

**American Board of Certification  
General Bankruptcy Law  
Multiple Choice Sample Questions**

NOTE: The Bankruptcy Multiple-Choice exam contains 50 questions. You must correctly answer 60%, or get at least 30 correct. We offer 16 sample questions here to give you an idea of the scope of the questions you are likely to encounter, as well as the types of subject matter covered.

1. During the pendency of the case and without obtaining an order lifting or modifying the automatic stay, the child support claimant may not take the following action:
- a. levy upon Don's exempt property.
  - b. garnish the wages Don will earn next week.
  - c. commence an action in state court to increase the amount of child support.
  - d. levy on property of the estate.

***D is correct. A levy on exempt property is allowed under § 522(c)(1). B and C (garnishment of postpetition wages and modification of child support actions) are allowed under § 362(b)(2).***

2. Don Debtor's principal residence, worth \$120,000, is subject to two encumbrances: (1) a first mortgage for \$100,000; and (2) a judicial lien in favor of Credit Card Inc. for \$60,000 that is junior to the mortgage in priority. Assume that under the relevant state's law, Don is entitled to claim a \$30,000 homestead exemption in the home. If Don files a petition under Chapter 7 and brings a lien avoidance action under §522(f), how much, if any, of the lien can be avoided?
- a. \$0, because the lien is not avoidable in any amount.
  - b. \$40,000, because that is the amount by which the sum of the mortgage and the lien exceeds the value of the residence.
  - c. \$30,000, because the lien is avoidable only to the extent of the exemption.
  - d. \$50,000, because the sum of the first mortgage and the exemption exceed the value of the home.

***D. is correct. Section 522(f)(2)(A) calculates impairment by adding the challenged judicial lien, all other liens, and the exemption, and then subtracting the value of the debtor's interest from that sum. The remainder is the amount that may be avoided. In this case, the \$60,000 judicial lien, the \$100,000 mortgage and the \$30,000 exemption = \$190,000, which exceeds by \$70,000 the value of the home. Because this sum is greater than the amount of the judicial lien, the whole lien may be avoided.***

3. In a Chapter 7 case, in order for a non-tax claim of a governmental unit to be timely, when must it be filed?

- a. within 90 days after the date of the order for relief
- b. within 90 days after the first date set for the §341 meeting of creditors
- c. within 180 days after the date of the order for relief
- d. within 180 days after the first date set for the §341 meeting of creditors

***C is correct under Bankruptcy Rule 3002(c)(1), which treats all government claims as timely if filed within 180 days of the order for relief. Other claims must be filed within 90 days after the first date set for the meeting of creditors.***

4. Prior to filing bankruptcy, the electric utility was threatening to discontinue service because the debtor owed \$1,000 in past-due charges for electrical service. If the debtor furnishes adequate assurance of payment for post-petition service, then:

- a. the electric utility can discontinue electrical service because of the unpaid pre-petition charges
- b. the debtor can continue to receive electrical service without paying the pre-petition charges
- c. the debtor can continue to receive electrical service only by paying \$1,000 for the pre-petition service
- d. the debtor can continue to receive electrical service only by promptly curing the pre-petition default and assuming the service contract under § 365

***B is correct. See § 366(b).***

5. Donna Debtor filed a voluntary petition under Chapter 7 on February 1. Almost two years earlier, Donna was libeled by Larry Lie. Under the relevant state statute of limitations, Donna had until April 1 to file a legal action against Larry. Tom Trustee was appointed as trustee in Donna's Chapter 7 case on March 1. The time within which Tom Trustee may commence a legal action against Larry on behalf of the estate expires:

- a. on April 1
- b. sixty days after February 1
- c. two years after February 1
- d. two years after March 1

***C is correct. See § 108(a).***

6. On Monday, June 1, the Bankruptcy Court announced its decision in a core proceeding from the bench. On Friday, June 5, a judgment was entered consistent with the decision announced from the bench. Absent an extension, if you wish to appeal the Bankruptcy Court's decision, your notice of appeal must be filed:

- a. within ten calendar days of June 1
- b. within ten calendar days of June 5
- c. within twelve calendar days of June 1, because the intervening Saturday and Sunday are excluded from the computation
- d. within twelve calendar days of June 5, because the intervening Saturday and Sunday are excluded from the computation

***B is correct. See Fed. R. Bankr. P. 8002(a), Fed. R. Bankr. P. 9006(a).***

7. This morning Donna Debtor filed bankruptcy. She owes Big Bank \$3,000 on an unsecured loan and has \$2,000 on deposit in her checking account. Under the relevant state law, Big Bank has a right to set off the checking account balance against the loan debt, but had not yet done so when the bankruptcy filing was made. Which of the following is most likely correct?

- a. Big Bank may place an administrative “freeze” on the account without obtaining court permission to do so
- b. Big Bank must turn over the account to the chapter 7 trustee
- c. Big Bank may set off the account against the loan debt without obtaining court permission to do so
- d. Big Bank no longer has a right of setoff, because the Bankruptcy Code does not respect state rights of set off

***A is correct. See Citizens Bank v. Strumpf, 516 U.S. 16 (1995). B is incorrect because of § 542(b). C is incorrect because of § 362(a)(7). D is incorrect under § 553(a).***

8. Which of the following statements about bankruptcy discharges is the most accurate?

- a. In a chapter 7, the debts are discharged 60 days following the first date set for the meeting of creditors.
- b. In a chapter 11, the confirmation of a plan discharges the debtor from any debt that arose before the date of confirmation
- c. In a chapter 13, the confirmation of a plan discharges the debtor from any prepetition debt, but not any debt arising after the filing
- d. A “superdischarge” under chapter 13 may be granted even if the distributions made pursuant to the plan are less than the unsecured creditors would have received if the debtor had been liquidated in a chapter 7

***B is correct. A is incorrect under § 727 (although objections to discharge must be filed within 60 days following the first date set for the meeting of creditors under Fed. R. Bankr. P. 4004(a). C and D are incorrect under § 1328.***

9. Howard has been a little lax in his payment of income taxes. In fact, he has not filed a return since 2003. Assuming he files for Chapter 7 bankruptcy in May, 2009, how will his tax liabilities be handled in the case?

