not permitted to coerce you into reaffirming your debts.
>
> If you choose to file a chapter 13 case in which you repay your creditors what you can afford over 3 to 5 years, you may also want help with preparing your chapter 13 plan and with the confirmation hearing on your plan which will be before a bankruptcy judge.
>
> If you select another type of relief under the Bankruptcy Code other than chapter 7 or chapter 13, you will want to find out what should be done from someone familiar with that type of relief.
>
> Your bankruptcy case may also involve litigation. You are generally permitted to represent yourself in litigation in bankruptcy court, but only attorneys, not bankruptcy petition preparers, can give you legal advice.[135]

Blocks of capital letters are harder to read than letters in upper and lowercase and thus represent poor formatting for consumer protection disclosures.[136] It should be permissible to change the caption and body of the form that are set forth in the statute in capital letters and instead present them in upper and lower case, with some other way to set them apart, such as bold, larger lettering and blank space to set them off.[137]

The substance of this long disclosure is also highly problematic. Although it might be possible to go through it and carefully correct misimpressions conveyed and come up with an improved alternative disclosure that is "substantially similar," as a practical matter attorneys are likely to choose to simply provide the disclosure as is. They should be able to put at the top of the page, "The following is a model disclosure set forth in the Bankruptcy Code. It was not written by anyone in our office." They should be able to supply another piece of paper correcting inaccuracies, such as that "You will have to pay a filing fee to the bankruptcy court," when in fact, the 2005 law provides for some low-income debtors to file without paying a filing fee.[138] Furthermore, attorneys are likely to disagree with the implications of the model disclosure form that "you can represent yourself" or "you

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[135] 11 U.S.C. § 527(b) (2006); *see* 3 COLLIER ON BANKRUPTCY, ¶ 527.03, at 527-10–527-11 (Alan N. Resnick et al. eds., 15th ed. rev. 2006) (discussing ambiguities in statute and noting it is unclear, unworkable, and misleading); Braucher, *Bench and Bar*, *supra* note 107, at 135 (noting errors in long disclosure).

[136] *See* KAREN A. SCHRIVER, DYNAMICS IN DOCUMENT DESIGN: CREATING TEXT FOR READERS 274 (John Wiley & Sons Inc. 1997) (listing studies showing text in all capital letters is less legible than text in upper and lower case letters).

[137] *See id*. ("Reading speed is optimal when uppercase and lowercase letters are used . . . [w]hen extra emphasis is needed, bold has been found to be a better cue than uppercase.").

[138] 28 U.S.C. § 1930(f) (2006) (providing for fee waiver). Another factual error is contained in 11 U.S.C. § 527(a)(2)(B) (2006), requiring disclosure of the "replacement value of each asset as defined in section 506." Section 506 concerns valuation of secured claims; it does not apply to all assets of a debtor, and exempt assets are to be valued instead on the basis of "fair market value." 11 U.S.C. §§ 506, 522(a)(2) (2006).

can get help in some localities from a bankruptcy petition preparer who is not an attorney" and that, "The following information helps . . . you evaluate how much service you need. Although bankruptcy can be complex, many cases are routine."[139] Lawyers should be able to state their views that filing without a lawyer is very risky and that using a petition preparer is not a good solution because only a lawyer will be able to identify whether many new complexities apply, such as use of the exemption list of another state because the debtor moved with 730 days[140] or nondischargeability of debts under nineteen separate paragraphs of section 523(a),[141] including child support obligations, certain tax obligations, and certain recently incurred debts (categories that apply in cases that might otherwise be considered "routine"). Lawyers will also be able to avoid pitfalls such as "automatic dismissal" for failing to provide certain paperwork, a problem that arises in "routine" pro se cases. If pro se cases were ever a good idea, this is no longer the case; debtors need lawyers to have a good chance of navigating the Bankruptcy Code post-2005. The information in the model disclosure does not in fact help a consumer debtor to evaluate "how much service you need."

There is a plausible case to be made that the requirement of the long disclosure form or something substantially similar involves compelled speech contrary to considered and wise professional judgment.[142] It is not an ideal solution to require debtors' lawyers to make a disclosure with misleading statements and then attempt to correct the misconceptions thus induced. This policy point could be used to shore up an interpretation that the DRA provisions do not apply to lawyers or that they are unconstitutional compelled speech because they are misleading. Alternatively, courts should allow better communication, either by supplementary documents or by rewriting the model disclosure in the statute to better comport with good legal advice.

One DRA provision has been held unconstitutional by numerous courts as applied to attorneys.[143] This provision bars DRAs from advising clients to incur debt in contemplation of bankruptcy, including payment of a fee for services of a

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[139] 11 U.S.C. § 527(b) (2006); *see* Braucher, *Bench and Bar*, *supra* note 107 at 135–36 ("[T]he 2005 Act has created so many traps that even a sophisticated debtor would have trouble negotiating them without an attorney.").

[140] 11 U.S.C. § 522(b)(3)(A) (2006).

[141] 11 U.S.C. § 523(a) (2006).

[142] Chemerinsky, *supra* note 126, at 577–78 (noting those objecting to disclosure requirements under sections 527 and 528 "are likely to argue that they violate First Amendment because they are not 'narrowly drawn' and . . . increase likelihood of misleading speech"). *But see* Robin Huffman, *Bankruptcy and Free Speech: New Bankruptcy Code Provisions Restrict Attorneys' Right to Properly Advise Clients*, 35 HASTINGS CONST. L.Q. 118, 131 (2007) (concluding "[t]he requirements of section 527, while possibly cumbersome for some attorneys, pass constitutional scrutiny under an undue burden test").

[143] 11 U.S.C. § 526(a)(4) (2006); *see supra* note 126 (citing two cases so holding); *see also* Zelotes v. Adams, 363 B.R. 660, 665 (D. Conn. 2007) (finding section 526(a)(4) "prohibits attorneys from advising their clients to take various lawful, financially prudent actions prior to filing for bankruptcy" and "these actions may even prevent the bankruptcy in the first place").

petition preparer or attorney.[144] Attorneys should not feel bound to comply with this provision, but obviously repeal or a Supreme Court decision in accord would add to their comfort in making that choice. In general, only Congress can completely fix problems with the credit counseling, financial education and DRA provisions, but the burden of these provisions can be ameliorated by judicial interpretation sensitive to their consumer protection purposes.

B. Provisions with Abuse Prevention Purposes

Abuse prevention is obviously a central purpose of the 2005 law. This purpose is reflected in the presumed abuse means test used in both chapter 7 and chapter 13,[145] discussed below, and in such provisions as those capping the homestead exemption in some cases.[146] It is also reflected in new paperwork requirements, such as the requirement of supplying payment advices (pay stubs) for the last six months.[147] Implicit in the purpose to prevent abuse is also a purpose not to impede nonabusers, who are, as *Marrama* stressed, the "vast majority" of chapter 7 filers.[148]

The paperwork requirements of section 521(a)(1) are enforced with a very strange remedy: cases are "automatically" dismissed 46 days after the filing of a petition if the paperwork is not filed within 45 days.[149] This concept of automatic dismissal has been a head-scratcher for the courts, particularly since the law also provides for parties in interest to request an order of dismissal for cases

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[144] 11 U.S.C. § 526(a)(4) (2006).

[145] *See* 11 U.S.C. § 707(b)(2) (2006) (containing elaborate test for presumed abuse); 11 U.S.C. § 1325(b)(3) (2006) (providing for use of presumed abuse expenses in disposable income calculation for debtors above median income); *In re* McVay, 371 B.R. 190, 201 n.11 (Bankr. W.D. Tex. 2007) (noting section 707(b)(2) was changed from presumption in favor of debtor to presumption of abuse).

[146] *See* 11 U.S.C. § 522(o)–(q) (2006) (listing limitations on homestead exemption); Wallace v. Rogers (*In re* Rogers), 513 F.3d 212, 217 (5th Cir. 2008) ("Enacted as part of BAPCPA, 11 U.S.C. § 522(p)(1) limits the state law homestead exemption under certain circumstances."). Unfortunately, the provision generally requiring debtors to use exemptions from a state they moved from until they are domiciled in their new home for 730 days has complicated the job of bankruptcy attorneys by requiring them to use other states' exemptions in many more cases. 11 U.S.C. § 522(b)(3)(A) (2006).

[147] *See* 11 U.S.C. § 521(a)(1) (2006); *In re* Calhoun, 359 B.R. 738, 739 (Bankr. E.D. Mo. 2007) ("The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA") requires debtors, unless otherwise directed by the Court, to file copies of all payment advices received within the 60 days before the petition date."); *In re* Luders, 356 B.R. 671, 673 (Bankr. W.D. Va. 2006) (citing 11 U.S.C. § 521(i) (2006), mandating dismissal of petition if advices not filed within 45 days).

[148] *See* Marrama v. Citizens Bank of Mass., 549 U.S. 365, 127 S. Ct. 1105, 1111 (2007) ("The class of honest but unfortunate debtors who do possess an absolute right to convert their cases from Chapter 7 to Chapter 13 includes the vast majority of the hundreds of thousands of individuals who file Chapter 7 petitions each year."); *see also* Braucher, *A Fresh Start*, *supra* note 21, at 1305–06 (noting 2005 law was presented to Congress as way to stop abuse, not impede filing for all debtors); A. Mechele Dickerson, *Regulating Bankruptcy: Public Choice, Ideology, & Beyond*, 84 WASH. U. L. REV. 1861, 1869 (2006) (noting even strong supporters of 2005 law recognized class of debtors whose debt was incurred without fault and who deserved quick discharge).

[149] *See* 11 U.S.C. § 521(a)(1), (i)(1) (2006); *In re* Hall, 368 B.R. 595, 598–99 (Bankr. W.D. Tex. 2007) (maintaining 45-day dismissal provision is to be read literally).

automatically dismissed[150] and also because all of the required paperwork, except the list of creditors, can be dispensed with if "the court orders otherwise."[151] The better view is to require an order of dismissal for automatic dismissal to occur[152] and to treat non-dismissal for failure to file required paperwork as res judicata after entry of a final order in a case.[153]

The abuse-prevention centerpiece of the 2005 law is means testing under a complicated "presumed abuse" test.[154] The idea was to exclude from chapter 7 those debtors with relatively higher incomes and the ability to repay some debt and thus push them into repayment plans in chapter 13.[155] Congress received submissions indicating that, depending on various assumptions, the portion of debtors in chapter 7 who could afford to pay a significant amount of their old debt ranged from twenty-five percent to low single digits.[156]

Congress chose median income as the threshold for presumed abuse testing,[157] meaning anyone at or below median income could not be a presumed abuser. The 2005 law also incorporated presumed abuse means testing into chapter 13 for above-median-income debtors, who must calculate amounts available to fund their plans using the expense formula of chapter 7 means testing.[158]

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[150] *See* 11 U.S.C. § 521(i)(2) (2006); *In re Luders*, 356 B.R. at 673, 673 n.4 (noting apparent conflict between sections 522(i)(1) and 522(i)(2)). *But see In re* Fawson, 338 B.R. 505, 510 (Bankr. D. Utah 2006) (holding provision for automatic dismissal and provision allowing party to request dismissal are consistent).

[151] 11 U.S.C. § 521(a)(1)(A), (B) (2006).

[152] *See In re* Spencer, 388 B.R. 418, 421 (Bankr. D.D.C. 2008) (stating section 521(i)(1) "does not mean that when § 521(i)(1) is triggered, the case **stands** automatically dismissed . . . ."); *In re* Parker, 351 B.R. 790, 801 (Bankr. N.D. Ga. 2006) (reasoning truly automatic dismissal would render section 521(i)(2) "mere surplusage"); *see also In re* Manalad, 360 B.R. 288, 296 & n.23 (Bankr. C.D. Cal. 2007) (referring readers to *Parker* for analysis of section 521(i) and automatic dismissal).

[153] *See In re* Ober, 390 B.R. 60, 64 (Bankr. W.D.N.Y. 2008) (holding res judicata doctrine precluded challenges to confirmation order premised on argument case had automatically been dismissed when trustees and creditors failed to object to plan confirmation); *see also* Montana v. United States, 440 U.S. 147, 153–54 (1979) (presenting rationales for precluding parties from relitigating issues "they have had a full and fair opportunity to litigate").

[154] 11 U.S.C. § 707(b)(2) (2006). *See* Perlin v. Hitachi Capital Am. Corp., 497 F.3d 364, 369 (3d Cir. 2007) (stating section 707(b) "create[s] a presumption of abuse against [consumer] debtors . . . who have sufficient income to repay their debts"); *see also In re* Naut, No. 07-20280REF, 2008 WL 191297, at *14 (Bankr. E.D. Pa. Jan. 22, 2008) (concluding application of section 707(b) means test subjected debtor to presumption of abuse).

[155] 11 U.S.C. § 707(b)(1)–(2) (2006); *see* H.R. REP. NO. 109-31, *supra* note 2, at 12 (explaining "needs-based" reforms would move debtors from chapter 7 to chapter 13, thus increasing payments to creditors and noting some courts did not consider debtor's "ability to repay a significant portion of his or her debts out of his or her future income" as substantial abuse under pre-reform Code).

[156] H.R. REP. NO. 109-31, *supra* note 2, at 5 n.18 (listing statistics pertaining to percentage of debtors with at least some ability to repay debts).

[157] *See* 11 U.S.C. § 707(b)(7) (2006) (setting presumptive-abuse level above median income); Schultz v. United States, 529 F.3d 343, 347 (6th Cir. 2008) ("If the debtor's current monthly income is equal to or below the median, then the presumption of abuse does not arise."); *In re* Harr, 360 B.R. 759, 761–62 (Bankr. N.D. Ohio 2007) (holding only above-median-income debtors may be subject to presumption of abuse).

[158] *See* 11 U.S.C. § 1325(b) (2006); *In re* May, 390 B.R. 338, 340–41 (Bankr. S.D. Ohio 2008) (recognizing section 1325(b) requires above-median-income debtors to use chapter 7 means test to determine disposable income); *In re* Crego, 387 B.R. 225, 228 (Bankr. E.D. Wis. 2008) ("At least for above-median

As we shall see, presumed abuse means-testing catches only a small number of debtors in either chapter.[159] Congress apparently thought many above-median-income debtors with means to repay old debt were getting a discharge in chapter 7 and that, in chapter 13, above-median-income debtors were not committing as much as they should to unsecured creditors. To deal with assumptions about these categories of abuse, Congress created an elaborate means testing formula, but it has turned out to affect few debtors.[160] In other words, there is little of the abuse Congress apparently targeted. The solution to congressional empirical error, however, should not necessarily be for the bankruptcy courts to make up their own more demanding tests, district by district and case by case.

In the first years under the new law, only eight or nine percent of chapter 7 debtors were above median income, the threshold for any possibility of presumed abuse.[161] Furthermore, being above median income does not usually force a debtor into chapter 13. Ninety percent of the above-median chapter 7 debtors in the first year and a half under the 2005 law passed the presumed abused test,[162] probably due to a combination of factors, such as high secured-debt payments (which are added to expenses),[163] income that is not much over median,[164] and use of IRS expense standards that are forgiving compared to what most debtors try to live on.[165]

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debtors, the [2005 law's] amendments to [c]hapter 13 redefine disposable income to mirror the outcome under the [c]hapter 7 means test.").

[159] *See infra* notes 161–78 and accompanying text (discussing how means test is ineffective way of catching debtors).

[160] *See* 11 U.S.C. § 707(b)(2) (2006) (detailing presumed-abuse-means-testing formula); *infra* notes 161–78 and accompanying text (describing method used in means testing and its flaws); *cf. In re* Barr, 341 B.R. 181, 185 (Bankr. M.D.N.C. 2006) (acknowledging many sources doubt effectiveness of means testing to prevent abuse).

[161] *See* White, *Year 2*, *supra* note 101, at 16 (reporting that, from October 2005 to March 2007, "[o]f chapter 7 debtors, 7.9 percent have income above the applicable state median income"); *see also* Clifford J. White III, *Update on the United States Trustee Program's Implementation and Enforcement of the BAPCPA*, 26 AM. BANKR. INST. J. 14, 14 (Nov. 2007) [hereinafter White, *Update*] (reporting that, from October 1, 2006 to June 30, 2007, "approximately 9 percent of chapter 7 debtors had income above their state median").

[162] *See* White, *Year 2*, *supra* note 101, at 16 (stating that, from October 2005–March 2007, 9.5 percent of above-median-income debtors in chapter 7 were presumed abusive); White, *Update*, *supra* note 161, at 14 (reporting that approximately 10 percent of above-median-income chapter 7 debtors were presumed abusive.).

[163] 11 U.S.C. § 707(b)(2)(A)(iii) (2006) (permitting debtors to deduct monthly secured debt payments contractually due).

[164] Historically, the curve of debtor income has tailed off rapidly above median income. *See* Jean Braucher and Charles W. Mooney Jr., *Means Measurement Rather Than Means Testing*, 22 AM. BANKR. INST. J. 6, 57 n.3 (Feb. 2003) (reporting data from research of Ed Flynn and Gordan Bermant showing median income of chapter 7 debtors who filed in 2000 to be $26,400, with 60th percentile of $30,492, 70th percentile of $36,000, 80th percentile of $42,000, 90th percentile of $81,180, and 99th percentile of $95,508). *See infra* notes 171, 187 and accompanying text (concerning evidence that the income patterns are the same post-2005 law).

[165] *See* Eugene R. Wedoff, *Means Testing in the New § 707(b)*, 79 AM. BANKR. L.J. 231, 255 (2005) ("[E]ven hypothetical taxpayers living in the Garden of Eden, with cost-free satisfaction of all their basic needs, would still be allowed a deduction from their income in the total amount set out in the National Standards."); Charles J. Tabb & Jillian K. McClelland, *Living With the Means Test*, 31 S. ILL. U. L.J. 463,

Furthermore, above-median-income debtors in chapter 7 who "flunk" the presumed abuse test can choose to attempt rebuttal based on special circumstances that justify additional expenses or that result in reduced real income, to overcome exclusion from chapter 7 on the basis of the backward-looking formula of the presumed abuse test.[166] Presumably anticipating successful rebuttal, in the first eighteen months of means testing, the US Trustee system exercised its discretion not to challenge twenty percent of presumed abusers in chapter 7, a figure that went up to thirty percent in the nine months ending June 30, 2007.[167] The 2005 law also provides for dismissal from chapter 7 for abuse based on the "totality of the circumstances" or "bad faith,"[168] but in the early period under the law, the US trustee system has not frequently found grounds for such challenges; it was bringing abuse challenges, presumed as well as on discretionary grounds, in only one in 140 chapter 7 cases (about .7 percent).[169]

Even in chapter 13, according to EOUST figures for the first year and a half under the new law, means testing was not a driving reason or concern for nearly three-quarters of filers.[170] Only twenty-seven percent of chapter 13 filers had above

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478 (2007) (noting debtors may use IRS monthly expense amount even if it exceeds debtor's actual expenses).

