

LITIGATING THE PRESUMPTION OF ABUSE UNDER SECTION 707

A. POST-BAPCPA CASE LAW § 707(b)(2)

1. *In re Heath*, 2007 WL 1982194 (Bankr. E.D. Mich. 2007).

Facts: The presumption of abuse arose, and Debtor attempted to rebut the presumption based upon a reduction in income after being forced into early retirement due to a disability.

Holding: The Court held that Debtor's unemployment, which is through no fault of her own, was a special circumstance sufficient to rebut the presumption of abuse arising from the application of the means test. The Court focused on the fact that Debtor was a 51 years old, unskilled assembly line worker with material restrictions due to carpal tunnel syndrome, was forced into early retirement resulting in a decrease in her income by half, from what it was over the six month period prior to the filing of the bankruptcy petition.

In deciding whether the alleged circumstances have left a Chapter 7 debtor with "no reasonable alternative" but to incur additional expense or to adjust his or her income downward, as required to rebut the presumption of abuse arising from the application of the means test, a court should distinguish between actions that are reasonable and conceivable in the long-term, such as moving or looking for employment, are not necessarily alternatives that are reasonable or feasible for the debtor to employ during the time it takes to confirm a chapter 13 case.

2. *In re Zaporski*, 366 B.R. 758 (Bankr. E.D. Mich. 2007).

Facts: Debtor, who was single, owned two cars free and clear. Debtor took reductions for both ownership and operation expenses for both vehicles. The United States Trustee filed a motion to dismiss chapter 7 debtor's case for abuse under 11 U.S.C. § 707(b)(2) and (3), arguing that Debtor was not entitled to either of these reductions since it is undisputed that Debtor owns the vehicles outright and makes no payments on either of them. **Holding:** Debtor was entitled to take reductions for (a) ownership expenses for two

vehicles even though Debtor even though he had no actual payments on either of them; and (b) for IRS Local Standards operation expenses for both vehicles.

With respect to the vehicle ownership reductions, the Court concluded that the IRS Local Standards are fixed allowances, and not caps on a debtor's actual expenses, and therefore permit a debtor to take a reduction for an ownership expense of vehicles even if the debtor owns a vehicle free and clear and has no actual payments for the vehicle. The Court relied on relevant case law including the decisions of the courts in *Grunert* and *Farrar-Johnson*. Moreover, the Court held that a plain reading of the statutory language makes clear that a debtor's actual expenses are irrelevant in determining reductions for National and Local Standards under Section 707(b)(2)(A)(ii)(I).

Similarly with respect to operating expense deductions, the Court held that in calculating such reductions under the means test, there is no specific statutory requirement that the debtor have *actual* transportation expenses under Local Standards for Transportation. The debtor gets the allowance without regard to actual operating costs.

Ultimately, the court, however, dismissed the debtor's case under section 707(b)(3)(B), because debtor had the ability to fund a chapter 13 plan. See discussion below for court's analysis under § 707(b)(3).

3. *In re Travis*, 353 B.R. 520 (Bankr. E.D. Mich. 2006).

Facts: The debtor included his non-filing spouse's income for means testing purposes but subtracted \$2,616 as a Marital Adjustment on line 17 of Form B22A. Line 17 allows a non-filing spouse to deduct income that is not contributed to household expenses. The UST objected to the debtor deducting the \$2,616, arguing that allowing the debtor to use the median income for a family of five, including the non filing spouse, and to deduct for income the debtor did not contribute to the household expenses, amounted to "double dipping."

Holding: The Court recognized the complicated nature of calculating current monthly income when there is a non-filing spouse. The Court held that to the extent that the non-filing spouse contributes income for food and utilities, which are clearly household

expenses, these expenses should be excluded from the marital adjustment calculation performed in ascertaining debtor's current monthly income for purposes of determining whether a presumption of abuse arose.

The Court also held that deductions included by non-filing spouse as an expense for taxes are already accounted for when the non-filing spouse included her payroll taxes and Social Security as part of the marital adjustment, thus should not be deducted as a marital adjustment on Line 17.

Moreover, the Court rejected the UST's argument that the non-filing spouse must exclude as a marital adjustment expense, costs such as clothing and personal items. The Court noted that Form B22 distinguishes between the debtor's expenses as fixed by the IRS local and national standards for housing and living expenses based on the number of members in the household; and the fact that Debtor is allowed deductions whether or not Debtor files with his/her spouse, and regardless of whether a spouse is a dependent. As opposed to the non-filing spouse's actual expenses on Line 17, which are defined as expenses not contributed to the household expenses of the debtor or debtor's expenses, and not fixed in amount.

See discussion below for court's analysis under § 707(b)(3).

4. *In re Mclvor*, 2006 WL 3949172 (Bankr. E.D. Mich. 2006).

Facts: Debtor's means test form listed a \$471.00 monthly transportation expense for a car the debtor owned free and clear, with no monthly car payment (Line 23, Form B22A). Trustee filed a motion to dismiss pursuant to 707(b)(2) and (3), arguing that the form understates the debtor's monthly income by including the \$471.00 expense, which debtor is not entitled to because he does not make any monthly payments on the vehicle. The Trustee argues that the debtor does not have an "applicable monthly expense" since he does not have a car payment. Debtor argues that the "applicable monthly expense" is a fixed deduction given to all debtors who own a vehicle, irrespective of whether the vehicle is owned outright, or is subject to a lien.

