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A Critical Analysis of Bankruptcy Code Section 707(b)

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A CRITICAL ANALYSIS OF BANKRUPTCY CODE SECTION 707(b)

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I. INTRODUCTION

After the passage of the 1978 Bankruptcy Reform Act,¹ the credit industry initiated a well-coordinated lobbying effort that utilized extensive surveys and the news media to demonstrate that the 1978

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¹ Pub. L. No. 95-598, 92 Stat. 2549 (principally codified in U.S.C. with scattered sections in 28 U.S.C.).

bankruptcy legislation made it too easy and profitable for an individual to file bankruptcy.² Indeed, the number of bankruptcy filings increased significantly after the adoption of the 1978 Act. The following tables demonstrate the rapid growth in bankruptcy filings in the years 1978 to 1982.

TABLE 1³

Year Ending June 30	Total Filings	Non- Business	Business
1972	182,869	164,737	18,132
1973	173,197	155,707	17,490
1974	189,513	168,767	20,746
1975	254,484	224,354	30,130
1976	246,549	211,348	35,201
1977	214,399	182,210	32,189
1978	202,951	172,423	30,528
1979	226,476	196,976	29,500
1980	360,957	314,856	45,857
1981	519,063	452,145	66,006
1982	527,811	449,839	77,503

Table 2 indicates the percentage change in filings for the same years.

TABLE 2⁴

Year Ending June 30	Total Filings	Numerical Increase or Decrease	Percentage Change
1972	182,869	-18,483	-9.2
1973	173,197	-9,672	-5.3
1974	189,513	+16,316	+9.4
1975	254,484	+64,971	+34.3
1976	246,549	-7,935	-3.1
1977	214,399	-32,150	-13.0
1978	202,951	-11,448	-5.3
1979	226,476	+23,525	+11.6

² Warren, *Reducing Bankruptcy Protection for Consumers: A Response*, 72 GEO. L.J. 1333 (1984). See also Black and Herbert, *Bankcard's Revenge: A Critique of the 1984 Consumer Credit Amendments to the Bankruptcy Code*, 19 U. RICH. L. REV. 845 (1985); Morris, *Substantive Consumer Bankruptcy Reform in the Bankruptcy Amendments Act of 1984*, 27 WM. & MARY L. REV. 91 (1985).

³ Annual Report of the Administrative Office of the United States Courts (1982). See also Breitowitz, *New Developments in Consumer Bankruptcies: Chapter 7 Dismissal on the Basis of Substantial Abuse* (pts. 1 & 2), 59 AM. BANKR. L.J. 327 (1985), 60 AM. BANKR. L.J. 33 (1986).

⁴ Annual Report of the Administrative Office of the United States Courts (1982). See also Breitowitz, *supra* note 3.

TABLE 2 *continued*

Year Ending June 30	Total Filings	Numerical Increase or Decrease	Percentage Change
1980	360,957	+ 134,481	+ 59.4
1981	519,063	+ 158,106	+ 43.8
1982	527,811	+ 8,748	+ 1.7

In response to criticism by the credit industry and the dramatic rise in the amount of consumer bankruptcy filings, a number of provisions relating to consumer credit, often referred to as the "Consumer Credit Amendments," were included in the Bankruptcy Amendments and Federal Judgeship Act of 1984.⁵ One of the stated purposes of the "Consumer Credit Amendments" was to decrease the number of personal bankruptcies. Senator Hatch, a strong supporter of the bill, made the following statement during consideration of the conference report:

The number of consumer bankruptcy cases filed has risen dramatically each year since the bankruptcy code was last amended in 1978. Several witnesses before the Senate Judiciary Committee pointed to these changes in the Code as the principal cause of the increase. The 1978 amendments generally eased a debtor's access to bankruptcy to avoid excessive indebtedness. Title II [Consumer Credit Amendments] contains over 30 substantive amendments to curb abuses of the bankruptcy code and make its use truly a last resort.⁶

Another concern prompting the legislation was the availability of affordable consumer credit. The Senate Report, in an early version of the bill which eventually became the Consumer Credit Amendments, included the following discussion:

The ever-increasing number of bankruptcies, and the resultant financial losses, constitutes a general burden on the economy of billions of dollars annually. In the short term, these costs are shifted from debtor to lender (and stockholders and owners of the institutions providing credit). In the long run, however, creditors will not continue to bear the losses; instead, the realities of the marketplace will force them to seek greater protection by increasing the cost of obtaining credit, requiring additional collateral or cosignors, and/or reducing their financial risks by eliminating some transactions completely. For example, testimony by credit

⁵ Pub. L. No. 98-353, 98 Stat. 333 (1984) (codified in scattered sections of 11 U.S.C.).

⁶ 130 CONG. REC. S8891, 8894 (daily ed. June 29, 1984).

industry experts revealed that some consumer credit companies—which previously made loans which were secured only by personal property—now are making a large proportion of loans secured by second mortgages on the consumer's residence. As a consequence of such creditor responses, credit will become more difficult to obtain, and the general cost of doing business will escalate. Such a result is directly at odds with congressional efforts to make credit more widely available—for example, by statutes such as the Equal Credit Opportunity Act, and the Fair Credit Reporting Act.⁷

Moreover, in explaining the need for the Consumer Credit Amendments, Congressman Anderson stated:

[The 1978 Act] made it easier for a debtor to obtain Chapter 7 relief because it does not require that he give serious consideration to a Chapter 13 repayment plan. This has worked to the detriment of creditors and consumers alike. A recent GAO report suggests that 40 percent of those who file for Chapter 7 relief have income, assets and debts comparable to those seeking Chapter 13 relief. These improper Chapter 7 filings may cost the lending industry as much as \$1.25 billion annually in lost revenues. And, as with anything else, these losses are passed along to consumers in the form of higher interest rates, credit fees, and increased prices for goods and services.⁸

Section 707(b)⁹ is one of the most significant changes included in the Consumer Credit Amendments. This entirely new provision allows bankruptcy courts to dismiss a Chapter 7 petition for substantial abuse when the case is filed by an individual debtor whose debts are primarily consumer debts. Section 707(b) reads as follows:

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. There shall be a presumption in favor of granting the relief requested by the debtor.¹⁰

⁷ S. REP. NO. 446, 97th Cong., 2d. Sess. 6 (1982) (footnote omitted).

⁸ 130 CONG. REC. H7499 (daily ed. June 29, 1984).

⁹ 11 U.S.C.A. § 707(b) (West Supp. 1987) (1986 amendment clarified that U.S. trustee could raise the issue of substantial abuse).

¹⁰ *Id.*

The purpose of the Consumer Credit Amendments is clearly expressed. However, the language of section 707(b) and the sparse and conflicting statements of legislative intent behind section 707(b) have given rise to four difficult issues that have not been resolved consistently by the courts: (1) What is the effect of a party in interest raising the issue of substantial abuse? (2) What is the appropriate definition of the phrase "primarily consumer debts"? (3) What circumstances would constitute substantial abuse? (4) What is the effect of the presumption in favor of relief?

The ultimate resolution of these issues will determine if the legislation will create an improved bankruptcy system or dramatically alter the traditional "fresh start" approach to individual bankruptcy. This Article reviews various court decisions and attempts to provide a workable framework for the application of the concepts embodied in section 707(b).

II. MOTION TO DISMISS

Motions to dismiss a Chapter 7 petition for substantial abuse may be brought by the court or the United States trustee, provided such action is not at the request or suggestion of any party in interest. Congress' intent to preclude creditors from raising the issue of substantial abuse is evidenced by the legislative history of the 1986 Amendment. In 1986, section 707(b) was amended to clarify that the United States trustee could raise the issue of substantial abuse.¹¹ The House Conference Report

¹¹ The essential duties of the trustee are as follows:

- (1) To collect and reduce to money the property of the estate and to close up such estate as expeditiously as is compatible with the best interests of parties in interest;
 - (2) To be accountable for all property received;
 - (3) To investigate the financial affairs of the debtor;
 - (4) If a purpose would be served (e.g., as where there are assets to be distributed), to examine proofs of claims and object to the allowance of any claim that is improper;
 - (5) If advisable, to oppose the discharge of the debtor if grounds for such objection exist, since the trustee represents the creditors as well as the debtor and the court;
 - (6) To furnish such information concerning the estate and the estate's administration as is requested by a party in interest;
 - (7) If the business of the debtor is authorized to be operated, to file with the court and with the appropriate governmental unit charged with the responsibility for collection or determination of any tax arising out of such operation, periodic reports and summaries of the operation of such business, including a statement of receipts and disbursements, and such other information as the court requires; and
 - (8) To make a final report and file a final account of the administration of the estate with both the court and with the United States trustee.
- See* 28 U.S.C.A. 586(a) (West Supp. 1987).

on the amendment noted that the "original intent . . . was to preclude creditors from exercising this function [bringing information on substantial abuse to the courts attention]."¹² Representative Fish, one of the legislative managers of the Amendment, made the following comment on the floor: "[T]he 'party in interest' phrase in section 707(b) was intended to mean creditors. . . ."¹³ The prohibition against a creditor raising the issue of substantial abuse was apparently included in the legislation to quell concerns that creditors would routinely move for dismissals, thereby burdening debtors with the additional expense and time involved in demonstrating that Chapter 7 bankruptcy relief is appropriate.¹⁴ Senator Metzenbaum's comments, as the Senate adopted the conference report, support this conclusion. He stated:

I also am extremely pleased that this bill prohibits creditors from filing motions attempting to deny bankruptcy relief to individuals because of substantial abuse. If a creditor asks a court to dismiss a case claiming that there has been substantial abuse [of the bankruptcy laws by the debtor, the court would not be] allowed to do so. Only a bankruptcy court, acting on its own initiative, could dismiss a case involving substantial abuse. This will preclude creditors from making bankruptcy too expensive for the debtor by filing harassing motions alleging substantial abuse.¹⁵

The statutory language and legislative intent clearly provide that the court can only exercise the power to dismiss for substantial abuse *sua sponte*¹⁶ or upon a motion by the United States trustee. Courts that have ruled upon motions by creditors to dismiss a case pursuant to section 707(b) have denied the use of such motions. However, a more troubling issue has arisen when a party in interest has merely suggested that the court consider holding a section 707(b) hearing, or has raised the possibility of dismissal in the course of other proceedings.

One of the earliest cases to address a motion by a creditor was *In re Christian*.¹⁷ In *Christian*, the Union Chelsea Bank, a creditor of Christian, made a motion requesting that the court hold a hearing to

¹² H.R. CONF. REP. NO. 958, 99th Cong. 2d Sess. 46-7, reprinted in 1986 U.S. CODE CONG. & AD. NEWS 5246, 5247-8.