[166] *See* 11 U.S.C. § 707(b)(2)(B) (2006) ("[P]resumption of abuse may only be rebutted by demonstrating special circumstances . . . ."); *see also In re* Close, 384 B.R. 856, 860 (Bankr. D. Kan. 2008) (noting need to rebut presumption of abuse with special circumstances). Because income under the means test is based on a six-month look back, it will be too high for those whose income has gone down in the last six months. *See* 11 U.S.C. § 101(10A) (2006) (defining "current monthly income," used in section 707(b)(2)(A)(i)); *see also In re* Celedio, No. 07-31389 TEC, 2008 WL 2557475 at *1 (Bankr. N.D. Cal. June 23, 2008) (interpreting section 101(10A)); *In re* Hayes, 376 B.R. 55, 65 (Bankr. D. Mass 2007) ("[I]ncome . . . is calculated based on the debtor's actual income received in the six months prior to the petition filing.").

[167] White, *Year 2*, *supra* note 101, at 16 (noting U.S. Trustees decided not to file motion to dismiss in about twenty percent of chapter 7 presumed-abuse cases); White, *Update*, *supra* note 161, at 68 (noting use of "statutory discretion to decline to file motions in about 30 percent of the 'presumed-abusive' cases"). *See* Tabb & McClelland, *supra* note 165, at 514 (discussing testimony from Acting Director of Executive Office of U.S. Trustees stating trustees chose not to challenge all presumed-abusive debtors).

[168] 11 U.S.C. § 707(b)(3) (2006); *see In re* Patterson, 392 B.R. 497, 502 (Bankr. S.D. Fla. 2008) (stating courts may dismiss chapter 7 cases under section 707(b)(3) if debtor filed in bad faith or "if the totality of circumstances of the debtor's financial situation demonstrates abuse"); *see also In re* Zaporski, 366 B.R. 758, 768 (Bankr. E.D. Mich. 2007) (acknowledging trustee can request section 707(b)(3) dismissal "for bad faith or based on a totality of circumstances").

[169] White, *Year 2*, *supra* note 101, at 16. *Cf. In re* Glunk, 342 B.R. 717, 732 (Bankr. E.D. Pa. 2006) (stating "bad faith dismissal doctrine in chapter 7 cases is a narrow doctrine, which should be employed only in extreme cases to protect the integrity of the bankruptcy system"); Tamecki v. Frank (*In re* Tamecki), 229 F.3d 205, 209 (3d Cir. 2000) (Rendell, J., dissenting) ("[B]ankruptcy and district courts have reserved bad faith dismissal for the truly egregious case . . . .").

[170] *See* White, *Year 2*, *supra* note 101, at 16; *see also* Elijah M. Alper, *Opportunistic Informal Bankruptcy: How BAPCPA May Fail To Make Wealthy Debtors Pay Up*, 107 COLUM. L. REV. 1908, 1931 (2007) ("[T]here is considerable doubt over whether the means test will have any practical effect in deterring opportunistic debtors from bankruptcy."); Marianne B. Culhane & Michaela M. White, *Catching Can-Pay Debtors: Is the Means Test the Only Way?*, 13 AM. BANKR. INST. L. REV. 665, 668 (2005) ("The means test . . . may deter or dismiss relatively few would-be chapter 7 debtors.").

median income,[171] which means they were not pushed into chapter 13 by presumed abuse means testing and not governed there by the expense guidelines of means testing. Rather, they were subject to the approach, carried over from pre-2005 law, of looking at whether there is disposable income after deduction of "reasonably necessary" expenses for the support of the debtor and the debtor's dependents.[172] Probably even most of the twenty-seven percent of chapter 13 filers above median income would have passed presumed abuse review in chapter 7 (based on their allowed deductions for expenses, particularly for regular secured debts payments as well as arrearages on secured debts, both of which can be deducted, along with a percentage figure to reflect trustee fees they pay in chapter 13).[173] Certainly for chapter 13 debtors at or below median income and probably for nearly all chapter 13 debtors, what drives them into chapter 13 is not failing the presumed abuse means test, but—as before the changes in the law—such considerations as being behind on secured debts (so that chapter 13 is needed to retain collateral), paying attorneys fees over time, and a desire to repay creditors as much as possible even though more debt could be discharged in chapter 7.[174]

The 2005 law provides for use of the expense list of the chapter 7 presumed abuse test for above-median-income chapter 13 debtors, and it has turned out that

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[171] White, *Year 2*, *supra* note 101, at 16. *See* Robert M. Lawless et al., *Did Bankruptcy Reform Fail? An Empirical Study of Consumer Debtors*, 82 AM. BANKR. L.J. 349, 354, 361, 369, 375–77 (2008) (in national random sample of debtors who filed in February and March 2007, compared to previous studies of debtors who filed in 1981, 1991 and 2001, finding 2007 debtors' household incomes, adjusted for inflation, were "essentially indistinguishable from the incomes of those filing in 2001 and 1991," with 2007 medians of $23,136 in chapter 7 and $35,688 in chapter 13, and also finding that debts were substantially higher in 2007, with 2007 debtors having, at the median in inflation-adjusted dollars, more than twice the negative net worth of 1981 debtors, meaning they were "in more desperate financial shape than their counterparts of earlier years"). Lawless et al. also discuss "the missing 800,000 families" in 2007, referring to the fact that half the number filed in 2007 compared to the period preceding 2005, and conclude that the most likely scenario, given the similarity of those who filed in 2001 and 2007, is that the missing families had income and debts like those who did file in 2007, meaning they had no higher incomes than in 2001 but much more debt and that the 2005 law randomly sorted some families out of receiving bankruptcy relief. *Id.* at 375–77.

[172] *See* 11 U.S.C. § 1325(b)(1)–(2) (2006) (stating court shall approve plan as long as all disposable monthly income is applied to make payments to unsecured creditors and disposable income includes all income not reasonably necessary for the maintenance and support of the debtor and his dependents).

[173] 11 U.S.C. § 707(b)(2)(A)(ii)–(iv) (2006) (detailing allowable deductions).

[174] U.S. DEPARTMENT OF JUSTICE, EXECUTIVE OFFICE OF THE U.S. TRUSTEES, REPORT TO CONGRESS: IMPACT OF THE UTILIZATION OF INTERNAL REVENUE STANDARDS ON DEBTORS AND THE COURT [sic] 4 (2007) [hereinafter EOUST, *Report to Congress*], http://www.usdoj.gov/ust/eo/public_affairs/reports_studies/docs/Rpt_to_Congress_on_IRS_Standards.pdf; RAND Institute for Civil Justice, *The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005: Evaluation of the Effects of Using IRS Expense Standards to Calculate a Debtor's Monthly Disposable Income*, in EOUST, *Report to Congress*, *supra*, 24, 42 [hereinafter *RAND Study*] (noting arrearages on secured debts, paying attorneys fees in the plan, and "responsibility-to-pay culture" as reasons below-median-income debtors file in chapter 13). Steering by attorneys for no particularly good reason may also continue to be a problem. *See* William C. Whitford, *The Ideal of Individualized Justice: Consumer Bankruptcy as Consumer Protection, and Consumer Protection in Consumer Bankruptcy*, 68 AM. BANKR. L.J. 397 (1994) (concerning problem of debtors' attorneys steering them into chapter 13 when a quick discharge in chapter 7 might be more appropriate).

the formula requires less payment in chapter 13 than under pre-2005 law.[175] The initial empirical results are in on this point: in a government-commissioned study mandated by the 2005 law, it was determined that the use in chapter 13 of the IRS expense standards incorporated into presumed abuse means testing has the effect of allowing above-median-income chapter 13 debtors to pay less than their reported actual expenses, with the advantage greater for the lower-end of the above-median income group.[176] On average, above-median-income chapter 13 debtors in the study had $490 less in actual reported expenses a month than the IRS standards allowed.[177] Only seventeen percent had greater reported actual expenses than the IRS amounts,[178] meaning more than eighty percent of above-median-income chapter 13 debtors are required to pay less than if their disposable income were determined according to pre-2005 law. In short, Congress chose an elaborate presumed-abuse test that most of the time does not require more repayment in chapter 13 by above-median-income debtors.

It is important to stress that these results do not mean debtors actually had the excess income that their schedules I (for income) and J (for expenses) reported. Debtors in bankruptcy are not great budgeters of their real expenses, and many stretch to pay for collateral and thus understate their other expenses to make their plans add up.[179] Failure to complete plans has been a problem for a long time,[180] and it may be that IRS standards are more realistic than debtors' budgets about what they need to live on.

Debtors who file in bankruptcy are often not realistic about budgeting, before or after filing, and lawyers should help them to list all their real expenses to make their plans sustainable in chapter 13 and to minimize conflict with trustees in either chapter 7 or chapter 13. This need to budget realistically for all expenses to avoid means testing issues is among the many reasons that filing *pro se* is a bad idea;[181]

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[175] *See* EOUST, *Report to Congress*, *supra* note 174, at 4 (reporting that calculating disposable income under IRS Standards is advantageous to chapter 13 debtors because "debtors are required to repay less money to creditors than under the pre-BAPCPA system"); *see also* Culhane & White, *supra* note 170, at 681–82 (remarking new definition of disposable income allows some chapter 13 debtors to pay less than under pre-2005 judicial tests).

[176] *See* EOUST, *Report to Congress*, *supra* note 174, at 3–4 (reporting that study of chapter 13 debtors who filed between April and November of 2006 showed those above median were allowed, "on average, $490 in expenses above the amount that debtors report they actually spend" and those with lower income are benefited more); White, *Year 2*, *supra* note 101, at 16 (stating lower-income–above-median–chapter-13 debtors benefited most from use of IRS Standards).

[177] *See* EOUST, *Report to Congress*, *supra* note 174, at 4; *see also* Tabb & McClelland, *supra* note 165, at 478 ("[D]ebtors may use the 'monthly expense amounts specified' by the IRS, *even if* those are higher than the debtor's actual expenses in those categories.").

[178] *See RAND Study*, *supra* note 174, at 29, Table 4.4 (2007).

[179] *See* Braucher, *Debtor Education*, *supra* note 102, at 565 (indicating successful chapter 13 plan requires debtor to create realistic budget).

[180] Scott F. Norberg & Andrew J. Velkey, *Debtor Discharge and Creditor Repayment in Chapter 13*, 39 CREIGHTON L. REV. 473, 476 (2006) (reporting in seven-district study, 33% discharge rate for chapter 13 debtors who filed in 1994).

[181] *See supra* notes 139–41 and accompanying text (concerning other reasons *pro se* filing is risky).

good lawyers gradually are learning to have debtors take expenses permitted under presumed abuse means testing and put them in schedule J.[182]

Congress sought to push more payment in chapter 13 but chose a test that has had small, but not trace, effect in excluding debtors from chapter 7 or making them pay more in chapter 13 than they otherwise would have. The rate of US Trustee abuse challenges in chapter 7 increased from one in 274 to one in 140, nearly double the pre-2005 rate.[183] In addition, about seventeen percent of above-median-income chapter 13 debtors (which means about 4.6 percent of all chapter 13 debtors) have to pay more in their plans than under prior law.[184] If Congress thought that the impact of its means testing would be greater, it was mistaken. This does not necessarily mean, however, that the courts should expand the reach of the statute. An alternative possible conclusion is that there is less abuse than supporters of means testing imagined, a point made by nearly all bankruptcy experts before the law was passed.[185]

As noted, very few debtors who file in chapter 7 are subject to dismissal for presumed abuse, either because they are below median income or because permitted expense deductions allow them to pass the presumed-abuse test.[186] One might conclude that means testing is a success because those with incomes above median who do not have expense deductions that allow them to pass the means test now file in chapter 13, bypassing any chance of dismissal in chapter 7. It is true that a low rate of dismissal for presumed abuse in chapter 7 does not necessarily show means testing has little impact in sorting between the two chapters. However, other information indicates that means testing has only marginal effect in chapter choice. Most debtors in both chapters have been and continue to be below median income.[187] Many debtors file in chapter 13 to save collateral when they are behind

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[182] Forms 22A and C permit many expenses that it would be wise to put on schedule J. *See* CHAPTER 7 STATEMENT OF CURRENT MONTHLY INCOME AND MEANS-TEST CALCULATION, OFFICIAL FORM 22A (01/08), http://www.uscourts.gov/rules/BK_Forms_08_Official/B_022A_0108f.pdf; CHAPTER 13 STATEMENT OF CURRENT MONTHLY INCOME AND CALCULATIONS OF COMMITMENT PERIOD AND DISPOSABLE INCOME, OFFICIAL FORM 22C (01/08), http://www.uscourts.gov/rules/BK_Forms_08_Official/B_022C_0108f.pdf; *see also* Lisa Barbacci Afarin, *Section 1325(b)(1)(B) and the Predicament of Determining Projected Disposable Income*, 17 J. BANKR. L. & PRAC. 2 Art. 5 (Apr. 2008) (explaining schedule J); Clifford J. White III, *On Our Watch: BAPCPA Implementation Update*, 27 AM. BANKR. INST. J. 1, 68 (Feb. 2008) (explaining changes to Form 22A and C).

[183] White, *Year 2*, *supra* note 101, at 16 (reporting US trustee program filed 2,580 motions to dismiss under sections 707(b)(2), (3) from October 2005 through March 2007).

[184] *See supra* note 178. The 4.6 percent figure comes from taking seventeen percent of twenty-seven percent (the percent of chapter 13 debtors found to be above median income). *See supra* note 170 and accompanying text.

[185] *See* NBRC Report, *supra* note 22, at 89–91 (1997) (rejecting analysis of credit industry that many debtors were getting more relief than needed and that means testing of chapter 7 was indicated).

[186] *See supra* notes 161–69 and accompanying text.

[187] *See* Norberg & Velkey, *supra* note 180, at 487 (stating chapter 13 debtors in study of 1994 filings had markedly lower incomes than U.S. population as a whole, with median debtor income "less than 60% of that for all households"); *see also supra* notes 161 and 171 and accompanying text (less than ten percent of chapter 7 debtors and twenty-seven percent of chapter 13 debtors in early period under 2005 law were above

on mortgage and car payments and need to be able to make up arrearages;[188] these debtors file in chapter 13 whether or not they are above median income. Third, chapter 13 has long been used by many relatively low-income debtors who are trying to pay as much as they can there.[189]

With few high income persons attempting to access either chapter, the stakes are, thankfully, relatively low in the interpretation of the many ins and outs of the presumed abuse test, particularly in chapter 7. Not only are less than ten percent of chapter 7 debtors above median income and thus subject to the presumed abuse test,[190] but, in addition, the Bankruptcy Rules Committee implemented means testing sensibly by developing a means testing form that allows chapter 7 debtors at or below median income to stop after the first 15 lines and skip 40 additional lines, reducing their paperwork burden.[191]

The cost of means testing, however, is still significant. Lawyers for debtors have to master its intricacies and be prepared to deal with them, which has contributed to increased attorneys fees.[192] Also, the judicial system has to wrestle with the questions the complex test raises,[193] and the trustee system has many new burdens, with the result that bankruptcy filing fees as well as attorneys fees have gone up, likely driving many people away from using bankruptcy even when they are in desperate financial shape.[194]

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median income); *see also* Lawless et al., *supra* note 171, at 360–61 & fig. 2 (showing relatively low incomes of chapter 7 and 13 debtors in national sample of those filing in 2001 and 2007; 2007 median household income in chapter 7 was $23,136 and in chapter 13 was $35,688).

[188] *See* EOUST, *Report to Congress, supra* note 174 and accompanying text; Braucher, *Lawyers and Consumer Bankruptcy*, *supra* note 130, at 528 ("The major reason [that debtors file under chapter 13] is to retain collateral, particularly where the debtor is in arrears on the debt.").

[189] *See supra* note 187 and accompanying text; *see also* Braucher, *Lawyers and Consumer Bankruptcy*, *supra* note 130, at 541 (concerning complex reasons debtors attempt to repay in chapter 13); Norberg & Velkey, *supra* note 180, at 461 (noting chapter 13 debtors typically have lower-than-average incomes).

[190] *See* White, *Year 2*, *supra* note 101, at 16 (indicating 7.9 percent of chapter 7 filers from October 2005 to March 2007 had income above state median); White, *Update*, *supra* note 161, at 14 ("Between Oct. 1, 2006, and June 30, 2007, approximately 9 percent of chapter 7 debtors had income above their state median.").

[191] *See* Official Form 22A, *supra* note 182 (directing chapter 7 debtors at or below median income to skip lines 16–56); *see also* Official Form 22C, *supra* note 182 (permitting chapter 13 debtors who are at or below median income to skip lines 24–60).

[192] *See* GAO, *Dollar Costs Report*, *supra* note 24, at 21–27, 29–30 (reporting increase in attorneys' fees and filing fees); Braucher, *A Fresh Start, supra* note 21, at 1311 (detailing increased costs caused by BAPCPA); Ronald J. Mann, *Bankruptcy Reform and the "Sweat Box" of Credit Card Debt*, 2007 U. ILL. L. REV. 375, 377 (2007) (noting increase in filing costs).

[193] *See In re* Briscoe, 374 B.R. 1, 12 (Bankr. D. Col. 2007) (determining Congress "intended for debtors to use the values set forth in the Local Standards in calculating their monthly housing and utility expenses without considering how those values are used by IRS agents pursuing delinquent taxpayers"); *In re* Perfetto, 361 B.R. 27, 28 (Bankr. D.R.I. 2007) (addressing "whether § 707(b) requires the means test form, B22A, to be filed in cases voluntarily converted from Chapter 13 to Chapter 7").

[194] *See* GAO, *Dollar Costs Report*, *supra* note 24, at 29–30 and accompanying text (discussing increases in attorneys' and filing fees under the 2005 law); *see also* Robert J. Landry, III & Amy K. Yarbrough, *An Empirical Examination of the Direct Access Costs to Chapter 7 Consumer Bankruptcy: A Pilot Study in the Northern District of Alabama*, 82 AM. BANKR. L.J. 331, 335–36 (2008) ("Chapter 7 filing fees have

Although the presumed abuse test touches a low percentage of chapter 7 debtors, it still produces quite a volume of cases. For example, assuming a million consumer cases a year, 666,000 in chapter 7 and 340,000 in chapter 13—figures that approximate 2008 levels[195]—and assuming eight percent are above median income in chapter 7 and twenty-seven percent are above median income in chapter 13,[196] that means there are about 53,000 chapter 7 cases and nearly 92,000 chapter 13 cases a year in which presumed abuse means testing matters. Based on the historical pass rate of ninety percent for above median income chapter 7 debtors,[197] 4,240 in a year would flunk presumed abuse means testing, potentially raising issues. In chapter 13, all 92,000 above-median-income debtors would be subject to the presumed abuse test to determine their disposable income, a sizable pool of cases to raise means testing issues and produce considerable litigation.