- a. his tax liabilities for each of the years for which he did not file a tax return will be priority claims

- b. a proof of claim filed by the government will be timely only if it is filed not later than 90 days after the first date set for the meeting of creditors
- c. his tax liabilities for 2006 – 2008 will not be discharged even if no claim is filed by the government
- d. an action may be brought in the United States Tax Court to determine Howard's tax liability for any prepetition period without violating the automatic stay

***C is correct under § 523(a)(1). A is incorrect under § 507(a)(8) because only the 2006-2008 tax liabilities would be priority claims. B is incorrect under Fed. R. Bankr. P. 3002(c)(1), which gives the government 180 days after the date of the order for relief, subject to extension. D is incorrect under § 362(a)(8).***

10. Debtor Inc. is in deep financial trouble. It has dozens of creditors and it has stopped paying its monthly bills. Among its creditors are three suppliers, Supplier A, Supplier B, and Supplier C. Each is owed \$2,000 in unsecured trade debt. Debtor Inc. also owes \$12,000 to Electric Co. for past due electrical bills. Another creditor is Contractor Inc., which asserts a \$12,000 unsecured breach of contract claim. Debtor Inc. disputes the Contractor Inc. claim and asserts, in good faith, that Contractor Inc. committed a material breach of the contract and is entitled to no payment whatsoever. Debtor Inc.'s only secured creditor is Finance Co. Finance Co. is owed \$15,000 and holds a perfected security interest in Debtor Inc.'s delivery truck, which has a value of \$6,000. Assume that the bankruptcy court will order relief against Debtor, Inc. if a proper involuntary petition is filed under §303 of the Bankruptcy Code. The petition will be successful if:

- a. Supplier A, Supplier B, and Finance Co. join in the petition.
- b. Supplier A, Supplier B, and Contractor Inc. join in the petition.
- c. Supplier A, Supplier B, and Electric Co. join in the petition.
- d. Electric Co., alone, files the petition.

***C is correct. Under § 303, if there are more than 12 unsecured creditors holding claims not contingent as to liability or the subject of a bona fide dispute as to liability or amount, three or more such creditors holding claims aggregating at least \$13,475 may file an involuntary petition. The***

**claimants in A have only \$13,000 of unsecured debt. (Finance Co. has a \$6,000 secured claim and a \$9,000 unsecured claim under § 506). The claimants in B include Contractor, whose claim is disputed. D does not include three creditors.**

11. In a divorce decree entered in a divorce action in a state court of record, Don Debtor was ordered to pay \$500 per month in child support to his ex-wife for the support of the minor children of the marriage. Don was \$1,000 in arrears on the child support payments at the time he filed Chapter 7. Which of the following statements is the most accurate?

- a. The automatic stay will prevent the collection of the \$1,000 arrearage from Don's future wages.
- b. The automatic stay will prevent the collection of future support payments from the property of Don's Chapter 7 estate.
- c. The automatic stay will prevent the collection of future support payments from Don's future wages.
- d. Don may be discharged from his past-due child support payments in the bankruptcy case.

***B is correct because §362(b)(2) exempts from the stay the collection of support from property that is not property of the estate. Thus, regardless of whether the support obligation accrued pre-petition, only collection against property of the estate is stayed. Since Don's future wages will not be property of his Chapter 7 estate, A & C are incorrect. D is incorrect under § 523(a)(5).***

12. May a plan of reorganization in a chapter 11 be confirmed if it violates the best interest of creditors test under §1129(a)(7)?

- a. Yes, so long as each class of creditors approves the plan by a vote of more than one-half in number and at least two-thirds in amount
- b. Yes, but only in a cramdown plan
- c. Yes, as long as no holder of an impaired claim has objected to confirmation of the plan on this ground
- d. No

***C is correct because the protection of §1129(a)(7) applies only to an impaired claimant who objects to the plan. A class vote cannot affect the individual creditor's rights, so A is incorrect. A cramdown plan under § 1129(b) must satisfy § 1129(a)(7), so B is incorrect. D is incorrect because the court may confirm the plan if no objection is made.***

13. Assume that an undersecured creditor makes the §1111(b) election in a Chapter 11 case. Which of the following statements is not accurate?

- a. The creditor must receive payments under the plan at least equal to the amount of its allowed claim.
- b. The creditor must receive payments under the plan having a present value at least equal to the value of the collateral securing its claim.
- c. The creditor loses its unsecured deficiency claim.
- d. The creditor must receive or retain under the plan on account of its claim property of a value, as of the effective date of the plan, that is not less than the amount that such creditors would so receive or retain if the debtor were liquidated under chapter 7 on such date.

***D is the best answer, because it is the incorrect statement. A and B are correct under the language of the §1129(b)(2)(A)(i)(II). C is correct under §1111(b)(2). D is incorrect because under § 1129(a)(7)(B), the holder of a claim held by an electing § 1111(b) creditor is not entitled to the same treatment as the other impaired creditors.***

14. On January 1, Debtor Inc., a company with more than \$100,000,000 in unsecured debt, filed a voluntary petition under Chapter 11. On February 1, a trustee was appointed in Debtor Inc.'s Chapter 11 case. Which of the following statements is correct (in the absence of a special court order)?

- a. Debtor Inc.'s right to file a plan terminated on February 1.
- b. A creditor may file a plan only if Debtor Inc. fails to file a plan within 120 days after January 1.
- c. A creditor may file a plan only if Debtor Inc. fails to file a plan that has been accepted within 180 days after January 1.
- d. A creditor may file a plan on or after February 1.

