No. 16-1358

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

In re: GABRIEL L. JACKSON and MONTE N. JACKSON,
Debtors.

MARJORIE K. LYNCH, Bankruptcy Administrator
for the Eastern District of North Carolina,
Appellant,
– v. –
GABRIEL L. JACKSON; MONTE N. JACKSON,
Debtors/Appellees; and
A. SCOTT MCKELLAR,
Trustee.

On Appeal from the United States Bankruptcy Court
For the Eastern District of North Carolina

BRIEF OF AMICUS CURIAE NATIONAL ASSOCIATION OF CONSUMER BANKRUPTCY ATTORNEYS IN SUPPORT OF APPELLEES AND SEEKING AFFIRMANCE OF THE BANKRUPTCY COURT'S DECISION

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July 5, 2016

RULE 26.1 CORPORATE DISCLOSURE STATEMENT

Lynch v. Jackson et al., No. 16-1358

Pursuant to FRAP 26.1 and Fourth Circuit Local Rule 26.1(b), Amicus Curiae, the National Association of Consumer Bankruptcy Attorneys, makes the following disclosure:

1) Is party/amicus a publicly held corporation or other publicly held entity? **NO**

2) Does party/amicus have any parent corporations? **NO**

3) Is 10% or more of the stock of party/amicus owned by a publicly held corporation or other publicly held entity? **NO**

4) Is there any other publicly held corporation or other publicly held entity that has a direct financial interest in the outcome of the litigation? **NO**

5) Does this case arise out of a bankruptcy proceeding? **YES**. If yes, identify any trustee and the members of any creditors' committee. **A. Scott McKellar, Chapter 7 Trustee**

This 5th day of July, 2016.

/s/ Tara Twomey
Tara Twomey, Esq.
Attorney for Amicus Curiae

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STATEMENT OF INTEREST OF AMICUS CURIAE

Incorporated in 1992, the National Association of Consumer Bankruptcy Attorneys (NACBA) is a non–profit organization consisting of approximately 3,000 consumer bankruptcy attorneys nationwide.

NACBA's corporate purposes include education of the bankruptcy bar and the community at large on the uses and misuses of the consumer bankruptcy process. Additionally, NACBA advocates nationally on issues that cannot adequately be addressed by individual member attorneys. It is the only national association of attorneys organized for the specific purpose of protecting the rights of consumer bankruptcy debtors. NACBA has filed *amicus curiae* briefs in various cases seeking to protect the rights of consumer bankruptcy debtors. *See, e.g., Harris v. Viegelahn*, 135 S. Ct. 1829 (2015); *Schwab v. Reilly*, 560 U.S. 770 (2010); *Ranta v. Gorman*, 721 F.3d 241 (4th Cir. 2013).

NACBA and its membership have a vital interest in the outcome of this case. The proper method of performing a means test calculation guides not only a debtor's eligibility for Chapter 7 bankruptcy protection, but also a Chapter 13 debtor's repayment plan, and is thus an important issue to consumer debtors who seek a fresh start under the Bankruptcy Code. NACBA member attorneys represent individuals in a large portion of these consumer bankruptcy petitions filed. These consumer debtors, and their attorneys, must be able to rely on the text

of the Bankruptcy Code, as well as the Official Forms and instructions implementing the Code, when performing Means Test calculations as part of their petitions. This Court's ruling will clarify whether a deeply rooted method of performing the Means Test calculation survives a recent U.S. Supreme Court case.

CERTIFICATION OF AUTHORSHIP

Pursuant to Fed. R. App. P. 29(c)(5), no counsel for a party authored this brief in whole or in part, and no person or entity other than NACBA, its members, and its counsel made any monetary contribution toward the preparation or submission of this brief.

CONSENT

The parties have consented to the filing of this amicus brief.

SUMMARY OF ARGUMENT

Congress created the Means Test in 2005 with two purposes in mind: ensuring that debtors who could repay debts did not abuse Chapter 7 bankruptcy, and creating a mechanical, uniform way to approximate a debtor's ability to repay. For years, it has been clear that a Means Test calculation requires the debtor to use expense deductions, as those amounts are specified in the National and Local Standards published by the Internal Revenue Service (IRS). The Supreme Court case of *Ransom v. FIA Card Services* does not change that result, and instead bolsters this well-established practice. Appellant's insistence to the contrary, based on a slim minority approach, threatens the very uniformity Congress sought when it created the Means Test.