In short, means testing produces plenty of devilishly complex work for the courts.[198] A set of questions that has divided the courts concerns whether, in either chapter 7 or chapter 13, to adjust the presumed abuse formula in light of reality: for example, should debtors who own cars outright still be able to take the IRS expense deduction for vehicle ownership;[199] and should owners of cars or homes who have surrendered or intend to surrender them be able to take ownership expenses.[200] One

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increased dramatically since the passage of the Reform Act."); Lawless et al., *supra* note 171, at 358, 365, 369, 375–76 (finding that 2007 debtors had similar incomes and more debt than debtors in earlier years and developing explanation that 2005 law randomly sorted out of bankruptcy half of those who would have otherwise filed in 2007 despite their desperate financial shape).

[195] *See* American Bankruptcy Institute, *Quarterly Non-business Filings by Chapter (1994–2008)*, *available at* http://www.abiworld.org/AM/AMTemplate.cfm?Section=Home&TEMPLATE=/CM/ContentDisplay.cfm &CONTENTID=54477 (last visited Oct. 26, 2008) (showing filings for first half of 2008 were about 333,000 chapter 7 cases and over 170,000 chapter 13 cases, equaling about 500,000 bankruptcy cases for first half of 2008).

[196] *See* White, *Year 2*, *supra* note 101, at 16 (showing figures for period October 2005 to March 2007).

[197] *See supra* notes 161–62 and accompanying text (concerning data that about ninety percent of above-median-income chapter 7 debtors pass presumed-abuse test and that only eight or nine percent of chapter 7 debtors are above median income).

[198] *See* GAO, *Dollar Costs*, *supra* note 24, at 14–16 ("[J]udiciary estimated that as a result of the Bankruptcy Reform Act, it takes at least 10 percent more time to process a bankruptcy case."); *see also* David Gray Carlson, *Means Testing: The Failed Bankruptcy Revolution of 2005*, 15 AM. BANKR. INST. L. REV. 223, 228 (2007) (arguing means test's most substantive effect is increased burden on judicial process); Tabb & McClelland, *supra* note 165, at 514 (questioning value of means test in light of increased burden on judiciary).

[199] *See* EOUST, *Report to Congress*, *supra* note 174, at 5 (noting "vehicle ownership expense allowance" was "area of developing case law"); *see also RAND Study*, *supra* note 174, at 15 ("The proper treatment of paid-off cars is unsettled."); Tabb & McClelland, *supra* note 165, at 486 (indicating split among courts about meaning of section 707(b)(2)(A)(ii)(I)).

[200] *See RAND Study*, *supra* note 174, at 15 ("Another question dividing the courts is whether a debtor may take an ownership expense deduction for cars and homes that the debtor plans to surrender . . . ."); *see also* David W. Allard & Katherine R. Catanese, *The Means Test, Part II: Deductions*, 26 AM. BANKR. INST. J. 14, 63 (Mar. 2007) (discussing whether debtor who intends to surrender vehicle may deduct vehicle expense); Tabb & McClelland, *supra* note 165, at 493–95 (discussing debate over whether debtor with intent to surrender may deduct).

line of argument is to adjust presumed abuse testing in light of these realities;[201] the other is to treat presumed abuse testing as mechanical, allowing certain expenses to be taken even if they will not necessarily continue or do not currently exist, with the objective being not perfect justice in each case but rough, nondiscretionary and efficient review of all cases[202] and possibly reflecting realities that would occur if a chapter 13 plan were attempted or, if a chapter 13 is in progress, are likely to come to pass at some point during a five-year plan.[203] Both the mechanical and reality-adjustment readings of section 707(b) are defensible.[204] Some courts say the

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[201] *See* EOUST, *Report to Congress*, *supra* note 174, at 5 (supporting adjustments based on debtor's actual "vehicle payment obligation to be entitled to the expense allowance"); Tabb & McClelland, *supra* note 165, at 493 (noting argument asserting debtor who "does not intend to make installment payments on his secured debt" should not be allowed deduction).

[202] *See* Whitford, *supra* note 174, at 401–03 (discussing difficulty of attaining individualized justice in consumer cases and desirability of using consumer bankruptcy to enforce consumer rights); A. Jay Cristol & Cheryl Kaplan, *11 U.S.C. § 707(b)(2)(A)(iii): Does It Mean What It Says and Say What It Means?*, 19 U. FLA. J.L. & PUB. POL'Y 1, 11–12 (2008) ("[A]lthough BAPCPA was intended to weed out those debtors who could repay a portion of their debts, the means test was also enacted to create a uniform and mechanical method for determining a certain level of 'abuse,' without regard to an individual's actual circumstances."); *see also In re* Wilkins, 370 B.R. 815, 819 (Bankr. C.D. Cal. 2007) (construing means test as "mechanical test that requires the debtor to assume as expenses certain IRS standards, rather than using the actual expenses of the debtor in these categories").

[203] *See* Carlson, *supra* note 198, at 282 ("[A] debtor eligible for chapter 13 (yet nevertheless in chapter 7) may include the 'actual' administrative expense of administering a chapter 13 plan."). Furthermore, the IRS expense amounts may be placeholders for likely expenses during the plan period, such as needing to buy a newer car on credit if the debtor has an old one owned outright at filing. *See* Carlson, *supra* note 198, at 277 ("[W]here the debtor owns the car free and clear it is probably . . . in need of replacement.").

[204] *Cf.* Sommer, *supra* note 3, at 197–98 (highlighting opposing views on how to compute transportation-expense deductions). *Compare* Tabb & McClelland, *supra* note 165, at 489 (suggesting mechanical test is a primary goal of means testing), *with In re* Edmunds, 350 B.R. 636, 649 (Bankr. D.S.C. 2006) (finding mechanical application of means test would create greater potential for "opportunistic filings"). Concerning taking an ownership expense for housing or transportation where the debtor owns the property outright, section 707(b)(2)(A)(ii)(I) refers to taking "the debtor's applicable monthly expense amounts" under the IRS national and local standards used in means testing (and covering housing and transportation), and the "the debtor's actual monthly expenses" for certain other categories of expenses for which the IRS does not set guideline amounts. Some courts treat the use of the word "applicable" as requiring actual expenses, but "applicable" could instead refer to the IRS standard amounts for a person of the debtor's family size or location. *See* Means Testing: Census Bureau, IRS Data and Administrative Expenses Multipliers, *available at* http://www.usdoj.gov/ust/eo/bapcpa/20080317/meanstesting.htm (setting out national standards in terms of family size and local standards in terms of both family size and location); *see, e.g.*, *In re* Farrar-Johnson, 353 B.R. 224, 230 (Bankr. N.D. Ill. 2006) (determining debtor's applicable monthly expense amounts via IRS standards); *cf. In re* Hardacre, 338 B.R. 718, 726 (Bankr. N.D. Tex. 2006) (discussing similar disagreement regarding the word *notwithstanding* in section 707(b)(2)(A)(ii)(I)). The contrast with the word "actual" in the next clause lends support to this reading. Congress could have clarified by changing the word "applicable" to a phrase, such as, "if the debtor has any actual expense in each category." On the other hand, section 707(b)(2)(A)(ii)(II) refers to taking actual expenses for care of a household member "if applicable," suggesting that the phrase is used in the sense of "if any," although this phrase is unnecessary in that context because redundant—one cannot take actual expenses that one does not have. Structural cues cut against requiring an actual expense. The debtor can have no current income but be considered to have "current monthly income" (CMI); the debtor with CMI needs to make rebuttal to show no or reduced income. *See generally* Tabb & McClelland, *supra* note 165, at 498 (discussing statutory guidelines for rebuttal). *Cf. In re* Barraza, 346 B.R. 724, 729 (Bankr. N.D. Tex. 2006) ("The means test does not distinguish those who have

question is different when the adjustment issue arises in chapter 7 as opposed to arising in chapter 13 for purposes of determining the projected disposable income of above-median-income debtors.[205] Neither the language nor the structure of the relevant provisions is clear, and the legislative purpose is also difficult to discern, stated as it is in generalities—abuse prevention but also "fairness."[206] Given

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tried hard from those who have hardly tried. It is a blind legislative formula that attempts to direct debtors to a chapter for at least some measure of repayment to unsecured creditors over a period of years."). Also, the expenses debtors are allowed under the local and national standards categories are not actual expenses, so there is no logical necessity that there be an actual expense in a category. When one turns to purposes, there are opposing purposes expressed in legislative history, to force as much payment as possible and to be fair to debtors and creditors. From a policy perspective, one should take into account perverse incentives; if debtors who own cars outright get no ownership expense, rather than hanging on to old cars to economize and get on a better financial footing, they are encouraged to enter bankruptcy owning expensive, shiny new cars with huge monthly payments, which can be taken in full under means testing. *See, e.g.*, *In re* Baughman, No. 07-63208, 2008 WL 4487879, at *4 (Bankr. N.D. Ohio Sept. 30, 2008) ("[I]f the applicable expenses must be actual expenses, a debtor would face the perverse incentive to splurge on a vehicle . . . ."); *see* Tabb & McClelland, *supra* note 165, at 492 (observing "perverse incentive" of rewarding debtor for having larger amounts of secured debt). Furthermore, even though the debtor has no payment on a mortgage or a car loan, the debtor may need to save either for higher-than-usual maintenance expenses on older property or, in the case of a car, to afford a replacement purchase within a few years. *See* Wedoff, *supra* note 165, at 258 ("[A] car for which the debtor no longer makes payments may soon need to be replaced (so that the debtor will actually have ownership expenses) . . . ."). *But see* Ransom v. MBNA America Bank, N.A. (*In re* Ransom), 380 B.R. 799, 808 (B.A.P. 9th Cir. 2007) (rejecting debtor's argument for vehicle ownership expense deduction due to "likelihood of major repairs and the costs of such repairs," when debtor's car was old and owned outright); *In re* Devilliers, 358 B.R. 849, 864 (Bankr. E.D. La. 2007) (indicating "deduction for costs associated with acquiring ownership . . . [are] not the equivalent of an allowance for depreciation or an invitation for a debtor to 'save' for the ultimate replacement of an existing vehicle").

Similar arguments arise concerning property the debtor intends to surrender. *Compare In re* Nockerts, 357 B.R. 497, 504–05 (Bankr. E.D. Wis. 2006) (permitting debtors to deduct secured debt expense notwithstanding their intent to surrender collateral), *with In re* Van Bodegom Smith, 383 B.R. 441, 455–56 (Bankr. E.D. Wis. 2008) (prohibiting such deduction). The debtor may need to buy another home or car soon, so using the ownership expense under IRS standards may make sense as a budgetary placeholder. Overall, the purpose of the presumed abuse test is to see whether the debtor has excess income under a crude approach of taking the average of the last six-month income and deducting certain standard amounts as expenses, even though they are not the debtor's actual expenses. The debtor with less income than CMI or more reasonable expenses than the IRS national and local standards has to make rebuttal. *See* Braucher, *A Fresh Start*, *supra* note 21, at 1306–07 (describing six-month income look-back and need for rebuttal upon means-test failure). *See generally* Tabb & McClelland, *supra* note 165, at 474–77 (discussing definition and method of computing current monthly income). *Cf.* David W. Allard & Katherine R. Catanese, *The Means Test: Seeing Clearly the CMI*, 26 AM. BANKR. INST. J. 12, 12 (Feb. 2007) (detailing CMI and rebuttal process). If the debtor happens to have more actual income or less actual expense than the presumed abuse test shows, often that may reflect temporary steps to try to make a budget balance and not grounds for pushing a debtor into chapter 13, which may not be feasible over the long term.

[205] *See In re* Gonzalez, 388 B.R. 292, 295, 305 (Bankr. S.D. Tex. 2008) (finding adjustment appropriate in chapter 13 under 11 U.S.C. § 1325(b)(2) and (3) but distinguishing chapter 7 means testing as calling for "snapshot" from chapter 13 calling for "a motion picture view."); *In re* Pfeiler, No. 07-22817-SBB, 2008 WL 4416759, at *5 (Bankr. D. Colo. Sept. 12, 2008) (agreeing with *Gonzalez*); *In re* Sanchez, 394 B.R. 574, 580 (Bankr. D. Colo. 2008) (discussing different application of "snapshot" view under chapters 7 and 13).

[206] *See* 11 U.S.C. §§ 707(b)(2), (3) (setting presumed abused and totality and good faith tests), 1325(b)(1)–(3) (2006) (setting different expectations for debtors who are median-income and below and for above-median-income debtors, with the latter required to use the expenses from section 707(b)(2) to determine projected disposable income); *see also* H.R. REP. NO. 109-31, *supra* note 2, at 2, 12 (stating purpose to

competing plausible readings, the bankruptcy courts should certainly parse the language and structure of the statute for clues, but they should also go further and explain what is at stake. It certainly matters as a practical matter whether above-median-income debtors can pass the presumed abuse test to stay in chapter 7 or have to go on to make rebuttal under a discretionary and thus expensive-to-use test[207] or get pushed into chapter 13, some without real means and ending up in unsustainable five-year plans and contributing to the chapter 13 failure rate, which has historically been high.[208]

Even more difficult questions concern whether a debtor who passes presumed-abuse means testing is subject to another round of challenge based on supposedly having excess income. Such a challenge might fit under the "totality of circumstances" or "bad faith" provisions in chapter 7; for above-median-income chapter 13 debtors who do not have excess disposable income under the presumed abuse formula, there is the possibility of interpreting "projected disposable income"[209] to require adjustments in light of excess real income (over the six-month lookback of "current monthly income") or lower expenses shown in schedules, based on any of three different theories: seeing "projected disposable income" as forward-looking, invoking the "good faith" test for confirmation of a plan[210] to find more disposable income than the means testing formula provides, or using modification[211] as another round of means testing. Since the latter two theories,

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restore "personal responsibility and integrity in the bankruptcy system and ensure that the system is fair for both debtors and creditors" and noting "substantial abuse" standard of prior law was "inherently vague, which has lead [sic] to its disparate interpretation and application by the bankruptcy bench"); *cf.* Stuart v. Koch (*In re* Koch), 109 F.3d 1285, 1288 (8th Cir. 1997) (remarking pre-2005 section 707(b) was meant to promote fairness to creditors, but lacked definition of "substantial abuse").

[207] *See* 11 U.S.C. § 707(b)(2)(B)(i) (2006) ("[T]he presumption of abuse may only be rebutted by demonstrating special circumstances . . . ."); Eisen v. Thompson, 370 B.R. 762, 773 (N.D. Ohio 2007) ("[T]he plain language of section 707(b)(2)(B) is clear—for a debtor to successfully obtain an additional expense or adjustment of [current monthly income], she must demonstrate a special circumstance which leaves her with no reasonable alternative but to incur the expense or cause the income adjustment." (quoting *In re* Haman, 366 B.R. 307, 313 (Bankr. D. Del. 2007))); *In re* Knight, 370 B.R. 429, 434 (Bankr. N.D. Ga. 2007) (discussing provisions of section 707(b) and debtor's ability to rebut presumption of abuse after failing means test).

[208] *See In re* Attanasio, 218 B.R. 180, 195 (Bankr. N.D. Ala. 1998) (calling chapter 13 failures "almost predictable"); Norberg & Velkey, *supra* note 180, at 476 (concerning high noncompletion rate in chapter 13).

[209] 11 U.S.C. § 1325(b)(1)(B) (2006) (if claims are not paid in full, setting forth the requirement that "the plan provides that all of the debtor's projected disposable income to be received in the applicable commitment period beginning on the date that the first payment is due under the plan will be applied to make payments to unsecured creditors under the plan").

[210] *See supra* note 205 (concerning view that "projected disposable income" is forward-looking); *see also* 11 U.S.C. § 1325(a)(3) (2006) (stating plan shall be confirmed if "the plan has been proposed in good faith and not by any means forbidden by law").

[211] *See* 11 U.S.C. § 1329 (2006) (providing for post-confirmation modification); *In re* Hilton, No. 08-25440, 2008 WL 4593381, at *6 (Bankr. E.D. Wis. Oct. 15, 2008) ("Section 1325(b) and its incorporated means test does not apply to modifications . . . ."); *In re* Ireland, 366 B.R. 27, 31 (Bankr. W.D. Ark. 2007) ("Subsections 1325(b)(2) and (3), which provide for how a debtor's plan payments must be computed

good faith and modification, are not limited to above-median income debtors, they might be used for means testing of median income or below chapter 13 debtors, who are already subject to screening based on whether they have disposable income in excess of reasonable expenses.

A potential worry for chapter 7 debtors who either fall below median income (ninety-one or ninety-two percent of chapter 7 debtors in the early period after the 2005 law)[212] or who pass the presumed-abuse test (most of the rest)[213] is whether they can be means tested again under non-presumptive provisions, allowing dismissal based on "totality of the circumstances" or "bad faith."[214] This statutory interpretation issue is more important than the ins and outs of the presumed abuse means test because all chapter 7 debtors, even those below median income and thus not vulnerable to presumed abuse dismissal, are potentially subject to this kind of review. The question is whether, to catch a few crafty abusers, all below-median-income chapter 7 debtors as well as all who pass the presumed abused test should be potentially subject to additional, highly discretionary means testing without benefit of any specific guidance in the statute.

To make the argument in the affirmative, Judge Eugene Wedoff used a hypothetical example of a former CEO who goes without income for six months to pass the means test, perhaps buying a Jaguar on secured credit to jack up his means testing expenses and make sure he passes.[215] This hypothetical is far from the ordinary below-median-income filer, who is typically significantly below median income and heavily over-indebted to boot, without any need for manipulation.[216]

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pursuant to Form B22C and the means test, have not been expressly made applicable to plan modifications filed under Section 1329.").

[212] White, *Year 2*, *supra* note 101, at 16 (noting approximately eight percent of chapter 7 debtors from October 2005 through March 2007 had income above state median income); White, *Update*, *supra* note 161, at 14 (stating "[b]etween Oct. 1, 2006 and June 30, 2007, approximately 9 percent of chapter 7 debtors had income above their state median").

