BANKRUPTCY "MEANS TEST" SYNOPSIS

With the passage of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (Public Law 109-8), before you can file either Chapter 7 or 13, you must pass muster under a "means test". The means test identifies those debtors who have the financial capacity to pay a significant portion of their debt to creditors. It involves comparing the debtor's income to the median income of the state where the debtor is located. If the debtor's income is higher, another set of calculations (based on ratios of debt to income) will identify whether he or she can file a Chapter 7 liquidation or Chapter 13 repayment case. In essence, a person must now qualify financially in order to file a Chapter 7 case.

The means test (Official Form 22A) is a form where a person must calculate the average income they have received over a period of six months prior to filing. For instance, if a person wanted to file a bankruptcy case on March 15, 2009, they would calculate all of the income the person received from September 1, 2008 through and including February 28, 2009, and then divide by six. This average would be the person's current monthly income (CMI) even though this may not be the person's actual current monthly income. If the individual filing is married, the spouse's income must also be calculated in the same manner regardless of whether the spouse is filing or not. Once the CMI is calculated, it is then compared to the national median income of the area in which the person lives. In short, if the person lives in Hillsborough County, their CMI will be compared to the median income in Hillsborough County. If the person's CMI is lower than the national median, the person is eligible to file a Chapter 7. This is what is considered the "short form." If the person's CMI is higher than the national median, the "long form" is utilized which will take into consideration the person's expenses.

The long form of the means test takes into consideration the person's living expenses such as mortgage payments, car payments, medical expenses, child care, etc. in addition to the national median for utilities and food. Other expenses that can help reduce the CMI is telecommunications (cell phone and telephone bills) as well as education expenses for private schooling and/or expenses for providing care for relatives such as an elderly parent or disabled child. A person could also reduce their CMI for extraordinary circumstances for expenses higher than the national median for utilities and food but would need receipts to verify the expense. Examples of such extraordinary circumstances are severe allergies or other medical conditions needing a special diet consisting of organic foods or other items that cause expenses to be higher than the national median.

The long form also takes into consideration the ability to pay secured creditors. A secured creditor is any creditor that holds collateral against payment. Secured creditors consists of mortgage holders, car loans, or any other item that can be repossessed for non-payment. As part of the long form calculations, payments to secured creditors are calculated over a period of five years (sixty months). An example of this calculation would be if a person has a mortgage payment of $1,000 for 30 years, the $1,000 payment would be calculated at $1,000 per month for 5 years. Another example would be if a person has a car loan of $500 but only as 48 payment left, the payment calculation would be $400 per month for 5 years ($500 multiplied by 48 divided by 60). Another consideration in the long form is whether or not there are any arrearages on the secured claims. If the person has any past due balances for secured creditors, the past due amounts are calculated over a period of 5 years as well. For example again using the $1,000 mortgage payment, if the person is one month behind on the mortgage payment the $1,000 is divided into 60 equal payments of $16.66. All of these factors are calculated and a final determination is made as to whether a person's income is higher or lower than the national median. Utilization of the long form qualifies many people for Chapter 7 even though they may have a higher income. In this way, income to debt ratio is taken into consideration.

Legally speaking, a person still could file a Chapter 7 even if their CMI was above the national median. However, this is a caution to such approach as the Chapter 7 would more than likely be objected to and thus dismissed or converted to a Chapter 13. In order to save the consumer time, effort, and money, the best option would be to file a Chapter 13 case with a $0 payment plan. In essence, a person could discharge their debts in a Chapter 13 much the same as a Chapter 7, provided that the person does not have any disposal income with which to pay creditors. An attorney could further advise you based on the circumstances of your case.