¹³ 132 CONG. REC. H9000-9001 (daily ed. Oct 2, 1986).

¹⁴ These concerns were expressed when an earlier version of the law was being considered which allowed creditors to challenge Chapter 7 filings. S. REP. NO. 446, 97th Cong., 2d Sess. 49-53 (1982) (minority views of Senators Metzenbaum and Kennedy).

¹⁵ 130 CONG. REC. S7624-25 (daily ed. June 19, 1984).

¹⁶ "Of his or its own will or motion; voluntarily; without prompting or suggestion." BLACKS LAW DICTIONARY 1592 (4th ed. 1968).

¹⁷ 51 Bankr. 118 (Bankr. D.N.J. 1985).

determine whether the bankruptcy petition should be dismissed pursuant to section 707(b).¹⁸ In denying the Bank's motion, the court relied upon the "plain meaning approach" to the statutory language and legislative history. After reviewing the legislative history of the 1978 Bankruptcy Act concerning the phrase "on request of a party in interest," the court stated:

Congress was clear that when it said "on request of a party in interest," it prohibited the court from acting *sua sponte*. A very simple reversal of that term leads to the conclusion that when it says not at the request of a party in interest, it is specifically directing the court to act *sua sponte*.¹⁹

The court also referred to Senator Metzenbaum's statement on the floor of the Senate as the conference report to the 1984 Amendments was adopted,²⁰ and discussed the consequences of permitting creditors to move for dismissal. In the court's opinion:

[T]he flood gates could open every time there is an adversary proceeding concerning the dischargeability of a debt or the granting of a discharge. If the creditor lost on substantive basis or lost for failure to file it within time, he would get another bite at the apple. The creditor would get a hearing on whether or not there has been substantial abuse. . . .²¹

The court further noted that unlike other code provisions concerning consumer cases, there are no penalties that can be imposed upon creditors for being wrong.²²

Under *Christian*, then, a court cannot respond to a motion by a creditor to hold a hearing in order to determine whether or not the petition should be dismissed for substantial abuse.²³ Additionally, although not clearly stated, the court indicated that the creditor's motion to dismiss may taint the entire case, precluding the court from raising the issue of substantial abuse.²⁴

The issue of substantial abuse arose in an interesting fashion in the

¹⁸ It should be noted that this case was decided prior to the 1986 amendment to section 707(b) permitting motions by the U.S. trustee. The United States trustee urged the court to have himself or the designated trustee pursue the motion. However, the court determined that trustees were parties in interest.

¹⁹ 51 Bankr. 118, 120 (Bankr. D.N.J. 1985).

²⁰ See *supra* text accompanying note 15.

²¹ 51 Bankr. 118, 120 (Bankr. D.N.J. 1985).

²² *Id.* at 121.

²³ *Id.* at 122. See also *In re Cecil*, 71 Bankr. 730 (Bankr. W.D. Va. 1987) (section 707(b) denies creditors standing to move for dismissal).

²⁴ 51 Bankr. 118, 120 (Bankr. D.N.J. 1985).

case of *In re Campbell*.²⁵ In *Campbell*, a creditor filed a document entitled "Suggestions of Lawrence National In Opposition to Discharge." The court noted that "[t]hese were filed, not as an adversary action, not as a motion, but apparently as an assistance to the court in the event that the court would otherwise fail to recognize the signal flags of substantial abuse."²⁶

In dealing with the Bank's suggestions, the court addressed the following questions:

- (1) [S]hould the pleading of the Bank be considered by the court in its . . . deliberations under section 707(b)?;
- (2) Do such suggestions poison the process, so that any independent investigation by the court is tainted and would constitute what in criminal practice parlance would be termed "fruit of the poison tree"?
- (3) [S]hould the court impose sanctions on an aggressive creditor who has overstepped the boundaries of the statute?²⁷

The court began answering these questions by noting the inconsistencies found in the Congressional intent of the 1978 Act and section 707(b). Under the 1978 Act, Congress intended creditors to participate fully in the bankruptcy process by policing the acts of debtors. However, in section 707(b), creditors were completely removed.²⁸

In answer to the first question, the court decided that the statute and Congressional intent were clear. The suggestions of the bank could not be considered.²⁹ Having so concluded, the court promptly disregarded the Bank's suggestions.³⁰

Turning to the second question, the court determined that the Bank's suggestions did not preclude the court from making an independent finding of substantial abuse.³¹ The court disagreed with Senator Metzbaum's reading of the statute and reasoned that to conclude otherwise would defeat the general spirit of the Bankruptcy Code and discourage creditors from participating in the process.³² The court stated:

Public policy which this court understands to be that honest debtors should have a fresh start would not be served by saying that a debtor who has abused the process should be rewarded as a result of an overzealous act upon the part of a good faith

²⁵ 63 Bankr. 702 (Bankr. W.D. Mo. 1986).

²⁶ *Id.* at 703.

²⁷ *Id.* at 704.

²⁸ *Id.*

²⁹ *Id.* at 705.

³⁰ 63 Bankr. 702, 705.

³¹ *Id.*

³² *Id.*

creditor. The court is put in mind of the old adage that "Two wrongs do not make a right." If the debtor has abused the system or its spirit, the sin of the creditor in pointing it out does not make the debtor's act proper.³³

Ultimately, the court reviewed the case for substantial abuse but determined that dismissal was not warranted.³⁴

The court also decided not to impose sanctions on the bank for suggesting that the court dismiss the case under section 707(b). In the court's opinion, the public policy and philosophy of creditor participation overshadowed the fact that the Bank suggested dismissal.³⁵ Furthermore, the court noted that "in weighing the potential harm to debtors by isolated acts of this type the court believes that the general restriction of substantial abuse outweighs any need for the imposition of penalties."³⁶ The court added, however, that a different result might be in order should the Bank persist in such conduct.³⁷

³³ *Id.*

³⁴ *Id.* at 706.

³⁵ 63 Bankr. 702, 705.

³⁶ *Id.*

³⁷ *Id.* See also *In re Hudson*, 56 Bankr. 415, 420 (Bankr. N.D. Ohio 1985) which employed the same analysis, but from the case it is unclear how the issue of substantial abuse was brought to the court's attention:

While it appears that the provisions of section 707(b) should be given their ordinary and plain meaning, to do so is to present the court with a practical difficulty in the event a party-in-interest should bring a case to the court's attention. On one hand, the court may not act pursuant to section 707(b) if a case has been brought to its attention by a party-in-interest. On the other hand, the court cannot ignore information which has been brought before it, regardless of how the information was obtained. If a rule were devised, whereby a court could not act pursuant to section 707(b) if a case was called to the court's attention by a party-in-interest, such a rule would have a deterrent effect on the parties who would otherwise make this information available. However, it would also have the effect of preventing the court from acting in cases where an abuse of Title 11 Chapter 7 is most likely to be occurring.

This court cannot sanction flagrant violations of the restrictions which limit parties-in-interest from suggesting the review of a case for dismissal under section 707(b). However, this court also cannot sanction abuse of Chapter 7, particularly when Congress has authorized the courts to challenge cases in which abuse is suspected. If given the choice as to which of these violations should be overlooked, this court believes that public policy and equity require that it be the former. This is not to say that repeated violations by any particular party-in-interest will go unattended. Rather, the court should retain the option of pursuing a case under section 707(b) dependent upon the intent and past practices of the party which calls attention to a case. Therefore, this court must conclude that unless a party or their counsel flagrantly, intentionally, or repeatedly violates the limitations under 11 U.S.C. § 707(b), the court will not necessarily be precluded from dismissing a case pursuant to 11 U.S.C. § 707(b), despite the fact that a

In the case of *In re Jones*,³⁸ the issue of substantial abuse was brought to the court's attention through a statement filed by Mr. Rankin, a non-interested party. Mr. Rankin, however, had signed the statement upon the request of an attorney for a creditor. The court determined that since the statement was initiated at the suggestion of a party in interest, the question of substantial abuse was improperly brought to the court's attention.³⁹ As a consequence, the court was precluded from considering whether the debtor's petition constituted a substantial abuse.⁴⁰

The facts giving rise to the possibility of substantial abuse were brought to the courts' attention during other bankruptcy proceedings in the cases of *In re Mastroeni*⁴¹ and *In re Keniston*.⁴² In *Mastroeni*, the court found no issue in the possibility that dismissal for substantial abuse came to the courts attention during a hearing on a motion by a creditor for relief from the automatic stay.⁴³

In *Keniston*, the application of section 707(b) may be affected by the resolution of constitutional questions.⁴⁴ However, the court discussed the issue of a proper motion. The possibility of substantial abuse was brought to the court's attention during a pre-trial hearing on a creditor's complaint objecting to the dischargeability of certain debts arising from divorce proceedings. In this hearing, the creditor's ex-wife contended that

party-in-interest brought to light information which subjects a case to scrutiny under that section.

³⁸ 60 Bankr. 96 (Bankr. W.D. Ky. 1986).

³⁹ *Id.* at 98.

⁴⁰ *Id.*

⁴¹ 56 Bankr. 456 (Bankr. S.D.N.Y. 1985).

⁴² 60 Bankr. 742 (Bankr. D.N.H. 1986).

⁴³ 56 Bankr. 456 (Bankr. S.D.N.Y. 1985).

⁴⁴ In *Keniston*, Bankruptcy Judge James E. Yacos raised five constitutional issues:

1. Does the statute deny procedural due process by constituting the judicial officer who must decide the ultimate question of the debtor's right to bankruptcy relief as in effect "accuser" or "prosecutor" initiating the complaint against the debtor?
2. Is the requisite "case and controversy" requirement for federal jurisdiction under Article III of the Constitution present when no other party besides the court itself has raised any issue or dispute requiring judicial determination?
3. If this statute is construed to require the judicial officer to review all bankruptcy petitions to determine whether some involve "substantial abuse" requiring objection and possible denial of bankruptcy relief, does the placing of that review and processing function with a judicial officer violate the separation of powers doctrine inherent in the Constitution?
4. Is there a violation of substantive due process by the arguably vague language of this statute giving no standard for its application and apparently indicating "abuse" of the bankruptcy laws is permissible but "substantial abuse" is not?
5. Does the statute deny equal protection of the law by drawing a distinction between "consumer" debtors and other debtors for relief under Chapter 7 without a rational basis?