***D is correct because the debtor's exclusive plan period expires upon the trustee's appointment under §1121(c)(1). A is incorrect because the debtor may file at any time under §1121(a). B and C are incorrect because they relate to time periods that would be applicable under §1121(c) if no trustee was appointed.***

15. On January 10, Debtor Inc. filed a voluntary petition under Chapter 11 and a trustee was appointed. On February 10, the trustee deposed the pre-bankruptcy attorney of Debtor Inc. and inquired into the contents of pre-bankruptcy attorney-client conversations between the attorney and the officers of Debtor Inc. If the attorney refuses to answer and asserts the attorney-client privilege:

- a. the attorney-client privilege will prevent the trustee from discovering the contents of the conversations
- b. the attorney can be required to testify because the attorney-client privilege does not apply in a bankruptcy case
- c. the trustee can waive the privilege on behalf of Debtor Inc. and require the attorney to testify
- d. the trustee can not waive the privilege because Debtor Inc. is a corporation and only the Board of Directors can waive the privilege

***C is correct under CFTC v. Weintraub, 471 U.S. 343 (1985).***

16. At the time the Chapter 11 petition was filed, Debtor Inc.'s pre-bankruptcy accountant was in possession of certain records relating to Debtor Inc.'s financial affairs. Although the records relate to Debtor Inc., they are the property of the accountant. The accountant was paid in full before bankruptcy and has not filed a claim or otherwise appeared in the case. If the trustee seeks an order requiring the accountant to turn over the records:

- a. the accountant can block the turnover request by asserting the accountant-client privilege
- b. the accountant can be required to turn over the records because the accountant-client privilege does not apply in a bankruptcy case
- c. the accountant can block the turnover request by asserting his/her ownership of the records

- d. the bankruptcy court lacks jurisdiction over the accountant because he/she is not a creditor and has not filed a claim or otherwise appeared in the case.

***B is correct because the accountant-client privilege is not recognized under federal law. In re International Horizons, Inc., 689 F.2d 996 (11th Cir. 1982). Thus A is incorrect. C is incorrect because §542(e) permits turn over regardless of ownership. D is incorrect because the § 542 power does not turn on the creditor status of the accountant.***

## **American Board of Certification -- Sample Exam**

### **Bankruptcy Ethics**

#### **Answer Two Questions out of Four**

#### **Total Time -- One Hour**

NOTE: The following questions and sample answers are based on questions used in past examinations. The sample answers are based on the status of the law as of the date the questions were written. In some instances, the sample answer may no longer reflect the prevailing view of the law. Although an excellent paper would discuss in detail all of the issues raised in the sample answer, a paper may receive a passing grade even though the analysis is less thorough. Historically, approximately 80 percent of the Ethics papers have received a passing score.

### **QUESTION A**

#### **(Suggested Time - One-Half Hour)**

You represent an individual in a Chapter 7 case who owns a vehicle pledged to secure the claim of Bank. The vehicle was purchased new in 2009. The monthly debt payments and insurance payments consume all of the individual's disposable income and actually exceed the rental payments on the Debtor's house. Even though it is not in the Debtor's best interest to keep the vehicle, the Debtor is proud of the vehicle and does not want to give it up. The Bank is willing to reaffirm the debt, but only if the original Note terms are reaffirmed. The vehicle is used primarily for pleasure and is not necessary for the Debtor's employment.

Can you represent your client in connection with a reaffirmation of the debt? Be sure to identify the state where you practice and indicate, if you know, whether the ethical rules in your jurisdiction are patterned after the ABA Model Code of Professional Responsibility (usually numbered as "DR 2-105," etc.), the ABA Model Rules of Professional Conduct (usually numbered as "Rule 7.4," etc.), or neither.

### **QUESTION B**

#### **(Suggested Time - One-Half Hour)**

You represent a husband and wife who filed joint Chapter 7 petitions. Both Debtors received their discharges several months ago, but the case has not yet been closed. You have been contacted by the husband, who explains that his wife has filed for divorce. He wants you to represent him in the divorce case.

Can you represent him? Be sure to identify the state where you practice and indicate, if you know, whether the ethical rules in your jurisdiction are patterned after the ABA Model Code of Professional Responsibility (usually numbered as "DR 2-105," etc.), the ABA Model Rules of Professional Conduct (usually numbered as "Rule 7.4," etc.), or neither.

### **QUESTION C**

#### **(Suggested Time - One-Half Hour)**

Your firm has represented Debtor Inc. for many years. The corporation has been slow in paying your fees, but always seems to come up with the money by the end of the year. The corporation has not made any payments in more than four months and currently owes the firm for fees and expenses extending over a six month period. Those fees relate to general corporate matters, and were not incurred in connection with or in contemplation of a bankruptcy filing.

Debtor Inc. has been unable to obtain an extension on its line of credit with Bank, and Bank is threatening to take immediate action to collect all accounts receivable. Debtor Inc. wants your firm to represent it in a Chapter 11 case and is willing to use its available cash to bring your firm current and to pay a retainer sufficient for you to undertake the representation. Debtor, Inc. also has unencumbered real property that it has offered to pledge to secure the payment of both past fees and future fees.

Please discuss the following questions. Be sure to identify the state where you practice and indicate, if you know, whether the ethical rules in your jurisdiction are patterned after the ABA Model Code of Professional Responsibility (usually numbered as "DR 2-105," etc.), the ABA Model Rules of Professional Conduct (usually numbered as "Rule 7.4," etc.), or neither.

- 1) May you represent Debtor Inc. in its bankruptcy case?
- 2) May you accept the proposed payments, retainer and pledge of unencumbered real property?

### **QUESTION D**

#### **(Suggested Time - One-Half Hour)**

You represent Bank, which has a duly perfected security interest in the inventory and accounts receivable of Debtor Inc. Debtor Inc. has not asserted any challenge to the perfection of your security interest, but has not been willing to acknowledge that this interest is unavoidable. You, as counsel for Bank, are not aware of any facts that would support an avoidance claim of Bank's interest. A Trustee has been appointed in Debtor Inc.'s case and is in the process of liquidating assets. The Trustee has refused to give Bank relief from stay and asserts that the Bank is fully secured.

The Trustee has initiated multiple preference actions against various trade creditors. The local rules require local counsel to represent any corporation in Bankruptcy Court. Your firm has been contacted by several preference defendants to represent them on the preference actions that have been brought against them. Each of the actions was brought as a separate adversary proceeding, and all are unrelated to each other.

Please discuss the following questions. (Be sure to identify the state where you practice and indicate, if you know, whether the ethical rules in your jurisdiction are patterned after the ABA Model Code of Professional Responsibility (usually numbered as DR 2-105," etc.), the ABA Model Rules of Professional Conduct (usually numbered as "Rule 7.4," etc.), or neither.)

