

CONSUMER BANKRUPTCY

Counseling High-Income Consumer Bankruptcy Debtors

Many debtors with significant income can file Chapter 7

By **Craig D. Robins**

In the past few years I've noticed a fascinating trend. I'm counseling more and more debtors with high income and high debt. Representing such debtors requires addressing certain special issues which I will address in this article.

Perhaps the current drawn-out recession is affecting an increasing number of consumers beyond the low and middle-class — long the bastion of typical bankruptcy filers. In addition, falling real estate values have wiped out the equity in many people's homes. Many middle and upper-class Americans have thus lost their ultimate source of long-term savings.

Chapter 7 is usually the consumer's best choice

Assuming that there's no need to consider Chapter 13 to stop foreclosure, I always strive to file Chapter 7 bankruptcy petitions for all my clients — but doing so requires that they qualify. After all, if a Chapter 7 case goes smoothly, the debtor will discharge most or all debts and ideally keep all assets.

For high-income debtors, Chapter 7 eligibility has become rather challenging considering that under the 2005 Bankruptcy Amendment Act (BAPCPA), a consumer debtor will almost certainly face opposition to getting a discharge if he or she does not pass the means test. The

U.S. Trustee is especially vigilant in reviewing any case that is deemed abusive, or that may even be close to being abusive.

Accordingly, analyzing the facts of a high-income debtor becomes critical and properly preparing the means test and other bankruptcy schedules becomes crucial.

How much income is "high-income"?

Lately I've been regularly filing Chapter 7 bankruptcy petitions for families with incomes well over \$100,000. I recently filed two Chapter 7 cases where the family income was over \$200,000. Considering the perceived income limitations for seeking Chapter 7 relief under the new bankruptcy laws, such high-income filings seem difficult or impossible yet in practice, they are not.

Generally, a high-income debtor is one who has income over \$100,000 per year or \$10,000 per month. In my bankruptcy practice, high-income debtors are often executives, doctors, assorted professionals, and families of double-income spouses.

A high-income debtor can file for Chapter 7 relief if the debtor a) passes the means test or conversely does not need to qualify for the means test; and b) passes a totality of circumstances test for filing in



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good faith — often meaning that all of their expenses are reasonable and necessary.

Many high-income debtors also have relatively high levels of debt. A former executive previously earning several hundred thousand dollars per year can easily have as much credit card debt. In such cases, the debt must have been incurred in good

faith and must not be unreasonably high in relation to the debtor's income at the time the debt was incurred. Counsel should devote extra time to reviewing the various debts in such cases.

The Business Debt Exception to the Means Test

Many high-income debtors have very substantial debt obligations from failed business ventures, often due to having signed a personal guarantee. A debtor is excused from preparing the means test if the debtor's debts are not primarily "consumer debts," and there is a box on the means test for this exclusion.

A "consumer debt" is defined as a debt incurred by an individual primarily for a personal, family or household purpose. On the other hand, some courts have defined "business debt" as debt that is incurred with a "profit motive." I hope to devote a future column to a more involved discussion about how courts

have defined debt as either business debt or consumer debt.

Variables making high-income debtors more eligible for filing

Certain individuals are able to pass the means test much more easily than others. Those that have large families with multiple dependants, large mortgages, two car loans or leases, mortgage arrears and tax arrears are more likely to qualify under the means test because these items can all be used as means test deductions.

Even if the debtor passes the means test, that alone is not enough to demonstrate that the case is not abusive, and that it is filed in good faith. All budget items must be reasonable and necessary; based on the debtor's actual income going forward. This requires a more subjective and equitable assessment of the debtor's circumstances.

For example, the U.S. Trustee is likely to object to an expense of \$2,000 per month for food for a family of four, but will not have any problem with an expense of \$1,200, even though that is on the high side.

Some expenses will not pass muster. The U.S. Trustee will likely argue that an expensive summer camp is unreasonable, as sending the kids there is being done at the expense of the creditors.

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High-Income Bankruptcy Debtors

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Issues with keeping rental property

High-income debtors are much more likely to have investment real estate in addition to their homes. In such cases, there is an issue as to whether keeping the rental property is reasonable. If the expenses of retaining the property exceed the amount of rental income, then keeping the property will result in a reduced amount of disposable income.

In such a case, the U.S. Trustee will argue that the debtor will have additional income each month to make payments to creditors if the investment property is abandoned.

Maintaining a Luxury Residence

A high-income debtor is much more likely to have an expensive home. However, there are some cases across the country in which the U.S. Trustee argued that it is unreasonable for a debtor to keep a luxury home with a very high monthly mortgage at the expense of the creditors. This issue has not been addressed in our Circuit.

Alternatives if debtor isn't eligible for Chapter 7 Relief

If the debtor fails the means test or simply has too much disposable income, then there are still a number of options available. The debtor can file for Chapter 13 relief if his or her secured debts are less than \$1,081,400 and unsecured debts are less than \$360,475. If the debt levels exceed these amounts, they can file for Chapter 11 relief. Debt Negotiation is also an option in which the attorney can negotiate settlements with the creditors.

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