Id. at 744-45. These issues remain unresolved pending further hearing and briefing.

the debtor's conduct constituted abuse. The court noted the following in a footnote:

The very fact that the ex-wife voiced these contentions at the pre-trial hearing could itself be construed as a violation of the § 707(b) language prohibiting the substantial [sic] issue to come forward "at the request or suggestion of any party in interest." However, it is not unusual for creditors to object generally to "abuse" by the debtor in conjunction with various adversary proceedings and that is all that occurred here. Left for another day is the question of *deliberate* efforts to provoke a "sua sponte" § 707(b) order by the artful use of an unrelated adversary proceeding to that end.⁴⁵

Arguably, however, the creditor in this case had deliberately tried to provoke a section 707(b) dismissal. After the court ordered the substantial abuse hearing, the creditor failed to take advantage of the opportunity to amend her dischargeability complaint. In addition, the court concluded that there was no doubt that the obligations objected to by the creditor were dischargeable.⁴⁶

Clearly, a bankruptcy court should not hold a section 707(b) hearing in direct response to a motion or suggestion of a party in interest. However, such a motion or suggestion should not foreclose the court from making an independent determination that the case may constitute substantial abuse. If, after an independent examination of the case, the court decides to hold a section 707(b) hearing, the court is acting *sua sponte* as required by the statute. Although this solution is in conflict with specific statements in the legislative history, it does not defeat the purpose which prompted Congress to include the prohibition against a creditor raising the issue: that creditors would harrass debtors and make bankruptcy too expensive. The independent determination by the court assures that creditors cannot use section 707(b) to harrass debtors in Chapter 7. Moreover, a debtor should not be granted relief under Chapter 7 when the case constitutes substantial abuse simply because a creditor has suggested dismissal under section 707(b).⁴⁷

⁴⁵ *Id.* at 744 n.1 (citation omitted).

⁴⁶ *Id.* at 743.

⁴⁷ Other commentators have suggested that the bankruptcy court impose a rebuttable presumption whenever a creditor takes action to raise the issue of substantial abuse, that it is at the request or suggestion of a party in interest, and therefore, improper. This presumption could then be rebutted by establishing that the party in interest's action did not affect the court's decision. See Black and Herbert, *supra* note 2, at 857.

III. PRIMARILY CONSUMER DEBTS

The second issue raised by section 707(b) is the definition of the phrase "primarily consumer debts." The phrase actually presents two separate issues: (1) what is a "consumer debt"?; and (2) what is "primarily" a consumer debt? The language of the section is subject to many different interpretations, as demonstrated in numerous court decisions to date.

A. *Consumer Debt vs. Non-Consumer Debt*

The term "consumer debt" is defined in the Bankruptcy Code as "debt incurred by an individual primarily for a personal, family or household purpose."⁴⁸ The legislative history indicates that the bankruptcy definition was "adapted from the definition used in various consumer protection laws."⁴⁹ Presumably, among the laws referred to by Congress were the Truth in Lending Act,⁵⁰ the Consumer Product Safety Act,⁵¹ and the Uniform Commercial Code.⁵² Under each of these laws, the definitions focus on the purpose of the transaction in an attempt to differentiate between personal, family, household, and business or commercial purposes.⁵³

The definition of consumer debt has been at issue in a number of bankruptcy cases concerning provisions other than section 707(b). The issue of consumer purpose as opposed to business purpose has been previously addressed. In *In re Nenninger*,⁵⁴ the court was called upon to decide whether attorney fees should be awarded following the debtors' successful defense of a credit union's claim that the debt was not dischargeable. Under 11 U.S.C. section 523(d), the debtor is entitled to attorney fees when the debt is a "consumer debt." The proceeds of the credit union loan were used to purchase a commercial campground. The court denied attorney fees stating that the appropriate test is the

⁴⁸ 11 U.S.C.A. § 101(7) (West 1979).

⁴⁹ H.R. REP. No. 595, 95th Cong., 1st Sess. 309 (1977); S. REP. No. 989, 95th Cong., 2d Sess. 22 (1978), reprinted in U.S. CODE CONG. & AD. NEWS S787.

⁵⁰ 15 U.S.C.A. § 1601-1693 (West 1982 & Supp. 1987).

⁵¹ 15 U.S.C.A. § 2051-2076 (West 1982 & Supp. 1987).

⁵² E.g., MINN. STAT. ANN. § 336.9-109 (West 1966).

⁵³ Regulation Z, issued to implement the Truth in Lending Act, defines "consumer credit" as "credit offered or extended to a consumer primarily for personal, family or household purposes." 12 C.F.R. § 226.2(12) (1987). The Consumer Product Safety Act defines consumer product as any article for sale or personal use to a consumer for in around a household or residence, a school or recreation. 15 U.S.C.A. § 2052(a)(1) (West 1982). Consumer good is defined in the Uniform Commercial Code as goods used or bought for use primarily for personal family or household purposes. MINN. STAT. ANN. § 336.9-109 (West 1966).

⁵⁴ 32 Bankr. 624 (Bankr. W.D. Wis. 1983).

“purpose of the loan”⁵⁵ and that “[u]nder the plain language of the statute [section 101(7)], a loan to purchase a commercial campground cannot be a consumer debt.”⁵⁶ In reaching this conclusion, the court referred to two earlier cases which arose in a similar context. The court in *In re Valley*⁵⁷ stated that a loan to purchase a truck-tractor for use in the logging business was not a consumer debt. The court in *In re McCourt*⁵⁸ ruled that a debt incurred to purchase an apartment complex was not a consumer debt. Subsequent to the decision in *Nenninger*, two bankruptcy courts determined that debts incurred in the contracting business were not for personal, family or household purposes.⁵⁹

Bankruptcy Code sections 1301⁶⁰ and 1201⁶¹ also contain provisions which treat consumer debt differently from other debt although in a different context. Both sections extend the stay of relief to co-debtors when the debt is a consumer debt. The court in *In re Stein*⁶² discussed section 1301 and the meaning of the term “consumer debt.” The debt at issue was a consolidation loan which enabled the debtors to pay off various business debts owed in connection with a family farming operation, including debts on a combine, cattle, fertilizer, farming equipment, hay, and seed. The loan was also used to pay some personal obligations incurred for items such as food and doctor bills. The vast majority of the loan, however, was used to repay farming obligations. The court concluded that section 1301 did not protect the co-debtors. The court stated that the debt was a non-consumer debt because “a large portion of the debt encompassed obligations relating directly to the family farming operation, an operation, which is, in fact, the debtor’s business.”⁶³

The same result was reached in *In re Circle Five, Inc.*⁶⁴ and in *In re Bigalk*,⁶⁵ both involving section 1201. *Circle Five* involved a \$402,000 real estate loan from the Federal Land Bank. In deciding whether the debt was a consumer debt, the court noted that the definition was adopted from the various consumer protection laws. In addition, under the Uniform Commercial Code the critical factor used to distinguish non-consumer goods from consumer goods “is the use of the goods in the production of income as opposed to normal consumptive activity by an

⁵⁵ *Id.* at 625.

⁵⁶ *Id.*

⁵⁷ 21 Bankr. 674 (Bankr. D. Mass. 1982).

⁵⁸ 20 Bankr. 388 (Bankr. D. Mass. 1982).

⁵⁹ *In re Nicholson*, 51 Bankr. 198 (Bankr. M.D. Fla. 1985); *In re Pelen*, 33 Bankr. 763 (Bankr. M.D. Pa. 1983).

⁶⁰ 11 U.S.C.A. § 1301(a) (West 1979).

⁶¹ 11 U.S.C.A. § 1201(a) (West Supp. 1987).

⁶² 18 Bankr. 768 (Bankr. S.D. Ohio 1982).

⁶³ *Id.* at 769.

⁶⁴ 75 Bankr. 686 (Bankr. D. Idaho 1987).

⁶⁵ 75 Bankr. 561 (Bankr. D. Minn. 1987).

individual.”⁶⁶ Accordingly, the court stated that “for a debt to be a consumer debt it must be incurred principally to achieve a personal, family or household [purpose],” and that “[d]ebts for a business purpose are not consumer debts.”⁶⁷ With regard to the Federal Land Bank loan, the court reasoned:

The Debtor is a family farm corporation. The debt incurred is secured by real property. The real property is for the purpose of the farm operation. The farm operation is a business for the production of income. Debt used to produce income is not a consumer debt primarily for a personal, family or household purpose.⁶⁸

As such, the cosigners were not protected by section 1201.⁶⁹ Along the same lines, the court in *Bigalk* stated that “extension of credit for the commencement or continuation of large-scale agricultural or business activity simply is not made for a personal, family or household purpose.”⁷⁰

In a different context, the court in *In re Constantino*⁷¹ was confronted with determining whether the debt, which arose from an agreement under which Interstate was to purchase and sell index options for the debtor, was a consumer debt. Bankruptcy Code section 523(a)(2)(C)⁷² creates a presumption of non-dischargeability of consumer debts which exceed \$500 for luxury goods or services. Using the same rationale as in *Circle Five*, the court concluded that the debt was not a consumer debt and thus, the presumption did not apply.⁷³

The only bankruptcy decision to discuss consumer purpose versus business purpose under section 707(b) is *In re Almendinger*.⁷⁴ In *Almendinger*, the debtor was a stockbroker. He had incurred debts totalling approximately \$120,000 on his credit card accounts. At the section 707(b) hearing, the debtor testified that, with the exception of purchasing some baby furniture for his newborn daughter, the debt represented cash advances which he used to pay off investment losses and to reinvest in the stock market. In deciding whether the debts were consumer debts, the court referred to the legislative history of section 101(7) which indicates that the definition of consumer debt was derived from the definition used

⁶⁶ 75 Bankr. 686, 688 (Bankr. D. Idaho 1987).

⁶⁷ *Id.* (footnote omitted).

⁶⁸ *Id.*

⁶⁹ *Id.*

⁷⁰ 75 Bankr. 561, 566 (Bankr. D. Minn. 1987) (footnote omitted).

⁷¹ 72 Bankr. 189 (Bankr. D.S.C. 1986).

⁷² 11 U.S.C.A. § 523(a)(2)(C) (West Supp. 1987).

⁷³ 72 Bankr. 189, 192 (Bankr. D.S.C. 1986).

