

Fall 2006

# Totality of the Circumstances of the Debtor's Financial Situation in Post-Means Test World: Trying to Bridge the Wedoff/Culhane & White Divide, The

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### Recommended Citation

John A. E. Pottow, *Totality of the Circumstances of the Debtor's Financial Situation in Post-Means Test World: Trying to Bridge the Wedoff/Culhane & White Divide, The*, 71 Mo. L. REV. (2006)

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# The Totality of the Circumstances of the Debtor's Financial Situation in a Post-Means Test World: Trying to Bridge the Wedoff/Culhane & White Divide

John A. E. Pottow\*

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## I. INTRODUCTION

Bankruptcy Judge Eugene Wedoff and Creighton Law School professors Marianne Culhane and Michaela White engage in a spirited debate over a series of law review articles about the proper scope of motions to dismiss a debtor's petition under section 707(b) of the freshly revised Bankruptcy Code.<sup>1</sup> It is an interesting and provocative dialogue, with both sides advancing their respective positions persuasively. As a result, I find myself in the unfortunate position of wanting to agree with both. Since that is impossible, however, this brief article is my attempt to find a middle ground between their two positions. It does so in five parts: Part II explains the debate; Part III takes issue with Judge Wedoff; Part IV takes issue with professors Culhane

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\* Assistant Professor of Law, University of Michigan Law School. Thanks to Rita Abro for research assistance and to all participants, especially Mechele Dickerson, at the University of Missouri-Columbia School of Law "Interdisciplinary Perspectives on Bankruptcy Reform" Conference.

1. Marianne B. Culhane & Michaela M. White, *Catching Can-Pay Debtors: Is the Means Test the Only Way?*, 13 AM. BANKR. INST. L. REV. 665 (2005); Eugene Wedoff, *Means Testing in the New § 707(B)*, 79 AM. BANKR. L.J. 231, 234 (2005) [hereinafter Wedoff, *Means Testing*]; Eugene R. Wedoff, *Judicial Discretion to Find Abuse Under Section 707(b)(3)*, 71 MO. L. REV. 1035 (2006) [hereinafter Wedoff, *Judicial Discretion*].

and White; Part V offers an attempt to strike a middle ground; and Part VI concludes.

## II. THE DEBATE

This analysis will not repeat the complete timeline of the section 707(b) amendments, nor will it try to parse their legislative history. Instead, it will look at section 707(b) as it formerly was and as it now is under the recently enacted Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (“BAPCPA”).<sup>2</sup>

The former section 707(b) was itself an amendment to the overhauled Bankruptcy Code of 1978.<sup>3</sup> When Congress passed the then-new Code in 1978, it allowed consumer debtors, not without some dissent,<sup>4</sup> to choose between Chapter 7 liquidation plans and Chapter 13 wage-earner plans.<sup>5</sup> Perhaps unhappy with the early workings of this new Code, or perhaps captured by a credit lobby that preferred Chapter 13, Congress was persuaded in 1984 to chip away at this debtor choice by adding section 707(b). While some advocated amending the Code to force certain debtors to file under Chapter 13, Congress took the time-honored approach of the compromise with the amendment. It declined *requiring* debtors to file Chapter 13 but allowed bankruptcy judges the *discretion* to make them do so.<sup>6</sup> It accomplished this procedurally by endowing judges with the power to dismiss a debtor’s Chapter 7 petition — which would require the debtor to refile under Chapter 13 to seek bankruptcy protection — if the judge felt that the debtor’s relief through Chapter 7 constituted “a *substantial abuse*.”<sup>7</sup>

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2. Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23 (codified as amended in scattered sections of 11 U.S.C.) [hereinafter BAPCPA].

3. The Bankruptcy Amendments and Federal Judgeship Act of 1984 added section 707(b) to the Bankruptcy Code, which allowed bankruptcy courts to dismiss a debtor’s Chapter 7 petition for relief if it found that granting the relief would be a “substantial abuse” of Chapter 7. *See Vandiver, infra* note 4, at 550.

4. *See Robert B. Vandiver, Jr., Bankruptcy – A Review of Recent Court Decisions Applying Section 707(b) of the Bankruptcy Code to Chapter 7 Proceedings*, 22 MEM. ST. U. L. REV. 549, 549-50 (1992) (discussing Congress’s decision to allow debtors to choose between filing for bankruptcy protection under either Chapter 7 or Chapter 13 of the Code when it enacted the Bankruptcy Reform Act in 1978 even though the consumer credit industry complained that too many individuals who could afford to repay their consumer debts would choose to discharge all their debts under Chapter 7).

5. Bankruptcy Reform Act of 1978, Pub. L. 95-598, 92 Stat. 2549 (1978) (codified as amended in scattered sections of 11 U.S.C.).

6. *See Vandiver, supra* note 4, at 549-50; *see also* 11 U.S.C. § 707(b) (1984) (current version at 11 U.S.C. § 707(b) (Supp. V 2005)).

