

## **The 15<sup>th</sup> Annual Frank W. Koger Bankruptcy Symposium**

### **The Modern Family Debacle: Bankruptcy Judges Decide Some of the Debtors' Loved Ones Do Not Count as Household Members**

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Assume that a husband and wife, Dale and Dee Smith, file for Chapter 13 bankruptcy relief. At the time of the filing, the Smiths have living in their home seven individuals. Beside the couple, the residential occupants include the Smiths' adult son, Mrs. Smith's elderly mother, Mrs. Smith's sister, an underage nephew (*i.e.*, the sister's son), and an adult niece (*i.e.*, the sister's daughter). The Smiths' adult son is recovering from a recent surgery and cannot work. The elderly mother gets a monthly Social Security check. Which occupants count as household members?

#### **I. The Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) Requires Calculations Based, in part, on Household Size in Consumer Bankruptcy Cases.**

- A. Means Test is set forth in 11 U.S.C. § 707. Subsection (b)(6) of § 707 states that a debtor's annualized income, "in the case of a debtor in a household of 2, 3, or 4 individuals, [should be compared to] the highest median family income of the applicable State for a family of the same number or fewer individuals." The term "household" is not defined. However, in reference to "household," the Bankruptcy Code uses the term "individuals" and did not use the term "relatives" or "dependents."
- B. Disposable Income Test in Chapter 13 – BAPCPA requires that a Chapter 13 plan commit all "disposable income" to unsecured creditors. "Disposable income" is defined as "current monthly income received by the debtor" less the "amounts reasonably necessary to be expended for the maintenance or support of the debtor or a dependent of the debtor." The calculation of "amounts reasonably necessary to be expended" is based, in part, on the size of a debtor's "household." A court must compare the debtor's income to the "highest median family income of the applicable State" for the household size. If the debtor's income is higher than that number, then § 707 (b)(2)(A)-(B) provides which expenses are allowed.

## II. Courts Follow Four Different Approaches When Determining the Size of Debtor's Household.

- A. U.S. Census or "Heads-on-Beds" Approach counts as household members all occupants of the debtor's physical residence. Courts rely on Bankruptcy Code § 101(39A)(A), which defines "median family income" as "the median family income both calculated and reported by the Bureau of the Census." *See, e.g., In re Ellringer*, 370 B.R. 905 (Bankr. D. Minn. 2007) (counting the debtor's "roommate" as household member).
- B. IRS Tax Dependent Approach narrows the number of occupants who can count as household members by counting only the occupants who can be claimed as dependents on the debtor's tax return. *See, e.g., In re Law*, No. 07-40863, 2008 Bankr. LEXIS 1198 (Bankr. D. Kan. Apr. 24, 2008) (adopting the Tax Dependent Approach and refusing to count as a household member the debtor's adult son who had a part-time job because he was not claimed as a dependent on the debtor's tax return).
- C. The Economic Unit Approach counts occupants who have financially interdependent relationships with the debtor as household members. *See, e.g., In re Herbert*, 405 B.R. 165, 170 (Bankr. W.D.N.C.2008) (counting all eleven occupants as household members, including the girlfriend's underage children because the debtor financially supported them even though he was not legally obligated to do so).
- D. The Fractional Economic Unit Approach treats children residing part-time with a debtor as a fraction of an individual. *See, e.g., In re Roch*, No. 20-12792-KHK, 2021 WL 5177442 (Bankr. E.D. Va. 2021) (holding that a child who resided with the debtor one-third of the time created a household size of one and one-third, and then rounding down—instead of up—to create household size of only one person).

## III. Application of the Approaches are Problematic for Debtors with Non-Traditional Families.

- A. The biggest problem is that courts may in effect impose a *financial penalty* on debtors with non-traditional families when applying the various approaches, except for the Census Approach. For non-traditional families, the Census Approach is best as it is simple and easy to apply. This approach is the only approach grounded in the language of the relevant Bankruptcy Code provisions due to references to U.S. Census. *See generally Ransom v. FIA Card Services, N.A.*, 131 S. Ct. 716 (2011) (stating that formulas like the Means Test "are by their

nature over- and underinclusive,” but “Congress chose to tolerate the occasional peculiarity that a brighter-line test produces”).