⁷⁴ 56 Bankr. 97 (Bankr. N.D. Ohio 1985).

in the various consumer protection laws. The court then noted that “the definition of ‘consumer credit’ transaction under the [Truth in Lending Act] is markedly similar to the definition of consumer debt under the Bankruptcy Code”⁷⁵ and that a review of the cases under the Truth in Lending Act “shows that when the credit transaction involves a *profit motive*, it is outside the definition of ‘consumer credit’ transaction for the purposes of the Act [Truth in Lending].”⁷⁶ Further, the court pointed out that the Truth in Lending Act exempts transactions involving business and commercial purposes, concluding that the profit motive was the decisive factor in distinguishing the type of transaction.⁷⁷ Thus, the court concluded that the credit card debt was not consumer debt because the purpose for the cash advances was to make a profit and, therefore, section 707(b) did not apply to the debtor.⁷⁸

As a result of the vast body of case law developed under the various consumer protection laws, the bankruptcy courts should have some assistance distinguishing consumer debt from business debt. However, troubling issues remain unresolved.

B. Mortgage Debt

A difficult and important issue yet to be resolved is whether a mortgage obligation is a consumer debt. As stated, section 101(7) provides that consumer debt is debt incurred for a personal, family, or household purpose. The definition makes no distinction between secured and unsecured debt. Nevertheless, legislative history includes statements by Senator DiConcini and Representative Edwards that the term “consumer

⁷⁵ *Id.* at 99.

⁷⁶ *Id.*

⁷⁷ *Id.* It is interesting to note that the Truth in Lending Regulations do not set forth a profit motive test for distinguishing between business or commercial purposes and consumer purpose credit. Instead, the following factors are used to determine whether credit to finance an acquisition, such as securities, is primarily for business purposes as opposed to consumer purposes.

1. The relationship of the borrower’s primary occupation to the acquisition. The more closely related, the more likely it is to be business purpose.
2. The degree to which the borrower will personally manage the acquisition. The more personal involvement there is, the more likely it is to be business purpose.
3. The ratio of income from the acquisition to the total income of the borrower. The higher the ratio, the more likely it is to be business purpose.
4. The size of the transaction. The larger the transaction, the more likely it is to be business purpose.
5. The borrower’s statement of purpose for the loan.

12 C.F.R. Comment 226.3 (a)(2)(1987).

⁷⁸ 56 Bankr. 97, 99 (Bankr. N.D. Ohio 1985).

debt" does not include any debt which is secured by real property.⁷⁹ Both Congressmen played central roles in the passage of the Bankruptcy Reform Act of 1978.

The bankruptcy courts which have addressed this issue outside the scope of section 707(b) have all reached the conclusion that a mortgage loan does not constitute a consumer debt.⁸⁰ Each decision simply refers, without further analysis, to the statements of Congressmen DiConcini and Edwards in the legislative history. One court made the comment that to hold otherwise would undermine the Congressional intent.⁸¹

When dismissal for substantial abuse under section 707(b) is at issue, the bankruptcy courts are split as to whether debts secured by real property are consumer debts. The Ninth Circuit Bankruptcy Appeals Panel, in the case of *In re Kelly*,⁸² held that debts secured by the debtor's residence were not consumer debts for the purposes of section 707(b).⁸³ In reaching this conclusion, the Appeals Panel noted the key roles that Congressmen DiConcini and Edwards played in the passage of the Bankruptcy Reform Act of 1978, but concluded that individual explanatory comments cannot be used to rewrite the plain language that Congress, as a whole, enacted in section 101(7).⁸⁴ The court then reasoned:

[T]he exclusion of debts secured by real property is logical and consistent with the purpose behind § 707(b). A debtor owning a family home usually has substantial debt secured by real property. The debt secured by the residence is usually three or four times (or greater) than the aggregate of unsecured debt. Therefore, unless that secured debt is disregarded, all such debtors could be denied relief because their indebtedness would be *primarily* consumer debt; certainly in dollar amount. In addition, it is common knowledge that the consumer loan industry proposed and lobbied heavily for the so-called consumer bankruptcy

⁷⁹ 124 CONG. REC. H11,090 (daily ed. Sept. 28, 1978) (remarks of Rep. Edwards); 124 CONG. REC. S17,406 (daily ed. Oct. 6, 1978) (remarks of Sen. DeConcini).

⁸⁰ *In re Ikeda*, 37 Bankr. 193 (Bankr. D. Hawaii 1984); *In re Nenninger*, 32 Bankr. 624 (W.D. Wis. 1983); *In re Randolph*, 28 Bankr. 811 (Bankr. E.D. Va. 1983); *In re Stein*, 18 Bankr. 768 (Bankr. S.D. Ohio 1982). See also *In re Burgess*, 22 Bankr. 771 (Bankr. M.D. Tenn. 1982).

⁸¹ *In re Ikeda*, 37 Bankr. 193, 195 (Bankr. D. Hawaii 1984).

⁸² 70 Bankr. 109 (Bankr. 9th Cir. 1986). It should be noted that the 1984 Act provides for a system of appeals in which the district court has the jurisdiction to hear appeals from final judgments, orders and decrees of its bankruptcy courts, and, with permission of such court, appeals from interlocutory orders and decrees. It also provides that the judicial council of the circuit may establish a bankruptcy appellate panel, comprised of three bankruptcy judges from districts within the circuit, to hear, with the consent of all parties, appeals generally heard by the district court. 28 U.S.C. § 158(d) (West Supp. 1987).

⁸³ *Id.* at 112.

⁸⁴ *Id.*

provisions, including § 707(b) and that the consumer loan industry is not generally concerned with debt secured by real estate.⁸⁵

The court's decision in *In re Walton*⁸⁶ is in direct conflict with the Appeals Panel decision. In *Walton*, the court noted that a mortgage obligation was a consumer debt.⁸⁷ The bankruptcy court in *In re Bryant* reached the same conclusion.⁸⁸ Neither of these decisions, however, mentions the legislative history to section 101(7) nor the fact that other courts have construed the term consumer debt to exclude mortgage debt.⁸⁹

The rationale used by the Appeals Panel in *Kelly* to conclude that mortgage obligations are not consumer debt is not persuasive. The Appeals Panel stated that unless the secured debt is disregarded, all debtors owning a family home could be denied relief because their indebtedness would be primarily consumer debt. However, under section 707(b), a debtor will be denied relief under Chapter 7 only if the granting of relief would be substantial abuse. When a case constitutes substantial abuse, a debtor should not be granted relief simply because he or she has a mortgage. Moreover, while the consumer loan industry may not be concerned with debt secured by real estate, excluding such debt from the definition of consumer debt could result in fewer dismissals under section 707(b), not because of the absence of substantial abuse, but because the debts are not primarily consumer debts. Accordingly, this interpretation defeats the goals of the consumer loan industry and the purpose of the Consumer Credit Amendments.

The preferred view is that mortgage obligations incurred primarily for personal, family, or household purposes are consumer debt. Clearly, this is the result reached by looking at the plain meaning of the language, and, as noted in *Kelly*, individual explanatory comments cannot be used to rewrite plain language. Furthermore, there is no reason to exclude mortgage debt incurred for personal, family, or household purposes from the term "consumer debt."

C. Focus On "Incurred"

Consumer debt is debt incurred by an individual primarily for a personal, family, or household purpose.⁹⁰ The court in *In re White*⁹¹ focused on the reason for incurring the obligation to determine if the

⁸⁵ *Id.* (footnote omitted).

⁸⁶ 69 Bankr. 150 (Bankr. E.D. Mo. 1986).

⁸⁷ *Id.* at 153-54 n.4.

⁸⁸ 47 Bankr. 21 (Bankr. W.D.N.C. 1984).

⁸⁹ Both of these cases were decided prior to the Appeals Panel decision in *Kelly*.

⁹⁰ 11 U.S.C.A. § 101(7) (West 1979).

⁹¹ 49 Bankr. 869 (Bankr. W.D.N.C. 1985).

obligation was a consumer debt. The specific issue in *White* was whether a \$375,000 judgment against the bankruptcy petitioner for a negligent automobile accident was a consumer debt. The court stated that the key words in the definitions of consumer debt are “incurred,” “primarily,” and “purpose.”⁹² The court then referred to Webster’s New Collegiate Dictionary (1985) for the meanings of these terms and noted:

In general, to “*incur*” an obligation is to meet with it, to become liable to or to bring it down on oneself. For an incurrence to have been “*primarily*” for a personal purpose means that this incurrence was of the first importance or was fundamental. To have a “*purpose*” is to have an intention or an object set before oneself as an aim.⁹³

In applying these definitions, the court stated:

Thus, to be a consumer debt within the meaning of § 101(7) the liability must have been acquired first and foremost to achieve a personal aim or objective. An automobile accident liability is not such a debt. Here the obligation was incurred incidental to and not first and foremost to achieving a personal aim; which was gaining transportation.⁹⁴

In support of its narrow interpretation of the language, the court observed that “there is no evidence of a congressional intention to give the consumer debt definition . . . an expansive scope within the parameters of § 707(b)”⁹⁵ and that “the sparse legislative history implies that a more narrow interpretation is favored.”⁹⁶ Moreover, in dictum, the court limited its definition of consumer debt to consumer credit debt, stating that this construction was consistent with the congressional concern which prompted the enactment of the 1984 Amendments, including section 707(b), that “credit costs were being driven upwards by the ready availability of discharge via Chapter 7 to persons seeking to sidestep *consumer credit obligations* who had the ability to pay.”⁹⁷

In *Walton*,⁹⁸ the United States District Court disagreed with the test utilized in *White*. The court stated,

[T]he actual language of § 707(b) does not support the narrow definition of consumer debt set forth in *White*. Rather, it suggests

⁹² *Id.* at 872.

⁹³ *Id.*

⁹⁴ *Id.*

⁹⁵ *Id.*

⁹⁶ 49 Bankr. 869, 872.

⁹⁷ *Id.*

⁹⁸ 69 Bankr. 150 (Bankr. E.D. Mo. 1986).

the term should include those debts a person would ordinarily expect to incur in his daily affairs other than business expenses. The distinction drawn by the Bankruptcy Court in *White* between purchases on credit and other types of transactions has no rational relation to whether a debtor is conducting his personal life within his means. Similarly, whether a debtor incurred a liability through volition has no real significance.⁹⁹

In applying the “debts that a person would ordinarily expect to incur in his daily affairs” test, the court determined that virtually all the debts, including liability for Aid to Families with Dependent Children back payments, were consumer debts.¹⁰⁰ Clearly, the broad approach utilized in *Walton* achieves the goals of the Consumer Credit Amendments while the test in *White* thwarts these objectives.

D. What is “Primarily a Consumer Debt”?

The second aspect of the phrase “primarily consumer debts” raises the issue of the meaning of the term “primarily.” The language lends itself to

⁹⁹ *Id.* at 153.