7. Prior to the 2005 amendments, section 707(b) read:

Congress left the amorphous standard of “substantial abuse” undefined, and so it was the courts who were given the task of filling it out. They did so by propounding an array of judicial tests, each with seemingly more prongs than the last.<sup>8</sup> An important difference among these judicial tests interpreting section 707(b) was the treatment of debtor income, or more precisely, the treatment of debtor net income after the deduction of court-approved expenses. Some courts (the “ability to pay” group) held that if the debtor had surplus net income after deducting his reasonable and necessary living expenses, and hence could pay some money into a wage-earner Chapter 13 plan, it was dispositively “substantial abuse” to liquidate under Chapter 7 instead of filing under 13.<sup>9</sup> Others held that the debtor’s choice to pick liquidation over a wage-earner plan, even in the face of surplus disposable income, could not be undone without amending the Code. They reserved section 707(b) dismissal for instances of bad faith or misconduct (the “misconduct” group), and held that ability to pay alone could not justify dismissal.<sup>10</sup> A third camp came out in the middle, saying that the debtor’s ability to pay his debts, measured by the presence of surplus disposable income after deducting reasonable and necessary living expenses, was one of the many factors that could be considered, but would not be dispositive when gauging “substantial abuse” under section 707(b) (the “totality of the circumstances” group).<sup>11</sup>

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After notice and a hearing, the court, on its own motion or on a motion by the United States trustee, but not at the request or suggestion of any party in interest, may dismiss a case filed by an individual debtor under this chapter whose debts are primarily consumer debts if it finds that the granting of relief would be a substantial abuse of the provisions of this chapter.

11 U.S.C. § 707(b) (2000), amended by 11 U.S.C. § 707(b) (Supp. V 2005).

8. See Susan Jensen, *A Legislative History of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 79 AM. BANKR. L.J. 485, 493 (2005).

9. See, e.g., *Zolg v. Kelly (In re Kelly)*, 841 F.2d 908 (9th Cir. 1988) (leading case setting out the ability to pay test and establishing per se rule that the debtor’s ability to pay debts under a hypothetical Chapter 13 repayment plan, standing alone, warrants dismissal under section 707(b)); *In re Attanasio*, 218 B.R. 180, 239 (Bankr. N.D. Ala. 1998) (“If a debtor *can* meet debts without difficulty as the debts come due, then use of Chapter 7 represents a substantial abuse . . . . If, on the other hand, a debtor *cannot* meet debts as the debts become due . . . dismissal of the case pursuant to 707(b) is unwarranted.”).

10. See, e.g., *Green v. Staples (In re Green)*, 934 F.2d 568, 572 (4th Cir. 1991) (“[T]he real concern behind Section 707(b) [is] abuse of the bankruptcy process by a debtor seeking to take unfair advantage of his creditors. . . . [S]olvency alone is not a sufficient basis for a finding that the debtor has in fact substantially abused the provisions of Chapter 7.”).

11. See, e.g., *In re White*, 49 B.R. 869, 873 (Bankr. W.D.N.C. 1985) (holding that to determine whether substantial abuse exists, a court must look at “the totality of the circumstances presented, including the effects upon the petitioner *and* his creditors should relief under Chapter 7 be granted, or alternatively, denied”); see also *In re May*, 261 B.R. 770, 773 (Bankr. M.D. Fla. 2001) (stating that “having income in

In enacting the BAPCPA last year, Congress apparently decided that the “substantial abuse” test was not working.<sup>12</sup> Perhaps it was dissatisfied with how that judicially administered test had been teased out in the courts, or perhaps it ignored the recommendations of a bipartisan commission and favored a bill drafted by credit industry lobbyists. That is a discussion for another day. Whatever its motivations, Congress replaced the judicially administered “substantial abuse” test with a painstakingly detailed statutory “means test,” ballooning section 707(b) into five single-spaced pages of Code.<sup>13</sup> In so doing, it seemed to align with the “ability to pay” case line under former section 707(b) or, more accurately, seemed to reject the “misconduct” case line that required some form of wrongdoing for dismissal.

The revised section 707(b)(2)(A) contains this means test. It establishes a regimented list of includable sources of income and deductible expenses that must be used to calculate a debtor’s surplus monthly income.<sup>14</sup> If that surplus is greater than a statutory amount (generally \$166), the debtor flunks the means test and is dismissed from Chapter 7: Congress says he is an abuser as a matter of law.<sup>15</sup> If the debtor’s surplus income is less than the threshold, he remains otherwise eligible for Chapter 7.<sup>16</sup>

So what is the debate between Judge Wedoff and Professors Culhane and White? It comes from Congress’s statutory caveat that the means test — formally, the “presumption of abuse” that is generated by flunking the surplus income test under section 707(b)(2)(A) — is not the exclusive ground for dismissing a debtor from Chapter 7.<sup>17</sup> Consider in this regard the ordering of the subsections of new section 707(b).

Section 707(b)(1) provides that “the court . . . may dismiss a case . . . if it finds that the granting of relief would be an abuse of the provisions of this chapter.”<sup>18</sup>

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excess of necessary expenses is not, by itself, sufficient to support a finding of substantial abuse of Chapter 7, and the bankruptcy court should engage in a ‘totality of the circumstances’ analysis in determining whether a discharge would be a substantial abuse of Chapter 7”). Note that Judge Wedoff, with more detailed analysis, accurately breaks the cases out into four groups. Wedoff, *Means Testing*, *supra* note 1, at 235. I am simplifying the taxonomy for convenience.