- 1) May you represent the Bank and one of the trade creditors?
- 2) May you represent more than one of the trade creditor?

### **SAMPLE ANSWER TO QUESTION A:**

Under § 524(c) any reaffirmation agreement which is filed with the court must be accompanied by a declaration of the Debtor's attorney stating that the agreement does not impose an undue hardship on the Debtor or a dependant of the Debtor. Under the facts of this case, it appears clear that any reaffirmation would impose an undue hardship on the Debtor and, thus, the attorney could not truthfully make the required declaration. The § 524 declaration presents a conflict for the attorney between his/her duty to zealously represent the client and the duty of candor owed to the court. Because the ethical rules prohibit the lawyer from making false statements in connection with his/her representation of the client, the lawyer must decline to file the declaration. The following options are available:

1. The attorney can withdraw as the Debtor's attorney and the Debtor could present the agreement to the court pursuant to § 524(c)(6) under which the court must approve the agreement as not imposing an undue hardship on the Debtor and being in the best interest of the Debtor.
2. Convince the Debtor that the Debtor should not enter into the reaffirmation agreement and should surrender the vehicle and purchase a less expensive means of transportation.
3. Explore the feasibility of the Debtor confirming a Chapter 13 plan and consider conversion to Chapter 13.

The key issue is that the attorney recognizes the dilemma caused by having to file an attorney declaration with the reaffirmation agreement.

### **SAMPLE ANSWER TO QUESTION B:**

Two related problems are presented here. First, the attorney has an obligation to both the husband and the wife to protect confidences and secrets. Further, the attorney should not use information acquired in the course of representing a client to the disadvantage of the client. This obligation continues after the termination of the employment. Here, it is likely that the attorney may have learned quite a bit about the wife's assets, interests, etc. that might be used against her in the divorce action. If so, then the representation would not be proper.

Next, the attorney must consider the potential for a conflict of interest. The analysis varies depending upon whether the attorney has completed the representation of the joint Debtors. If both Debtors are current clients, then the general rule would prohibit the proposed representation because the Debtors are directly adverse in the divorce action. Further, this conflict probably could not be waived because representation of the husband in the

divorce likely would adversely affect the attorney's relationship with the wife. Here, since the Chapter 7 case has not been closed, the representation would be continuing. Even if the representation has been concluded, there may still be a conflict that prevents the representation of the husband. The lawyer must first determine whether the divorce action is substantially related to the bankruptcy and whether the obligations to the wife (the duty of confidentiality for example) will impair his/her ability to exercise independent professional judgment. Because many issues will overlap, it is likely that the matters are substantially related and thus, the attorney must make full disclosure to the wife and gain her consent before representing the husband in the divorce. However, if the duties to the wife (such as confidentiality) will adversely affect the attorney's representation of the husband, the representation should be declined.

The key issue is that the attorney recognizes the obligation to protect confidences and secrets of the wife and recognize the conflict of interest.

### **SAMPLE ANSWER TO QUESTION C:**

1. Section 327 permits a debtor to employ an attorney that is disinterested as defined under § 101(14) and does not hold or represent an interest adverse to the estate. Technically creditor status would cause the attorney not to be disinterested under § 101(14). Thus, to represent Debtor Inc. either you must waive your pre-petition fees or be paid in full prior to the filing of the bankruptcy petition. The acceptance of payments, however, may disqualify you as well. While you may be disinterested as technically defined under the Code, the acceptance of a preference may cause you to hold or represent an interest adverse to the estate and thus still disqualify you under § 327. This is a fact issue that would be determined by the court on a case-by-case basis and would depend upon the amount of the preference and perhaps the likelihood that the creditors would not be paid in full.

2. Debtor's cash – that it proposes to use to pay your bill and to create the retainer – may constitute proceeds of Bank's collateral. Generally a transferee of money takes it free of a security interest unless the transferee acts "in collusion" with the debtor in violating the rights of the secured party. UCC § 9-332(a). As a lawyer, you may be found to be acting in collusion, in which case the funds would remain subject to the Bank's security interest.

Most courts have permitted security interests intended to secure post-petition services. The most notable of these is In re Martin decided by the First Circuit in 1987. Securing pre-petition fees would mean that the firm is a creditor and thus not disinterested. It would also constitute a preference and would be avoidable. In considering whether a pledge of assets to secure post-petition fees should be allowed courts look at such factors as:

1. Reasonableness of the arrangement.
2. Whether the fee arrangement was negotiated.
3. Whether the security was commensurate with the magnitude and value of the future services.
4. Whether the security was a necessary means to insure engagement.
5. Whether there are signs of overreaching.
6. The nature and extent of any potential conflict of interest.
7. The likelihood that the potential conflict may turn into an actual conflict.
8. Whether the potential conflict may influence the attorney's subsequent decision making.
9. Whether the arrangement appears improper to other parties in interest.
10. Whether the existence of the security interest threatens to hinder or delay effectuation of a plan.
11. Whether fundamental fairness may be unduly jeopardized.

**SAMPLE ANSWER TO QUESTION D:**

1) A lawyer should exercise independent professional judgment on behalf of a client. This means that the lawyer must weigh carefully the possibility that his judgment may be impaired or his loyalty divided if he accepts or continues employment of multiple clients. He should resolve all doubts against the propriety of the representation and should not represent in litigation multiple clients with different interests if that would adversely affect the representation. If the interests vary only slightly and he can retain his independent judgment on behalf of each client, the client must be given the opportunity to evaluate his need for representation free from potential conflict and obtain other counsel if the client so desires. Thus, the attorney must make full disclosure to the clients and obtain their consent to the multiple representations. It would also be important for the attorney to consider the disruptive effect that withdrawal might have if the potential conflicts of interest become actual conflicts.

There always exists a conflict between a secured creditor and an unsecured creditor. In this case, even though the security interest of Bank

appears to be uncontested, it has not been determined to be valid and thus is subject to attack by other creditors. Additionally, the value of the collateral has yet to be determined and the parties may have different interests as to how the property would be sold. Thus, it would be problematic for a firm to represent both an unsecured and a secured creditor unless all issues regarding the security interests and the value of its collateral have been previously determined.