¹⁰⁰ *Id.* at 153-54. The schedule filed by the debtor reflected the following debts:

Judgments

Laclede Gas	\$ 965.00
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Taxes

Internal Revenue Service	400.00
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Secured Debt

U.S. Dept. of Housing and Urban Development (HUD) (Home Mortgage)	55,000.00
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Unsecured Debts

James Criscione, M.D. (Feb., 1983 operation)	600.00
Cardinal Glennon Hospital (1982-83 Amelda Walton)	600.00
Anheuser-Busch Credit Union (1983 note)	6,000.00
Laclede Gas (gas service)	900.00
Cashex (check cashing service)	1,100.00
Security Storage System (furniture storage 1984)	100.00
Medical Dental Account (children's teeth)	300.00
Jewish Hospital (for spouse 1983-84)	600.00
Metropolitan Sewer (sewer service 1983)	100.00
Union Electric Co. (electric service 1984)	300.00
Incarinate Word Hospital (operation)	500.00
Gateway Account Service	500.00
Internists, M.D. (medical bills)	400.00
G.C. Services	400.00
Division of Family Services (AFDC to State)	6,984.00
Century 21—Halls Ferry (management of house)	1,600.00
Roue Motors (payment of repossession)	800.00
Home Cinema (movie rentals)	300.00

Total scheduled unsecured debts	22,084.00
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Id. at 151-52.

many possible interpretations: (1) Compare the total dollar amount of consumer debt to the total dollar amount of non-consumer debt, and if the total consumer debt is greater then there is consumer debt; (2) look to the total number of debts, rather than total dollar amount, and, if more than half the debts were consumer obligations, that would constitute primarily consumer debts; or (3) look to the intent of the bankrupt in filing the bankruptcy petition, and if the intent was to avoid paying consumer debts, that would constitute primarily consumer debts even if the type and amount of debts would not meet the total dollar test or total number test.

There is very little case law which addresses the meaning of the term “primarily” in the phrase “primarily consumer debts.” In *In re Bryant*,¹⁰¹ the debtor’s attorney argued that the debtor had primarily consumer debts if the aggregate amount of the debtor’s consumer debts exceeded the aggregate amount of non-consumer debts. In response, the court stated:

The court cannot agree with such a narrow interpretation. Certainly the relative aggregate amounts of consumer versus nonconsumer debts are important considerations, but they are by no means the only way by which a court can find a case to involve “primarily consumer debts.” . . . [t]he court concludes a debtor’s obligations may be adjudged “primarily consumer debts” not only by the aggregate amount but by their relative numbers as well.¹⁰²

Thus, the court retained the flexibility to dismiss a petition if only one of the two factors were present. According to the court, this was Congress’ intent. The court reasoned that:

Given the numerous instances in the code where Congress has established specific benchmarks to guide the Bankruptcy Court, I can only conclude that had it intended to narrow this definition as Debtor suggests, it would have so stated in the code provisions. That lacking, it is my firm impression that Congress intended to leave the definition of this term to the Bankruptcy Judge who has the case file before him and who can make the decision in light of all the facts and circumstances presented.¹⁰³

Under the facts of *Bryant*, however, the court determined that the aggregate dollar amount of consumer debt was more than the aggregate dollar amount of non-consumer debt. It also determined that the total number of consumer obligations¹⁰⁴ exceeded the total number of non-con-

¹⁰¹ 47 Bankr. 21 (Bankr. W.D.N.C. 1984).

¹⁰² *Id.* at 26.

¹⁰³ *Id.*

¹⁰⁴ *Id.*

sumer obligations. Specifically, the debtor had consumer debts of \$46,844 as compared to \$40,248 of non-consumer debt, and twelve of the debtor's fifteen or sixteen obligations were consumer debts.¹⁰⁵

The logical approach for the bankruptcy courts to follow is to look at the total aggregate dollar amount of consumer debt and the total aggregate dollar amount of non-consumer debt. If the consumer debt exceeds the non-consumer debt, the requirement of primarily consumer debt will be fulfilled. However, it should be noted that this position was not taken in *In re Restea*.¹⁰⁶ In *Restea*, the court concluded that consumer debt amounting to fifty-three percent of the total debt did not constitute primarily consumer debt for purposes of section 707(b).¹⁰⁷ The court stated, "[m]indful of the statutory presumption in bankruptcy of granting debtors relief and the underlying 'fresh start' policy basis, the court cannot find that 53 percent constitutes the principal debt."¹⁰⁸

IV. SUBSTANTIAL ABUSE

Substantial abuse is not defined in the legislation. As such, courts have been forced to construe the meaning of this phrase. At the crux of that interpretation is whether a "future income test" is mandated by section 707(b). A "future income test" would require the bankruptcy court to evaluate the debtor's future earning capacity to determine if he has the ability to make substantial payments to his creditors.

A. Legislative History

One of the concerns that prompted enactment of section 707(b) was that consumer debtors with the ability to repay their debts were taking advantage of bankruptcy. The primary basis for the concern was a consumer bankruptcy study (Purdue Study), conducted by the Credit Research Center located at the Krammert Graduate School of Management at Purdue University, which concluded that a substantial minority of consumers who file for Chapter 7 have considerable debt-paying ability.¹⁰⁹ A review of the legislative history provides conflicting evidence, however, as to whether section 707(b) includes a "future income test." Early versions of what eventually became section 707(b) specifically provided that Chapter 7 relief would be unavailable to individuals who could pay a reasonable portion of their debts out of anticipated future

¹⁰⁵ *Id.*

¹⁰⁶ 76 Bankr. 728 (Bankr. D.S.D. 1987).

¹⁰⁷ *Id.* at 734.

¹⁰⁸ *Id.* (footnote omitted).

¹⁰⁹ CREDIT RESEARCH CENTER, KRANNERT SCHOOL OF MANAGEMENT, PURDUE UNIVERSITY, CONSUMER BANKRUPTCY STUDY (1982). See also S. REP. NO. 446, 97th Cong., 2d Sess. 7-14 (1982).

earnings.¹¹⁰ This “future income test” was severely criticized by Senators Kennedy and Metzenbaum.¹¹¹ As a result of this opposition, a compromise was reached that deleted the “future income” language and replaced it with a provision permitting the court to dismiss a Chapter 7 petition upon a showing of substantial abuse.¹¹² At this juncture, a number of Senators, including Senator Metzenbaum, believed that the “future income test” had been completely eliminated from the bill.¹¹³ However, the Senate Report indicated otherwise, concluding that if a debtor could meet his debts without difficulty as they came due, use of Chapter 7 would be considered substantial abuse.¹¹⁴

This brings us to the bill as finally enacted. The legislative history is sparse and contradictory. During the house debate, many congressmen indicated that a “future income test” was intended. Representative Daub remarked:

The basic problem with the 1978 law and that [which] we seek to correct . . . is the fact that credit is granted on a prospective basis, that is one’s future earnings are considered in providing the credit. All we are asking is that when debts are discharged the same analysis be allowed instead of the current process whereby a snapshot of sorts is taken of the debtor’s financial position¹¹⁵

¹¹⁰ H.R. 4786, 97th Cong., 1st Sess. (1981); S. 2000, 97th Cong., 1st Sess. (1981).

¹¹¹ S. REP. NO. 446, 97th Cong., 2d Sess. 49-53 (1982) (dissenting views). Senator Metzenbaum stated that the future income language “would have made it more difficult for the debtor to go bankrupt and it would have provided a mortgage on his or her future.” 130 CONG. REC. S5361 (daily ed. April 27, 1983).

¹¹² S. 1013, 98th Cong., 1st Sess. (1983); S. 445, 98th Cong., 1st Sess. (1983). The “substantial abuse” language contained in these bills is substantially similar to section 707(b) as enacted.

¹¹³ 130 CONG. REC. S5361 (daily ed. April 27, 1983).

¹¹⁴ S. REP. NO. 65, 98th Cong., 1st Sess. (1983). The report summarized the section of the bill concerning dismissal for substantial abuse as follows:

This provision represents a balancing of two interests. It preserves the fundamental concept embodied in our bankruptcy laws that debtors who cannot meet debts as they come due should be able to relinquish non-exempt property in exchange for a fresh start. At the same time, however, it upholds creditors’ interests in obtaining repayment where such repayment would not be a burden.

Crushing debt burdens and severe financial problems place enormous strains on borrowers and their families. Family life, personal emotional health, or work productivity often suffer. By enabling individuals who cannot meet their debts to start a new life, unburdened with debt they cannot pay, the bankruptcy law allows troubled borrowers to become productive members of their communities. Nothing in this bill denies such borrowers with unaffordable debt burdens bankruptcy relief under Chapter 7. However, if a debtor can meet his debt without difficulty as they come due, use of Chapter 7 would represent a substantial abuse.

Id. at 53.

¹¹⁵ 130 CONG. REC. H1823 (daily ed. March 21, 1984); *see also id.* at H1811 (remarks of

Representative Anderson stated, "a bankruptcy court could dismiss a Chapter 7 filing if, in its opinion, the filing constitutes a substantial abuse of the bankruptcy code because the debtor is found capable of fulfilling the terms of a Chapter 13 repayment agreement."¹¹⁶

However, as the conference report was adopted by the Senate, Senator Metzenbaum stated that "both the House and Senate have agreed to the total elimination of the future income language . . . the availability of bankruptcy relief would not be limited by a future earnings standard."¹¹⁷ In Senator Metzenbaum's opinion, to have included a "future income test,"

[w]ould . . . force bankruptcy judges to become soothsayers and engage in the impossible task of predicting someone's earnings and financial obligations. Bankruptcy relief would . . . become hostage to a judge's guesses about how much an individual would earn, what their financial burdens would be, whether they would become sick, unemployed, and so on. In some cases, because judges are human, they simply would be wrong.¹¹⁸

Chairman Rodino also clearly stated, during consideration of the conference report in the House, that the provision contained no threshold or "future income test."¹¹⁹

Obviously, these contradictions in stated legislative intent have forced the courts to attempt to fashion a reasonable definition of what constitutes substantial abuse with little guidance from the legislative record. Not surprisingly, the courts have utilized three different approaches to the "future income" question: (1) use the "future income test" as the only criteria to determine substantial abuse; (2) use the "future income test" as one of several criteria; and (3) reject the "future income test" entirely.