12. This decision took the better part of eight years. See Consumer Bankruptcy Reform Act of 1997, S. 1301, 105th Cong. (1998).

13. See 11 U.S.C. § 707(b) (Supp. V 2005); see also Culhane & White, *supra* note 1, at 668.

14. 11 U.S.C. § 707(b)(2)(A). “Current Monthly Income” is defined in 11 U.S.C. § 101(10A).

15. *Id.* § 707(b)(2)(A).

16. Note that most debtors, specifically those with below-median income, bypass the means test, “passing” as a matter of law. *Id.* § 707(b)(7).

17. *Id.* § 707(b)(2)(A).

18. *Id.* § 707(b)(1).

Section 707(b)(2) in turn instructs that “[i]n considering under paragraph (1) whether the granting of relief would be an abuse of the provisions of this chapter, the court shall presume abuse exists if [the means test is failed].”<sup>19</sup>

Section 707(b)(3) then eliminates doubt regarding the means test’s non-exclusivity as grounds for dismissing debtors from Chapter 7. It endows the judge with the additional discretion to dismiss a case under Section 707(b)(1) “in which the presumption [of abuse] in [p]aragraph [(2)](A)(i) . . . does not arise or is rebutted.”<sup>20</sup> To do so, the judge must consider:

(A) whether the debtor filed the petition in bad faith; or

(B) *the totality of the circumstances* (including whether the debtor seeks to reject a personal services contract and the financial need for such rejection as sought by the debtor) *of the debtor’s financial situation* demonstrates abuse.<sup>21</sup>

Clause (A) of (b)(3) doesn’t cause much fuss. Who denies the judge of an equitable proceeding the power to dismiss a petitioner who comes in bad faith? Clause (B), however, does. Judge Wedoff reads “the totality of the circumstances . . . of the debtor’s financial situation” as conferring authority on bankruptcy judges to boot debtors out of Chapter 7 who pass the means test if those debtors nonetheless have, in those judges’ second-look views, an “ability to pay” their debts.<sup>22</sup> Professors Culhane and White disagree and think that this exception narrowly applies only to serious forms of misconduct that are “manifestly unreasonable,” such as, for example, “cheating” on the means test by manipulating a revenue stream.<sup>23</sup> Absent wrongdoing, the professors contend, dismissal under section 707(b)(3)(B) would be improper. Note how both find cognates in the pre-BAPCPA case law: the “ability to pay” group and the “misconduct” group of cases. Both of these positions, at least as just characterized, have merit but are not without difficulty.

### III. PROBLEMS WITH JUDGE WEDOFF’S POSITION

#### *A. The Means Test, Despite Its Label, Is Not A Presumption*

Judge Wedoff’s position suffers from two impediments, one operational and the other theoretical. The operational problem is that he mistakenly inter-

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19. *Id.* § 707(b)(2)(A)(i).

20. *Id.* § 707(b)(3).

21. *Id.* § 707(b)(3)(A)-(B) (emphasis added).

22. Wedoff, *Judicial Discretion*, *supra* note 1, at 1040 (omission in original).

23. Culhane & White, *supra* note 1, at 666, 668, 687-88.

prets the means test of section 707(b)(2)(A) as an evidentiary presumption.<sup>24</sup> This is not surprising, as Congress has explicitly called it that (“[T]he court shall *presume* abuse exists.”).<sup>25</sup> It similarly styles section 707(b)(2)(B) as the means of rebutting that “presumption” (“[T]he presumption of abuse may only be rebutted by”).<sup>26</sup> Following this linguistic miscue of Congress, Wedoff reasons that if the means test is merely a presumption, and that presumption can be rebutted, then it must serve as “merely one” of several possible routes to show income-related abuse of Chapter 7.<sup>27</sup> He likens the means test to the paternity presumption that arises with regard to the husband of an infant’s mother.<sup>28</sup> The gentleman is presumed to be the baby’s father, but genetic or other evidence can also show his paternity directly if he is unmarried to the mother and hence the presumption does not apply.<sup>29</sup>

The means test is not, however, an evidentiary presumption in the sense of a foundational fact (marriage) that assists in proving a presumed fact (paternity). While unquestionably styled as a “presumption,” the means test is more accurately viewed as a jurisdiction-stripping statute. Leaving aside the difference between a fact (paternity) and a legal determination (abuse of Chapter 7 of the Bankruptcy Code), the function of the means test is to require dismissal, and hence forbid jurisdiction, for Chapter 7 debtors whose monthly surplus income is greater than \$166. This reading of the means test as a jurisdiction-stripper rather than an evidentiary presumption is enforced by the fact that Section 707(b)(2)(B) is the *exclusive* method by which the debtor can “rebut” the so-called presumption.<sup>30</sup> Contrary to what one would expect from a real evidentiary presumption, section 707(b)(2)(B) only allows a debtor to challenge the method by which the court has calculated the surplus income under section 707(b)(2)(A). She may not, as Judge Wedoff himself concedes, introduce evidence that notwithstanding her surplus monthly

24. Wedoff, *Judicial Discretion*, *supra* note 1, at 1037 (“The key to understanding the proper role of the means test in Chapter 7 is to recognize that it is simply a mechanism for generating a presumption; it does not result in any final determination.”).