ARGUMENT

This question is answered squarely by the text of the Bankruptcy Code. Under the Section 707 Means Test:

> The debtor's monthly expenses shall be:
> [a] the debtor's applicable monthly expense *amounts specified* under the National Standards and Local Standards, and
> [b] the debtor's actual monthly expenses for the categories specified as Other Necessary Expenses issued by the Internal Revenue Service for the area in which the debtor resides"

11 U.S.C. § 707(b)(2)(A)(ii)(I) (emphasis added). A plain reading of this text shows that the amounts to be used are those "specified under the National Standards and Local Standards." *Id*. The congressional intent behind the Means Test bolsters this common sense reading of the statute.

Further, as Appellant "readily acknowledges[, …] the weight of persuasive authority on this issue supports affirmance" of the bankruptcy court's order. (Appellant's Br. at 23.) Yet Appellant also claims that its "ultimate goal is harmonization of the conflicting jurisprudence within the Eastern District of North Carolina regarding the court's interpretation of § 707(b)(2)(A)(ii)(I)." (Appellant's Br., 8.) Remarkably, the "harmonization" sought by Appellant requires this Court to reject a near-uniform national practice, and adopt an outlier interpretation of Section 707.

I. Pre-BAPCPA Methods Of Evaluating Abuse Were Inadequate And Inconsistent.

Appellant's argument about the Means Test harkens back to the standards in place before the Means Test was created in 2005. In order to understand the folly in Appellant's position, it is thus important first to understand the procedure that the Means Test replaced.

As originally enacted in 1984, Section 707(b) allowed for dismissal of a consumer debtor's Chapter 7 bankruptcy case if the Court found "that the granting of relief would be a substantial abuse of the provisions of this chapter." Pub. L. No. 98-353, § 312, 98 Stat. 333, 355 (1984). However, there was "a presumption in favor of granting the relief requested by the debtor." *Id*.

The ability for the Court to dismiss abusive Chapter 7 filings was a legislative response to "an increasing number of Chapter 7 bankruptcies being filed by non-needy debtors. Prior to 1984, debtors enjoyed a virtually unfettered right to a 'fresh start' under Chapter 7." *In re Green*, 934 F.2d 568, 570 (4th Cir. 1991). Unfortunately, Congress neither defined "substantial abuse," nor provided any guidance on what that term was to mean. *See id.* at 570-571.

To evaluate "substantial abuse," courts largely developed a test based on the totality of the circumstances. *Green*, 934 F.2d at 570-572; *see also In re Lamanna*, 153 F.3d 1, 3-5 (1st Cir. 1998); *In re Kelly*, 841 F.2d 908, 915-15 (9th Cir. 1988). Although there were some variations in the way the test accounted for a debtor's

ability to repay,[1] it was clear that the ability to repay debts was at least an important factor that most courts used in this totality test. *See Lamanna*, 153 F.3d at 4-5. In the end, these factors always depended on case-by-case determinations. *See Green*, 934 F.2d at 572.

This case-by-case analysis under the totality of the circumstances test "led to varying and often inconsistent determinations." *Ransom v. FIA Card Services, N.A.*, 131 S. Ct. 716, 722 (2011). Some courts may have viewed a debtor's expenses as excessive, thus indicating that a debtor could repay debts with some adjustments to his budget, while other courts could view the same expense as entirely reasonable. Even after accounting for reasonable expenses, courts often reached different conclusions as to how much net income would be required for a debtor to have the ability to repay debts.

