

MEANS TEST PART FOUR – BAD FAITH OR THE TOTALITY OF CIRCUMSTANCES AS ABUSE OF CHAPTER 7

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Merely defeating the presumption of abuse under §707 (b)(2) is not enough. Passing the means test is not a “safe harbor” against scrutiny of debtors’ schedulesⁱ; the court is also to consider “bad faith” or the “totality of circumstances” in the determination of whether there has been an abuse of Chapter 7.ⁱⁱ

Therefore, debtors who “pass” the means test but have substantial net income on their Income and Expense Schedules (Schedules I and J) remain at risk of being forced into Chapter 13 or having their case dismissed. This is true for both above-median income debtorsⁱⁱⁱ and below-median income debtors.^{iv}

The following cases have particularly caught my attention.

Consideration of Post-Petition Changes in Income

In re Quintana, 4-05-BK-08497, May 3, 2006: Judge Marlar granted the U.S. Trustee’s Motion to Dismiss under 707(b)(3) a ruling that, under its “totality of circumstances provision,” the debtor was abusing the provisions of Chapter 7. Debtor’s means test reflects no “presumption of abuse.” However, six days after he filed, he resumed work following a lay-off due to a four-month lockout; once back to work, the difference between his income and his expenses was a net \$1,500, and he would be able to fund in excess of \$94,000 through a five-year Chapter 13 plan and pay in full his \$55,000 in scheduled unsecured debt.

Judge Marlar’s decision is very similar to that in *In re Pak*, 343 B.R. 239 (Bankr. N.D. Cal. 2006) decided 15 days later. See also *In re Henebury*, 361 B.R. 595 (Bankr.S.D.Fla.) [Wife’s employment as teacher four days after petition for relief filed.]

Other Cases

In re Ashraf, 367 B.R. 151 (Bankr.D.Ariz. 2007). The Court found that the debtors’ failure to list significant information in their schedules, including undisclosed debts and income, “combined with the debtors’ timing to file a bankruptcy petition shortly after a judgment has been obtained by one of their creditors, reflect that, based on the ‘totality of the circumstances,’ the debtors’ petition must be dismissed as an abuse of Chapter 7.”

In re Mitchell, 357 B.R. 142 (Bkrtcy.C.D.Cal. 2006) involves a debtor who had been unemployed for nearly two years pre-petition but had spent over \$29,000 on “dining out,” “women’s fashions and accessories,” “electronics and personal property,” and “beauty treatments and related products” during the same period. Debtor was found to have made her filing in bad faith and, additionally, was barred from filing another Chapter 7 petition for 180 days.

In re James, 345 BR 664 (Bankr. N.D. Iowa 2006): The Court granted a 707(b)(3) Motion to Dismiss filed by the U.S. Trustee for “abuse” where the debtor spent \$13,000 of salary bonuses on luxury purchases within the six months prior to filing, rather than paying any debts.

In re Richie, 353 BR 569 (B.E.D.Wis. 2006): The judge found abuse because a below-median-income out-of-work debtor was not treating her creditors fairly by filing for bankruptcy. Debtor had just received a master’s degree in outdoor therapeutic recreation administration. With the degree, she was qualified to work with at-risk youth or disabled individuals in a camp or clinical setting. The Court found that she pursued employment opportunities only in her chosen field and only in geographic area in which she lived. In granting the U.S. Trustee’s Motion to Dismiss, the Court viewed the “undue hardship” analysis in student loan cases as instructive.

“The Court finds that a debtor’s failure to seek any but very limited – possibly non-existent – employment, and thus her failure to make a real attempt to pay something to her creditors before seeking discharge of her debts, is not behavior that treats her creditors fairly. It is not behavior that indicates that the debtor has tried her best to repay her debts before throwing in the towel and seeking Chapter 7 discharge as a last resort.” 353 BR at p. 580.

ⁱ *In re Quintana*, 4-05-bk-08497 JMM (Bankr. Ariz. 2006); *In re Pak*, 343 B.R. 239 (Bankr. N.D. Cal. 2006). This is entirely consistent with the Ninth Circuit’s interpretation of 707(b) [now 707(b)(1)] that the Court’s finding that a debtor’s ability to pay his debts, standing alone, can support a conclusion of substantial abuse. *In re Kelly* 841 F.2d 908 (1988). See also *In re Price*, 353 F.3d 1135, 1139-1140 (9th Cir.2004). See also Hon. Eugene Wedoff, “Means Testing in the New 707(b)”, 79 *Am. Bankr.L.J.* 231 (2005).

ⁱⁱ §707(b)

ⁱⁱⁱ For example, *In re Mestemaker*, 359 B.R. 849 (Bank.N.D.Ohio 2007); *In re Henebury*, 361 B.R. 595 (Bankr.S.D.Fla.).

^{iv} For example, *In re Pfeifer*, 365 B.R.187 (Bankr.D.Mont 2007) [Motion to Dismiss denied as debtors could not make a meaningful payment to a Chapter 13 plan]; *In re Schoen*,--- B.R. ----, 2007 WL 643295 (Bankr.D.Kan. 2007); *In re Pak*, 343 B.R. 239 (Bankr. N.D.Cal. 2006); *In re Paret*, 347 B.R. 12 (Bankr.D.Del.2006); *In re Pennington*, 348 B.R. 647 (Bankr.D.Del.2006); *In re Simmons*, 357 B.R. 480 (Bankr.N.D.Ohio 2006).