25. 11 U.S.C. § 707(b)(2)(A)(i) (Supp. V 2005) (emphasis added).

26. *Id.* § 707(b)(2)(B).

27. Wedoff, *Judicial Discretion*, *supra* note 1, at 1040 (“The function of the means test as a presumption has one final critical feature. A presumption is merely one method of establishing a fact. Where a presumption does not arise, a party may prove the necessary fact directly, using the same kind of evidence that could be used to rebut the presumption.”).

28. *Id.* at 5 (citing 750 ILL. COMP. STAT. 45/5(b) (2005) (providing for rebuttal of the marital paternity presumption by clear and convincing evidence)).

29. Just as, presumably, a husband seeking to disclaim paternity could rebut the presumption through DNA or other evidence.

30. 11 U.S.C. § 707(b)(2)(B)(i) (Supp. V 2005) (“In any proceeding brought under this subsection, the presumption of abuse may only be rebutted by demonstrating special circumstances, such as a serious medical condition or a call or order to active duty in the Armed Forces . . .”).

income of \$167, she is not abusing the provisions of Chapter 7.<sup>31</sup> As such, the means test is not a rebuttable evidentiary presumption in the traditional sense. It is an irrebuttable jurisdictional rule that permits exception only for miscalculation.

Let us examine with more scrutiny the only permissible way the debtor may “rebut” the means test “presumption” regarding his surplus monthly income. Section 707(b)(2)(B) provides that “the presumption of abuse *may only be rebutted* by demonstrating special circumstances, such as a serious medical condition or a call or order to active duty in the Armed Forces, *to the extent such special circumstances justify additional expenses or adjustments of current monthly income for which there is no reasonable alternative.*”<sup>32</sup> On the income side, a reservist whose \$167 surplus income was unfairly high under the means test’s trailing six-month formula could seek an adjustment to his calculation by showing that his substantial overtime pay will evaporate as he gets called up for active service next month. Similarly, on the expense side, a disease sufferer could show that his recurrent illness, presently in remission, requires him to build up a reserve account to deal with future onsets such that an additional “sickness reserve” expense (which is not allowed under the means test) is necessary. But there would be no room to “rebut” the “presumption” of abuse by a debtor with surplus income of \$167, who, for example, wants to submit evidence that he has worked hard, had his debts incurred in good faith, and would only be able to pay a 1% dividend to creditors if subjected to a five-year wage-earner plan: in short, that it would be a waste of time for such a debtor to file in Chapter 13. He is abusive as a matter of law and is barred from Chapter 7. There is not jurisdiction, however sensible it might be, to let such a debtor in.

This operation of the means test enables debtors to challenge the metric, but not the merits, of their surplus income. Professors at law schools, such as my own, that strip faculty of jurisdiction to change grades after submission to the registrar but provide for an exception for mistabulated grades should find this framework familiar.<sup>33</sup> It is a bright-line rule. To say that it creates a “rebuttable presumption” that the submitted grade is the final grade when the only way of rebutting the presumption is to show that the grade was added up incorrectly is doublespeak of the highest order. It is not a *presumption*, let

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31. Wedoff, *Judicial Discretion*, *supra* note 1, at 1047 (“Disposable income of more than \$166.66 per month . . . is always an abuse requiring denial of Chapter 7 relief.”). Wedoff summarizes that a debtor seeking Chapter 7 relief may “rebut the means test’s calculation of disposable income in an amount above the abuse threshold; [but § 707(b)(2)(B)] does not allow any argument that the threshold itself is too low.” *Id.* at 1046-47.

32. 11 U.S.C. § 707(b)(2)(B)(i).

33. The rationale behind this rule is a commendable anti-whining principle.



alone a rebuttable one, that submitted grades are final. It is a *rule* that submitted grades are final, absent calculation error. There is no appeal.<sup>34</sup>

### B. Congress Legislated “Should Pay,” Not “Can Pay”

The parts of Judge Wedoff’s analysis that go astray cannot all be blamed on Congress’s poor diction. Another problem arises from the more theoretical conflation of the means-test-calculated surplus income with the concept of the “ability to pay” that finds its roots in Chapter 13.<sup>35</sup> This is again not the fault of Wedoff; Culhane and White also use the label “can pays” to describe those who flunk the means test.<sup>36</sup> This is another unfortunate word choice, because a more accurate label would have been “should pays.”