2) As for representing more than one of the trade creditors, it is likely that their interests would be very similar, although the goal of each creditor is to maximize the preference recovery from the other creditors and minimize the preference recovery from that creditor. Once the amount of the claims is determined, however, the interests would be identical. Whether you could represent more than one defendant in a preference action would be determined on a case-by-case basis. Important factors would be:

1. The amount of the preference claim in relation to the other potential clients; and
2. The common defenses that the parties may have.

If the amounts are relatively equal and the defenses are the same, then it is likely that the attorney would be able to represent each without impairing his independent professional judgment. A practical problem exists in small communities where there may be more claims than attorneys. In such instances, competent local counsel may be very difficult to find unless local attorneys represent multiple clients.

**American Board of Certification -- Sample Exam  
Consumer Sub-Specialty Essay  
Answer Two Questions  
Total Time -- 3 Hours plus a 15 Minute Reading Period**

NOTE: The following questions and sample answers are based on questions used in past examinations. In some instances, the sample answer may no longer reflect the prevailing view of the law. Although an excellent paper would discuss in detail all of the issues raised in the sample answer, a paper may receive a passing grade even though the analysis is less thorough. Historically, more than 90 percent of the Consumer papers have received a passing score.

**Question A**  
**(Suggested Time - 1 1/2 hours)**

Don Debtor, a 44 year old single man, was doing O.K. until he got sick in late March 2008. His illness forced him to quit his job and caused him to incur substantial medical bills. Don is now in good health and was rehired by his employer in early September 2008. He has come to you for help handling the debts he incurred while ill.

Don's employer, Giny Goodheart, has been good to him. Don earns \$500 per week in take home pay. Unfortunately, two weeks ago, Don's salary was garnished by Mel Practice, a doctor who had obtained a \$1,000 judgment against Don for an unpaid medical bill. Don asserted his rights under the federal garnishment limitation statute and his employer withheld only \$125 from each week's paycheck (for a total of \$250 so far). Under state law, the service of the garnishment summons creates a lien on the garnished wages as of the date of service. No funds have yet been turned over to the Court or to Dr. Practice. Under state law, the garnished funds will be turned over to the Court by the employer on the return date, which is six weeks hence. Giny Goodheart was so upset about the garnishment and Don's other problems that she made a personal loan to Don of \$2,000 to help him out. Don has promised to pay her back at the rate of \$200 per week as soon as the garnishment ends. Don is very mad at Dr. Practice for garnishing Don's wages just as he was getting back on his feet and he wonders what can be done about the garnishment.

While he was ill, Don was unable to make his monthly mortgage payments of \$900. He is now six months in arrears. Big Bank has filed for foreclosure and, yesterday, Don received a notice that the foreclosure sale will be held in 30 days. Although he has no equity in the house, Don would like to delay the foreclosure to give himself more time to work out a payment plan with Big Bank.

Don also missed three of the \$300 monthly payments on his car. The secured creditor, Auto Mart Inc., is willing to work with Don and would be happy to restructure the loan as long as there is no reduction in either the principal balance or the interest rate. Unfortunately, Don still owes \$8,500 on the car and it is only worth \$4,500 wholesale and \$5,000 retail. Further, the contractual interest rate is 13.5%. Don really needs the car and, because of his recent financial problems, will not be able to obtain financing for a different car.

While Don was unemployed, he had to rely on credit to cover living expenses and to cover the costs of his expensive prescription drugs. Since his credit had been good prior to his illness, he had a \$15,000 credit limit on his Master Card and only a \$4,000 balance. During the first three months of his illness (April through June of 2008), Don was very sick and his doctors told him that he had only a very small chance of survival. During that period, Don charged \$4,000 in prescription drugs and \$3,000 in cash advances to cover living expenses (and the minimum payment on the charge card).

Don's health improved rapidly during the next two months. During that period (July and August of 2008), Don charged \$3,000 in prescription drugs and \$1,500 in cash advances to cover living expenses (and the minimum payment on the charge card). Don knew that he was exceeding his credit limit and in mid-August he was notified by Master Card that he was \$500 over his \$15,000 credit limit and that no further charges would be honored. Don was desperate, but, just in the nick of time, on August 20th, Don received an unsolicited, "pre-approved" credit card from Crazy Credit. The mailing included a check for \$2,000 and the following instructions:

"You are pre-approved! No applications forms, no credit check, just MONEY MONEY MONEY to use as you wish. Old bills got you down? Need a get away vacation? Or, just MAD money? All you need to do to activate your account is SIGN AND DEPOSIT THE ENCLOSED CASH ADVANCE CHECK."

Don signed the check, deposited it in his checking account, and used it for living expenses. In the past two months, Don has made no further charges. Although Don knew that he would survive his illness by early July, he also knew by then that he was deeply in debt, and he had been advised by his employer that his position had been filled and that there was virtually no chance he would be rehired. (As it turned out, the employee who replaced Don quit abruptly in early September and Don was rehired.)

Don has one other problem that he finds embarrassing. Early last year he discovered that his long-time girlfriend, Sara Sweet, was two-timing with another man, Sam Slime. Don broke off the relationship and heard nothing further until last December when he was served with a complaint in a state court paternity action. Don is convinced that the child's father is Sam and that Sara named Don only because Sam is a bum and has never held a steady job. Don was so sure he would win ("The kid looks just like Sam") that he represented himself in the paternity action. Don lost and the state court ordered him to pay \$200 per month in child support, and also ordered him to pay \$1,000 directly to Ann Attorney for attorney's fees earned in establishing paternity. Don did not appeal, but he is convinced that a blood test would prove he is not the father. Don has made no payments and would really like you to do something to relieve him of this obligation. Since the child has been living on public assistance, the \$1,800 in past due support payments have been assigned to the state Department of Child Welfare.