[213] White, *Year 2*, *supra* note 101, at 16 (finding "presumed abusive" 9.5 percent of above-median-income chapter 7 debtors who filed between October 2005 and March 2007); White, *Update, supra* note 161, at 14 (noting approximately 10 percent of above-median-income chapter 7 debtors who filed between October 2006 and June 2007 were "presumed abusive").

[214] 11 U.S.C. § 707(b)(3) (2006); *see In re* Haar, 373 B.R. 493, 503 (Bankr. N.D. Ohio 2007) (granting trustee's motion to dismiss chapter 7 case under section 707(b)(3)); *see also In re* Zaporski, 366 B.R. 758, 768 (Bankr. E.D. Mich. 2007) (noting "[j]ust because there is no statutory presumption of abuse does not somehow create a safe harbor for a debtor" and that "[t]he [United States Trustee] can still request dismissal . . . either for bad faith or based on a totality of circumstances analysis that can properly take into consideration a debtor's actual income and expenses . . . .").

[215] *See* Wedoff, *supra* note 165, at 1

> Imagine a person with a high income . . . whose company goes out of business and who finds himself temporarily unemployed . . . . [H]e maintains his lifestyle by depleting his personal savings and incurring substantial debt, both secured (his normal annual purchase of a new Jaguar . . .) and unsecured . . . .

[216] *See* Lawless et al., *supra* note 171, at 360 & fig. 2 (showing incomes of 2007 and 2001 debtors bunched at the low-end of the spectrum) and 365, 369 (concerning increasing debt burdens of debtors in bankruptcy,

Having to be prepared for a second gauntlet of means testing increases the cost of bankruptcy for all, including desperate lower-income chapter 7 debtors.

While dismissal based on totality of the circumstances or bad faith is a looming possibility, the US trustee system has been bringing abuse challenges, presumed as well as on discretionary grounds, in only one in 140 chapter 7 cases (about .7 percent),[217] so totality and bad faith challenges were not—at least in the initial phase under the 2005 law—being mounted frequently. The provision on standing to bring abuse challenges against debtors at or below median income is restricted to the judge or US trustee (or bankruptcy administrator) for all of section 707(b), so creditors cannot raise section 707(b)(3) against them.[218] On the other hand, we do not know how often trustees informally raised the possibility of totality or bad faith challenges, leading debtors to convert to chapter 13 without a battle.

With the open-ended tests of section 707(b)(3), "totality of the circumstances" and "bad faith," and nothing explicit about the relationship between paragraphs (2) and (3) of section 707(b), text does not answer whether paragraph (3) is supposed to include new rounds of discretionary means testing to catch debtors who pass the paragraph (2) test. Furthermore, no distinction is made in the text of section 707(b)(3) between debtors below or above median income, so reading paragraph (3) as allowing more means testing could result in no debtor being safe from this kind of review. Legislative history gives conflicting messages about the purpose of having both paragraphs (2) and (3) of section 707(b): in its general statement of purposes, the House Judiciary Report states that means testing is "intended to ensure that debtors repay creditors the maximum they can afford."[219] On the other hand, in its discussion of "Needs-Based Reforms,"[220] the same report criticizes the old "substantial abuse" test for dismissal as "inherently vague, which has led to its disparate interpretation and application by the bankruptcy bench,"[221] showing a concern with lack of uniform means testing produced by a discretionary approach. Thus, legislative history supports a pair of plausible, opposing arguments: Congress wanted two levels of means testing, one presumptive followed by another discretionary level with judges free to make their own normative judgments about what expenses are illegitimate and how much extra income is too much, or

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doubling their negative net worth since 1981); Norberg & Velkey, *supra* note 180, at 478 (noting median chapter 13 debtor's income was "less than 60% of the median for all households").

[217] *See* White, *Year 2*, *supra* note 101, at 16.

[218] 11 U.S.C. § 707(b)(6) (2006); *see* Tabb & McClelland, *supra* note 165, at 507 ("[I]n a below-medium-income case, the only parties with standing to file a motion . . . are the judge and the United States trustee.").

[219] H.R. REP. NO. 109-31, *supra* note 2, at 2; *see, e.g.*, *In re* Close, 384 B.R. 856, 869 (D. Kan. 2008) (citing House Report language regarding ensuring maximum debtor payments in support of holding); *In re* Naut, No. 07-20280REF, 2008 WL 191297, at *8 (Bankr. E.D. Pa. 2008) (invoking congressional intent of maximum repayment to hold debtors' scheduled secured debt payments could not be used in means test because they intended to surrender (citing *In re* Harris, 353 B.R. 304, 309–10 (Bankr. E.D. Okla. 2006))).

[220] H.R. REP. NO. 109-31, *supra* note 2, at 10–15. *See generally In re* Delbecq, 368 B.R. 754, 760–61 (Bankr. S.D. Ind. 2007) (noting congressional discussion of needs-based reforms).

[221] H.R. REP. NO. 109-31, *supra* note 2, at 12.

alternatively, that Congress included "totality of the circumstances" and "bad faith" as tests to pick up bad behavior other than simply passing its detailed means test, enacted to address lack of uniformity under a vague standard. Under the former approach, debtors have to worry about a second level of means testing review in every single chapter 7 bankruptcy case, likely increasing attorneys fees because of the time needed to make sure scheduled expenses are stated with thoroughness so that no excess income is shown. Under the latter approach, the discretionary review under section 707(b)(3) could be used not to do another round of means testing but to address scheming and dishonesty, such as intentionally misrepresenting information in the means testing calculation, timing filing to make income look low, unnecessarily getting large secured loans on the eve of bankruptcy, or serially filing to forestall foreclosure.[222] This approach would, by the way, catch Judge Wedoff's hypothetical scheming CEO,[223] who both manipulated his income downward and made a highly discretionary and not reasonably necessary purchase on secured credit—both ways of gaming the means test.

Another factor for courts to take into account is that kicking more above-median-income debtors into chapter 13 on the basis of section 707(b)(3) does not necessarily mean they will pay more, because if they passed presumed abuse testing in chapter 7, they will pass it in chapter 13, too, unless chapter 13 also has a second round of means testing. This brings us to a knotty set of issues concerning means testing of above-median-income chapter 13 debtors. As we have seen, using the presumed-abuse means testing expenses for above-median-income chapter 13 debtors typically results in them paying less than they would have to pay if expenses from schedule J were used.[224] Sometimes debtors show zero disposable income using the formula and substantial disposable income using schedules.[225] The courts have split on what to do in these circumstances, with some treating "projected disposable income" as subject to adjustment based on actual income or expenses.[226] The alternative approach is to treat means testing of above-median-income debtors in chapter 13 as formulaic. A recent Ninth Circuit case, *Maney v.*

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[222] *See generally* Culhane & White, *supra* note 170, at 687–99 (discussing forms of misbehavior other than simply passing presumed abuse means test as better way to interpret "totality of the circumstances" and "bad faith" under section 707(b)(3)). *Cf.* Tabb & McClelland, *supra* note 165, at 477 (noting policing via section 707(b)(3) "will be difficult and erratic").

[223] *See supra* note 215 and accompanying text (discussing Judge Wedoff's hypothetical).

[224] *See supra* notes 176–78 and accompanying text.

[225] *See, e.g.*, Maney v. Kagenveama (*In re* Kagenveama), 527 F.3d 990, 993 (9th Cir. 2008) (showing debtor's monthly disposable income as $1,523.89 using schedules and negative $4.04 using formula); *In re* Gonzalez, 388 B.R. 292, 295 (Bankr. S.D. Tex. 2008) (noting "[t]he Gonzalezes' initial Form B22C projected disposable income calculation resulted in negative $1,815.00 per month . . . [but their] schedules I and J estimated an average monthly income of $7,464.73 and expenses of $6,401.00").

[226] *See In re Gonzalez*, 388 B.R. at 303–04, 306 (holding court must consider future circumstances of chapter 13 debtors to project their disposable income and citing cases on both sides of issue concerning interpretation of "projection;" also noting that using housing expense from a particular date could underestimate or overestimate future expense over the life of a plan and calling for use of evidentiary hearings to forecast expenses).

Kagenveama,[227] unfortunately labels this a "plain meaning" approach,[228] a highly debatable assertion,[229] but an examination of its method shows that it backs up his analysis based on text with both legislative history and policy.

The language analysis in that case is that the words "disposable income" appear only twice in section 1325(b), once in (b)(2) defining "disposable income," and once in (b)(1)(B), calling for "projected disposable income" to be committed in the plan.[230] The court concludes that the definition would be surplusage unless it is used in defining "projected disposable income."[231] Furthermore, since the definition in (b)(2) is modified in (b)(3) for above-median-income debtors to call for use of section 707(b)(2) expenses, those expenses are not to be adjusted in light of income and expenses shown on schedules I and J.[232]

The *Kagenveama* court's use of legislative history is to note that, during the debate over the 2005 law, chapter 13 trustees notified Congress of concerns that higher-income debtors would pay less using the presumed-abuse means test than under prior law, which has turned out to be true.[233] Its policy argument is that the purpose of the 2005 law's means testing is to create a formula; the court states that "eliminating flexibility was the point" and that having "clear, defined standards" avoids leaving the disposable income calculation for above-median-income debtors to "the whim of a judicial proceeding."[234] If the legislation reflects "poor policy choices," the court says, Congress should amend the statute.[235]

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[227] *In re Kagenveama*, 527 F.3d 990.

[228] *Id.* at 994.

[229] *See* Coop v. Frederickson (*In re* Frederickson), __F.3d __, No. 07-3391, 2008 WL 4693132 at *3, 6–7 (8th Cir. Oct. 27, 2008) (before adopting forward-looking approach, noting that the statute is not clear and that although both the formulaic and reality-based interpretations of "projected disposable income" are supported by authority, neither fits neatly into the statutory structure); *In re* Sanchez, 394 B.R. 574, 578–81 (Bankr. D. Colo. 2008) (holding *Kagenveama*'s "snapshot" view incorrect); *In re* DeThample, 390 B.R. 716, 724–25 (Bankr. D. Kan. 2008) (arguing *Kagenveama* ignored important contradictions); *In re Gonzalez*, 388 B.R. at 305 (disagreeing with snapshot view in context of chapter 13).

[230] *See In re Kagenveama*, 527 F.3d at 994.

[231] Maney v. Kagenveama (*In re* Kagenveama), 527 F.3d 990, 995 (9th Cir. 2008); *cf. In re* Alexander, 344 B.R. 742, 749 (Bankr. E.D.N.C. 2006) ("[P]rojected disposable income has been traditionally calculated in conjunction with the definition of disposable income.").

[232] *See In re Kagenveama*, 527 F.3d at 995 n.1, 995–96; *In re* Winokur, 364 B.R. 204, 206 (Bankr. E.D. Va. 2007) (discussing and upholding use of formula approach); *cf. In re* Farrar-Johnson, 353 B.R. 224, 231 (Bankr. N.D. Ill. 2006) (noting creation of explicit standards for chapter 13 debtors was aim of new approach).

[233] *See In re Kagenveama*, 527 F.3d at 997 (citing Culhane & White, *supra* note 170, at 682); *In re Alexander*, 344 B.R. at 747 (noting in above-median income debtor cases, "the debtors uniformly have less disposable income using the new calculation method"); *see also* EOUST, *Report to Congress*, *supra* note 174, at 4 (reporting that above-median-income chapter 13 debtors usually pay less under presumed abuse test than under pre-2005 law approach of looking at actual disposable income in excess of reasonable expenses).

[234] *In re Kagenveama*, 527 F.3d at 997 (quoting *In re Farrar-Johnson*, 353 B.R. at 231) (stating "eliminating flexibility was the point" of new approach)); *see In re* Davis, 392 B.R. 132, 140 (Bankr. E.D. Pa. 2008) (noting "Congress excluded several sources of income from the disposable income calculation, including repayment of . . . Social Security Act benefits, thereby calling into doubt whether maximum repayment to creditors was its main intent," and finding goal in means testing "to replace judicial discretion

Another possible policy explanation for the choice of the higher IRS expense standards, as opposed to expenses listed on debtors' schedules, is to give debtors more sustainable budgets.[236] Furthermore, allowing a debtor to use the ownership expense for an old car owned outright avoids penalizing a frugal debtor who, unlike more aggressive debtors, does not acquire a late model car, incurring a large secured debt.[237] This choice might inform determination of disposable income for chapter 13 debtors who are at or below median income[238] and lead courts to

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with specific statutory standards and formulas"). *But see In re* May, 381 B.R. 498, 506–07 (Bankr. W.D. Pa. 2008) (finding congressional intent of preserving some judicial discretion under 2005 law).

[235] *See In re Kagenveama*, 527 F.3d at 997 (finding Congress, not courts, should amend section 330(a)(1) if changes under 2005 law created unwanted results (citing Lamie v. U.S. Tr., 540 U.S. 526, 542 (2004))); *In re* Neclerio, 393 B.R. 784, 790 (Bankr. S.D. Fla. 2008) (noting Congress enacted "mechanical formula" that "eliminates judicial discretion and . . . will necessarily lead to peculiar results").

[236] *See In re* Cox, 393 B.R. 681, 692 (Bankr. W.D. Mo. 2008) (finding deductions allowed by IRS standards and section 707(b)(2) "are often more generous than debtors' actual expenses"); *In re* Phillips, 382 B.R. 153, 162–63 (Bankr. D. Mass. 2008) (holding debtor entitled to take housing deduction under IRS standards even if her rent was lower than IRS standards); *In re* Swan, 368 B.R. 12, 17 (Bankr. N.D. Cal. 2007) (concluding debtor entitled to take IRS vehicle-ownership deduction even if vehicle owned outright). Above-median-income debtors who file in chapter 13 can engage in rebuttal there, at least as to justified higher expenses than the formula allows, 11 U.S.C. § 1325(b)(3) (2006) (effective April 1, 2007) (incorporating 11 U.S.C. § 707(b)(2)(B) as well as (A)), as they can in chapter 7, to attempt to show they really have less disposable income than the formula indicates, showing concern with realism to allow greater leeway to debtors. *See In re* Lanning, 380 B.R. 17, 25 (B.A.P. 10th Cir. 2007) (citing 11 U.S.C. § 707(b)(2)(B)(ii), (iii) (2006), *amended by* Pub. L. No. 110-438 (2008)) ("Chapter 7 debtors seeking to rebut the abuse presumption are required to itemize their increased expenses or changes in income, to provide both documentation and a detailed explanation of the 'special circumstances' they claim, and to attest to them under oath."); *In re* LaPlana, 363 B.R. 259, 266 (Bankr. M.D. Fla. 2007) ("[C]ourts must consider changes in circumstances, both increases and decreases to income and expenses, to a debtor's financial situation, being always guided by the allowed methodology set forth in the means test.") (emphasis omitted); *In re May*, 381 B.R. at 507 (finding Form 22C projected income figures create "rebuttable presumption"); *In re* Haman, 366 B.R. 307, 312 (Bankr. D. Del. 2007) (finding 'special circumstances' to rebut presumption of abuse when debtor forced to repay ill son's student loan); *In re* Pfeifer, 365 B.R. 187, 192–93 (Bankr. D. Mont. 2007) ("[A] debtor's ability to pay is still an important factor under § 707(b)(3), notwithstanding the means test of § 707(b)(2)." (citing *In re* Sorrell, 359 B.R. 167 (Bankr. D. Ohio 2007))).

[237] *See* Pearson v. Stewart (*In re* Pearson), 390 B.R. 706, 714–15 (B.A.P. 10th Cir. 2008) (Thurman, J., concurring) (determining "fair reading" of sections 1325(b)(3) and 707(b)(2)(A)(ii)(I) allows deduction of vehicle expenses to debtor owning vehicle outright when establishing return to unsecured creditors); *see also* Hildebrand v. Kimbro (*In re* Kimbro), 389 B.R. 518, 524 (B.A.P. 6th Cir. 2008) (concluding "plain meaning of 11 U.S.C. § 707(b)(2)(A)(ii)(I) allows the debtor to deduct the applicable ownership expense in the IRS Local Transportation Standard even if the debtor has no debt or lease expense"). *But see In re* White, 393 B.R. 436, 443 (Bankr. N.D. Miss. 2008) (finding above-median-income-chapter-13 debtor owning vehicle outright not allowed vehicle ownership expense deduction).

[238] *See* 11 U.S.C. § 1325(b)(1), (2) (2006) (largely carrying forward expense approach of pre-2005 law for debtors at or below median income, which asks whether expenses are "reasonably necessary to be expended . . . for the maintenance or support of the debtor or a dependent of the debtor"); *see also* Kibbe v. Sumski (*In re* Kibbe), 361 B.R. 302, 314 (B.A.P. 1st Cir. 2007) (concluding bankruptcy court rightly denied confirmation of below-median-income debtor’s plan when debtor obtained higher-paying job before bankruptcy; mechanical resort to Form B22C projected disposable income "would result in a windfall to a debtor"); *In re* Plumb, 373 B.R. 429, 435–36 (Bankr. W.D.N.C. 2007) (finding Form B22C is starting point for projected disposable income and Schedules I and J should be considered in calculation to ascertain debtor's actual ability to pay).

examine schedules for missing or understated expenses before finding that they have disposable income to commit to a plan.

The formula approach to means testing would also reject using the confirmation requirement that the plan be proposed in good faith[239] as a form of open-ended means testing for those who pass the presumed abuse means test without manipulation or bad behavior. Furthermore, *Kagenveama* suggests that modification should not be another round of means testing but rather should be used only for changes after confirmation, particularly an increase in income.[240] It should also be noted that making above-median-income debtors who pass presumed abuse review in chapter 13 subject to another round of means testing based on their schedules is likely to drive some to file instead in chapter 7, where they may escape section 707(b)(3), which has so far not been used frequently, and end up paying nothing to unsecured creditors. The big picture question is whether the 2005 law intends to create two levels of means testing in each chapter—the first based on a formula and the second based on judicial discretion—or whether it intends the formulaic approach to occupy the means testing field.

Means testing under the 2005 law is a fraught field for purpose- and policy-based statutory interpretation. The reason is that Congress stated twin goals of pushing for more repayment in chapter 13 and limiting judicial discretion to means test without guidance[241] and then adopted a formulaic approach that catches relatively few debtors.[242] Obviously, the goals of Congress appear to be in conflict, and the statute is open-textured enough to leave different courses of action open to the judiciary. The courts have the options of engaging in discretionary means testing, without benefit of congressional guidance and contrary to stated congressional desire to limit judicial discretion, or instead applying the means test formula and catching only a small number of debtors. The latter approach is defensible as reflecting a congressional purpose to toughen up means testing only to the point of the formula it enacted, even if Congress thought more people would be caught than in fact are. On policy grounds, this approach could be defended as

[239] 11 U.S.C. § 1325(a)(3) (2006) (stating court shall confirm plan made in good faith and "not by any means forbidden by law"). For a case finding that this test could be used for means testing, see *In re* Sanchez, 394 B.R. 574, 581 (Bankr. D. Colo. 2008). *See also In re Pearson*, 390 B.R. at 715 (stating good faith could be used to deviate from presumed abuse means test in chapter 13); *In re* Anstett, 383 B.R. 380, 385 (Bankr. D.S.C. 2008) (finding court has freedom to use good faith to make "independent review of the propriety of plan confirmation"); *In re* Martin, 373 B.R. 731, 736 (Bankr. D. Utah 2007) (noting section 1325(b) analysis is "distinct and independent" from section 1325(a)(3) good-faith analysis).