Consider, by way of contrast (and contrasts are important in statutory interpretation),<sup>37</sup> Chapter 13, in which a debtor deducts his “reasonable and necessary expenses” in arriving at what Chapter 13 explicitly calls his “disposable income.”<sup>38</sup> BAPCPA modifies this rule for certain above-median income debtors, but the old law still holds for the vast majority of Chapter 13 filers.<sup>39</sup> If the debtor only deducts his reasonable and necessary living expenses, that which remains is all that he “can” pay to his creditors (assuming we want the debtor to continue living). By contrast, under the Chapter 7 means test, the debtor deducts a particularized list of allowed expenses; the term “disposable income,” familiar from Chapter 13’s text, is assiduously avoided by Congress in Section 707. Some of these allowed expenses are

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34. I am led to believe (*seulement par les autres*) that many states adopt similar “presumptions” regarding radar-recorded evidence of motorists’ speed; they permit “rebuttal” only by showing mechanical default. My colleague, Professor James J. White, may have further insight from experience.

35. *See, e.g., Wedoff, Judicial Discretion, supra* note 1, at 1040 (“Given that the means test is directed at measuring debt-paying ability as a presumption, this direction confirms that where the presumption does not arise, the debtor’s actual debt-paying ability must be assessed in ruling on a motion under § 707(b)(1).”).

36. Culhane & White, *supra* note 1, at 700 n.1 (“We use ‘can-pay’ to describe debtors who fail the means test, and ‘can’t-pay’ for those who pass it.”).

37. *See, e.g., Guarantee Title & Trust Co. v. Title Guar. & Sur. Co.*, 224 U.S. 152 (1912) (holding that when different language is used in different parts of a statute, it is presumed that the language is used with a different intent).

38. 11 U.S.C. § 1325(b)(1)(B) (Supp. V 2005) (“If the trustee . . . objects to the confirmation of the plan, then the court may not approve the plan unless . . . the plan provides that all of the debtor’s projected *disposable income* to be received in the applicable commitment period . . . will be applied to make payments to unsecured creditors under the plan.”) (emphasis added); *id.* § 1325(b)(2) (“[T]he term ‘disposable income’ means current monthly income received by the debtor . . . less amounts reasonably necessary to be expended.”).

39. *Id.* § 1325(b)(3).

fixed by IRS schedules for food, housing, and such.<sup>40</sup> Others are limited by what the debtor actually spends.<sup>41</sup> Thus we cannot envision surplus income calculated under the means test as what the debtor *can* pay. Rather, we must say it is what Congress, as a policy determination, has decided that the debtor *should* pay (whether under his current circumstances he can afford to or not).<sup>42</sup> Any doubt about the difference between what a debtor *can* and *should* pay under Section 707(b) should be removed by Section 707(b)(2)(D) in which Congress expressly exempts certain disabled veterans from the jurisdictional bar of the means test.<sup>43</sup> We are unable to pretend these vets *can't* pay; a simple calculation of surplus income over \$166 would refute that contention. Instead we must say that Congress made a normative, value-laden judgment that although other similarly situated debtors *should* pay, these veterans, perhaps as thanks for their service, *should not* (and do not) have to pay. Such is Congress's prerogative.

The confusion of Chapter 13's can-pay test with Chapter 7's should-pay test leads Wedoff to conclude that the means test's routinized calculations are simply a rough and ready proxy for the more particularized, case-specific investigation of "can-pay" that occurs under Chapter 13.<sup>44</sup> This in turn explains Wedoff's reading of Section 707(b)(3). If the means test, with its *allowed* living expenses, is simply a rough first cut at finding debtors who can pay, a judge or U.S. Trustee can use Section 707(b)(3) to do the individual, case-specific follow-up analysis of the debtor's *actual* reasonable and necessary expenses that is traditionally performed under Chapter 13. If the judge conducting this second inquiry finds the debtor can pay (based on the \$166 threshold), he may dismiss the debtor under this judicially administered Alternative Minimum Means Test.

Judge Wedoff's interpretation thus rests on equating Chapter 13's can-pay analysis with Section 707(b)'s should-pay algorithms. It is not clear, however, that Congress intended to use these textually different provisions interchangeably. Indeed, surely Congress did not care, other than in rare cases such as a medical illness sufferer or a member of the military, whether the debtor had expenses that were *higher* than those allowed under the IRS-

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40. See, e.g., *id.* § 707(b)(2)(A)(ii)(I) ("[T]he debtor's monthly expenses may include an . . . allowance for food and clothing categories as specified by the National Standards issued by the Internal Revenue Service.").

41. See, e.g., *id.* § 707(b)(2)(A)(ii)(II) ("[T]he debtor's monthly expenses may include . . . the continuation of actual expenses paid by the debtor that are reasonable and necessary for care and support of an elderly, chronically ill, or disabled household member . . . who is unable to pay for such reasonable and necessary expenses.").

42. Cf. *id.* § 101(10A) (excluding by statute certain sources of arguably available income from creditor recovery).

43. *Id.* § 707(b)(2)(D) ("[T]he court may not dismiss or convert a case based on any form of means testing, if the debtor is a disabled veteran.").

44. Wedoff, *Judicial Discretion*, *supra* note 1, at 1041.

controlled means test.<sup>45</sup> The question, therefore, is whether Congress cared if a debtor had actual expenses that were *lower*.

