

WE'VE GOT CALIFORNIA COVERED

Official online publisher of California case law & much more

lexis.com®

Law.com Home Newswire LawJobs CLE Center LawCatalog Our Sites Advertise

Sign Out

THE RECORDER

ESSENTIAL CALIFORNIA LEGAL CONTENT An ALM Web site

This Site | Law.com Network | Legal Web

HOME NEWS CASES & COURTS IN PRACTICE SPECIAL REPORTS EVENTS LAWJOBS ABOUT US

Home > 'Hamilton' Redefines Consumer Bankruptcy Practice

Font Size: + -

'Hamilton' Redefines Consumer Bankruptcy Practice

Reno Fernandez
The Recorder | July 01, 2010

Print Share Email Reprints & Permissions Write to the Editor



Reno Fernandez, Macdonald & Associates
Image: courtesy photo

The United States Supreme Court has come to the rescue of some chapter 13 bankruptcy debtors at the risk of delivering others into the hands of creditors.

In *Hamilton v. Lanning*, 10 C.D.O.S. 6973, the justices ruled, 8-1, that the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 does not prohibit a bankruptcy court from taking into account a debtor's likely future income in determining the minimum payments to be made under a chapter 13 plan. In upholding the Tenth Circuit U.S. Court of Appeals' "forward looking" approach, the court overruled the Ninth Circuit's "mechanical" approach established by *In re Kagenveama*, 541 F.3d 868 (2008), which held that a debtor's income for purposes of calculating minimum Chapter 13 plan

payments is deemed to be the average income received in the six months before filing the bankruptcy petition, without regard to later increases or decreases in income.

The Supreme Court's ruling cuts both ways in that bankruptcy courts now possess the discretion to take into account a debtor's post-petition income and adjust the payments that must be made to unsecured creditors.

THE MEANS TEST

In 2005, Congress radically changed consumer bankruptcy practice by enacting the BAPCPA. Among other changes, BAPCPA limits a person's ability to file for a Chapter 7 liquidation. Specifically, to qualify for Chapter 7, a debtor's gross income averaged over the six months prior to filing (the debtor's "current monthly income") must be less than the median set for the state in which the debtor resides. If greater, a debtor may still qualify if her "disposable monthly income" is less than a certain threshold. Disposable monthly income is determined by deducting from current monthly income certain statutory and actual expenses, which together are different from and may in fact be higher than the debtor's actual living expenses. This is the so-called "Means Test."

DISPOSABLE MONTHLY INCOME

BAPCPA significantly altered Chapter 13 practice in that it imposed minimum payments that must be made to unsecured creditors under a Chapter 13 plan if the trustee or a creditor objects to the plan (in fact, a trustee will always object if the debtor proposes a plan that does not provide for the minimum payments). The plan must provide for full repayment of unsecured claims or payments equal to the debtor's "projected disposable income." While BAPCPA provides a detailed definition of disposable monthly income, it does not define the term "projected disposable income."

'HAMILTON V. LANNING'

Stephanie Lanning commenced a Chapter 13 bankruptcy case shortly after receiving a one-time "buyout" from a previous employer. Because the buyout was unlikely to recur, the bankruptcy court disregarded this income in calculating the minimum payments Lanning must have proposed in order to confirm a Chapter 13 plan. The trustee objected to confirmation the plan and ultimately appealed the bankruptcy court's ruling to the Tenth Circuit, which affirmed the bankruptcy court. The trustee advocated a so-called "mechanical" approach, arguing that the BAPCPA's detailed definition of "disposable monthly income," which is calculated on the basis of current monthly income (the six-month average, pre-bankruptcy income), eliminated a bankruptcy court's discretion to take into account post-petition adjustments in the debtor's income in determining projected disposable income. The Supreme Court disagreed and upheld

Advertisement

Industry Experts in Legal & Corporate Staffing

Profile: Founded in 1969 Pathways Personnel uses its strong regional network of legal professionals that has been built from our stable and continuous presence in the bay area legal industry for the last 40 years. All Pathways recruiters are legal industry veterans. Our experience lets us better understand the challenges that our clients and candidates face working in and running a law firm. Equipped with state of the art technology and a Fiber Ethernet internet/data connection Pathways has the capacity to house up to 70 attorneys in our Project facilities.