[240] *See* Maney v. Kagenveama (*In re* Kagenveama), 527 F.3d 990, 997 (9th Cir. 2008) ("[I]f the debtor's income increases after the plan is confirmed, the trustee may seek plan modification under § 1329."); *see also In re* Hilton, No. 08-25440, 2008 WL 4593381, at *6 (Bankr. E.D. Wis. Oct. 15, 2008) (stating courts modifying plans could "assess the debtor's ability to pay going forward, as opposed to applying set amount based on six-month period prior to bankruptcy"); *cf. In re* Wetzel, 381 B.R. 247, 252 (Bankr. E.D. Wis. 2008) (stating court would "take into account the essential components of the disposable income test while upholding the plain language of § 1329 that omits the test").

[241] *See supra* notes 219–21 and accompanying text.

[242] *See supra* notes 161–79 and accompanying text.

follows: those using the bankruptcy system, even those above median income, overwhelming need debt relief, and, with 20-20 hindsight, we know that Congress enacted the 2005 law near the height of a bubble economy. Thus, there is reason to doubt that it wants the bankruptcy courts to spend time now going after debtors who pass its formulaic means test. Congress could always enact further legislation to state a clear intention to direct the courts to engage in discretionary means testing of more debtors than the presumed abuse test catches, if that is really what it wants the courts to do.

C. Provisions with Fairness Purposes

A prominent purpose of the 2005 law is "to ensure that the system is fair for both debtors and creditors."[243] A section of the legislation carries the caption, "Giving Secured Creditors Fair Treatment in Chapter 13,"[244] an indication that treatment of secured claims is among the issues the 2005 law deals with under the banner of fairness. On the other hand, the more general statement of purposes at the outset of the House Report by the Judiciary Committee[245] does not leave out fairness to other creditors or to debtors. To be sure, car lenders and other secured lenders with personal property collateral have come in for increased solicitude in both chapters 7 and 13.[246] In chapter 7, the 2005 law eliminates ride-through with court protection on loans secured by personal property,[247] and redemption now must be at retail value for collateral acquired for personal, family or household purposes,

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[243] H.R. REP. NO. 109-31, *supra* note 2, at 2. *See In re* Purdy, 373 B.R. 142, 148 (Bankr. N.D. Fla. 2007) ("The Congressional intent behind BAPCPA was to improve bankruptcy law and practice by restoring personal responsibility and integrity in the bankruptcy system and to ensure that the system is fair for both debtors and creditors."); *see also* Todd J. Zywicki, *Bankruptcy Law as Social Legislation*, 5 TEX. REV. L. & POL. 393, 428–29 (2000) (discussing bankruptcy reform goals of "restoring personal responsibility and integrity in the bankruptcy system" and fairness to debtors and creditors).

[244] Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, § 306, 119 Stat. 23 (2005). *See In re* Duke, 345 B.R. 806, 809 (Bankr. W.D. Ky. 2006) (noting 2005 law included heading, "Section 306—Giving Secured Creditors Fair Treatment in Chapter 13," which indicates "Congress intended to provide more protection to creditors with purchase money security interests"); *In re* Herrin, 376 B.R. 316, 320 (S.D. Ala 2007) (asserting section 306 title was only evidence of congressional intent).

[245] *See supra* note 243 and accompanying text.

[246] *See* William C. Whitford, *A History of the Automobile Lender Provisions of BAPCPA*, 2007 U. ILL. L. REV. 143, 150–56 (2007) [hereinafter Whitford, *Automobile Lender*] (describing changes favorable to auto lenders); *see also* Norberg & Velkey, *supra* note 180, at 478–79 ("[T]he new provision limiting strip-down of certain purchase money security interests in Chapter 13 might be expected to further increase the share of Chapter 13 disbursements paid to secured creditors and to correspondingly reduce payments to unsecured creditors."). *But see* Jean Braucher, Rash *and Ride-Through Redux: The Terms for Holding on to Cars, Homes and Other Collateral Under the 2005 Act*, 13 AM. BANKR. INST. L. REV. 457, 469–74 (2005) [hereinafter Braucher, Rash *and Redux*] (discussing chapter 13 provisions possibly generating interpretations unfavorable to auto lenders).

[247] *See infra* notes 271–72 and accompanying text (discussing chapter 7 debtor's general inability under new laws to ride through on vehicle loan without creditor's consent); *see also In re* Caraballo, 386 B.R. 398, 401 (Bankr. D. Conn. 2008) (stating, unlike for real property, 2005 law abrogated ride through option as it pertains to personal property).

rather than at wholesale value.[248] In chapter 13, certain recent car and other personal property loans are apparently no longer subject to cramdown to collateral value,[249] reducing chapter 13 distributions to unsecured creditors at the expense of undersecured personal property lenders, particularly auto lenders, while also adding somewhat to debtors' disincentives to use chapter 13.

The provisions on secured claims suffer from some of the same problems as other aspects of the 2005 law, in particular mind-numbing complexity.[250] Luckily, once again, a lot of that complexity will have fairly limited impact.[251] The emphasis here is on the desirability of courts focusing, when interpreting the 2005 law, on interaction between what is possible in chapters 7 and 13, particularly thinking about how the provisions on collateral may drive debtors' choice of chapter. In particular, this section addresses interpretation of two issues about collateral that are among the most difficult because there is no evidence that Congress thought about either issue at all. One is treatment of claims for recently acquired autos when the debtor surrenders the collateral in chapter 13;[252] the other is whether cramdown becomes possible for these claims in chapter 13 when negative equity on a loan for a trade-in vehicle has been rolled into the new loan.[253] Allowing surrender in full satisfaction and cramdown of negative equity loans may encourage more use of chapter 13 and more repayment of unsecured creditors.

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[248] 11 U.S.C. §§ 506(a), 722 (2006) (section 722 incorporates section 506(a) method of valuation, and section 506(a)(2) now calls for valuation at retail value for collateral acquired for personal, family or household use; section 722 now makes explicit redemption must be by payment in full at time of redemption). *See In re* Morales, 387 B.R. 36, 41–42 (Bankr. C.D. Cal. 2008) (remarking 2005 law's amendments require chapter 7 debtors electing redemption to value certain personal property securing debt at retail value at filing of petition); *In re* Clark, No. 06-31965, 2007 WL 671346, at *1–2 (Bankr. N.D. Ohio Feb. 27, 2007) (discussing 2005 law's change to valuation standard under section 506(a) from judicially determined standard to statutory standard of retail value).

[249] *See* 11 U.S.C. § 1325(a) (2006) (providing section 506 does not apply to certain claims arising from recent secured automobile or other property purchases); *see also infra* notes 282–91 (examining effects of hanging paragraph on rights of secured creditors).

[250] *See In re* Kaplan, 331 B.R. 483, 484 (Bankr. S.D. Fla. 2005) (observing 2005 law is "not a model of clarity" and hypothesizing courts will find implementing its amendments "a daunting challenge"); Alvin C. Harrell, *Did the Seventh Circuit make the "Wright" decision in resolving the BAPCPA "Hanging Paragraph"?*, 61 CONSUMER FIN. L.Q. REP. 598, 598, 600 (2007) (highlighting complexity of 2005 law and difficulties in applying its amendments, including hanging paragraph); discussion *supra* Part II.B (concerning congressional intent to prevent perceived abuses in both chapter 7 and 13 proceedings using presumed abuse means testing, yet, in practice, creating relatively forgiving formula catching very few debtors).

[251] *See supra* notes 159–78 and accompanying text (analyzing relatively low impact of means testing on debtors in chapters 7 and 13).

[252] *See infra* notes 297–320 and accompanying text (reasoning, contrary to circuit courts' view, that chapter 13 debtor's surrender of vehicle in full satisfaction of 910 claims could be justified as best reading of statutory text and also in terms of incentives to use chapter 13, fairness to unsecured creditors, and efficiency of bankruptcy system).

[253] *See infra* notes 321–40 and accompanying text (explaining technical arguments to exclude negative equity financing from protection of hanging paragraph and discussing purpose of hanging paragraph as not extending to encouraging risky negative equity financing).

Debtors often seek to deal with secured loans in bankruptcy, whether to "save" homes and cars[254] or, alternatively and less frequently, to tighten their belts to a manageable budget by surrendering collateral, something that should perhaps be encouraged.[255] In many cases, chapter 7 is a more desirable place to do either of these things; the 2005 law seems to have added reasons for debtors to prefer chapter 7. Keeping in mind that at least seventy-three percent of chapter 13 debtors (and probably considerably more) are there for reasons other than flunking means testing,[256] we also see that making retaining or surrendering collateral in chapter 13 more difficult creates incentives to file in chapter 7. In other words, the collateral provisions of the new law risk undermining the overall purpose to push more debtors into more repayment in chapter 13.[257] Courts would be well advised to keep such effects in mind when interpreting the new law.

Turning first to chapter 7, some debtors who seek to retain a home in chapter 7 are in better legal shape under the 2005 law than before. Debtors who have managed to stay current on mortgage payments now have a stronger argument for court-protected ride-through, meaning reaffirmation is unnecessary, by simply continuing to make payments; this is so because ride-through on secured loans was the majority rule in the circuits before the 2005 law was passed,[258] and the legislation's new anti-ride-through provisions are all explicitly focused on personal property collateral and silent about home loans.[259] The advantage of ride-through on

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[254] *See* DaimlerChrysler Fin. Servs. Ams. LLC v. Barrett (*In re* Barrett), Nos. 07-14796, 07-14797, 2008 WL 4378739, at *2 (11th Cir. Sept. 29, 2008) (providing debtor could retain property in chapter 13 proceeding by making monthly payments equivalent to fair market value); Price v. Del. State Police Fed. Credit Union U.S. Trustee (*In re* Price), 370 F.3d 362, 364 (3d Cir. 2004) (stating section 521(2)(A) does not stop debtors from keeping secured property as long as they continue to make loan payments); Melissa B. Jacoby, *Bankruptcy Reform and Homeownership Risk*, 2007 U. ILL. L. REV. 323, 329–38 (2007) (discussing that it is not always possible or desirable for debtors to save home).

[255] *See* Jacoby, *supra* note 254, at 338 (discussing need to sort in bankruptcy for homeownership sustainability); *cf.* Wright v. Santander Consumer USA Inc. (*In re* Wright), 492 F.3d 829, 830 (7th Cir 2007) (finding debtors who surrender collateral still have deficiency obligations); Daimlerchrysler Fin. Servs. Ams., L.L.C. v. Waters, No. 5:07cv00057, 2007 WL 2107428, at *3 (W.D. Va. July 18, 2007) (discussing majority bankruptcy court view allowing debtors to surrender collateral in full satisfaction of their obligations).

[256] *See supra* notes 170–74 and accompanying text (noting data showing only twenty-seven percent of chapter 13 debtors have income above median).

[257] *See* H. REP. NO. 109-31, *supra* note 2, at 12 (noting goal of shifting more debtors into chapter 13, where they repay at least portion of old debts); *cf.* Americredit Fin. Servs., Inc. v. Long (*In re* Long), 519 F.3d 288, 290 (6th Cir. 2008) (observing 2005 law "does not provide for the situation in which a Chapter 13 debtor proposes to surrender the collateral to the creditor holding the . . . security interest").

[258] *See In re Price*, 370 F.3d at 370–74 (noting circuit split and holding debtor may retain collateral by staying current on loan without redeeming or reaffirming); *see also* Capital Commc'ns Fed. Credit Union v. Boodrow (*In re* Boodrow), 126 F.3d 43, 53 (2d Cir. 1997) (holding under pre-2005 law's section 521(2) that debtors could keep collateral while staying current on loans); Lowry Fed. Credit Union v. West, 882 F.2d 1543, 1546–47 (10th Cir. 1989) (finding section 521 permitted debtor current on obligations to retain collateral without reaffirmation or redemption).

[259] *See* Braucher, Rash *and Redux*, *supra* note 246, at 479–81 (arguing ride-through on homes is court-protected under 2005 law); *see also In re* Caraballo, 386 B.R. 398, 401 (Bankr. D. Conn. 2008) (explaining 2005 law abrogated ride-through for personal, but not real property); *In re* Bennet, No. 06-80241, 2006 WL

a home for a debtor is that the debtor does not impair the fresh start by making a commitment to repay, as in reaffirmation.[260] The debtor can discharge the personal obligation and, if repayment proves impossible, surrender the home.

If the debtor is behind on mortgage payments and wants to be sure to be able to retain a home after discharge in chapter 7, the debtor will need the creditor's agreement to reaffirm the debt.[261] Even if the debtor is current on the home loan, the debtor may want a reaffirmation agreement in a situation where the mortgage payment is hardly manageable and the house has lost significant value compared to the debt outstanding. The complexity of mortgage finance, using special purpose financing structures[262] and mortgage servicers with little incentive to do workouts,[263] has made it harder in recent years for debtors to locate the real party in interest with whom to negotiate for a workout on a home loan.[264] However, this

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1540842, at *1 (Bankr. M.D.N.C. May 26, 2006) (holding real-property ride-through protected under 2005 law, and finding reaffirmation not in best interests of *pro se* debtors because they could hold on to their homes without reaffirmation).

[260] 11 U.S.C. § 524(c) (2006). *See In re Caraballo*, 386 B.R. at 402 ("[D]ebtors are permitted to take advantage of the ride through option with respect to relevant real property. As a result, the court also must find and/or conclude that the Reaffirmation Agreements are not in the Debtor's best interest and must be disapproved.").

[261] 11 U.S.C. § 524(c). The creditor's *in rem* claim against the collateral remains after the bankruptcy discharge of the personal obligation, so if the debtor is in default, foreclosure is possible after the case. *See* Joann Handerson, *The Gaglia-Lowry Brief: A Quantum Leap from Strip Down to Chapter 7 Cram Down*, 8 BANKR. DEV. J. 131, 139 (1991) ("The bankruptcy discharges any personal obligation, but the secured claim survives bankruptcy. The secured claim becomes a nonrecourse lien with only in rem rights, because strip down voids the unsecured part of the lien.").

[262] *See* Kathleen C. Engel & Patricia A. McCoy, *Turning a Blind Eye: Wall Street Finance of Predatory Lending*, 75 FORDHAM L. REV. 2039, 2045–46 (2007) (explaining loan pools are sold "to a special purpose vehicle . . . that is owned by, but legally distinct from, the lender" in order to protect assets from liability to creditors); Steven L. Schwarcz, *Structured Finance: The New Way to Securitize Assets*, 11 CARDOZO L. REV. 607, 607 (1990) (describing how special-purpose financing is used to protect assets from bankruptcy liability).

[263] *See* Alan M. White, *Rewriting Contracts, Wholesale: Data on Voluntary Mortgage Modifications from 2007 and 2008 Remittance Reports*, *available at* http://www.ssrn.com/abstract=1259538, 7–8 (concerning lack of incentives for servicers to renegotiate mortgages); Raymond H. Brescia, *Capital in Chaos: The Subprime Mortgage Crisis and the Social Capital Response*, 56 CLEV. ST. L. REV. 271, 298–99 (2008) (describing limits placed on servicers' ability to renegotiate loans and requirement for servicers to act in interest of investors as opposed to debtor); Engel & McCoy, *supra* note 262, at 2079 ("[S]ervicers have reduced incentives to assist borrowers who go into default. Servicers can earn higher fees if they march borrowers to foreclosure rather than reform the borrowers' loan terms or reschedule payments.").

[264] *See* Brescia, *supra* note 263, at 298 (suggesting securitization "makes it more difficult to handle default and avoid foreclosure" because borrower is forced to deal with parties with whom there is no established relationship); Georgette C. Poindexter, *Subordinated Rolling Equity: Analyzing Real Estate Loan Default in the Era of Securitization*, 50 EMORY L.J. 519, 535 (2001):

> [T]he biggest change in the securitization era is the increase in the number of people who now have an interest and voice in the workout and the sometimes conflicting goals of parties. Whereas in the pre-securitization era the workout was bilateral (between the lender and the borrower), a myriad of parties with differing agendas now can be involved in the negotiations.

situation could improve in the wake of the bursting of the housing bubble,[265] at least once there is a thaw in the credit markets.[266] Mortgage lenders should have incentives to keep debtors in their homes, paying something, rather than foreclosing on seriously depreciated real estate that is very hard to resell; these economic conditions should make home lenders more willing to accept a reaffirmation agreement in which the debtor pays less than the full amount owing and rolls arrearages, if any, into the new financing arrangement. The transaction costs of this approach, however, are why allowing mortgage cramdown in chapter 13 appears to be a more efficient solution to dealing with upside-down mortgages produced by the bursting of the housing bubble,[267] something Congress may eventually get around to enacting into law.[268] Congress itself increased the transaction costs of reaffirmations in the 2005 law by adding elaborate new disclosure mandates to warn debtors against impairing their fresh starts by making personal commitments to repay.[269]

When a home has dropped in value so that it is worth less than the debt, and whether or not the debtor is behind on payments, chapter 7 allows the debtor to surrender the home and discharge any deficiency that would otherwise be

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White, *supra* note 263, at 7 (discussing layers of difficulty caused by securitization when it comes to mitigating losses).

[265] *See generally* Yuliya Demyanyk & Otto Van Hemert, *Understanding the Subprime Mortgage Crisis* (Federal Reserve Bank of St. Louis, Supervisory Policy Analysis Working Paper No. 2007-05, 2008), *available at* http://stlouisfed.org/banking/SPA/WorkingPapers/SPA_2007_05.pdf (analyzing causes and effects of subprime housing crisis); Kristopher Gerardi, et al., *Subprime Outcomes: Risky Mortgages, Homeownership Experiences, and Foreclosures* (Federal Reserve Bank of Boston, Working Paper No. 07-05, 2008), *available at* http://www.bos.frb.org/economic/wp/wp2007/wp0715.pdf (assessing impact of subprime lending); Christopher L. Foote et al., *Federal Reserve Bank of Boston, Subprime Facts: What (We Think) We Know about the Subprime Crisis and What We Don't* (Federal Reserve Bank of Boston, Public Policy Discussion Paper No. 08-2, 2008), *available at* http://www.bos.frb.org/economic/ppdp/2008/mppdp0802.pdf (discussing subprime housing finance crisis).