There is reason to doubt that Congress did. The basis for this hesitance is the possibility that it wanted the rehabilitated debtor to reap the “frugality dividend” of having his actual expenses be lower than the means-test allowed ones. Wedoff seems to accept too quickly that such a dividend should inure to the benefit of the debtor’s creditors. He would allow a dismissal motion under Section 707(b)(3) to punish such a tight-belted debtor and enable her creditors to reap that surplus. While it may be impossible to prove that the structure of the statute or the legislative history inexorably require that this excess should go to the debtor,<sup>46</sup> neither can Wedoff prove, without at least some critical analysis, that it should go to the creditors. Indeed, given the absence of express statutory command, if we want to theorize from first principles, we can readily envision some *ex ante* policy reasons why Congress would be disinclined to penalize frugal, means-test-passing debtors. Allowing a judge the power to bar them from Chapter 7 would surely create perverse incentives of moral hazard.

#### IV. PROBLEMS WITH CULHANE AND WHITE

Why not simply agree with Culhane and White? The problem with their analysis is that it swings too far the other way and would hobble the wide swath of discretion deliberately conferred on judges under Section 707(b)(3)(B). Their gloss of “serious misconduct” or “manifestly unreasonable” — basically “bad faith lite” — is too narrow. It is also unsupported by the language of the new Code.

Consider in this regard at least three possible ways a court could interpret “the totality of the circumstances . . . of the debtor’s financial situation.” First, a court could say the “totality of the circumstances” means anything, anywhere, remotely related to the debtor’s finances. Second, a court could say that the “totality of the circumstances” must be read in the context of a means-test-dominated BAPCPA statute. As such, it is merely a safety valve for a defective application of the means test and should only be applied to remedy “cheating” or other misconduct problems that evince a debtor’s compliance with the letter but not spirit of the Code (similar to the way some courts interpreted the “substantial abuse” standard pre-BAPCPA).<sup>47</sup> Third, a

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45. One way of thinking about this is that Congress determined that unenumerated expenses were unreasonable as a matter of law.

46. Consider, however, the debtor’s ability to deduct IRS expenses, even if greater than actual expenses. See *supra* note 40.

47. See, e.g., *Stewart v. United States Trustee (In re Stewart)*, 215 B.R. 456, 467, 468 n.8 (B.A.P. 10th Cir. 1997) (“Bad faith, inaccurate representations to the Bankruptcy Court, and eligibility for Chapter 13 are all factors to be considered under the totality of the circumstances test . . . .”); see also *In re Krohn*, 886 F.2d 123, 126 (6th Cir. 1989) (noting that, based on legislative history, Congress meant to deny Chapter

court could say something in between, such as “totality of the circumstances” means all relevant factors of a debtor’s financial situation *except those revisiting the means test*.

The reason to shy away from the first test is because it parses the phrase “totality of the circumstances . . . of the debtor’s financial situation” in isolation from the rest of the section and the statute as a whole. Under general principles of statutory construction, when a statute “occupies a field” and establishes a comprehensive scheme for determining one type of abuse (“should pay”), the inclusion of a caveat for finding other types of abuse should not be allowed to bootstrap a revisit of the same ground.<sup>48</sup> Consider again law school faculty policy. Suppose we say at the University of Michigan Law School that any student with an average lower than C will be expelled, and then we develop a complex formula for which courses to include in that average and how to weight them (perhaps, picking up on the BAPCPA methodology, we say the six most recent courses). We then allow a student to “rebut” that calculation by showing that the six most recent courses were aberrational (*e.g.*, she was away at another school with different grading norms for her last six courses). Ever the risk-averse lawyers, we say that nothing in our “C rule” precludes us from expelling a student for bad faith, or for any other reason considering the totality of the circumstances of the student’s academic situation.

Could we kick out a student for embezzlement? Of course we could; that would be bad faith. Could we kick out a student for plagiarizing? Yes, that would be bad faith, too. It might also overlap with the totality of the circumstances of her academic situation (she thinks copying is an acceptable form of learning). But two overlapping grounds of discretion should cause angst only to the overly fastidious.<sup>49</sup> The point is we could do it under the policy. Could

7 relief to “the dishonest or non-needy debtor” and pointing out that the court should determine if the debtor is honest by looking at whether debtor has acted with “good faith and candor in filing schedules and other documents”).

48. This principle finds frequent outlet in the federal law “preemption” cases. *See, e.g.*, *Fidelity Fed. Savings & Loan Ass’n. v. De la Cuesta*, 458 U.S. 141, 153 (1982) (reasoning that even in the absence of an express congressional command, state law is nevertheless preempted if federal law so thoroughly occupies a legislative field “as to make reasonable the inference that Congress left no room for the States to supplement it”).

49. *See Culhane & White, supra* note 1, at 684 (explaining that the overlapping grounds of Sections 707(b)(3)(A) and 707(b)(3)(B) stem from Congress’s decision to adopt two different tests from former 707(b) case law). Pre-BAPCPA, “filed in bad faith” and “totality of the circumstances” were:

frequently and sometimes interchangeably used in cases under former section 707, before ability to pay was measured by the means test. Bad faith was used both under section 707(a) as ‘cause’ for dismissal, as well as under former subsection 707(b) in substantial abuse cases, where it sometimes stood alone but often was considered in addition to judicial tests of ability to pay.

