

BANKRUPTCY BY THE NUMBERS
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Measuring Means-testing: It's All in the Words

The major bankruptcy reform bills, (H.R. 3150 and S. 1301) seek to shift petitioners with relatively high incomes into repayment plans in chapter 13 or dismiss them entirely from bankruptcy. Both bills measure projected debtor income against national median income as a threshold for finding eligibility for chapter 7. But subtle differences in wording between the two bills can have significant consequences regarding the number of debtors who would be excluded from chapter 7. The important terms that distinguish the bills are "**family**," "**household**," and "**earner**."

The House bill is based on "national median **family** income" (emphasis added) and specifically refers to the definition used by the Bureau of the Census. By contrast, the income threshold in the Senate bill is based on "national median **household** income" (emphasis added), and does not provide a definition of this term. We estimate that under the income thresholds created by the Senate bill approximately 118,000 more debtors per year would be liable for conversion or dismissal than under the income thresholds created by the House bill. The reason for the difference is the large number of single filers, living alone, whose incomes fall between the Senate and House income thresholds.

The Language of H.R. 3150

As passed by the House on June 10, 1998, H.R. 3150 creates new Bankruptcy Code Section 109(h), which establishes a three-prong means test for determining a consumer debtor's eligibility for chapter 7. The first prong of the test is the calculation of the difference between the debtor's "current monthly total income"--which the bill defines in an amendment to Section 101--and national median income.

A debtor is considered to have income available to pay creditors "if the individual, or, in a joint case, the individual and the individual's spouse combined...have--

(A) current total income of not less than the highest

^{1/} All views expressed in this article are those of the authors, and do not necessarily represent the views of the Executive Office for United States Trustees or the Department of Justice.

national median **family** income reported for a family of equal or lesser size, or, in the case of a **household** of 1 person, of not less than the national median household income for 1 **earner**...."[emphasis added].^{2/}

This language is clarified in a new subsection of Section 101, which reads as follows:

"(40A) 'national median family income' and 'national median household income for 1 earner' shall mean during any calendar year, the national median family income and the national median household income for 1 earner which the Bureau of the Census has reported as of January 1 of such calendar year for the most recent previous calendar year;"

This language directs us to income Tables 4 and 1 published annually by the Bureau of the Census. Table 4 includes a breakdown of median incomes by "size of family," ranging from two persons to seven persons or more. Family median income grows between size two and size four, and then falls off.

H.R. 3150 permits debtors in families sized five or more to use the median income of family size four. In 1996, for example, debtors claiming families of size four or greater would subtract \$4,293 from their current monthly total incomes to determine if they have income available to pay creditors under the first prong of the means test.

The fact that Table 4 establishes the minimum size of a "**family**" as two persons gives rise to H.R. 3150's instruction to consider "national median **household** income for 1 **earner**" for a debtor who claims no family. This instruction points to Census Table 1, "Median Incomes of Households by Selected Characteristics....,"^{3/} which includes a value for households of size one.

Table 1 also presents median incomes for different numbers of **earners** within a household, and it is to this list that the House language apparently directs us. This is an important distinction. The 1996 national median monthly income for a one-person **household** was

^{2/} This language is repeated without change in amendments to Section 1325(a), where the income test is applied to determine whether a debtor's chapter 13 plan shall be not less than five years (for debtors who exceed the threshold) or not less than three years (for debtors who do not).

^{3/} Appendix A to the income tables states: "Households consist of all persons who occupy a housing unit.... A household includes the related family members and all the unrelated persons, if any, such as lodgers, foster children, wards, or employees who share the housing unit. A person living alone in a housing unit or a group of unrelated persons sharing a housing unit as partners is also counted as a household."

\$1,491, but the national median monthly income for one **earner** in a household was \$2,325.^{4/}

Putting these references together, and still using 1996 data for purposes of example, the House bill establishes the following values for national median monthly incomes: Household of Size One, \$2,325; Household of Size Two, \$3,006; Household of Size Three, \$3,676; and Household of Size Four or greater, \$4,293. A debtor whose current monthly total income falls below these thresholds would not, by virtue of gross income, be liable for dismissal or involuntary placement into chapter 13.

Finally, note that Section 109(h) does not require spousal income to be included in the current monthly total income of a debtor who does not file jointly.