B. Criticism of the Other Three Approaches – Most courts have opted for three other approaches that have devolved over time into complicated legal analyses that not only impose a financial penalty but that dehumanize underage children, that require an intrusive detailed analysis of debtors and their families, that disclose potentially embarrassing information about family members, and that stray far away from Congressional intent to have standards that are uniform.

C. Examples

1. *In re* Law, No. 07-40863, 2008 Bankr. LEXIS 1198, at \*7 (Bankr. D. Kan. Apr. 24, 2008). By refusing to count debtor’s adult son as a household member under the Tax Dependent Approach, the court’s ruling imposed a financial penalty on the debtor. The debtor could only claim \$916 as his allowed IRS standardized expenses for a household of one, instead of the \$1,306 for a two-person household. As a result, the debtor’s projected disposable income rose by \$390 per month, thereby requiring \$23,400 in additional payments over the course of his sixty-month Chapter 13 plan.
2. *In re* Skiles, Case No. 13–61565 (Bankr. N.D. Ohio January 9, 2014) (purporting to adopt the Economic Unit Approach but creating a presumption that persons claimed as dependents on a debtor’s tax return count as household members, then creating shifting burdens of proof, and finally identifying numerous evidentiary items to prove financial interdependency).
3. *In re* Morrison, 443 BR. 378, 388 (Bankr. M.D.N.C. 2011) (The court created the following seven-factor test for applying the Economic Unit Approach: “1) the degree of financial support provided to the individual by the debtor; 2) the degree of financial support provided to the debtor by the individual; 3) the extent to which the individual and the debtor share income and expenses; 4) the extent to which there is joint ownership of property; 5) the extent to which there are joint liabilities; 6) the extent to which assets owned by the debtor or the individual are shared, regardless of title; and 7) any other type of financial intermingling or interdependency between the debtor and the individual.”)

4. *In re Ford*, 509 B.R. 695 (Bankr. D. Idaho 2014) (purporting to adopt the Economic Unit Approach but not allowing an underage stepson to count as a household member even the debtor-stepdad had been financially supporting the stepson since he was a baby).
5. *Johnson v. Zimmer*, 686 F.3d 224, Bankr. L. Rep. (CCH) P 82291 (4th Cir. 2012) (adopting a *fractional* Economic Unit Approach and holding that the debtor's underage children, who were part-time occupants, counted as a fraction of individual; specifically the debtor's two biological children counted as .56 members each and her stepchildren counted as .49 members each).
6. *In re Fraleigh*, 474 B.R. 96, 108–11 (Bankr. S.D.N.Y. 2012) (adopting the *Morrison* seven-factor Economic Unit Approach and applying the approach in manner that resulted in the disclosure that the debtor's boyfriend required the debtor's teenage children to pass regular drug tests while residing in the boyfriend's home).

#### IV. Solution

- A. Congress should amend the Bankruptcy Code to adopt Professor Johnson's proposed "Household Size Test." *See The Modern Family Debacle: Bankruptcy Judges Decide That Some Debtors' Loved Ones Do Not Count as Household Members*, 111 CAL. L. REV. 101 (publication pending 2023).  
([https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4191890](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4191890))
- B. Let's apply the proposed test to the occupants residing in the home of the aforementioned debtors, Dale and Dee Smith.<sup>1</sup> Does the household consist of seven people or a smaller number?
  1. Although the debtors' adult son is unable to work due to recent surgery, is his return to work expected in the near future and is he expected to be self-sufficient?
  2. Does any of the elderly mother's Social Security check go towards the payment of the debtors' living expenses?
  3. Are the debtors financially supporting the sister and her underage son (Mrs. Smith's nephew)?
  4. Is the adult niece gainfully employed and self-sufficient?
  5. How much of sister's and adult niece's incomes go towards the payment of expenses for the debtors and their living expenses?

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1. *See In re Poole*, No. 21-32224, 2022 WL 5224087 (Bankr. N.D. Tex. Sept. 30, 2022).

C. By adopting the proposed test, Congress would (1) enable consumer bankruptcy attorneys to give legal advice with certainty and predictability, (2) prevent trustees and creditors from wasting judicial resources, (3) relieve debtors from being burdened with additional attorneys' fees in litigation over household size, (4) protect debtors from intrusive and hairsplitting analyses of their personal lives, and (5) protect minor children from dehumanizing treatment in bankruptcy proceedings.