[266] *See* Randall W. Forsyth, *A Thaw in the Freeze*, BARRONS, Oct. 20, 2008, at 22 (discussing credit crisis during fall 2008); Martin Crutsinger, *Fallout From Credit Crisis Hammers Housing*, ABC NEWS, Oct. 17, 2008, http://abcnews.go.com/Business/wireStory?id=6054182 (noting severity of credit crisis on housing markets); John Parry, *Crisis Turning Point May Yet Mirror Recent History*, REUTERS, Oct. 20, 2008, http://www.reuters.com/article/gc06/idUSTRE49J86020081020 (analyzing signs of recovery from credit crisis in late fall 2008).

[267] *See* Adam J. Levitin & Joshua Goodman, *The Effect of Bankruptcy Strip-Down on Mortgage Markets* 2 (Georgetown Univ. Law Ctr., Working Paper No. 1087816, 2008), *available at* www.ssrn.com/abstract=1087816 (concluding chapter 13 debtors should be permitted to modify mortgages secured only by debtor's residence); *see also* Sarah W. Carroll & Wenli Li, *The Homeownership Experience of Households in Bankruptcy* 6 (Federal Reserve Bank of Philadelphia, Working Paper No. 08-14, 2008), *available at* http://www.philadelphiafed.org/research-and-data/publications/working-papers/2008/wp08-14.pdf (arguing many chapter 13 debtors likely to lose homes under any circumstances).

[268] Congress considered such measures in 2008. *See* Emergency Home Ownership and Mortgage Equity Protection Act of 2007, H.R. 3609, 110th Cong. (2008) (legislation to protect homeowners in the credit crisis); Helping Families Save Their Homes in Bankruptcy Act of 2008, S. 2136, 110th Cong. (2008) (addressing "treatment of primary mortgages in bankruptcy"). They are likely to be on the legislative agenda again in 2009.

[269] H.R. REP. NO. 109-31, *supra* note 2, at 2 (noting legislation "strengthens the disclosure requirements for reaffirmation agreements").

collectible under state law.[270] The situation for vehicle loans in chapter 7 is a little different, with added complexity, but also with many similar ins and outs as for home loans. As noted above, court-protected ride-through of a current loan secured by personal property collateral is no longer generally available in chapter 7,[271] but debtors may be able to ride-through with creditor acquiescence in continued payment,[272] with the result that the debtor avoids personal liability after discharge and is subject only to losing the car for nonpayment. Alternatively, as with homes, the debtor can reaffirm and, when the collateral is worth less than the loan outstanding, attempt to negotiate for reduced payments, or the debtor can surrender the vehicle and discharge any deficiency.[273] Surrender may also be followed by getting a new loan for a replacement vehicle. Unlike for home loans, the Bankruptcy Code provides for redemption of personal property collateral,[274] and in

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[270] *See In re* Casenove, 306 B.R. 367, 370 (Bankr. M.D. Fla. 2004) (observing debtor, under 11 U.S.C. § 521(2)(A), has option to "surrender property that debtor does not wish to retain and discharge any remaining liability on the debt"); *see also* Bank of Boston v. Burr (*In re* Burr), 160 F.3d 843, 848 (1st Cir. 1998) (noting debtor in chapter 7 proceeding "can always surrender the property and be discharged of the underlying debt"); John R. Dowd, Jr., *Allowing Current Debtors to Retain Collateral Without Reaffirming or Redeeming: A Healthy Balance Between Creditor and Debtor Rights*, 17 MISS. C. L. REV. 131, 137 (2006) (observing "debtor who surrenders collateral in a Chapter 7 proceeding receives a discharge and the creditor is barred by such discharge from seeking a deficiency judgment"). Some states, such as California, already prohibit collection of deficiencies after home mortgage foreclosure. *See* CAL. CIVIL PROC. CODE § 580(b) (1996) (providing "[n]o deficiency judgment shall lie in any event after a sale of real property"). *Contra* Carter v. Derwinski, 987 F.2d 611, 618 (9th Cir. 1993) (observing "states like Idaho . . . allow deficiency judgments"); United States v. Rezzonico, 32 F. Supp. 2d 1112, 1113 (D. Ariz. 1998) (noting Arizona law only prohibits deficiency judgment "[i]f no action is maintained for a deficiency judgment within [ninety days of the trustee sale]") (alteration in original).

[271] The 2005 law, 11 U.S.C. §§ 521(a)(6), (d), 362(h)(1), provides that as to personal property, ride through is no longer a court-protected option and depends on creditor acquiescence because the automatic stay lifts if the debtor does not reaffirm or redeem. *See* Dumont v. Ford Motor Credit Co. (*In re* Dumont), 383 B.R. 481, 488 (B.A.P. 9th Cir. 2008) (holding stay lifted when debtor retained car without reaffirming or redeeming); *In re* Steinhaus, 349 B.R. 694, 700 (Bankr. D. Idaho 2006) (finding 11 U.S.C. § 362(h) "provides for termination of automatic stay under certain circumstances"); *see also In re* Rowe, 342 B.R. 341, 345 (Bankr. D. Kan. 2006) (asserting ride through no longer available). There is an exception to the lifting of the stay, however, when debtors propose to reaffirm at the full debt amount but a personal property lender spurns the offer. 11 U.S.C. § 362(h)(1)(B) (2006). Furthermore, since *pro se* debtors need court approval for reaffirmation, 11 U.S.C. § 524(c)(6)(A)(ii) (2006), it has been held that if the debtor proposes a reaffirmation that the court decides it cannot approve as in the debtor's best interests, the debtor has a right of ride through. *In re* Moustafi, 371 B.R. 434, 439–40 (Bankr. D. Ariz. 2007).

[272] Creditor acquiescence in ride through has been a longstanding practice; a creditor often prefers to take the full payment on the debt as opposed to taking back collateral and realizing less. *See* Marianne B. Culhane & Michaela M. White, *Debt After Discharge: An Empirical Study of Reaffirmation*, 73 AM. BANKR. L.J. 709, 740–41 (1999) (concerning debtors who retain their cars after bankruptcy without reaffirming or redeeming); *see also In re* Laynas, 345 B.R. 505, 517 (Bankr. E.D. Pa. 2006) ("[I]t is not obvious that court disapproval of the reaffirmation agreement would necessarily result in creditor efforts to retake possession of the vehicle if the Debtor continues to make her monthly payments."); *cf.* Braucher, Rash *and Redux*, *supra* note 246, at 476 ("It is particularly difficult to choose foreclosure when the collateral is worth less than the debt.").

[273] *See supra* notes 261, 270 (concerning same possibilities of reaffirmation or surrender as to secured loans for homes).

[274] 11 U.S.C. § 722 (2006).

recent years, prior to the new law, redemption lenders were making this option feasible for more debtors seeking to retain cars.[275] However, redemption has become less attractive and less feasible on credit under the new law because of a new provision calling for higher valuation (replacement value rather than, as before, wholesale value).[276] So-called redemption lenders as a result have switched in many cases to making loans for replacement vehicles rather than for redemption.[277] With repossessed cars piling up as excess inventory these days, some very good replacement vehicle deals are likely.[278] Statutes cannot change the market value of property; redemption versus replacement lending is an example of the reality that attempts to inflate values by statute merely prompt work-arounds.

In chapter 13, now as before the new law, purchase money secured loans for a principal residence cannot be crammed down to collateral value.[279] An issue that predates the 2005 law, but one with added importance during the current housing finance crisis, is stripping junior mortgages. Using the analysis from the Supreme Court's decision in *Nobelman v. American Savings Bank* that a loan is secured by a home when there is some value in the home to stand behind the loan,[280] courts have held that where a second or even lower priority mortgage has no collateral value to support it, it is an unsecured debt and can be modified.[281] This type of analysis gives an incentive for some debtors to file in chapter 13; stripping junior mortgages may not only make the home affordable, allowing the debtor to stay in the home, but it also means other unsecured creditors may get paid more.

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[275] *See, e.g.*, http://www.722redemption.com (website of 722 Redemption Funding, a credit arm of US Bank, and a leading provider for both redemption funding and funding for replacement vehicles after surrender).

[276] *See supra* note 248; *see also In re* Till, 301 F.3d 583, 597 (7th Cir. 2002) (observing "replacement value of an automobile to the debtor will normally be significantly higher than the wholesale value"), *rev'd and remanded by* Till v. SCS Credit Corp., 541 U.S. 465 (2004); *In re* Scott, 248 B.R. 786, 792 (Bankr. N.D. Ill. 2000) ("The difference between retail and wholesale values of used vehicles is substantial.").

[277] *See supra* note 275 (noting Redemption Funding, Inc. offers financing for replacement vehicles).

[278] *See* C. J. Hughes, *For the Repo Man, Business is Brisk*, N.Y. TIMES, Oct. 3, 2008, at NJ3 (linking souring economy with twenty-five percent rise in repossessions in metropolitan area since 2007); Posting of Jesus Sanchez to L.A. Now—LATimes.com, http://latimesblogs.latimes.com/lanow/2008/03/beware-the-repo.html (Mar. 31, 2008, 9:51) (stating auto auction company claims repossessions have risen fifteen percent from last year); *Car Buyers Get Good Deals on Repossessed Cars*, NBC, May 14, 2008, http://www.nbc6.net/money/16263075/ detail.html ("General Motors' reposessions are up 2 percent.").

[279] *See* Nobelman v. American Savings Bank, 508 U.S. 324, 329–30 (1993) (holding under 11 U.S.C. § 1322(b)(2) cramdown not permitted on loans secured only by debtor's principal residence).

[280] *See Nobelman*, 508 U.S. at 328–31 (where there was some value in home serving as collateral, reasoning loan was secured by home); *see also* Roger M. Whelan & Mandy S. Cohen, *Consumer Bankruptcy Reform: Balancing the Equities in Chapter 13*, 2 AM. BANKR. INST. L. REV. 165, 181–82 (1994) (discussing *Nobelman*).

[281] *See, e.g.*, Zimmer v. PSB Lending Corp. (*In re* Zimmer), 313 F.3d 1220, 1225 (9th Cir. 2002) (asserting unsecured creditors' rights may be modified); Lane v. Bancorp (*In re* Lane), 280 F.3d 663, 668 (6th Cir. 2002) ("Section 1322(b)(2) says, without qualification and in the plainest of English, that a Chapter 13 plan 'may' modify the rights 'of holders of unsecured claims.'"); Pond v. Farm Specialist Realty (*In re* Pond), 252 F.3d 122, 126 (2d Cir. 2001) (reasoning "wholly unsecured claim, as defined under Section 506(a), is not protected under the antimodification exception of Section 1322(b)(2)").

Probably the change concerning collateral with the biggest impact on chapter choice is the apparent elimination of cramdown on recent car loans under the so-called "hanging paragraph" of section 1325(a).[282] This provision is applicable, inter alia, to claims secured by a purchase money security interest on a debt for a motor vehicle when the purchase was of a vehicle for the personal use of the debtor and made within the 910 days preceding the bankruptcy filing (known as "910 claims").[283] The hanging paragraph provides that "section 506 shall not apply" to 910 claims;[284] section 506 is the Bankruptcy Code section for determining the extent to which claims are secured in bankruptcy.[285]

By removing 910 claims from the reach of the provision for valuation of secured claims, the hanging paragraph leaves the question what valuation approach courts should use instead. In a paragraph headed "Protections for Secured Creditors,"[286] the legislative history supplies this cryptic answer: the hanging paragraph is a "prohibition against bifurcating a secured debt."[287] Nothing could be less plain. The legislative history does not say that cramdown is prohibited; rather, it says that bifurcation is not permitted. The debt cannot be divided for different sorts of treatment, but what sort of unitary treatment is indicated? Perhaps the claim should be treated as fully unsecured or perhaps valued at wholesale value of the collateral less the cost of obtaining that value;[288] another possibility is that the

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[282] *See* 11 U.S.C. § 1325(a) (2006), hanging paragraph at end; Bankruptcy Abuse Prevention and Consumer Protection Act § 306 (codified at 11 U.S.C. § 1325) (directing inclusion of this paragraph at end of section 1325(a), but without alphanumerical designation to fit it into overall structure of section); *see also In re* Moon, 359 B.R. 329, 331 (Bankr. N.D. Ala. 2007) (discussing hanging paragraph); Braucher, *Bench and Bar*, *supra* note 107, at 120 (detailing divergent arguments regarding interpretation of hanging paragraph).

[283] Bankruptcy Abuse Prevention and Consumer Protection Act § 306 (codified at 11 U.S.C. § 1325) (providing, for purposes of 11 U.S.C. § 1325(a)(5) setting forth what plans must provide for allowed secured claims, "section 506 shall not apply" either to secured motor vehicle debts incurred within 910-days of filing to acquire vehicle for personal use or to secured claims on debts incurred within one year of filing for purchase of other personal property). Section 506 is the section on determination of the extent to which an allowed claim is a secured claim. 11 U.S.C. § 506 (2006). *See* David Gray Carlson, *Cars and Homes in Chapter 13 after the 2005 Amendments to the Bankruptcy Code*, 14 AM. BANKR. INST. L. REV. 301, 341 (2006) (explaining section 1325 does not say there can be no cramdown of new car loans, but says section 506 does not apply to determine the secured claim).

[284] 11 U.S.C. § 1325(a) (2006), hanging paragraph at end. *See In re* Jackson, 338 B.R. 923, 925 (Bankr. M.D. Ga. 2006) (calling unnumbered paragraph of 11 U.S.C § 1325(a) added by 2005 law "hanging paragraph"); *In re* Johnson, 337 B.R. 269, 273 (Bankr. M.D.N.C. 2006) (referring to "hanging paragraph" of section 1325(a)(9), because the paragraph is placed after paragraph (9) of subsection (a)).

[285] 11 U.S.C. § 506 (2006) (with caption, "Determination of secured status").

[286] H.R. REP. NO. 109-31, *supra* note 2, at 17. This paragraph of the legislative history also cryptically covers a number of other issues concerning secured claims.

[287] *Id.*

[288] Treating the whole claim as unsecured is structurally the most plausible reading; by taking these claims out of the section for determining secured claims, the suggestion of the language is that they are unsecured. *See* Braucher, Rash *and Redux, supra* note 246, at 472–74 (discussing possibilities claim should be treated as unsecured or valued in some other way than under section 506, such as by value debtor would recover on collateral by selling at wholesale, less costs of obtaining wholesale price). *But see In re* Brooks, 344 B.R.

claim should be subject to discretionary modification as a whole according to fairness principles under section 1322(b)(2).[289] Given the goal of providing protection for secured creditors, a widely-accepted assumption has been that the hanging paragraph requires valuing secured claims within its scope at the amount of the underlying debt, even when that is a fiction because the collateral is worth less than the underlying debt.[290] Problematic for this reading is some language in section 1325(a); Congress demonstrated that it knows how to say "payment of the underlying debt" in the very same subsection of the Bankruptcy Code as the hanging paragraph.[291]

Debtors' lawyers are rightly very leery of having debtors reaffirm car loans in chapter 7 when the loan balance is greater than the car value. If the debtor is unable to sustain the payments, the debtor will not be able to pay off the debt by selling or surrendering the car and will end up with an impaired fresh start. The problem of impairing the fresh start is recognized by the new disclosures concerning reaffirmation,[292] yet the 2005 law also seems to promote reaffirmation of car loans by taking away the court-protected ride-through option,[293] which has the advantage of not impairing the fresh start. Thus, if a debtor's choices are reaffirmation or surrender, surrender is the more conservative choice because it avoids impairing the fresh start. Furthermore, the debtor who surrenders an underwater car in chapter 7

417, 421 (Bankr. E.D.N.C. 2006) (holding claim not subject to bifurcation and fully secured based on "plain language" of section 506(a), "regardless of the inapplicability of § 506").

[289] *See* 8 COLLIER ON BANKRUPTCY ¶ 1325.06[1](a) (Alan N. Resnick & Henry J. Sommer eds., 15th ed. rev. 2005) ("A debtor is presumably bound only by the dictates of good faith and the other provisions of the Code in determining how such claims may be modified. Some courts, understandably, may look to prior law for guidance regarding what modifications are equitable."); *see also In re* Wampler, 345 B.R. 730, 737 (Bankr. D. Kan. 2006) ("The statutory construction explained by *Collier* and adopted by this Court is most in concert with the plain reading of the amendment and, hence, in conformity with the interpretive dictate of the U.S. Supreme Court . . . ."); Braucher, Rash *and Redux, supra* note 246, at 474 (concurring in result of *Collier* analysis).

[290] *See, e.g.*, *In re* Moon, 359 B.R. 329, 333 (Bankr. N.D. Ala. 2007) (stating that because hanging paragraph applies to section 1325(a)(5)(B), (C), surrender will satisfy creditor's claims in full); *In re* Sparks, 346 B.R. 767, 773–74 (Bankr. S.D. Ohio 2006) (asserting hanging paragraph is "unambiguous and clear" and applies to section 1325(a)(5)(C) (quoting *In re* Payne, 347 B.R. 278, 282–83 (Bankr. S.D. Ohio 2006))); *In re* Ezell, 338 B.R. 330, 340 (Bankr. E.D. Tenn. 2006) ("[A] creditor holding a secured claim falling within the scope of the Anti-Cramdown Paragraph is fully secured for the amount of its claim, which is, in actuality, the debt owed.").

[291] *See* 11 U.S.C. § 1325(a)(5)(B)(i)(aa) (2006) (requiring, absent creditor acceptance of plan, plan must provide for secured creditor to retain lien until "payment of the underlying debt" or until discharge, typically by completion of plan); *see also* Braucher, Rash *and Redux, supra* note 246, at 471–72 (discussing language of section 1325(a)(5)(B)(i)(aa)).

[292] *See* 11 U.S.C. § 524(k) (2006) (setting forth required disclosures before reaffirmation is valid); 11 U.S.C. § 524(c)(2) (2006) (requiring that debtor receive disclosures described in subsection (k) at or before the time of reaffirmation.); *see also In re* Mendoza, 347 B.R. 34, 36–37 (Bankr. W.D. Tex. 2006) (noting judicial obligation to review reaffirmation agreements for hardship).