Don's debts, including those discussed above are set out below:

Big Bank (mortgage)	\$100,000
Auto Mart, Inc. (car loan)	<u>8,500</u>
Sub Total	\$108,500
Happy Hospital	\$28,000
Mel Practice	1,000
Giny Goodheart	2,000

Master Card	15,500
Crazy Credit	2,000
Dept. of Child Welfare	1,800
Ann Attorney	<u>1,000</u>
Sub Total	\$51,300
 TOTAL	 \$159,800

Since Don exhausted his savings while he was sick, he has relatively little in the way of assets. In addition to the house and car discussed above, Don has \$20,000 in an ERISA qualified retirement plan and \$1,000 in cash in his checking account. Don is also owed \$4,000 for a federal income tax refund. Since Don was sick, he filed his 2008 return only four weeks ago. A friend at the IRS checked the computer for Don and discovered that Don's return has been processed and that the refund check will be issued next week. You have reviewed Don's budget and it appears that he needs about \$400 to \$500 per month to cover his basic living expenses other than housing and transportation (not counting his child support obligation).

Don has expressed concern about his elderly father. It seems that a few years ago his father placed his life's savings in a joint bank account titled in both Don's and his father's names. Don has never deposited money into the account and has never withdrawn money from the account. The joint tenancy account was set up solely as a device to avoid probate. There is currently \$50,000 in the account. Since Don's father is in good health and is expected to live for many years, he will need those funds and Don does not want to do anything that might harm his father.

Don has also indicated that he wants to "Treat Giny right" both because she helped him out and because he is afraid she might fire him if he doesn't repay her loan. In addition, he wonders about the effect of bankruptcy on his credit.

Analyze and discuss Don's options under Chapter 7 of the Bankruptcy Code. Do not discuss Chapter 13 issues, unless they are essential to the resolution of the Chapter 7 issues. Be sure to support your conclusions with appropriate discussion of the applicable law and of your reasons for taking the action(s) proposed. You should assume that the applicable state exemption law is identical to § 522(d) of the Bankruptcy Code.

1. When will you file Don's petition?
2. How will the filing affect Don's credit?
3. Is Don eligible for chapter 7?
4. How can Don deal with his debt to Giny?
5. How will the bankruptcy affect the garnishment?

6. Can Don keep the car in a bankruptcy?
7. Will the ERISA plan and the joint bank account be included in the bankruptcy estate?
8. What property may Don exempt?
9. Will any of Don's debts be excluded from discharge?

### **SAMPLE ANSWER TO QUESTION A:**

1. A number of factors must be considered in determining when to file Don's petition. Since the stay will stop the garnishment, he may wish to file immediately. On the other hand, if he wishes to attempt to recover the garnished funds as a preference (see below), he may prefer to wait until the total sum exceeds the § 547(c)(8) \$600 limit. Since he is already beyond the § 523(a)(2)(C) 20-day "cash advance" period for non-dischargeability of the credit card charges, that is not a factor here. The imminent receipt of the tax refund must be considered. If Don wishes to and can exempt the refund, he can file before its receipt. If he can not exempt all of it, then he may wish to wait until after he receives the refund. He can then use the non-exemptible part of the refund to pay Giny or other potentially non-dischargeable debts (preferably paying less than \$600 to each in order to avoid the possibility of a preference recovery by the trustee).

The most important timing consideration, however, is the foreclosure of the home. If the foreclosure is complete before he files, the stay is inapplicable and he can not take advantage of any state redemption period.

Under the BAPCPA amendments, Don is not eligible for bankruptcy unless he has, within the 180-day period preceding the filing, obtained credit counseling under § 109(h). Some courts will excuse prebankruptcy counseling in the case of a pending foreclosure under the exigent circumstances exception of § 109(h)(3), but others do not.

2. Don's concern about his credit is legitimate and he should be advised that the bankruptcy will present a serious problem to him in the future. However, his credit is already bad and will likely get worse if the foreclosure proceeds, and the credit card companies and hospital bring suits, obtain judgments, and institute garnishments. Thus, there may be little additional negative impact from the bankruptcy. Indeed, some creditors may view him as a better credit risk because of the effect of the discharge on his cash flow, especially if he demonstrates an ability to use credit responsibly in the future. Under the Fair Credit Reporting Act, the bankruptcy can show up on his credit report for 10 years (or longer for credit transactions over \$50,000).

3. Although there is a possibility of dismissal under § 707(b), it seems unlikely here for several reasons. Don's current monthly income seems to be about \$2,160, an

annual amount of \$26,000. This is likely to put him below the median family income for his state. Therefore, pursuant to § 707(b)(7), no party in interest may move for dismissal under the presumption of abuse means-test of § 707(b)(2), and pursuant to § 707(b)(6), only the trustee or the bankruptcy judge may seek dismissal for "abuse" under § 707(b)(1). Don's debt arises from his illness and his exemptions are moderate. He has very limited ability to fund a Chapter 13 plan. Therefore, his case should not be dismissed for abuse.

4. Don can deal with Giny's debt in several different ways. Don should be advised that he can always repay the debt voluntarily, notwithstanding the discharge. In addition, as noted above, he can use some of his non-exempt cash to partially satisfy the debt pre-petition. Alternatively, Don could reaffirm the debt. However, this may not be in his best interest. Don should be advised that § 525 prevents Giny from firing him "solely" because of the bankruptcy or the discharge of the debt. However, that protection may be of little use because Don needs the job and because Giny could easily find some other reason to fire Don (especially in those jurisdictions that read § 525 narrowly).

5. As noted above, the automatic stay will stop the garnishment with respect to post-petition wages. However, since under the relevant state law a lien was created as of the service of the summons, the funds garnished pre-petition will be subject to a lien in favor of Mel. Possibly, since the lien is "judicial," Don can avoid it under § 522(f)(1) if, and to the extent that, he chooses to assert his "wildcard" exemption in the garnished funds. Alternatively, Don may avoid the lien as a preference since it attached within the 90-day look-back period and permitted the unsecured creditor (Mel) to obtain more than his Chapter 7 payout. The problem here is the § 547(c)(7) defense for transfers aggregating less than \$600, unless Don waits to file until after \$600 has been garnished. Because the transfer was involuntary, Don could assert his "wildcard" exemption in the recovery under § 522(g), and, if the trustee fails to bring the action, Don could bring it under § 522(h).