*Id.*

we expel a student for having bad study habits or for making persistently inane comments in the classroom that evince a total misunderstanding of the law? Probably so; both seem relevant to the totality of the circumstances of her academic situation. But could we kick out a student for having a C+ average, on the theory that C+ is a pretty crummy grade point average in its own right? Here is where we move to thin ice. To allow that would do violence to the whole point of setting the mechanized formula in the first place for how to count the C average and implement the C rule. Trying to boot a C+ student who passes the C rule just sounds like a faculty member unhappy with where that bar was set.<sup>50</sup>

But other than an anti-bootstrapping limitation to deal with the professor who wants to expel the C+ student, any and all other circumstances of the student's "academic situation" should be fair game for consideration. This is the problem with the Culhane and White stance. Further qualifications, such as "serious misconduct," appear to be cut out of whole cloth: possibly sensible refinements, to be sure, but not compelled by the faculty's deliberations. Bringing the discussion back to bankruptcy law, this creates misgivings with Culhane and White's proposed interpretation of Section 707(b)(3)(B). For example, Culhane and White do not believe a debtor's portfolio of exempt assets is a permissible ground to consider within the totality of the debtor's financial situation, absent some misconduct like eve-of-bankruptcy transfers.<sup>51</sup> Why not? While some may say it is foolish policy to consider them, and that it may even undermine the very purpose of having exemptions in the first place (which is in part to protect a debtor's fresh start by ensuring a post-bankruptcy baseline of available assets), others may disagree.<sup>52</sup> In any event, unwise policy on its own does not accord a sufficient basis to bar a bankruptcy judge from noticing a debtor's enormous retirement plan account in deciding whether it offends the spirit of the Code to let that debtor use Chapter 7.<sup>53</sup>

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50. The better and tougher question is would I allow kicking someone out who makes semi-inane comments in class *and* has "only" a C+ average? Would considering the C+ average there, as part of the totality of the circumstances, be problematic? That is a much closer call. I might foreclose this for prudential reasons alone for fear of the dangerous pretextualism it could engender (or abet).

51. Culhane & White, *supra* note 1, at 690-691.

52. See, e.g., *Stuart v. Koch (In re Koch)*, 109 F.3d 1285, 1290 (8th Cir. 1997).

53. For a former § 707(b) case holding that exempt assets are appropriately considered under the "totality of the circumstances," see *Kornfield v. Schwartz (In re Kornfield)*, 164 F.3d 778, 781 (2d Cir. 1999) ("A totality of circumstances inquiry is equitable in nature and the existence of an asset, even if exempt from creditors, is relevant . . .").

## V. TRYING TO FIND A MIDDLE GROUND

Trying to find a middle ground between the powerful arguments of Judge Wedoff and Professors Culhane and White is not easy. Among other challenges, it involves giving content to the amorphous “totality of the circumstances” standard in a principled, usable manner. This cannot be done by simply relying on pre-BAPCPA case law interpreting former Section 707(b). Recall that some courts then adopted a “totality of the circumstances” approach that considered multiple factors, including the debtor’s income.<sup>54</sup> But those tests sought to define the open-ended standard of “substantial abuse,” with many including factors such as bad faith and misconduct.<sup>55</sup> By contrast, new Section 707(b)(3)(B) covers financial factors independent from bad faith, which is already covered by Section 707(b)(3)(A), rendering much of former Section 707(b)(3) precedent inapposite.

Nor is the task helped much by Congress’s single cryptic clue in the text of Section 707(b)(3)(B). Specifically, Congress says that a court must consider whether “the totality of the circumstances (*including whether the debtor seeks to reject a personal services contract and the financial need for such rejection as sought by the debtor*) of the debtor’s financial situation demonstrates abuse.”<sup>56</sup> Culhane and White explain how this was a compromise for the recording industry that lobbied unsuccessfully to insert a blanket prohibition on rejecting certain personal service contracts by debtors in bankruptcy.<sup>57</sup> But how does one generalize from this parenthetical clause in the statute? Is it an example? Is it a factor? On the one hand, there is the canon of *ejusdem generis*,<sup>58</sup> which states that illustrations should be seen of the same genus of the general. On the other hand, it could be argued that Congress was not providing an example, but rather was simply ensuring that one specific circumstance would not be forgotten by the judge. We also have history, where some courts held that rejecting personal services contracts under former Sec-

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54. See *Stewart v. United States Trustee (In re Stewart)*, 215 B.R. 456 (B.A.P. 10th Cir. 1997).

55. See *id.* (stating that bad faith is one of many factors to be considered under the totality of the circumstances test).

56. 11 U.S.C. § 707(b)(3)(B) (Supp. V 2005) (emphasis added).

57. Culhane & White, *supra* note 1, at 692 n.123 (citing *In re Carrere*, 64 B.R. 156, 157 (Bankr. C.D. Cal. 1986) (dismissing case of actress who admitted she wanted to reject contract with one TV network in order to sign one with another that would pay her substantially more money).