B. *Substantial Abuse: Exclusive Future Income Test*

In *In re Edwards*,¹²⁰ the court defined the term "substantial abuse" by utilizing a "future income test." The court stated, "a debtor whose income and reasonable expenses indicate that he could pay over three years an amount equal to 100% of the principal owed to his creditors is not suffering from sufficient economic hardship to warrant use of Chapter

Rep. Brooks); *id.* at H1812 (remarks of Rep. Montgomery); *id.* at H1831 (remarks of Rep. Anthony); *id.* at H1832 (remarks of Rep. Brown). However, after the debate, Chairman Rodino had inserted into the *Congressional Record* that the substantial abuse provision "would not create a future income test." 130 CONG. REC. H1941 (daily ed. March 26, 1984).

¹¹⁶ 130 CONG. REC. H7499 (daily ed. June 29, 1984).

¹¹⁷ 130 CONG. REC. S7624 (daily ed. June 19, 1984).

¹¹⁸ *Id.*

¹¹⁹ 130 CONG. REC. H7489 (daily ed. June 29, 1984).

¹²⁰ 50 Bankr. 933 (Bankr. S.D.N.Y. 1985).

7.”¹²¹ In applying this “future income test” to the facts of the case, the court determined that the petition should not be dismissed on the basis of substantial abuse of Chapter 7.¹²²

The “future income test” was the only criterion used by the court in *In re Cord*.¹²³ The court found that the debtor had sufficient income to pay a substantial portion of her unsecured debt,¹²⁴ and stated, “[u]nder such circumstances, it makes little sense for the protection of the bankruptcy laws to be extended to the debtor.”¹²⁵ Interestingly, the court gave the debtor ten days to convert the case to Chapter 13 before entering the order for dismissal as “substantial abuse” of Chapter 7.¹²⁶

In *In re Hudson*,¹²⁷ the measure of “substantial abuse” was the debtor’s ability to complete a Chapter 13 plan. The court noted that Congress did not set forth a standard by which the term “substantial abuse” was to be measured, and reasoned:

It is well established that the provisions of Chapter 7 were intended to afford relief to a debtor when he finds himself in financial circumstances which threaten his immediate well-being. If a debtor has the ability to repay all or a substantial portion of his debts within a reasonable time, while at the same time maintaining a reasonable standard of living, then he cannot be so financially destitute that his immediate welfare is in question. In the absence of such jeopardy, it is morally and legally unconscionable that a person should be able to extinguish his obligations without first making a reasonable effort to fulfill them.¹²⁸

The court stated, “substantial abuse, for purposes of 11 U.S.C. section 707(b), occurs when a debtor, who has filed under Chapter 7, has the ability to repay all or a substantial portion of his debts under the auspices

¹²¹ *Id.* at 937. In the text of the opinion, the court justified the use of a “high screening standard.” *Id.* at 938. Nonetheless, in a footnote, the court indicated that it would not be bound by the 100% figure that “[n]inety-nine percent would do as well, and in some cases even considerably lower figures might suffice.” *Id.* at 938 n.6. Moreover, the court added that the “debates respecting the minimum Chapter 13 payments are a mirror to the Code § 707(b) considerations.” *Id.*

¹²² *Id.* at 939. The court stated that it was “satisfied that the debtor’s have little prospect of being able to propose or complete a meaningful Chapter 13 plan.” *Id.* Thus, while the ability to pay out of projected income is a threshold question to Chapter 7 relief, the percentage or amount of debt required to be paid is not clear. *See supra* note 20.

¹²³ 68 Bankr. 5 (Bankr. W.D. Mo. 1986).

¹²⁴ *Id.* at 7. The court found that all of the unsecured creditors could “easily be paid well within the 60 months allottable to a Chapter 13 plan.” *Id.* at 6.

¹²⁵ *Id.* at 7.

¹²⁶ *Id.*

¹²⁷ 56 Bankr. 415 (Bankr. N.D. Ohio 1985).

¹²⁸ *Id.* at 419 (citation omitted).

of Title 11 Chapter 13"¹²⁹ and "the debtor's ability to support a Chapter 13 plan is to be the measure of substantial abuse."¹³⁰

The court tempered this strong language, however, by noting other factors that could be considered in examining the question of substantial abuse. These factors included: (1) the motivation for filing under Chapter 7; (2) whether the debtor fully and accurately disclosed his or her financial condition; and (3) whether the debtor exhibited good faith.¹³¹

The court did not explain the effect of these factors on the case, nor under what circumstances they would be examined. It appears that the court simply did not want to foreclose the possibility of considering factors other than the debtor's ability to pay. However, it seems clear that the only criterion the court planned to use in reviewing the Hudsons' petition for substantial abuse was their ability to pay their debts.

The court was unable to rule on whether the granting of relief in this case would result in substantial abuse of Chapter 7, as the financial information before the court contained discrepancies and inconsistencies. Therefore, the court ordered the debtor to file an Amended Schedule of Current Income and Current Expenses, together with any explanations, before determining if a dismissal under section 707(b) was appropriate.¹³²

In *In re Bell*,¹³³ the court stated:

The primary, if not exclusive, factor to be considered in determining whether a debtor's petition constitutes a substantial abuse of the Bankruptcy Code under Section 707(b) is whether the debtor will have sufficient income to repay a meaningful part of his or her debts, within the context of either Chapter 11 or Chapter 13.¹³⁴

Moreover, the court declared that it would not even consider the "debtor's pre-petition conduct or circumstances, nor his fraud or bad faith

¹²⁹ *Id.* (citation omitted).

¹³⁰ *Id.* at 420. To determine if a successful Chapter 13 plan is a realistic possibility, the court stated that the decision was to be made after considering the following factors:

1. The total amount of the debtor's income.
2. The ratio between reasonable monthly income and expenses.
3. The percentage of income that could be paid to unsecured creditors.
4. The hardship that would be imposed under a Chapter 13 plan.
5. The number of unsecured creditors.
6. The total amount of unsecured debt.
7. The nature of the unsecured debt.

Id. at 419-20.

¹³¹ *Id.* at 420.

¹³² 56 Bankr. 415, 421.

¹³³ 56 Bankr. 637 (Bankr. E.D. Mich 1986)

¹³⁴ *Id.* at 641.

in filing the petition itself,"¹³⁵ as other bankruptcy provisions remedy this type of abuse.¹³⁶

In fact, the only factor the court considered was the debtor's ability to pay. The court concluded that the petitioner in *Bell* could repay a "meaningful part of his debt"¹³⁷ (\$64,573 or 51% of his unsecured debt over three years).¹³⁸ In reaching this conclusion, some expenses were considered unreasonable and thus eliminated or reduced. For example, the court reduced the \$480 per month expense for food, of which \$430 was for dining in restaurants, to \$300.¹³⁹ The \$608 per month for automobile transportation expense on an Audi was decreased to \$300 per month.¹⁴⁰ The court remarked that it could simply not justify the expense for a luxury automobile.¹⁴¹ The \$820 per month being paid to an annuity was deleted.¹⁴² In dismissing the Chapter 7 petition, the court stated "it is unfair and inequitable for the debtor to request that this court discharge his debts while he accumulates substantial disposable income over the next several years while living a relatively high lifestyle."¹⁴³

¹³⁵ *Id.*

¹³⁶ *Id.*

¹³⁷ *Id.* at 643.

¹³⁸ In reaching this conclusion, the court utilized the Bankruptcy Code's criteria for Chapter 13 plans. U.S.C. § 1325(b) provides:

(b)(1) If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the court may not approve the plan unless, as of the effective date of the plan

(A) the value of the property to be distributed under the plan on account of such claim is not less than the amount of such claim; or

(B) the plan provides that all of the debtor's projected disposable income to be received in the three-year period beginning on the date that the first payment is due under the plan will be applied to make payments under the plan.

(2) For purposes of this subsection, "disposable income" means income which is received by the debtor and which is not reasonably necessary to be expended

(A) for the maintenance or support of the debtor or a dependent of the debtor; or

(B) if the debtor is engaged in business for the payment of expenditures necessary for the continuation, preservation, and operation of such business.

Interestingly, these criteria were applied even though the debtor was ineligible for Chapter 13 relief because of the amount of his unsecured debt. The court opined that a Chapter 11 plan similar to the Chapter 13 plan could be confirmed. 56 Bankr. 637, 641. *Contra In re Mastroeni*, 56 Bankr. 456 (Bankr. S.D.N.Y. 1985).

¹³⁹ 56 Bankr. at 642.

¹⁴⁰ *Id.*

¹⁴¹ *Id.*

¹⁴² *Id.*

¹⁴³ *Id.* at 643.

C. *Substantial Abuse: Future Income Test One Factor*

One of the earliest cases to confront the issue of what constitutes substantial abuse was the previously-discussed case of *In re Bryant*.¹⁴⁴ The court determined that it should use the traditional "ordinary and plain meaning"¹⁴⁵ test to interpret the statutory language, and that test would not allow the debtor to "lead the life of Riley at his creditor's expense."¹⁴⁶

The court noted that the intent of the Bankruptcy Code was to provide a "fresh start" for financially troubled persons, not "a means for the unscrupulous to avoid their creditors."¹⁴⁷ In effect, the court applied a "good faith" test to the specific facts and determined that the individual debtor should be denied Chapter 7 relief under section 707(b). In its analysis of substantial abuse, the court looked at three factors:

1. Did the debtor fully and accurately disclose all of the relevant financial information? If not, this fact would help support a finding that "substantial abuse" was present.¹⁴⁸
2. Was the financial trouble caused by unemployment, sickness, or other calamity? If so, these facts would tend to establish that "substantial abuse" was not present.¹⁴⁹
3. Does a review of the potential income and expenses demonstrate the likelihood that most of the creditors could be paid off in the future? If so, this factor would indicate "substantial abuse" may be present.¹⁵⁰

In applying the first factor to the facts of this case, the court found that the debtor had an "utter disregard of his duties . . . to truthfully list all of his obligations, his monthly expenses, and to disclose his general financial position. . . ."¹⁵¹ In fact, the court characterized the debtor's conduct concerning the financial statements as "fraud upon the court,"¹⁵² "misrepresentative"¹⁵³ and in "bad faith."¹⁵⁴ Additionally, the debtors

¹⁴⁴ 47 Bankr. 21 (Bankr. W.D.N.C. 1984).

¹⁴⁵ *Id.* at 24.

¹⁴⁶ *Id.* at 26.

¹⁴⁷ *Id.* at 24.

¹⁴⁸ *Id.* at 25.

¹⁴⁹ 47 Bankr. 21, 24 (Bankr. W.D.N.C. 1984).

¹⁵⁰ *Id.* at 24-25.

¹⁵¹ *Id.* at 25.