Advertisement

WHY THESE SAN FRANCISCO ATTORNEYS HAVE ALL CHOSEN THE SAME NEW ADDRESS

www.duanemorris.com

CLICK TO FIND OUT.

TOP JOBS

Banking & Finance Associate
Jones Day
San Francisco, California

ANTITRUST LITIGATION MID-LEVEL ASSOCIATE
Morgan, Lewis & Bockius LLP
San Francisco, California

MORE JOBS >>
POST A JOB >>

the Tenth Circuit's "forward looking" approach, ruling that Congress' failure to define "projected disposable income" left unchanged the pre-BAPCPA practice of taking into account post-petition changes in the debtor's income.

The high court interpreted the term "projected" to mean more than a simple calculation that assumes past events will repeat themselves, but rather, something akin to projections of sales, cash flow, election results or sports victories, which take into account likely future circumstances, not just past data. If Congress intended a simple multiplication, the court noted, it could have used the term "multiplied" as it has elsewhere in the Bankruptcy Code. The court found further support in the fact that the Bankruptcy Code refers to projected disposable income as income "to be received in the applicable commitment period." The mechanical approach would require a debtor with reduced income to do the impossible and pay amounts not actually received, while at the same time, allow a debtor with increased income to avoid paying the excess to creditors. The court found that this is contrary to Congress' apparent intent in enacting BAPCPA — to channel debtors who are able to pay a portion of their unsecured debtors into chapter 13.

The trustee had also argued that a debtor may mitigate any harsh results by delaying filing bankruptcy, moving for an alternative look-back period, voluntarily dismissing the Chapter 13 case and re-filing at a later date, filing under Chapter 7, or moving to convert the case to chapter 7. The court found that these strategies provide cold comfort in that (1) delaying bankruptcy is not a viable option for a debtor facing a foreclosure sale, an automobile repossession or wage garnishment; (2) if the mechanical approach is in fact mandated by the Bankruptcy Code, then convoluted attempts to alter the look-back period would undermine the statute; (3) serial filings risk raising the appearance of bad faith and may result in involuntary dismissal; and (4) Congress did not intend for Chapter 7 to serve as a safety valve for the mechanical approach.

OVERRULING THE NINTH CIRCUIT

Hamilton v. Lanning overrules the Ninth Circuit's mechanical approach established in *Kagenveama*, and the consequences cut both ways. Whereas under *Kagenveama*, a Chapter 13 debtor was generally entitled to retain any increased earnings, the trustee is now entitled to object to a proposed Chapter 13 plan that does not adequately account for likely increases in future income. The justices instruct bankruptcy courts to begin by calculating disposable monthly income, and caution that "it is only in unusual circumstances that a court may go further and take into account other known or virtually certain information about the debtor's future income or expenses." However, it is not clear when a change in a debtor's income will not constitute unusual circumstances. In fact, Justice Antonin Scalia filed a dissenting opinion highlighting the fact that the text of the Bankruptcy Code does not provide a procedure to account for unusual circumstances or changed income. Trustees and debtors alike will undoubtedly take advantage of the Supreme Court's flexible forward-looking approach to determining minimum Chapter 13 plan payments.

Reno F.R. Fernandez III is an associate attorney with Macdonald & Associates, with offices in San Francisco and Modesto.

In Practice articles inform readers on developments in substantive law, practice issues or law firm management. Contact Vitaly Gashpar with submissions or questions at vgashpar@alm.com.

Subscribe to The Recorder

[Print](#) [Share](#) [Email](#) [Reprints & Permissions](#) [Write to the Editor](#)

[About ALM](#) | [About Law.com](#) | [Customer Support](#) | [Reprints](#)
Copyright 2010. ALM Media Properties, LLC. All rights reserved.

**ALM**
An Integrated Media Company