58. *Norfolk & W. Ry. Co. v. Am. Train Dispatchers’ Ass’n*, 499 U.S. 117, 129 (1991) (“Under the principle of *ejusdem generis*, when a general term follows a specific one, the general term should be understood as a reference to subjects akin to the one with specific enumeration.”).

tion 707 constituted bad faith.<sup>59</sup> Perhaps Congress was simply endorsing this case law and clarifying that a court may permissibly dismiss a debtor for rejecting a personal services contract.

Section 707(b)(3)(B) is thus a morass, and the struggle to tame it cannot escape a fundamental difficulty. If the text had simply said “the totality of the circumstances,” it might have made sense to follow the Culhane and White approach. The problem is that the text continues to say that the totality of the circumstances must affect the debtor’s “*financial* situation,”<sup>60</sup> which must in turn be an instruction to weigh primarily financial matters, not primarily ethical or conduct-based matters. Thus, Culhane and White are likely moving in the wrong direction by looking at conduct. Yet one equally encounters the countervailing consideration, raised above, that Congress’s comprehensive treatment of permissible income under the means test renders unlikely the probability that it wanted revisitation of the debtor’s “grade” by an unhappy judge under subsection (b)(3)(B). Accordingly, if we want to construct a reading of (b)(3)(B) that does not render it superfluous, we need to come up with financial factors of a debtor *unrelated* to his monthly income that might warrant dismissal from Chapter 7.

This may seem to be a fine needle to thread, but perhaps it can be done by focusing on *assets* rather than *income*. The means test addresses the debtor’s income in painful detail but is silent on her assets.<sup>61</sup> To be sure, assets, especially business assets, generally exist to generate income, but Section 707(b) deals with consumer debtors with primarily consumer debts. And surely a debtor’s asset base, even her exempt assets, pertains to her “financial situation.” Thus I submit, although Culhane and White think it contrary to the spirit of Congress, that not only is consideration of exempt assets permissible under Section 707(b)(3)(B), but it is one of the few considerations that must be permitted to make sense of this maddening provision. Indeed, using Section 707(b)(3)(B) to examine the assets, exempt or otherwise, could also address the concern some commentators have about the build-up of secured debt to take advantage of the means-test deduction.<sup>62</sup> Plausibly a judge could inquire whether a debtor with such a handsome portfolio of secured assets requires relief under the Bankruptcy Code, when selling such assets might alleviate financial distress.<sup>63</sup>

59. *In re Sammons*, 210 B.R. 197 (Bankr. N.D. Fla. 1997) (holding that case filed by debtor, at time when he was not in financial distress, solely for purpose of rejecting agreement was filed in bad faith and could accordingly be dismissed).

60. 11 U.S.C. § 707(b)(3)(B) (emphasis added).

61. Culhane & White see this silence as insulating a debtor’s assets from scrutiny. Culhane & White, *supra* note 1, at 690.

62. *Id.* at 688.

63. It certainly would improve cash flow. Of course, such an interpretation might undermine the unlimited secured debt deduction under the means test. 11 U.S.C. § 707(b)(2)(A) (Supp. V 2005) (“Notwithstanding any other provision of this clause, the monthly expenses of the debtor shall not include any payments for debts.”).

## VI. CONCLUSION

Both Culhane and White and Wedoff agree that Section 707(b)(3)(B) means Congress wanted judges to have some discretion to dismiss debtors for reasons other than flunking the means test of (b)(2) and straight-out bad faith under (b)(3)(A). Culhane and White contend that Congress did not intend this caveat to be an end-run around the means test by a judge who would have preferred the \$166 allowable income threshold to have been set at a lower level. Surely that is right. Similarly, it seems difficult to believe that Congress would have wanted to divest the debtor of any frugality dividend resulting from his *actual* net income being higher than his *allowable* net income under the means test. The detail and structure of the means test suggest that Congress intended it to be the exclusive manner of scrutinizing the debtor's permissible monthly income — what he “should pay” — under the Code.<sup>64</sup> But other than that income-based carveout, all other financial considerations should be fair ground for an equitable decision to dismiss for the totality of the circumstances under section 707(b)(3)(B). Judge Wedoff is thus correct to part ways with Professors Culhane and White on that score.

My proposal to bridge the divide between these two positions is to focus on a debtor's financial *assets* when considering a 707(b)(3)(B) motion. This approach would give meaning to this provision of the Code in a way that grants judges the discretion they need but does not tread on Congress's clear occupation of the income scrutiny field. This reading might just make sense of the “totality of the circumstances . . . of the debtor's financial condition” in a post-means-test world.

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64. Other than, for instance, income manipulation sufficient to rise to the level of bad faith, such as (perhaps) suspending work irregularly to distort six-month trailing income. Indeed, conceivably bad faith could deal with Judge Wedoff's hypothetical CEO who is willing to sacrifice her professional reputation by filing personal bankruptcy under Chapter 7. Wedoff, *Judicial Discretion*, *supra* note 1, at 1035-36.