¹⁵² *Id.* The debtor intentionally omitted a number of debts from his petition. *Id.* Further, when questioned about unlisted credit card balances, the debtor indicated that the amounts were insignificant yet he allocated \$400.00 a month for these obligations in the expense schedule. *Id.*

¹⁵³ *Id.*

¹⁵⁴ 47 Bankr. 21, 25 (Bankr. W.D.N.C. 1984). For example, the debtor claimed more than \$200.00 a month for medical expenses although the family basically had no recurrent

sought bankruptcy relief not because of some calamity, but because he “simply decided to shuck a couple of his debts.”¹⁵⁵ Finally, although the debtor’s future ability to pay was not part of the discussion, the court was concerned with the “relatively exorbitant lifestyle”¹⁵⁶ the debtor sought to maintain and, in the statement of facts, remarked that with “only a modicum of restraint,”¹⁵⁷ the debtor could pay \$28,000 (67%) of his unsecured obligations over three years. Therefore, the court concluded that the case was one of substantial abuse of Chapter 7 and dismissed it pursuant to section 707(b).¹⁵⁸

*In Re Grant*¹⁵⁹ is a vivid example of the type of situation that prompted the enactment of section 707(b). The following facts were presented in the *Grant* case. The filing was a joint petition by petitioners with two minor children, ages fifteen and twelve. The husband was employed as Vice-President of Human Resources and Personnel at a hospital. His gross income was \$65,000, the family’s total income. At the section 707(b) hearings, the Grants testified that they had recently purchased a \$700 men’s suit from Saks Fifth Avenue and \$2,100 worth of women’s clothing from an exclusive dress shop. Moreover, a loan for \$9,000 was primarily for Christmas items. In their original Schedule of Current Income and Expenditures, the debtors included the cost of leasing a 1982 Mercedes 240D. This expense was eliminated in their amended schedule, but two lease payments for a 1985 Nissan and Cutlass Sierra were added. This netted a monthly savings of \$1.

In deciding whether the petition should be dismissed, the court considered four factors:

- (1) Whether the debtors have a likelihood of sufficient future income to fund a Chapter 13 plan which would pay a substantial portion of unsecured creditors.
- (2) Whether the debtors have exhibited bad faith in filing petitions and schedules.
- (3) Whether the debtors have engaged in eve of bankruptcy purchases.
- (4) Whether the debtors have suffered an unforeseen calamity.¹⁶⁰

According to this court, the “[k]ey to the analysis is whether the debtor

medical expenses and \$100.00 per month for laundry when the family owned a washing machine. *Id.*

¹⁵⁵ *Id.* at 24.

¹⁵⁶ *Id.* at 26. For instance, the debtor claimed \$65.00 a month for cable television and \$100.00 per month for dining out and movies. *Id.*

¹⁵⁷ *Id.* at 23.

¹⁵⁸ *Id.* at 26.

¹⁵⁹ 51 Bankr. 385 (Bankr. N.D. Ohio 1985).

¹⁶⁰ *Id.* at 393-94.

could realistically fund a Chapter 13 plan which would pay a significant portion of their claims.”¹⁶¹ In this case, the court found that with a “reasonable reduction in the style and cost of living,” the Grants could pay approximately 68% of their unsecured claims over five years.¹⁶²

In considering the other factors, the court determined that the Grants exhibited bad faith in both the filing of the Chapter 7 petition and in preparing the list of expenses on the Schedule of Current Income and Expenditures.¹⁶³ With regard to the filing, the court stated, “[a]t no time in their recent history have the debtors displayed a sincere resolve to tighten their belts, or to incur debts with a clear intent to pay their creditors their just due.”¹⁶⁴ The court also found “excesses in the majority of their cost-of-living expenses.”¹⁶⁵

In applying the third factor, the court noted that the debtors had incurred extravagant expenses for consumer items within 180 days of filing for relief and amassed \$28,000 of other consumer debts the past two years.¹⁶⁶ Lastly, the Grants had not suffered from any unforeseen calamity.¹⁶⁷ In denying bankruptcy relief under Chapter 7, the court stated, “a discharge . . . would give them [the Grants] a ‘headstart’ in the race for conspicuous consumption and its concomitant status at the expense of their deserving creditors.”¹⁶⁸

In both *Bryant* and *Grant*, the petitioners had the ability to pay their creditors out of future income, yet under the facts of those cases, it was not the only factor that led the courts to dismiss under section 707(b).¹⁶⁹

¹⁶¹ *Id.* at 394. The court reached the conclusion after reviewing the legislative history. Further, the court noted:

A recent GAO report suggests that forty percent of those who file for Chapter 7 relief have income, assets, and debts comparable to those seeking Chapter 13 relief. These improper Chapter 7 filings may cost the lending industry as much as \$1.25 billion annually in lost revenues. And as with anything else, these losses are passed along to consumers in the form of higher interest rates, credit fees, and increased prices for goods and services.

Id. at 391.

¹⁶² *Id.* at 394.

¹⁶³ *Id.* at 394-95.

¹⁶⁴ 51 Bankr. 385, 394 (Bankr. N.D. Ohio 1985).

¹⁶⁵ *Id.*

¹⁶⁶ *Id.* at 397. The amount of money spent on Christmas prompted the court to quip that the “Grants Christmases must be quite an extravaganza.” *Id.* at 396.

¹⁶⁷ *Id.* at 397.

¹⁶⁸ *Id.*

¹⁶⁹ *See also In re Kress*, 57 Bankr. 874, 878 (Bankr. D.N.D. 1985). This court listed five criteria:

1. Whether the debtors have a likelihood of sufficient future income to fund a Chapter 13 plan which would pay a substantial portion of the unsecured claims;
2. Whether the debtors petition was filed as a consequence of illness, disability, unemployment, or some other calamity;

How important the other factors were in the finding of “substantial abuse” is unclear. The court in *In re Deaton*¹⁷⁰ determined that the other factors are critical. The debtors in *Deaton* could “comfortably support” a Chapter 13 plan.¹⁷¹ Nevertheless, the court refused to consider dismissing the petitions holding that the “mere ability to fund a Chapter 13 plan is not sufficient to constitute substantial abuse.”¹⁷²

In accord is *In re Shands*.¹⁷³ In *Shands*, the court stated that an ability to pay 100% within three years, when coupled with some egregious circumstance, warrants dismissal for substantial abuse of Chapter 7.¹⁷⁴ The court dismissed the case finding that the debtor could pay all of her debts within thirty-three months and that the debtor filed for bankruptcy to spite her former husband.¹⁷⁵

In *In re Walton*,¹⁷⁶ the court disagreed with this analysis. The court embraced the concept that the debtor’s ability to pay a substantial portion of his debts in the future is the most important factor in determining if a section 707(b) dismissal was appropriate, but indicated that it was not the only relevant factor.¹⁷⁷ However, under the analysis employed in *Walton*, a petition will be dismissed as “substantial abuse” of Chapter 7 upon the finding that a Chapter 13 plan is feasible unless other factors, such as the presence of illness, disability, unemployment or other calamity, full disclosure, good faith, or non-extravagant lifestyles strongly militate against dismissal.¹⁷⁸

It is difficult to argue with the application of a “future income test” in the dismissal of Chapter 7 petitions pursuant to section 707(b) given facts such as those presented in *Bell* and *Grant*. To allow such individuals to eliminate their debts would be inequitable to their creditors. However, the application of a “future income test” leaves a great deal of discretion to the individual bankruptcy judges to determine which expenditures are appropriate and which are not.

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3. Whether the schedules suggest the debtors incurred cash advancements and consumer purchases in excess of their ability to repay them;
 4. Whether the debtors proposed family budget is excessive or extravagant;
 5. Whether the debtors Statement of Income and Expenses is misrepresentative of their true financial condition.

¹⁷⁰ 65 Bankr. 663 (Bankr. S.D. Ohio 1986).

¹⁷¹ *Id.* at 664.

¹⁷² *Id.* at 665.

¹⁷³ 63 Bankr. 121 (Bankr. E.D. Mich. 1985).

¹⁷⁴ *Id.* at 124.

¹⁷⁵ *Id.* The only debts that would not have been repaid were a small claim owed to Consumers Power Company and a substantial claim to her former husband. Moreover, the debtor testified that her “main purpose” in seeking bankruptcy relief was to discharge the debt owed to her ex-husband. *Id.* at 123-24.

¹⁷⁶ 69 Bankr. 150 (Bankr. E.D. Mo. 1986).

¹⁷⁷ *Id.* at 154.

¹⁷⁸ *Id.*

Obviously, such discretion can lead to very disparate results. A clear example of the inequity that may arise from broad discretion is *In re Gaukler*.¹⁷⁹ In applying a "future income test," the court determined that a \$700 per month contribution to the debtor's church was reasonable and, therefore, that amount was not to be considered as "future income" available to pay creditors pursuant to a Chapter 13 plan.¹⁸⁰ Clearly, other courts could hold that such an expenditure was inappropriate and that the money should be available to creditors.

D. Substantial Abuse: No Future Income Test

The application of a "future income" test in determining dismissal under section 707(b) was questioned by the Ninth Circuit Bankruptcy Appeals Panel in *In re Kelly*.¹⁸¹ The court did not make a specific determination as to the propriety of using a "future income test" as a standard for section 707(b) dismissals since it reversed the bankruptcy court on other grounds. However, dicta indicated that the Appeals Panel may not agree with the trend established by the bankruptcy courts relating to the applicability of the "future income test."¹⁸²

The Appeals Panel noted that the bankruptcy judge, relying in part upon remarks by Congressman Andersen in the Congressional Record, placed considerable weight upon the debtor's perceived ability to pay under a Chapter 13 plan.¹⁸³ The Appeals Panel cautioned that the statements in the Congressional Record are sometimes inconsistent and not a reliable source for interpreting a statute.¹⁸⁴ Then the Appeals Panel referred to Senator Metzenbaum's statement that "both the House and Senate has [sic] agreed to the total elimination of the future income language" and Chairman Rodino's remark that the 1984 Amendments "contain no threshold or future income test" in the Congressional Record.¹⁸⁵

The Appeals Panel remanded with instructions that, "[u]pon remand the bankruptcy judge should reconsider the application of a future income test in determining substantial abuse under § 707."¹⁸⁶ Although not clearly stated, one could well interpret this language to mean that the

¹⁷⁹ 63 Bankr. 224 (Bankr. D. N.D. 1986).

¹⁸⁰ *Id.* at 225. It should be noted that the debtors were members of the Worldwide Church of God which requires its members to donate ten percent of their income to the church. *Id.* at 226.

¹⁸¹ 70 Bankr. 109 (Bankr. 9th Cir. 1986).