II. In 2005, BAPCPA Moved Away From Actual Expenses, And Towards An Objective Test Incorporating National Standards.

By 2005, Congress recognized the inconsistent results created by the case-by-cases determinations of "abuse" under Section 707(b). As a result, as part that year's overhaul of the Bankruptcy Code, Congress outlined a roadmap to

[1] Some courts adopted a per se rule examining a debtor's income and expenses, *see e.g., Kelly*, 841 F.2d at 915, while others incorporated the debtor's ability to repay as a primary factor in the analysis, *see Lamanna*, 153 F.3d at 5.

determine whether a filing was to be presumed to be "abuse," creating both an objective test and a subjective test.[2]

The objective test, known as the Means Test, tackled the biggest source of inconsistency under prior law: consideration of the debtor's ability to repay. *See* Pub. L. No. 109-8, § 102(a)(2)(C), 119 Stat. 23, 27-29 (2005). Its simple aim was to create a "uniform standard to bankruptcy judges to evaluate the ability of bankruptcy filers to repay debts." 151 Cong. Rec. S1842-S1843 (Mar. 1, 2005) (statement of Sen. Hatch). The mechanical test functions by "appl[ying] clear and well-defined standards to determine whether a debtor has the financial capability to pay his or her debts." 151 Cong. Rec. H2053 (Apr. 14, 2005) (statement of Rep. Goodlatte). Thus, from its inception, the Means Test balanced the legislative desire to steer debtors who could repay debts into Chapter 13 with the administrative need to do so in a uniform way, applying "well-defined standards" instead of subjective inquiry into the debtor's expenses.

That balance is most obvious in the safe harbor provision that completely protects debtors who are below the median income from means testing. *See* 11

[2] The subjective test, not applicable here, (*see* R.131-132,) allows for dismissal of a Chapter 7 if filed in bad faith, or based on the totality of the circumstances. 11 U.S.C. § 707(b)(3). Although much of the previous "totality of the circumstances" tests were imported to Section 707(b)(3), that did not include the vague examination of the debtor's ability to repay, which was accounted for in the objective Means Test determination. *See In re Walker*, 381 B.R. 620 (Bankr. M.D. Pa. 2008); *In re Nockerts*, 357 B.R. 497 (Bankr. E.D. Wis. 2006).

U.S.C. § 707(b)(7). Rather than subjecting such debtors to any testing regarding their ability to repay debts, the Code simply presumes that they are not abusing the provisions of Chapter 7. The entitlement of these debtors to relief is not based on their expenses and ability to repay at all, but simply based on how their income relates to statewide standards. *See* H.R. Rep. No. 109-31, pt. 1 at 51 (2005)(this section prevents "a motion to dismiss based on the debtor's ability to repay.").

For debtors with a household income above the median, the Means Test mechanically determines their "ability to repay." It "takes into account the debtor's monthly income and certain deductible expenses such as the cost of housing, utilities, taxes, health insurance and an allowance for food and clothing. Some of these expenses may be calculated by using national or local standards." *Calhoun v. United States Trustee*, 650 F.3d 338, 341 (4th Cir. 2011). Thus, just as standard income data serves as the yardstick for below-median debtors, standard expense data serves as the yardstick for above-median debtors, with some allowance for actual non-standard expenses.

By creating this formula, "Congress intended the means test to *approximate* the debtor's reasonable expenditures on essential items." *Ransom*, 131 S. Ct. at 725 (emphasis added). As described by this Court, "in requiring above-median debtors to use the means test to assess their 'amounts reasonably likely to be expended,' the BAPCPA moved away from permitting such debtors to claim their

actual expenses and toward requiring them to use a more standardized amount." *Johnson v. Zimmer*, 686 F.3d 224, 238 n.12 (4th Cir. 2012). The congressional intent to create such a mechanization is further seen in the way the statute specifies the amounts in the National and Local Standards for certain expenses, but looks to "actual" expenses for certain other categories. *See* 11 U.S.C. § 707(b)(2)(A)(ii)(I) (referring to the "monthly expense amounts specified under the National Standards and Local Standards," but separately referring to "the debtor's actual monthly expenses for the categories specified as Other Necessary Expenses").

The use of these standardized dollar amounts from the National and Local Standards, rather than the debtor's actual expenses, serves various purposes. First, it accounts for the fact that a debtor may spend more in one category, but less in another. "By comparing the *total* of allowed expenses to the debtor's current monthly income, Congress clearly intended that a debtor might spend more than the allowance for one category (e.g., rent) and less for another (e.g., food), as long as the end result did not leave $207.92 per month in disposable income." 6 Collier on Bankruptcy ¶ 707.04[4][b] at 707-47 (16th ed.). Thus, a suburban debtor who has housing expenses below the Local Standards, may have that frugal expense offset by increased transportation expenses to a job in an urban center. This case exemplifies this feature of the Means Test, as the Jacksons have actual housing

expenses below the Local Standards, but actual transportation expenses above the standards. (*See* Appellee's Br., 19-20).