The Language of S. 1301

The Senate bill places its income thresholds in Bankruptcy Code Section 707. Significantly, S. 1301 permits creditors to request or suggest dismissal or, with the debtor's consent, conversion into chapter 13. A new provision, Section 707(b)(5), limits creditors as follows:

"(5) However, a party in interest may not bring a motion under this section if the debtor and the debtor's spouse combined, as of the date of order for relief, have current monthly total income equal to or less than the national median household monthly income calculated on a monthly basis for a household of equal size. However, for a household of more than four individuals, the median income shall be that of a household of 4 individuals, plus \$583 for each additional member of that household."

"**Household**" is not defined in the Bankruptcy Code, and S. 1301 does not provide a definition. It is unlikely that the Senate intends to bind bankruptcy courts to the expansive definition used by the Bureau of the Census (see Footnote 3)--for example, to permit a chapter 7 debtor to shelter income by increasing household size with boarders or the debtor's employees. The bill's language apparently directs us to household incomes as reported in Table 1, but only for household sizes up to four.

As noted above, the national median income for all households of size one is markedly smaller than for households with one earner. The result is that the income threshold for single filers living alone is

^{4/} The legislation could as well have directed us to the part of Table 4 that lists earners within families. Table 4 reports 1996 national median income for one-earner families as \$2,365 per month, which is only \$40 more than the value for a one-earner household.

\$834 per month less under S 1301 than it is under H.R. 3150. On the other hand, for households of size greater than four, S 1301's addition of \$583 month for each additional member creates income thresholds considerably larger than those in H.R. 3150.

Note also that S. 1301 requires spousal income to be included in current monthly total income without reference to whether the bankruptcy case is filed jointly. This marks another distinction between the Senate and House provisions.

The following table summarizes the monthly national income thresholds established in the two bills for sizes one through five.

SIZE	H.R. 3150	S. 1301
1	\$2,325	\$1,491
2	\$3,006	\$3,107
3	\$3,676	\$3,735
4	\$4,293	\$4,284
5	\$4,293	\$4,867

As noted, the allowance under H.R. 3150 reaches a maximum at \$4,293 irrespective of further growth in family size, while the allowance under S. 1301 grows linearly with each increase in household size. So, for example, for a household of eight the Senate bill allows a monthly income of \$6,616, while the House bill allows a monthly income of \$4,293, before creditors could request or suggest that a debtor's petition should be dismissed for abuse.

What difference do these differences make?

All else equal, the income thresholds specified in S. 1301 will make many more debtors liable for dismissal or conversion into chapter 13 than those specified in H.R. 3150.

There is a preponderance of low income single filers in the population of debtors. Preliminary work in our office suggests that approximately 38% of current chapter 7 debtors nationwide claim households of size one, and nearly one-third of these have a gross monthly income between \$1,491 and \$2,325. Thus, with Chapter 7 filings running at about one million per year, approximately 125,000 would be liable for dismissal or conversion under the Senate bill but not the House bill.

The more generous income thresholds for larger families in S. 1301 would have almost no offsetting effect upon the total number of cases liable for dismissal or conversion into chapter 13. We estimate that, nationally, approximately 7,000 debtors in families size two or more have incomes between the different thresholds established by the House and Senate.

Putting the estimates together, we conclude that S. 1301 would subject approximately 118,000 more chapter 7 filers to the possibility of conversion or dismissal than H.R. 3150 would.

As noted, the bills also provide different treatments of spousal income. H.R. 3150 includes spousal income only in joint filings, while S. 1301 includes it without regard to joint filing. In our experience, very few married debtors who file as individuals include spousal income on their income schedules at the time of filing. It is reasonable to believe that there is more spousal income in the population of individual filers than is reported. It is, however, impossible to estimate the impact of this difference between the bills by reviewing information readily available.

Conclusion

The difference between the bills' treatment of gross income has implications for the administration of the bankruptcy system by courts, private trustees, United States Trustees, and practitioners. For example, under the Senate proposal, the number of conversions to chapter 13 will depend on the aggressiveness of the parties in interest, especially major creditors, in pursuing actions under § 707. Debtors' attorneys will no doubt contest these actions in many cases, or attempt to prevent them by preparing materials showing the court that special circumstances support allowing the debtor to remain in chapter 7. Chapter 7 trustees and United States Trustees will also have roles to play in these disputes. It is certainly not too soon for the courts and the trustee communities to do some contingency planning in preparation for the administrative consequences of means testing for chapter 7 petitioners.