¹⁸² *Id.* at 113.

¹⁸³ *Id.* at 112.

¹⁸⁴ *Id.*

¹⁸⁵ *Id.* at 113.

¹⁸⁶ 70 Bankr. 109, 113 (Bankr. 9th Cir. 1986).

Ninth Circuit Appeals Panel has rejected the use of a "future income test" in applying section 707(b).

An interesting example of a case that utilized a section 707(b) dismissal without considering future income was *In re Bruno*.¹⁸⁷ In *Bruno*, the debtor was convicted of murdering his wife and filed a Chapter 7 petition for the discharge of her funeral bills. The court stated that the purpose of section 707(b) was "to prevent the use of the Bankruptcy Code to promote injustice in any form"¹⁸⁸ and concluded that "[b]ankruptcy has too grand and lofty a purpose to allow debtors to gain freedom from indebtedness . . . incurred as a result of their crimes."¹⁸⁹

Other situations where substantial abuse may be found without considering future income could include: (1) willful nonpayment of debts with the ability to pay these debts and (2) the careless incurrence of debts knowing bankruptcy would provide an easy way out.¹⁹⁰

E. Solution

It is clear that the term "substantial abuse" in section 707(b) has created a great deal of confusion and inconsistent bankruptcy court results. This confusion stems primarily from the lack of clear legislative intent. It is unlikely that the courts will soon be able to arrive at a consistent and equitable resolution of whether or not section 707(b) has mandated a "future income test."

Two expeditious solutions are possible:

- (1) Congress could enact a revised version of section 707(b) that defines the term "substantial abuse," thereby clearly establishing whether or not section 707(b) creates a mandatory "future income test."
- (2) The United States Supreme Court could promulgate a rule defining the phrase "substantial abuse."¹⁹¹ The Court's interpretation would then be consistently applied by the lower courts.

Unfortunately, neither of these solutions seems probable. Congressional action is unlikely in light of the amount of compromise which was required to secure the passage of the 1984 Amendments, including

¹⁸⁷ 68 Bankr. 101 (Bankr. W.D. Mo. 1986).

¹⁸⁸ *Id.* at 103.

¹⁸⁹ *Id.*

¹⁹⁰ Breitowitz, *supra* note 3.

¹⁹¹ Pub. L. No. 98-353, § 320, 98 Stat. 357, (1984) set out as a note under section 2075 of Title 28, Judiciary and Judicial Procedure, "The Supreme Court shall prescribe general rules implementing the practice and procedure to be followed under section 707(b) of Title 11. . . ."

section 707(b). Moreover, the Supreme Court to date has demonstrated no inclination to promulgate a rule defining "substantial abuse."¹⁹²

As neither of these solutions is expected, the authors urge the bankruptcy courts to follow the analysis used by the *Deaton* and *Shands* courts. Under this analysis, for a finding of substantial abuse, the ability to pay must be combined with other factors which indicate that Chapter 7 relief should be unavailable.

The authors' rationale for rejecting the position of a "future income test" as the exclusive measure of substantial abuse is that such a definition changes the basic structure of our bankruptcy system from asset-based to income-based. Such a dramatic change should only be a result of clear legislative action.

Nevertheless, a "future income test" is an important part of finding substantial abuse. The use of ability to pay as a factor is consistent with the concern which prompted enactment of section 707(b) and with the requirement that the debtor submit a schedule of current income and expenses.¹⁹³ Moreover, coupling a "future income test" with other factors gives meaning to the term "substantial" in the phrase "substantial abuse."

V. EFFECT OF THE PRESUMPTION TOWARD RELIEF

As previously discussed, section 707(b) provides a presumption in favor of the relief requested by the debtor. Since the United States Supreme Court has not promulgated rules pursuant to section 707(b), the courts have been forced to decide what protection this presumption affords a debtor.

Perhaps the best analysis was provided in *In re Grant*.¹⁹⁴ The court summarized the problem by saying, "[a] troublesome [issue] presented by this new section is how the court is to treat the presumption in favor of granting the relief requested by the debtor."¹⁹⁵

¹⁹² In fact, the Court has thus far failed to act upon an amendment to Bankruptcy Rule 1017 proposed by the Committee of the Judicial Conference which merely provides procedural guidelines for section 707(b) dismissals. Proposed Bankruptcy Rule section 1017(e) provides:

(e) DISMISSAL OF INDIVIDUAL DEBTOR'S CHAPTER 7 CASE FOR SUBSTANTIAL ABUSE. An individual debtor's case under Chapter 7 may be dismissed for substantial abuse only after a hearing on notice to the debtor and the trustee and such other parties in interest as the court directs. The notice shall advise the debtor of all matters which the court will consider at the hearing.

Proposed Court Rules, 107 F.R.D. 403 (1985).

¹⁹³ 11 U.S.C.A. § 521 (1) (West Supp. 1986).

¹⁹⁴ 51 Bankr. 385 (Bankr. N.D. Ohio 1985).

¹⁹⁵ *Id.* at 394.

The court applied Federal Rule of Evidence 301¹⁹⁶ and, in doing so, decided that its application to section 707(b) is that: If the court found substantial abuse, bad faith, substantial future income, eve of bankruptcy purchases, or other similar factors, the presumption was rebutted.¹⁹⁷

One of the few other cases to address the issue of the presumption was *In re Kress*.¹⁹⁸ In *Kress*, the court simplistically, and perhaps accurately, determined that the presumption, “merely requires the Court to view the facts of a given case in light of a presumption in favor of the debtor, a presumption that he is entitled to Chapter 7 relief. It is not a conclusive presumption, however, but may be rebutted by the facts themselves.”¹⁹⁹

If these decisions are correct, as they appear to be, there is really very little practical value to the presumption because if there is evidence of “substantial abuse,” it will almost always be sufficient to rebut the presumption in favor of relief.

However, no discussion of section 707(b) and the effects of the presumption would be complete without citing Bankruptcy Judge A. Jay Cristol in *In re Robin E. Love*.²⁰⁰ In that decision, Judge Cristol included the following poem:

Once upon a midnight dreary, while I pondered
 weak and weary
 Over many quaint and curious files of chapter
 seven lore
 While I nodded nearly napping, suddenly there
 came a tapping
 As of someone gently rapping, rapping at my
 chamber door,
 “Tis some debtor” I muttered, “tapping at my
 chamber door
 Only this and nothing more.”
 Ah distinctly I recall, it was in the early fall
 And the file still was small
 The Code provided I could use it
 If someone tried to substantially abuse it
 No party asked that it be heard.

¹⁹⁶ FED. R. EVID. 301 provides:

[A] presumption imposes on the party against whom it is directed the burden of going forward with evidence to rebut or meet the presumption, but does not shift to such party the burden of proof in the sense of the risk of nonpersuasion, which remains throughout the trial upon the party is whom it was originally cast.

¹⁹⁷ 51 Bankr. 385 (Bankr. N.D. Ohio 1985).

¹⁹⁸ 57 Bankr. 874 (Bankr. D.N.D. 1985).

¹⁹⁹ *Id.* at 877.

²⁰⁰ 61 Bankr. 558 (Bankr. S.D. Fla 1986).

"*Sua sponte*" whispered a small black bird.
The bird himself, my only maven, strongly looked
to be a raven.
Upon the words the bird had uttered
I gazed at all the files cluttered
"*Sua sponte*," I recall, had no meaning; none at
all.
And the cluttered files sprawl, drove a thought
into my brain.
Eagerly I wished the morrow—vainly I had sought
to borrow
From BAFJA, *surcease* of sorrow—and an order
quick and plain
That this case would not remain as a source of
further pain.
The procedure, it seemed plain.
As the case grew older, I perceived I must be
bolder.
And must *sua sponte* act, to determine every
fact,
If primarily consumer debts, are faced,
Perhaps this case is wrongly placed.
This is a thought that I must face, perhaps I
should dismiss this case.
I moved *sua sponte* to dismiss it for I knew I
would not miss it.
The Code said I could, I knew it.
But not exactly how to do it, or perhaps some day
I'd rue it.
I leaped up and struck my gavel.
For the mystery to unravel
Could I? Should I? *Sua sponte*, grant my motion
to dismiss?
While it seemed the thing to do, suddenly I
thought of this.
Looking, looking towards the future and to what
there was to see
If my motion, it was granted and an appeal came
to be,
Who would be the appellee?
Surely, it would not be me.
Who would file, but pray tell me, a learned brief
for the appellee
The District Judge would not do so
At least this much I do know.
Tell me raven, how to go.

As I with the ruling wrestled
 In the statute I saw nestled
 A presumption with a flavor clearly in the
 debtor's favor.
 No evidence had I taken
Sua sponte appeared foresaken.
 Now my motion caused me terror
 A dismissal would be error.
 Upon consideration of section 707(b), in anguish,
 loud I cried
 The court's *sua sponte* motion to dismiss under
 section 707(b) is denied.²⁰¹

VI. CONCLUSION

The enactment of section 707(b) lead to a great deal of confusion and inconsistent application of its provisions primarily because evidence of legislative intent has been so limited. It is unlikely that the problem areas will be resolved consistently by the courts in the near future.

The promulgation of rules by the United States Supreme Court may clear up some of the troublesome issues, but that alone is unlikely to resolve all of the problem areas.

It may well be that a revised enactment of section 707(b) that addresses the major issues raised to date is needed, now that Congress can be advised of the ambiguity and uncertainty that has resulted from the statutory language and minimal documentation of legislative intent. However, with the difficulty encountered in the original enactment of the statute, an amended version of section 707(b) is highly unlikely. Therefore, the authors suggest the following approaches to the four primary problem areas.

(1) A bankruptcy court should not hold a section 707(b) dismissal hearing pursuant to a suggestion of, or at the request of, a party in interest. However, the fact that the issue was raised in this context should not foreclose the court from making its own independent determination of the presence or absence of substantial abuse.

(2) To determine if the petitioner's debts are primarily consumer debts, the court should utilize the broad test of whether debts were incurred in the normal course of daily affairs. If the total aggregate dollar amount of such debt exceeds the total aggregate

²⁰¹ *Id.* at 558-59.

dollar amount of the other debts, then the requirement of primarily consumer debts is satisfied.

(3) To determine whether substantial abuse is present or lacking, the courts should utilize a test that includes potential future income as one factor, but the ability to pay must be combined with other factors that indicate Chapter 7 relief should be unavailable to the petitioner.

(4) The presumption of dischargeability should be constructed to require the court to view a case in favor of granting the debtor bankruptcy relief.