Second, it ensures that debtors with a particularly low expense in one category are not punished for their frugality. *Id* ("by permitting debtors to deduct the amounts specified in the IRS guidelines rather than limiting debtors to actual expenses, Congress has chosen not to penalize debtors for their frugality in spending less than the IRS allowances."). Otherwise, such frugal debtors who barely exceed the threshold for qualifying for Chapter 7 would be motivated to increase their expenses, and live a more lavish lifestyle, just so that they could file Chapter 7 bankruptcy.

Last but not least, the use of standardized amounts relieves the court from inquiring into the debtor's actual expenses to determine what is reasonable. As described above, such a method, in use before BAPCPA, was time-consuming to administer, and led to inconsistent results.

As Appellant concedes, this interpretation of the Means Test, requiring use of the National and Local Standards, instead of actual expenses, has become deeply rooted in bankruptcy practice. *See In re Kimbro*, 389 B.R. 518, 522-23 (6th Cir. B.A.P. 2008); *In re Musselman*, 394 B.R. 801, 817 (E.D.N.C. 2008); *In re Briscoe*, 374 B.R. 1, 6-7 (Bankr. D.C. 2007). It is so engrained in bankruptcy practice that the Official Forms prescribed by the Judicial Conference of the

United States, which debtors are required to use, adopt this interpretation of the Code. *See* Official Form 122A-2 at 2. And these "forms shall be construed to be consistent with… the Code." Fed. R. Bankr. P. 9009.

In the end, arguments, like Appellant's, that focus only on the ability to repay completely ignore the competing interest that Congress sought to strike with the Means Test: creating a uniform method to determine the ability to repay. This uniform and widely-accepted method serves various purposes that are important to the functioning of bankruptcy practice.

III. The *Ransom* Case Did Not Change This Widely-Accepted Interpretation Of The Code.

The Supreme Court's 2011 *Ransom* decision does nothing to change the above analysis. If anything, it is difficult to square the *Ransom* analysis with Appellant's proposed rule.

The *Ransom* decision turned entirely on the definition of the word "applicable" as it is used in the Code. "[A]n expense amount is 'applicable' within the plain meaning of the statute when it is appropriate, relevant, suitable, or fit." *Ransom*, 131 S. Ct. at 724. As the Court applied the term to the facts in *Ransom*:

> A debtor may claim a deduction from a National or Local Standard table (like [Car] Ownership Costs") if but only if that deduction is appropriate for him. And a deduction is so appropriate only if the debtor has costs corresponding to the *category* covered by the table-that is, only if the debtor will incur that *kind* of expense during the life of the plan.

Id (emphasis added). With this analysis, the Supreme Court clearly found that the word "applicable" relates to whether a particular category of expense could be invoked at all. If a debtor pays for a vehicle, then that category applies. If a debtor does not pay for a vehicle, then that category does not apply, and the debtor cannot take the deduction. It is quite a leap to extrapolate from this decision that the term "applicable" also limits debtors to their actual expenses, with the National Standards only acting as a ceiling. Indeed, the definition for "applicable" cited by the *Ransom* Court contains no limiting features.

The *Ransom* Court, while noting that the United States has adopted the position expressed in the brief, expressly did not reach this particular issue. *See Ransom*, 131 S. Ct. at 727 n.8. However, the Court's

> reasoning makes it difficult to see how anything but the amount in the IRS table is to be used once the ownership allowance is found to be 'applicable.' The statute refers to the 'amount specified' in the standards and the Court's decision described the standards as 'tables that the IRS prepares listing standardized expense amounts for basic necessities.' Although the creditor in *Ransom* argued that this amount serves as a cap, the relevant language in the decision refers to treating the standards as a cap as "IRS practice" rather than any result dictated by the IRS standards. Since the IRS also has discretion to deviate from the standards in other ways if it chooses, including upwards, it is clear that the IRS practice cannot be simply imported wholesale into the section 707(b)(2) means test.