[293] *See supra* note 271 and accompanying text; *see also In re* Donald, 343 B.R. 524, 539–40 (Bankr. E.D.N.C. 2006) (asserting Congress accomplished intention to eliminate ride-through option through 2005 law); *In re* Rowe, 342 B.R. 341, 351 (Bankr. D. Kan. 2006) (concluding Congress successfully eliminated ride through in amendments to sections 521 and 362).

discharges the deficiency.[294] Apparently the full debt must be paid in chapter 13, but if the debtor cannot handle it, the debtor can convert to chapter 7,[295] surrender the car and discharge the deficiency.[296]

It turns out that litigation has not focused on what must be paid on 910 claims when the debtor retains the collateral in chapter 13; rather it has focused on what must be paid when the debtor surrenders the collateral. Four circuits have already ruled on this issue.[297] While what treatment is required in either situation is exceedingly unclear, the language of the paragraph calls for the same treatment in cases of retention and surrender. The hanging paragraph begins, "For purposes of paragraph (5) . . . ." Paragraph (5) of section 1325(a) includes subparagraph (C) on surrender; thus section 506, providing for bifurcation according to value of the collateral, does not apply in cases of surrender; if the hanging paragraph dictates treating the claim as fully secured in cases of retention, it dictates treating it as fully secured in cases of surrender. The bankruptcy courts have come overwhelmingly to this conclusion,[298] but the circuit courts that have ruled on the issue[299] have

[294] *See In re* Vanduyn, 374 B.R. 896, 902 (Bankr. M.D. Fla. 2007) (asserting debtors' right under hanging paragraph to surrender motor vehicle "in full satisfaction of the debt owed to the secured creditor"); *In re* Pinti, 363 B.R. 369, 376 (Bankr. S.D.N.Y. 2007) (equating "surrender of 910 Vehicle to full payment of the claim, denying the creditor an unsecured claim for any deficiency after it liquidates the claim by sale of the vehicle"); *In re* Brown, 346 B.R. 868, 877 (Bankr. N.D. Fla. 2006) ("[S]urrender would . . . satisfy the creditor's allowed secured claim in full and the creditor would not be entitled to an unsecured deficiency claim.").

[295] *See* 11 U.S.C. § 1307(a) (2006) ("The debtor may convert a case under this chapter to a case under chapter 7 of this title at any time."); *see also In re* Donovan, No. 6:04-bk-01564-ABB, 2006 WL 3804676, at *4 (Bankr. M.D. Fla. Nov. 8, 2006) (holding debtor was authorized under section 1307(a) to convert chapter 13 case to chapter 7); *In re* Spencer, 137 B.R. 506, 513 (Bankr. N.D. Okla. 1992) (explaining 11 U.S.C. § 1307(a) might have been amended to avoid "locking Chapter 13 debtors into an involuntary servitude"); *supra* Part I (discussing *Marrama* case).

[296] *See* 11 U.S.C. § 727(b) (2006) (explaining discharge releases "debtor from all debts that arose before the date of the order for relief"); *In re* Marshall, 302 B.R. 711, 716 (Bankr. D. Kan. 2003) (explaining debtors' pre-petition debt may be discharged under section 727(b), subject to exceptions); *In re* May, 141 B.R. 940, 942 (Bankr. S.D. Ohio 1992) (applying section 727(b)).

[297] *In re* Wright, 492 F.3d 829, 831–33 (7th Cir. 2007) (holding, upon surrender, creditor entitled to unsecured deficiency judgment unless contract provides no recourse against borrower). The Seventh Circuit was the first circuit to so hold. The Fourth, Sixth and Tenth Circuits followed suit. *See* Tidewater Fin. Co. v. Kenney, 531 F.3d 312, 320 (4th Cir. 2008) (adopting *Wright* court's reasoning "when a [c]hapter 13 debtor surrenders a 910 vehicle in accordance with § 1325(a)(5)(C), the hanging paragraph does not extinguish a 910 creditor's unsecured deficiency claim so long as state law, in conjunction with the parties' contract, allows for such a claim"); DaimlerChrysler Fin. Servs. Ams. LLC v. Ballard (*In re* Ballard), 526 F.3d 634, 638 (10th Cir. 2008) (agreeing with *Tidewater* and *Wright*); Americredit Fin. Servs., Inc. v. Long (*In re* Long), 519 F.3d 288, 291 (6th Cir. 2008) ("In the absence of any clear bankruptcy law covering how to handle the surrender of cars and other collateral, we agree with the Seventh Circuit that the bankruptcy courts should not simply allow the debtor to surrender the car and then wipe out the deficiency . . . .").

[298] *See, e.g.*, *In re* Payne, 347 B.R. 278, 283 (Bankr. S.D. Ohio 2006) (holding lender is prevented from asserting unsecured deficiency claim when debtor surrenders vehicle because section 506 bifurcation is inapplicable); *see also In re* Ezell, 338 B.R. 330, 341 (Bankr. E.D. Tenn. 2006) (stating "were the court to find that a secured creditor whose collateral has been surrendered under [section 1325(a)(5)(C)] is entitled to file either a secured or unsecured deficiency claim, the method of determining the amount of the allowed deficiency claim would be demonstrably at odds with [section 506(a)]"); *In re* Kenney, Nos. 06-71975-A,

followed the Seventh Circuit to conclude that undersecured 910 claims should be bifurcated after surrender of the collateral, so that the lender has an unsecured deficiency claim.[300] The opinion of the Seventh Circuit in *In re Wright*,[301] written by Judge Easterbrook, ignores the introductory phrase of the hanging paragraph of section 1325(a) and also takes the position that state law calls for bifurcating claims in bankruptcy in the absence of the applicability of section 506.[302] There is no text to support this analysis, which turns section 506 into surplusage; if undersecured claims are already bifurcated in bankruptcy under state law, there is no need for section 506 to do the bifurcation work.

The Sixth Circuit in *In re Long* reached the same result as the Seventh Circuit, rejecting surrender in full satisfaction in chapter 13, while also finding the literal statutory language to the contrary; it relied instead on "the equity of the statute,"[303] that is, Congress intended "only good things for car lenders" under the hanging paragraph.[304] This is an overreading of legislative history, which refers to fairness for creditors, including unsecured creditors, as well as for debtors.[305] Furthermore,

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07-70359-A2007, 2007 WL 1412921, at *5 (Bankr. E.D. Va. May 10, 2007) (labeling creditor inability to obtain deficiency judgment "majority view"). The Seventh Circuit called this the "majority position" when rejecting it. *In re Wright*, 492 F.3d at 830 ("The majority view among bankruptcy judges is that, with section 506(a) gone, creditors cannot divide their loans into secured and unsecured components."). *See also* KEITH M. LUNDIN, CHAPTER 13 BANKRUPTCY 446, ¶¶ 2, 3 (3d ed., Bankruptcy Press, Inc. 2000 & Supp. 2007-1) (explaining because 2005 law requires treating claims in hanging paragraph as fully secured, section 506 is not available to split claim, so surrender of collateral eliminates claim).

[299] *See In re Wright*, 492 F.3d at 833; *Tidewater*, 531 F.3d at 318; *In re Ballard*, 526 F.3d at 638; *In re Long*, 519 F.3d at 294.

[300] *See supra* note 297 and accompanying text.

[301] 492 F.3d at 829.

[302] *See id*. at 832 (relying on Butner v. United States, 440 U.S. 48 (1979), for proposition "state law determines rights and obligations when the Code does not supply a federal rule"); *Tidewater*, 531 F.3d at 318 (following reasoning that state law applies when Bankruptcy Code fails to provide rule); Wells Fargo Fin. Acceptance v. Rodriguez (*In re* Rodriguez), 375 B.R. 535, 545 (B.A.P. 9th Cir. 2007) ("The answer, according to *Wright*, is found in the parties' contract to the extent the deal is enforceable under state law."). This analysis begs the question whether bankruptcy law supplies a federal rule. *Compare In re Long*, 519 F.3d at 291 (finding deficiency judgements should not be left to state law because Congress intended to "federalize . . . treatment of purchase-money mortgages in bankruptcy"), *with* DaimlerChrysler Fin. Servs. Ams. LLC v. Barrett (*In re* Barrett), Nos. 07-14796, 07-14797, 2008 WL 4378739, at *5 (11th Cir. Sept. 29, 2008) (determining 2005 law did not create federal deficiency rule), *and In re Ballard*, 526 F.3d at 639 ("The Bankruptcy Code does not . . . qualify a creditor's state-law entitlement to a deficiency claim.").

[303] Americredit Fin. Servs., Inc. v. Long (*In re* Long), 519 F.3d 288, 297 (6th Cir. 2008) ("In determining how to fill the gap left by Congress after the 2005 amendments, we employ a well-established common-law principle of interpretation known as the 'equity of the statute.'"). *See* North Dakota v. Fredericks, 940 F.2d 333, 337 (8th Cir. 1991) (explaining "equity of the statute" as applicable "in cases within the spirit of the enactment, but not within its letter").

[304] *In re Long*, 519 F.3d at 294 (quoting KEITH M. LUNDIN, CHAPTER 13 BANKRUPTCY 451.5-1 (3d Ed. Supp. 2007). *See* Margaret Howard, *The Law of Unintended Consequences*, 31 S. ILL. U. L.J. 451, 454 (2007) (noting hanging paragraph "makes automobile lenders big winners when debtors choose to keep their cars in chapter 13"); Whitford, *Automobile Lender*, *supra* note 246, at 150 (discussing "improvements in the auto lender's position" after 2005 law).

[305] *See supra* note 243 and accompanying text; *cf. In re* Brown, 346 B.R. 868, 875 (Bankr. N.D. Fla. 2006) ("While the Court agrees that some changes to the Code were made with secured creditors in mind, it is

the Sixth Circuit opinion by Judge Merritt[306] finds fault with Judge Easterbrook's reasoning in *In re Wright* because it undermines national uniformity in bankruptcy by making deficiency judgments in bankruptcy "depend entirely on the vagaries of state laws as to foreclosures, repossession, sale and judicial remedy."[307] Judge Merritt instead called for application of pre-2005 law to determine the secured and unsecured claims of an undersecured 910 claimholder after surrender of collateral,[308] which means applying section 506 even though the 2005 law says in the hanging paragraph that section 506 "does not apply" to 910 claims for purposes of section 1325(a)(5).[309]

There is no indication in legislative history that Congress thought about surrender, but policy analysis supports surrender in full satisfaction in chapter 13. The Seventh Circuit was troubled by applying the hanging paragraph in the same way to both retention and surrender cases, despite the language of the hanging paragraph, because in cases of surrender this has the effect of "making all purchase-money secured loans non-recourse."[310] The court's analysis, however, leaves out that this is exactly what surrender in chapter 7 does in no-asset cases; the personal obligation is discharged in chapter 7 and the secured creditor has recourse only against its collateral.[311] It is not so extraordinary to provide for the same treatment in

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equally clear to the Court that some of the changes may have been made for the benefit of unsecured creditors, such as credit card companies.").

[306] *In re Long* was decided 1-1-1, with Circuit Judge Merritt writing for the court, another judge concurring on other grounds and the third judge dissenting. 519 F.3d at 290, 299, 301.

[307] *Id*. at 291.

[308] *Id*. at 298 ("We hold that claims subject to the hanging paragraph where the debtor elects to surrender the collateral pursuant to § 1325(a)(5)(C) will be governed and adjudicated the same as they were before the 2005 amendments.").

[309] 11 U.S.C. § 1325(a) (2006), hanging paragraph at end. *See* Capital One Auto Fin. v. Osborn, 515 F.3d 817, 821 (8th Cir. 2008) ("By the plain language of the hanging paragraph, § 506 does not apply to a 910-claim."); DaimlerChrysler Fin. Servs. Ams. LLC v. Ballard (*In re* Ballard), 526 F.3d 634, 637–38 (10th Cir. 2008) (finding hanging paragraph prevents section 506 from applying to 910 car claims).

[310] *In re* Wright, 492 F.3d 829, 832 (7th Cir. 2007); *accord* Americredit Fin. Servs., Inc. v. Long (*In re* Long), 519 F.3d 288, 300 (6th Cir. 2008) ("The majority position that deficiency claims are no longer allowed for 910 claims by virtue of the hanging paragraph's elimination of § 506 effectively renders 910 secured loans non-recourse, without regard to the contractual terms."); Capital One Auto Fin. v. Osborn, 515 F.3d 817, 821 (8th Cir. 2008) (reasoning surrender of 910 car fully satisfies claim and "essentially turns a recourse loan into a non-recourse loan, to the benefit of unsecured creditors").

[311] 11 U.S.C. § 727(b) (2006) ("[A] discharge under subsection (a) of this section discharges the debtor from all debts that arose before the date of the order for relief under this chapter . . . ."); *see* Everly v. 4745 Second Ave., Ltd. (*In re* Everly), 346 B.R. 791, 794 (B.A.P. 8th Cir. 2006) ("Pursuant to 11 U.S.C. § 727(b), a discharge in a Chapter 7 case discharges the debtor from all debts that arose before the date of filing . . . ."); Schott v. WyHy Fed. Credit Union (*In re* Schott), 282 B.R. 1, 5 (B.A.P. 10th Cir. 2002) (stating chapter 7 relieves debtors of in personam liability). It should be noted that the overwhelming majority of chapter 7 cases are no asset. *See* NATIONAL BANKRUPTCY REVIEW COMMISSION, BANKRUPTCY: THE NEXT TWENTY YEARS 137 (1997), http://govinfo.library.unt.edu/nbrc/report/05ccons.pdf (reporting five percent of chapter 7 cases are no asset and most of revenue from that five percent is from business, not consumer, cases); *In re* Ambotiene, 316 B.R. 25, 37–38 n.4 (Bankr. E.D.N.Y. 2004) (citing Administrative Office of U.S. Courts data reporting "overwhelming majority of cases administered by Chapter 7 trustees [in E.D.N.Y.] have few or no assets to administer").

chapter 13 when the debtor surrenders the collateral in that chapter. The Supreme Court in *Associates Commercial Corp. v. Rash* has already reasoned that, from the point of view of the secured creditor, collateral retention by the debtor is quite different from surrender; when collateral is retained by the debtor, the creditor faces dual risks of default and depreciation in the meantime.[312] With surrender, the creditor gets its collateral value immediately and faces no further risks in that transaction.[313]

The advantage of extinguishing the deficiency upon surrender of 910 collateral in chapter 13 is primarily to other unsecured creditors. If the secured creditor gets to have a deficiency claim and then to share pro rata with other unsecured creditors, there will be less for them. Furthermore, there is an efficiency gain to the system from surrender in full satisfaction because there is no issue of valuation of the secured and unsecured portions of the claim.[314] The debtor also gets an advantage, in that the deficiency claim is extinguished and the debtor does not have to worry about it in the event the plan fails and no discharge is obtained in chapter 13, a common occurrence.[315] On the other hand, this gain is not huge over current law because if the plan fails, the debtor has the options to convert to chapter 7[316] or refile there, in either case with the effect of discharging the deficiency.[317] The primary benefit to the debtor, then, from surrender in full satisfaction is in saving procedural costs to get discharge of the deficiency upon plan failure. Otherwise, giving the undersecured car lender an unsecured deficiency claim after surrender only hurts other unsecured creditors, because their distributions in chapter 13 are reduced when they have to share pro rata with the car lender's deficiency claim.

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[312] *See* Associates Commercial Corp. v. Rash, 520 U.S. 953, 962–63 (1997); *see also In re* Turkowitch, 355 B.R. 120, 129–30 (Bankr. E.D. Wis. 2006) (making point in context of surrender case); *In re* Chubb, 351 B.R. 478, 490 (Bankr. E.D. Tenn. 2004) (citing *Rash* for proposition retention is riskier for creditor than surrender).

[313] *See Rash*, 520 U.S. at 962–63 (noting creditor free to reinvest proceeds after surrender of collateral, avoiding risks associated with debtor retaining property); *In re* Chubb, 351 B.R. at 490 (recognizing Supreme Court in *Rash* found creditor may sell debtor's surrendered property and reinvest proceeds).

[314] *See In re* Brown, 346 B.R. 868, 876–77 (Bankr. N.D. Fla. 2006) (noting this advantage); *see also In re* Blanco, 363 B.R. 896, 900–01 (Bankr. N.D. Ill. 2007) ("Most of the cases that have addressed this issue conclude that the surrender of a vehicle to a creditor under § 1325(a)(5)(C) constitutes full satisfaction of the allowed secured and unsecured claim components.").

[315] *See* Norberg & Velkey, *supra* note 180, at 476 (noting two-thirds of chapter 13 debtors historically have not received discharge).

[316] 11 U.S.C. § 1307(a) (2006). *See* Tidewater Fin. Co. v. Williams, 498 F.3d 249, 252 (4th Cir. 2007) ("[A] debtor, as a matter of right, may at any time dismiss his [c]hapter 13 petition or convert it to a [c]hapter 7 proceeding."); *In re* Baker, 289 B.R. 764, 769 (Bankr. M.D. Ala. 2003) (finding conversion from chapter 13 to chapter 7 "matter of right" when no previous conversion has taken place); *see also supra* Part I (discussing *Marrama* case).

[317] *See* 11 U.S.C. § 727(b) (2006); *see also, e.g.*, *In re* Marshall, 302 B.R. 711, 716 (Bankr. D. Kan. 2003) (explaining debtors' prepetition debt may be discharged under section 727(b), subject to exceptions); *In re* May, 141 B.R. 940, 942 (Bankr. S.D. Ohio, 1992) (concluding discharge under section 727(a) discharges debtor from all other debts under chapter 7 pursuant to section 727(b)).

The fairness objective of the hanging paragraph,[318] if the paragraph is applied equally to retention and surrender as the language directs, could be to recognize the increased risk to the secured creditor in cases of retention and to promote use of chapter 13 by debtors intending to surrender; they get an immediate release from the secured claim, as they would with a chapter 7 discharge, and they get the satisfaction of seeing more paid to the rest of their unsecured creditors, often an objective of chapter 13 debtors.[319] Debtors in chapter 13 are already required to commit their disposable income when they are not paying creditors in full,[320] so the primary effect of giving an undersecured lender an unsecured claim for the deficiency is to reduce distributions to other unsecured creditors.

A new front has opened under the hanging paragraph, concerning who is in and who is out of the 910 claim category, as opposed to the treatment 910 loans get. The most complex issue[321] concerning scope of the 910 category is whether a claim on a debt that includes rollover of negative equity on a previous loan for a vehicle traded in as part of purchase of another vehicle is nonpurchase money in whole or part, thus not getting 910 claim status so that it can be crammed down.[322] As with the issue of surrender in full satisfaction, there is no indication Congress gave the

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[318] *See supra* notes 243–44 and accompanying text (discussing congressional intent of ensuring fairness to both debtors and creditors).

[319] *See supra* note 174 and accompanying text (noting debtors often choose chapter 13 out of desire to pay as much of debts as possible).