6. The problem indicates that Don can not obtain a different car, so he must save this one. He has a couple of options. If the creditor is willing to restructure the payments, the most obvious possibility is to reaffirm the car loan. However, as the car is worth far less than the debt amount, this course of action may not be to Don's advantage. If the creditor has not yet declared a default and accelerated the loan (or if state law permits a cure and reinstatement), the best option may be to bring the loan current and do nothing about the car in the Chapter 7 case. Absent a bankruptcy default clause, many courts will hold that bankruptcy is not an automatic default and, therefore, the creditor can not repossess unless the debtor misses a payment post-petition. The advantage here is that, unlike a reaffirmation, Don has no personal liability on the loan after the discharge is granted. The disadvantage is that Don must continue regular payments as long as he wishes to keep the car. A better option, and the only other option in those districts not following the position mentioned above, is to redeem the car. The car is tangible personal property used for consumer purposes and the debt is a dischargeable consumer debt. Therefore, Don can redeem by paying the amount

of the allowed secured claim. Don should be able to keep the car free and clear of the lien by paying between \$4,500 and \$5,000 (the courts are split on which value is appropriate). In order to redeem, either Don must claim the car as exempt or the trustee must abandon it (likely here because of the lack of equity). In addition, virtually all courts require a lump sum payment, and do not permit installment redemption. Don can use the cash he exempts with his "wildcard" plus some post-petition wages to pay the redemption amount. This should not be a problem because, under § 521, he should have at least 75 days to get the money together and may be able to get an extension.

7. With respect to the property of the estate and exemptions, the entirety of Don's ERISA plan will be excluded from the estate. The joint checking account may pose a problem in some jurisdictions. Under Bitner, state law should determine the nature and extent of Don's property interest in the joint account. Because Don contributed none of the funds, has never attempted to exercise control over the account, and his name was added to the account solely as an estate planning device, the trustee should not be able to reach the deposited funds. [See also § 522(2)(B)]

8. With respect to exemptions, Don must use the § 522(d) list (see instructions). Since he lacks equity in the home and car, those exemptions do him no good. The only real exemption he has is the § 522(d)(5) "wildcard." Here he gets to exempt "any property" to the extent of \$1,075 plus \$10,125 of his unused homestead exemption. The only real assets left are the \$1,000 checking account, the \$4,000 tax refund and, possibly, the recovered garnished funds. Thus, he can protect an aggregate of \$11,200. A weak argument could be made that the tax refund is exempt until received by Don, as most creditors can not reach a tax refund while in the hands of the IRS. If this view prevails in the local jurisdiction, Don may wish to file before he receives the refund.

9. Although Don should be able to get a discharge without encountering § 727 problems, he will face some dischargeability problems under § 523. First, the child support obligation is non-dischargeable under 523(a)(5). This is also true with respect to the past due portion assigned to the Department of Child Welfare. Although assignment ordinarily renders the claim dischargeable, 523(a)(5)(A) specifically accepts assignments to the state. The attorney's fee presents a more difficult question. Most courts see the fee award as integral to the support award and treat such awards as non-dischargeable. However, some courts focus on the language of the section (owed "to a spouse, former spouse, or child") or on the question of whether payment of the fee award serves a support function by relieving the spouse/child of the obligation to pay the fee. If this view is followed, Don may be able to discharge the fee award. Under Garner, the state court judgment will be binding in the bankruptcy dischargeability action and Don will not be able to relitigate the issue of paternity.

The charge card debts present a variety of discharge issues, several of which have split the courts. First, none of the charges are for luxury goods or services so as to those charges the presumption of § 523(a)(2)(C) does not apply. Most courts would find that the intentional over-limit charges are non-dischargeable under the §

523(a)(2)(A) "actual fraud" provision. The cash advances may be subject to the presumption of § 523(a)(2)(C) if bankruptcy if Don files within 70 days of August 20, the date he signed the Crazy Credit check. At the other extreme, the charges pre-dating the illness should be dischargeable. The charges incurred while Don was sick and after he lost his job present a very difficult question. While the use of the card when Don's financial condition was hopeless is fraudulent, § 523(a)(2)(B) requires a "statement in writing" before a debt is non-dischargeable based on a misrepresentation of financial condition. If his use of the card is viewed as an implied representation of financial condition, the debts are dischargeable. However, many recent cases view such credit card use as an implied representation of intent or willingness to repay and hold the debts non-dischargeable under § 523(a)(2)(A).

**Question B**  
**(Suggested Time - 1 1/2 hours)**

Jerry Crandall had been very fortunate throughout the 1980s. He started a small business in 1982 (Crandall Cleaning "CC") that provided janitorial services to manufacturing companies. The primary customer of the business was Kaboom Corp., a manufacturer of guidance systems for air-to-ground missiles. There were some other customers, but Kaboom was the largest customer by far.

As the defense industry grew, so too did the demands on Jerry's business. By the end of 2006, there were fifteen full-time employees and a net profit of approximately \$175,000 per year. While the business continued to be quite healthy through 2007 and early 2008, international events and domestic economic difficulties conspired to cause a significant downturn in defense spending. Consequently, Kaboom substantially cut back its production and eventually decided to have its own employees take care of the janitorial needs of the business. Kaboom gave Jerry notice of its intention to cancel the janitorial service contract with CC on April 1, 2008. Because the contract with Kaboom generated 80% of CC's total annual revenues, Jerry faced the daunting task of replacing the \$400,000 annual revenue created by the contract with Kaboom. Unfortunately, Jerry was unable to attract any significant new accounts. In 2008, CC had total revenues of \$220,000 with expenses of \$270,000. For the first nine months of 2009, the company had revenues of \$100,000 and expenses of \$140,000. Jerry's salary is now \$47,000 per year (down from a high in 2007 of \$145,000). The business now seems to have stabilized and is operating on a break-even basis.

Jerry's wife, Roberta, worked for the company from 1983 to 2006. At that time, she commenced a career in real estate sales. She specialized in selling homes comparable to or more expensive than the one she and Jerry had purchased in 2006. They purchased their house for \$145,000 at a time when the housing market was at its peak. Roberta has had some limited success in sales and had total commissions of \$38,000 in 2008. Her commissions in 2007 totaled \$26,000.

Jerry and Roberta have found it difficult to get by on their current combined income of approximately \$80,000. Roberta drives a 2007 Cadillac which requires a

monthly lease payment of \$500. Roberta claims that she needs the car to transport prospective home buyers to the upscale houses that she sells. Jerry is driving a 2007 Jeep Cherokee that he purchased for \$23,500 one year ago. Jerry financed the entire amount on a 60-month note, and the present loan balance is approximately \$21,000. The interest rate on the note is 10%. His monthly car payment is \$500.