Holding: Adopting the bankruptcy court's reasoning in *Fowler*, the Court held that

Section 707(b)(2)(A)(iii)(1) allows a Debtor to take the Local Standard deductions for ownership of a car regardless of whether they make a payment on the vehicle or not. Therefore, the presumption of abuse does not arise.

The Court relied on the plain meaning of the term “applicable” in Section 707(b)(2)(A)(ii)(1). The Court also agreed that the debtor should not be penalized for paying off his/her vehicles prior to the bankruptcy filing. *Id.* at *3 (*citing Wedoff, Means Testing in the New World*, 79 Am. Bankr. L.J. at 255-57). The Court also held that policy considerations, including the avoidance of litigation and the fact that standard deductions could be uniformly applied, supports the use of fixed standard. *Id.* (*citing, Fowler*, 349 B.R. at 420-21).

See discussion below for court’s analysis under § 707(b)(3).

B. POST-BAPCPA CASE LAW § 707(b)(3)

1. *In re Travis*, 353 B.R. 520 (Bankr. E.D. Mich. 2006)

Facts: The debtor's non-filing spouse's income and expenses were included on Schedules I and J, including the non-filing spouse's separate expenses for her own credit cards of \$300 per month.

Holding: The Court held that abuse is to be viewed utilizing the pre-BAPCPA standard and factors found in *In re Krohn*, 886 F.2d 123 (6th Cir. 1989); a totality of the circumstances. The Court also held that a non-filing spouse's income and expenses are relevant, but should be considered only if the debtor's income is high enough to "significantly raise the debtor's standard of living".

2. *In re Zaporski*, 366 B.R. 758 (Bankr. E.D. Mich. 2007)

Facts: Debtor had a large 401(k), stable employment and was solvent using a balance sheet analysis. He contributed to a 401(k) and had a 401(k) loan.

Holding: Even if the debtor passes the means test and there is no statutory presumption as defined at § 707(b)(2)(A), the Court can still dismiss a case under § 707(b)(3) using a totality of the circumstances analysis. Additionally even though a debtor is entitled to a 401(k) contribution deduction and loan repayment deduction in a Chapter 13, the Court can consider these expenses as income in a Chapter 7, "totality of the circumstances" analysis.

3. *In re Bender*, ____ B.R. ____ 2007 WL 2482247 (Bankr. E.D. Mich. Sept. 5, 2007)

Facts: Debtor increased charitable contributions before filing Chapter 7. She also had 401(k) loan repayments and had other inflated expenses. The debtor also continued to incur debt post-petition.

Holding: In reviewing the statute related to charitable giving, the Court held that only those charitable contributions in an amount the debtor "has made or continues to make" are allowed. An increase in contributions just before filing or post-petition cannot be allowed and must be considered income when reviewing an ability to repay. The Court must also consider the "debtor's actual anticipated and financial situation over the applicable Chapter 13 commitment period" in determining whether the case should be dismissed. In applying a totality of the circumstances test, the Court granted the U.S. Trustee's Motion to Dismiss.

4. *In re Mclvor*, 2006 WL 3949172 (Bankr. E.D. Mich. 2006)

Facts: The debtor recently divorced, had regular living expenses that the U.S. Trustee believed were excessive. If reduced by 50%, the Debtor could have funded a Chapter 13 Plan.

Holding: Using a totality of circumstances standard and viewing the entire situation of the debtor's life, the Court denied the U.S. Trustee's motion. The Court viewed certain of the expenses high but not "unreasonable under the circumstances". The Court based their decision on the debtor's testimony, demeanor and credibility at trial. The decision is currently on appeal with the District Court, case no. 06-15232-PVG

5. *In re Tonia Shelby*, Slip Opinion July 25, 2007, 06-48745-WS.

Facts: The debtor originally filed a Chapter 13 which she voluntarily converted to a Chapter 7. The debtor was a teacher with regular income, a leased Mercedes Benz and had expenses for a "hypothetical new home". She also had other discrepancies in her budget and schedules.

Holding: The difference between pre-BAPCPA § 707(b) substantial abuse and post-BAPCPA "abuse" is "too subtle to articulate". Courts must view totality of circumstances, including neediness of the debtor, debtor's ability to pay out of future earnings and dishonesty of debtor. The Court conditionally dismissed the case allowing the debtor a limited amount of time to convert to a Chapter 13.

6. *In re Cameron*, Slip Opinion Sept. 14, 2007, 07-42321-WS.

Facts: Debtor supported one (1) adult child and mother in the household. They amended their schedules after inquiry by the U.S. Trustee, but their total expenses remained the same.

Holding: The U.S. Trustee must prove its case by a preponderance of the

evidence. Applying the factors in *In re Krohn*, 886 F.2d 123 (6th Cir. 1989), the Court held that while the debtor appeared to reduce some regular living expenses, the deductions for 401(k) contributions and the eventual 401(k) loan payoff provided the debtor enough to repay some debt to unsecured creditors.