6 Collier on Bankruptcy ¶ 707.04[3][c][i] at 707-34 (16th ed.).

As Appellant also concedes, the "statute does not incorporate or otherwise import the IRS guidance." (Appellant's Br., 19 (quoting *Ransom*, 131 S. Ct. at 726

n. 7) (internal quotation marks omitted).) Yet, much of Appellant's argument, including the cases it relies upon, is based on the purported persuasiveness of the IRS Manual after *Ransom*. (*See* Appellant's Br., 20-23 (citing *In re Fields*, 534 B.R. 126, 140 (Bankr. E.D.N.C. 2015); *In re Harris*, 522 B.R. 804, 816-17 (Bankr. E.D.N.C. 2014).) But these cases, and Appellant, fail to recognize the other ways that the IRS Manual interprets the National and Local Standards, such as the discretionary upward deviations, that are indisputably contrary to the way the tables are to be used for bankruptcy purposes.[3]

Other cases relied upon by Appellant contain very little analysis on this issue. For instance, the *Daniel* Court decided that *Ransom* "is virtually on all fours with the instant case." *In re Daniel*, 2012 Bankr. LEXIS 2440, *2 (Bankr. M.D. Ala. May 29, 2012). But the Court did not provide any reasoning for this purported similarity, and seemed to overlook entirely the fact that the *Ransom* Court expressly did not decide the instant issue. *See id.* Similarly, the *Wilkerson* Court cited some post-*Ransom* decisions on this issue, and without any analysis, summarily concluded that *Harris* is "the better reasoned of the post-*Ransom*

[3] The IRS itself recognizes that its method of applying the National Standards is different than in bankruptcy law, and provides a disclaimer at the top of its website warning visitors of such: "[t]hese Standards are… for purposes of federal tax administration only. Expense information for use in bankruptcy calculations can be found on the website for the U. S. Trustee Program." *See* Collection Financial Standards, https://www.irs.gov/businesses/small-businesses-self-employed/collection-financial-standards (Last visited Jun. 28, 2016).

decisions addressing this issue." *In re Wilkerson*, 2015 Bankr. LEXIS 2081, *5 (Bankr. D.C. Jun. 25, 2015).

By contrast, the majority of courts have rejected Appellant's approach post-*Ransom*, often engaging in detailed analysis, weighing much of the above argument. (*See* Appellee's Br. 31-35 (discussing post-*Ransom* cases).) For example, the *Scott* Court thoroughly examined the arguments presented by the United States in its *Ransom* amicus curiae brief, the importance of the instructions on the Official Forms, and the balance sought by Congress when it created the Means Test. *In re Scott*, 457 B.R. 740, 743-747 (Bankr. S.D. Ill. 2011). The *Miranda* Court also carefully weighed those arguments when it decided that the majority approach survived *Ransom*. *In re Miranda*, 449 B.R. 182, 191-194 (Bankr. P.R. 2011).

Both pre- and post-*Ransom*, the weight of the authority has always been in support of the well-established approach used in bankruptcy courts across the country, allowing debtors to take the full deductions as "specified" under the IRS National and Local Standards.

IV. Appellee's Admittedly Minority Approach Disrupts The Uniformity Sought By Congress When It Created The Means Test.

Appellant's concession that it takes an outlier position highlights an important flaw in its proposed rule. (*See* Appellant's Br. 11 (the above interpretation enjoys "near universal judicial interpretation").) As described above, the means test was explicitly adopted to create a "uniform standard" for bankruptcy courts to evaluate "abuse." That uniformity is undermined if this Circuit were to adopt Appellant's interpretation of Section 707, and create a standard that is unique to the Fourth Circuit and contrary to the language used on the mandatory national bankruptcy forms.

CONCLUSION

For the reasons stated above, *amicus curiae* asks this court to affirm the decision of the Bankruptcy Court of the Eastern District of North Carolina below.

/s/ Tara Twomey

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CERTIFICATE OF COMPLIANCE

1. This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because this brief contains 3,258 words, excluding parts exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

2. This filing complies with Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Microsoft Word in Times New Roman 14 point type.

3. This brief has been scanned for viruses pursuant to Rule 27(h)(2).

/s/ Tara Twomey
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CERTIFICATE OF SERVICE

I hereby certify that I electronically filed the foregoing with the Clerk of the Court for the United States Court of Appeals for the Fourth Circuit by using the appellate CM/ECF system on July 5, 2016. I certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the appellate CM/ECF system.

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