[320] 11 U.S.C. § 1325(b) (2006). *See* Waldron v. Brown (*In re* Waldron), 536 F.3d 1239, 1245 (11th Cir. 2008) (noting amount that must be paid in chapter 13 plan depends on debtors' disposable income at time of confirmation); U.S. Trustee v. Cortez (*In re* Cortez) 457 F.3d 448, 457 (5th Cir. 2006) (holding all disposable income of debtor must be accounted for under chapter 13 plan).

[321] Another issue, not discussed in the text, concerns the scope of purchase "for the personal use of the debtor," a phrase that is different from the phrase used in 11 U.S.C. § 506(a)(2) ("acquired for personal, family, or household purposes"). Courts have had to wrestle with whether the "personal use of the debtor" requirement excludes loans for a vehicle for someone else in the debtor's household, for use by the family as a whole, or loans for a combination of business and personal purposes. *See In re* Cross, 376 B.R. 641, 646–47 (Bankr. S.D. Ohio 2007) (discussing divergent approaches and stating "application of the personal-use test to each [c]hapter 13 debtor's unique family situation will inevitably involve consideration of myriad different factual permutations"); *see also In re* Martinez, 363 B.R. 525, 527 (Bankr. S.D. Texas 2007) (adopting totality of circumstances test to conclude car was used for business purposes where debtor drove it to and from work and for work errands); *In re* Finnegan, 358 B.R. 644, 647–48 (Bankr. M.D. Penn. 2006) (concluding personal use did not include use by debtor's husband for his business, thus restrictions on cramdown under hanging paragraph of 1325(a) did not apply). Loans for 910 vehicles acquired for business purposes only can be crammed down. *See In re* Garrison, No. A06-00396-DMD, 2007 WL 1589554 at *2 (Bankr. D. Alaska June 1, 2007) (holding where there was "substantial business use for the vehicle" debtor not barred from bifurcating creditor's claim under section 506(a)(2), which provides for valuation of business collateral at replacement value, not retail value); *cf. In re Cross*, 376 B.R. at 645 (asserting debtor may not cram down if car acquired for personal use).

[322] *See* 11 U.S.C. § 1325(a) (2006), hanging paragraph at end (stating "section 506 shall not apply to a claim . . . if the creditor has a purchase money security interest securing the debt that is the subject of the claim"); *In re* Mitchell, 379 B.R. 131, 136 (Bankr. M.D. Tenn. 2007) (deciding whether debt was part of price of vehicle, and thus, purchase money security interest); *In re* Sanders, 377 B.R. 836, 845 (Bankr. W.D. Texas 2007) (discussing "lively dispute" embodied in two lines of cases addressing whether negative equity was purchase money entitled to protection of 910-day provision).

negative equity issue any thought at all. The first circuit court to reach this issue, the Eleventh Circuit, concluded that rollover of negative equity into a loan for another car does not impair purchase money status.[323] The court noted that dozens of lower courts have confronted the issue and reached contrary conclusions;[324] the courts that find financing negative equity on trade-ins is not purchase money lending have further split on whether these loans lose purchase money status entirely in such cases or instead have dual status, partially secured and partially unsecured.[325] The transformation rule, that the loan becomes entirely nonpurchase money when negative equity is rolled in, finds support in the lack of "to the extent of" language concerning debts secured by a purchase money security interest.[326]

The negative equity issue is actually more important for debtors than the issue whether there is an unsecured deficiency on surrender, which as noted above, primarily affects other unsecured creditors.[327] If a debt is not purchase money, it can be crammed down under the 2005 law,[328] but only to retail value where the debt is for personal, family, or household purposes as opposed to business purposes.[329] Still, from the debtor's point of view, some cramdown is better than none. When debtors can bifurcate and pay retail value to the secured creditor, rather than the full amount of the outstanding debt, debtors are more likely to be able to afford to retain cars in chapter 13. In addition, they are more likely to have something left over to pay unsecured creditors.

The Eleventh Circuit case may not be indicative of how other circuits will hold on the issue of impact on purchase money status of rolling in negative equity from a prior loan; that court relied on a nonuniform Georgia motor vehicle statute to come

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[323] Graupner v. Nuvell Credit Corp. (*In re* Graupner), 537 F.3d 1295, 1300–01 (11th Cir. 2008) (holding negative equity was purchase money because it was "'debt for the money required to make the purchase' of the new vehicle" (quoting Snap-On Tools, Inc. v. Freeman (*In re* Freeman), 956 F.2d 252, 255 (11th Cir. 1992))). *See In re* Myers, 393 B.R. 616, 622 (Bankr. S.D. Ind. 2008) (holding purchase money includes negative equity); *see also* General Motors Acceptance Corp. v. Peaslee, 373 B.R. 252, 259–60 (W.D.N.Y. 2007) (noting routine nature of including negative equity in purchase of new vehicle, and "that the unpaid balance . . . can and should be . . . entitled to a purchase money security interest") (see Peaslee v. GMAC, LLC (*In re* Peaslee), No. 07-3962-bk(L), 2008 WL 4614524 (2d Cir. Oct. 20, 2008), certifying issue to New York Court of Appeals).

[324] *In re Graupner*, 537 F.3d at 1300 (acknowledging some courts hold "certain components of the loan, most notably negative equity in a trade-in-vehicle, do not constitute a purchase money security interest"). *See, e.g.*, *In re* Acaya, 369 B.R. 564, 570 (Bankr. N.D. Ca. 2007) (holding negative equity is not purchase money security interest); *In re* Bray, 365 B.R. 850, 862 (Bankr. W.D. Tenn. 2007) ("[C]ourts typically find that [] negative equity is not included within a party's purchase money security interest . . . .").

[325] *In re Graupner*, 537 F.3d at 1300. *Compare In re Mitchell*, 379 B.R. at 142 (holding "only claims secured entirely by the PMSI are excepted from 11 U.S.C. § 506"), *with In re Acaya*, 369 B.R. at 571 (adopting dual-status rule).

[326] *Compare* 11 U.S.C. § 506(a)(1) (2006) (providing claim secured "*to the extent of* the amount subject to setoff") (emphasis added), *with* 11 U.S.C. § 1325(a) (2006), hanging paragraph at the end (lacking "to the extent of" language).

[327] *See supra* notes 313–17 and accompanying text.

[328] 11 U.S.C. §§ 506(a), 1325(a) (2006).

[329] 11 U.S.C. § 506(a)(2) (2006).

to that conclusion.[330] It went on to rely on the Uniform Commercial Code,[331] but that part of the opinion could be considered unnecessary and therefore dicta.

Since the Bankruptcy Code contains no definition of purchase money security interest either in section 101 or in section 1325, the best solution is to apply the U.C.C.[332] The Bankruptcy Code does make use of the purchase money security interest concept, without using those words, in section 547 on preferences[333] and the concept there is consistent with the U.C.C. definition, in section 9-103.[334] There is a good argument that the courts that have found rollover of negative equity does not impair purchase money status are misreading the U.C.C. The technical argument has been made at length in an amicus brief filed in *In re Peaslee* by a group of law professors.[335] In summary, the argument is that Article 9's definition covers two

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[330] *See* Graupner v. Nuvell Credit Corp. (*In re* Graupner), 537 F.3d 1295, 1301 (11th Cir. 2008); *see also* Snap-On Tools, Inc. v. Freeman (*In re* Freeman), 956 F.2d 252, 253 (11th Cir. 1992) (permitting debtor to avoid creditor's lien as non-possessory, non-purchase money security interest).

[331] *In re Graupner*, 537 F.3d at 1301–02 (noting "the focus of the definition of a purchase money security interest under the U.C.C. is on the 'purchase-money obligation' that is secured by the collateral, and this definition contains two prongs: (i) the price of the collateral; and (ii) value given to enable the debtor to buy the collateral"). *See* Peaslee v. GMAC, LLC (*In re* Peaslee), No. 07-3962-bk(L), 2008 WL 4614524, at *1 (2d Cir. Oct. 20, 2008) (noting issue regarding negative equity turns on U.C.C. section 9-103 definition of "purchase-money obligation" and certifiying the question to the New York Court of Appeals); *In re* Dale, No. 07-CV-3176, 2008 WL 4287058, at *4 (S.D. Tex. Aug. 14, 2008) (recognizing importance of U.C.C. section 9-103 in determining issue of negative equity).

[332] S*ee* Butner v. United States, 440 U.S. 48, 54–55 (1979) (concerning use of state law when Bankruptcy Code does not address an issue); *see also In re* Muldrew, No. 08-11866, 2008 WL 4458798, at *8–9 (E.D. Mich. Oct. 3, 2008) (applying state law definition of purchase money security interest to bankruptcy case because Bankruptcy Code lacks official definition). The definition of "purchase money security interest in goods" in U.C.C. section 9-103(b)(1) (2006) incorporates a definition of "purchase-money collateral," which in turn incorporates a definition of "purchase money obligation," providing in pertinent part in section 9-103(a)(2) that it means "an obligation of an obligor incurred as all or part of the price of the collateral or for value given to enable the debtor to acquire rights in or the use of the collateral if the value is in fact so used."

[333] 11 U.S.C. § 547(c)(3)(A)(iii)–(iv) (2006):

> The trustee may not avoid under this section a transfer . . . that creates a security interest in property acquired by the debtor (A) to the extent such security interest secures new value that was . . . (iii) given to enable the debtor to acquire such property; and (iv) in fact used by the debtor to acquire such property . . . .

See In re Alexander, 219 B.R. 255, 259 (Bankr. D. Minn. 1998) (noting usage of section 547(c)(3)(A) in connection with determination of purchase money security interest); c*f.* Kuhnel v. Kuhnel (*In re* Kuhnel), 495 F.3d 1177, 1181 (10th. Cir. 2007) (discussing purchase money security agreement as avoidable under section 547 if creditor fails to perfect security interest).

[334] *See supra* note 332 (detailing U.C.C. definition of "purchase money security interest"); *see also In re* Munzberg, 388 B.R. 529, 535–36 (Bankr. D. Vt. 2008) (finding courts should use state commercial laws to define "purchase money security interest" in bankruptcy context); *In re* Dunlap, 383 B.R. 113, 117 (Bankr. E.D. Wis. 2008) (acknowledging lack of "purchase money security interest" definition in Bankruptcy Code and using state code definition).

[335] Ingrid M. Hillinger, of counsel, *Defs. Amicus Cuirae Br*., (Dec. 19, 2007) [hereinafter Hillinger, *Amicus Brief*] *available at* http://www.nacba.org/s/45_50fc1f2acc4e329/files/PeasleeSupportBrief.pdf (the author was one of the professors who signed this amicus brief); *see In re* Mierkowski, No. 08-44196-399, 2008 WL 4449471, at *2–3 (Bankr. E.D. Mo. Sept. 29, 2008) (noting differing views on negative equity effect on

kinds of purchase money loan, credit sales and third-party loans.[336] Credit sales are covered by the language concerning loans for "the price" and third-party loans are covered by the final part of the definition, that is, that the obligation is "for value given to enable the debtor to acquire rights in or the use of the collateral if the value is in fact so used."[337] A number of bankruptcy courts and the Eleventh Circuit have misread this language to cover loans for negative equity because the lender will not permit the buyer to get a loan unless the negative equity is paid off,[338] but that does not mean that the negative equity financing is for purchase of the collateral, the new car. The key point is that a refinancing of a loan for a car already owned and being traded in is not a purchase money loan even if it is rolled into one consolidated loan also financing the new car.

Policy arguments can support this position in bankruptcy. Rollover of negative equity creates large and risky loans that are undersecured, often seriously undersecured, from the outset, before the debtor even drives the new car off the lot. In the climate of credit mania in recent years, negative equity financing increased dramatically, reaching perhaps as high as thirty-eight percent of new car loans in 2005 and 2006.[339] Negative equity lending goes further even than the risk of zero-down new car financing, in which auto lenders know they will be undersecured as soon as the car goes from being new to being used.[340] Debtors who rollover

purchase money status). *But see In re* Look, 383 B.R. 210, 219 (Bankr. D. Me. 2008) (discussing loss of purchase money status in negative equity financing).

[336] Hillinger, *Amicus Brief*, *supra* note 335, at 13–15.

[337] U.C.C. § 9-103(a)(2) (2006). *See In re* Johnson, 380 B.R. 236, 245 n.8 (Bankr. D. Or. 2007) ("[T]he UCC recognizes a greater need to protect the PMSI which is based on the 'price of the collateral' than the PMSI based on the enabling loan."); *In re* Conyers, 379 B.R. 576, 580 (Bankr. M.D.N.C. 2007) ("[T]he two essential phrases included in the definition of purchase-money obligation are 'the price of the collateral' and 'value given to enable the debtor to acquire rights in or the use of the collateral.'").

[338] *See* Graupner v. Nuvell Credit Corp. (*In re* Graupner), 537 F.3d 1295, 1302 (11th Cir. 2008) (calling negative equity financing part of "package deal" with new car financing); *see also In re Dunlap*, 383 B.R. at 118 (holding negative equity was purchase money security interest, and reasoning "payment of the balance due on the trade-in car was a prerequisite to consummating this transaction. . . . There is a close nexus in this case between the acquisition by the debtors of the new car and the entire secured obligation, including the negative equity portion."); *cf. In re* Austin, 381 B.R. 892, 897 (Bankr. D. Utah 2008) (combining purchase price of the new vehicle and negative equity from trade-in as acceptable purchase money security interest).

[339] *See In re Graupner*, 537 F.3d at 1303 (quoting industry sources stating negative equity financing used in twenty-nine to thirty-eight percent of new car lending "in past years, and that figure appears to only be on the rise"); Michael Martinez, *Vehicle Repos in High Gear*, CHICAGO TRIBUNE, May 19, 2008, at C1 (describing in March 2008, average negative equity on new car purchase was $4,305, an increase from $3,270 six years prior); *cf.* Michelle Singletary, *Cars Worth Less Than the Loans*, WASH. POST, Apr. 29, 2007, at F1 ("In the first quarter of 2007, 29 percent of consumers were upside down on their vehicles . . . .").

[340] Depreciation on new cars is often in the range of twenty-five to thirty percent as soon as they are driven long enough to be considered used cars. *See* FEDERAL TRADE COMMISSION, A DEALER'S GUIDE TO THE USED CAR RULE 1 (2004), http://www.ftc.gov/bcp/edu/pubs/business/autos/bus13.pdf ("[A]ny vehicle driven for purposes other than moving or test driving . . . is considered a used vehicle . . . ."); Phillip Reed, *Drive a (Nearly) New Car for (Almost) Free!*, http://www.edmunds.com/advice/strategies/articles/77147/article.html (last accessed Nov. 4, 2008) (estimating loss of value at twenty percent moment car leaves lot).

remaining balances on old car loans into consolidated loans for the old debt as well as to acquire another car build up a snowball of debt, one that becomes progressively less manageable with repetitive negative equity financing. Congress might want auto lenders to be more cautious about making such loans. Treating these risky, undersecured loans as fully secured in chapter 13 bankruptcy, at the expense of other unsecured creditors, is not a good way to encourage prudence. Another way to think about the policy question is that the idea of "fairness to secured creditors" behind the hanging paragraph may have been focused on debtors who take out ordinary new car loans right before filing and then cram them down on an unsuspecting creditor. The congressional purpose to achieve fairness did not necessarily extend to creditors who promoted over-borrowing by negative equity financing. These creditors not only gave a loan for the new car, they also encouraged debtors to take out big loans by telling them they could finance not only their new car, but also continue to finance their previous car. This is the kind of lending that leads to more bankruptcy, and fairness to secured creditors need not entail bailing out those who made the most aggressive, risky and high-cost loans.

Collateral issues are among the trickiest in the 2005 bankruptcy law. Part of the problem is lack of signs that Congress thought about many of these issues or figured out how provisions in chapter 7 and chapter 13 might interact. Courts can help to make sense of the provisions on secured lending by attempting to reconcile fairness to secured creditors with fairness to unsecured creditors and debtors and also by taking account of perverse incentives to avoid chapter 13 if retention or surrender of collateral is more difficult there than in chapter 7.

CONCLUSION

The many interpretation issues created by the 2005 bankruptcy law are working their way through the bankruptcy courts and up to the appellate level. In this context, bankruptcy courts and the rest of the federal judiciary should take note that the U.S. Supreme Court nearly always considers purpose and policy arguments when interpreting bankruptcy law and sometimes treats this type of analysis as more important than statutory language and structure. The legislative history of the 2005 law shows that Congress had three main purposes: consumer protection, abuse prevention and fairness to debtors and creditors. This article has reviewed how these purposes and related policies can inform interpretation of some of the most difficult questions of interpretation under the new law. It has also explored why purpose and policy analysis is so frustrating and difficult when it comes to this particular law; the reason is that the facts have turned out to be different from what Congress seems to have assumed.

Courts should interpret the provisions of the 2005 law that have consumer protection purposes to help consumer debtors and minimize unintended consequences of impairing their access to bankruptcy and confusing them. Thus, debtors who filed in bankruptcy without first getting a required briefing on available credit counseling should be given a chance to fix their temporary ineligibility by getting the counseling and filing a new petition, particularly in light of a government study finding no benefit in the requirement and legislative silence about the remedy for not getting counseling before filing. Furthermore, debtors' lawyers at a minimum should be permitted to improve upon confusing "model" disclosures required of "debt relief agencies" (a term that seems to take in both debtors' lawyers and nonlawyer petition preparers, thus potentially confusing consumers).

The consumer protection provisions of the 2005 law involve relatively easy questions of interpretation from a purpose and policy perspective when compared to the new law's abuse prevention provisions, particularly the question whether the detailed presumed abuse means test used in both chapters 7 and 13 should be backstopped with additional judicially-designed means testing. Government data show little impact from the new "presumed abuse" approach in either chapter. However, given that Congress sought to limit judicial discretion with its detailed new test, the best course for the judiciary is not to attempt to compensate for legislative factual error by inventing its own secondary layers of highly discretionary means testing in both chapters. If Congress wants to revisit reform, it can decide whether to toughen the test or alternatively perhaps go back to trusting the courts to police abuse under a broad discretionary test. The least desirable policy approach is to burden debtors and the courts with two levels of means testing in each chapter, one formulaic and the other discretionary.

The most difficult issues of all may be those concerning treatment of secured claims under the 2005 law. Congress sought fairness for secured creditors but also fairness for all involved in the bankruptcy system, which means for debtors and unsecured creditors, too. Thus, it is entirely appropriate for the courts to interpret the new provisions on secured loans to avoid creating disincentives to use chapter 13 and to discourage the riskiest types of loans, setting some limits on new solicitude for secured creditors in pursuit of the overall fairness purpose of the new law.