

The Debt Considered in a Bankruptcy Case May Surprise You

By Camille J. Iurillo and Gina M. Pellegrino

Generally speaking, if an individual debtor, having primarily consumer debt, files a Chapter 7 bankruptcy and his or her income is above the mandatory median income then a presumption of abuse arises and a motion to dismiss the case may be filed by a party in interest, such as the Chapter 7 Trustee, the U.S. Trustee, or a creditor. The Bankruptcy Code, specifically section 707(b)(1), provides that the bankruptcy court may grant such a motion to dismiss if the court finds that it would be an abuse of the Bankruptcy Code for the debtor to obtain Chapter 7 relief. *See*, 11 U.S.C. § 707(b)(1). However, generally speaking, if an individual debtor has primarily business debt then that debtor is not subject to the mandatory median income in order to file a Chapter 7 bankruptcy. This article does not focus on what constitutes “abuse” under the Bankruptcy Code; rather, this article focuses on further understanding the phrase “primarily consumer debt,” and whether equitable or contingent debt is to be considered when calculating the amount of debt owed.

This article is intended only as a starting point and is by no means an exhaustive discussion of primarily consumer debt or section 707(b)(1) of the Bankruptcy Code.

11 U.S.C. § 707(b)(1) states, in pertinent part, “[a]fter notice and a hearing, the court, on its own motion or on a motion by the U.S. trustee, ...or any party in interest, may dismiss a case filed by an individual debtor under this chapter whose debts are primarily consumer debts, or, with the debtor’s consent, convert such a case to a case under chapter 11 or 13 of this title, if it finds that the granting of relief would be an abuse of the provisions of this chapter...”

In addition, the Bankruptcy Code defines “debt” as “liability on a claim.” 11 U.S.C. § 101(12). Moreover, the Bankruptcy Code defines “claim” as the “right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured; or...” 11 U.S.C. § 101(5)(A) (emphasis added).

If a debtor’s non-filing spouse owns real property in his or her own name, and is solely obligated on the note and mortgage, is this deemed an equitable debt of the debtor that may be considered by the court when it is determining whether the debtor has primarily consumer debt? In other words, is equitable debt and contingent debt considered by the court in making its determination as to whether a debtor’s debt is primarily consumer debt for section 707(b)(1) purposes? If the debt is a marital liability incurred during the marriage, then it is arguable that the debtor has an equitable obligation to pay the mortgage on the real property titled solely in the non-filing spouse’s name, in which case, such debt would be deemed equitable debt. According to the applicable law, equitable debt and contingent debt should be considered by a court in making its determination as to whether a debtor’s debt is primarily consumer debt. *See, In re Hall*, 258 B.R. 45, 48-9 (Bankr. M.D. Fla. 2001); *see also*, 11 U.S.C. § 101(12) and 11 U.S.C. § 101(5)(A).

In Hall, the U.S. Trustee moved to dismiss the debtor’s Chapter 7 bankruptcy case, pursuant to section 707(b) of the Bankruptcy Code, claiming that the debtor’s bankruptcy filing

was a substantial abuse of the Bankruptcy Code, as the debtor's debts were primarily consumer debts and the debtor had the present and future ability to pay creditors. Hall, 258 B.R. at 46. However, in response, the debtor argued that her debts were primarily business debts, making section 707(b) of the Code not applicable. Id. at 47. In ruling on the motion, the Court in Hall first had to determine whether the debtor's debts were primarily consumer debts. Id. at 48.

In Hall, the debtor had mortgage debt on her marital home, but since the divorce court had ordered only her former husband to pay the mortgage on the marital home, the debtor reasoned that the mortgage debt was merely a contingent debt and should be excluded from the Court's determination. Id. at 48. The Court in Hall disagreed with the debtor, relying upon the leading case, In re Kelly, 841 F.2d 908, 913 (9th Cir. 1988), wherein the Ninth Circuit considered the definitions of "debt" and "claim" as set forth in the Bankruptcy Code and concluded that debt secured by real property should be included in the determination of whether a debt is primarily consumer debt. Id. at 48. Moreover, the Court in Hall held that a contingent debt must be considered in its determination as to whether the debtor's debts are primarily consumer debts, under section 707(b) of the Bankruptcy Code. Id. at 49.

In conclusion, it is important to keep in mind that there are instances where a bankruptcy court will consider equitable and contingent debts that the debtor is not specifically obligated on, in his or her name directly, such as, in making its determination as to whether or not a bankruptcy case should be dismissed, pursuant to section 707(b)(1) of the Bankruptcy Code.

Iurillo & Associates, P.A., located in downtown St. Petersburg, is comprised of **Camille J. Iurillo**, Shareholder, **Gina M. Pellegrino**, Associate, and **Sabrina C. Beavens**, as Of Counsel. **Ms. Iurillo** has been active in the St. Petersburg Bar Association for several years, and she is on the Executive Committee of The Florida Bar's General Practice Solo and Small Law Firm Section. **Ms. Pellegrino** joined the Firm in 2006 and is an active member of the St. Petersburg Bar Association Young Lawyers Section.

The primary areas of practice of **Iurillo & Associates, P.A.** are Commercial and Bankruptcy Litigation and Debtors' and Creditors' Rights.