While Roberta's commissions are down for 2009 and real estate sales are lagging, it is the significant downturn in the business of CC that has created the biggest problem for Jerry and Roberta. For the last 18 months, the CC losses have been substantial. Jerry and Roberta's savings were depleted. Unfortunately, Jerry has attempted to keep the business afloat by "borrowing" from his withholding tax account. Consequently, CC owes withholding taxes of \$22,000. Jerry and Roberta also have a personal federal income tax liability for 2008 in the amount of \$7,000. Furthermore, they owe \$1,000 for state income taxes due for 2006.

The decline of CC also resulted in the business falling behind in its payments to some of its suppliers. Three months ago, one of the cleaning solution supply companies refused to ship any further goods to CC unless all past due amounts were paid in full. As a result, Jerry wrote a check for \$3,000 to the supply company, and the goods were delivered. Unfortunately, there was only \$300 in the account when Jerry wrote the check. The vendor responded by filing a criminal complaint with the local authorities who have charged Jerry with violating the states bad check law. The county prosecutor has indicated that the pending charges will be dropped if Jerry makes good on the check within the next thirty days.

On the personal front, Jerry and Roberta are four months behind in their payments on their mortgage. They purchased their home in 2006 for \$145,000. The mortgage is payable over thirty years at a rate of 9 1/2%. The monthly payment (including escrowed amounts for taxes and insurance) is \$1,200. The mortgage contained no provision regarding either the effect of late payments or the application of interest to amounts paid later than required under the agreement. Currently, the Crandalls are four months behind in their payments, and they do not appear to be able to meet their next mortgage payment which is due in one week.

Jerry and Roberta's complete list of assets and liabilities is set out below. Also set out below is the Crandall family monthly budget. It includes the living expenses of Jerry and Roberta, as well as their three children, one of whom is a college student.

### **Assets/Liabilities/Budget**

#### **ASSETS:**

House	\$110,000
Cadillac (lease)	-0-
Jeep	16,000
Furniture	2,500

Clothing	500
Ski Boat	11,000
IRA	14,000
Business Equipment	<u>14,000</u>
<b>TOTAL</b>	<b>\$168,000</b>

**LIABILITIES** (all claims identified as secured are properly perfected)

1st Bank	\$127,000	(secured by mortgage on house)
Auto Finance Co.	21,000	(secured by Jeep)
IRS	29,000	(22,000 in withholding taxes: 7,000 for 1990 income taxes)
State Income Tax	1,000	(1988 income taxes)
Visa	7,000	(for general purchases)
American Express	6,000	(for general purchases)
Mastercard	4,000	(for general purchases)
Commercial Credit Corp.	15,000	(secured by business equipment)
Discover Credit Card	5,000	(for general purchases)
Corner Finance Co.	5,000	(debt consolidation loan)
Cleenze, Inc.	3,000	("bad check") for company cleaning supplies)
Ward Worker	800	(last two weeks wages for employee of CC)
Nautical Lenders, Inc.	7,000	(secured by ski boat)
<b>TOTAL</b>	<b>\$230,800</b>	

**BUDGET**

Mortgage (incl. tax and insurance escrow).	\$1200
Cadillac Lease.....	500
Jeep Payment .....	500
Utilities (Phone/Gas/Electric).....	200
Cable TV (includes HBO) .....	35
Food .....	400
Transportation .....	200
Recreation .....	100
Newspapers/Magazines .....	25
Haircuts .....	50
Boat Payment .....	200
Tithe to Church.....	100
Son's Miscellaneous College Expenses.....	300
Life and Disability Insurance for Jerry .....	<u>140</u>
<b>TOTAL</b>	<b>\$ 3950</b>

Jerry's current monthly income is \$2650. Roberta's current monthly income is \$1,800. (her income fluctuates between \$500 and \$3000 per month)

Jerry and Roberta have come to you for help. The holder of the mortgage on their home has commenced foreclosure proceedings. In fact, they brought the foreclosure complaint with them, and it appears that the time to file a responsive pleading will expire in five days. Jerry and Roberta want to do all that they can to retain their home and other possessions. They are especially interested in the possibility of obtaining relief under Chapter 13 of the Bankruptcy Code. Please discuss the following:

- 1) Are the Crandalls eligible for Chapter 13?
- 2) Can the Crandalls keep their home in Chapter 13?
- 3) What will happen to their cars in Chapter 13?
- 4) How would you compute disposable income under a Chapter 13 plan for the Crandalls?
- 5) Will a Chapter 13 plan satisfy the best interests test of § 1325(a)(4)?
- 6) Will the Crandalls be able to propose a plan that satisfies the required treatment of priority claims under § 1322(a)(2)?
- 7) Can the Chapter 13 plan provide for payment of the Cleenze bad check in full to avoid prosecution?

**SAMPLE ANSWER TO QUESTION B:**

1. The debtors appear to be within the debt limits of § 109(e). The total secured debt equals is \$147,000. After applying § 506, the secured claims include the \$110,000 secured claim of 1st First Bank, the \$16,000 secured claim of Auto Finance Co., the \$14,000 secured claim of Commercial Credit Corp., and the \$7,000 secured claim of Nautical Lenders. These total \$147,000, well below the \$922,975 maximum. The total unsecured debt is \$230,800 minus \$147,000, which is \$83,800; also well below the \$307,675 maximum. Thus, the debtors meet the eligibility requirements of §109(e) with regard to their secured and unsecured liabilities.

A second eligibility question could arise in the case. The facts indicate that the business has now stabilized and is operating on a break-even basis. Thus, Jerry's current salary of \$47,000 is sufficiently "stable and regular" to meet the requirements of §101(30). His income, however, is not sufficient alone to fund a plan. Therefore, one must consider Roberta's income if the debtors are to meet the definitional requirements for individuals with regular income set out in § 101(30). The problem indicates that Roberta's average after-tax income is \$1800 per month. Of course, her income also

fluctuates between \$500 and \$3,000. Although the amount of her income is not as stable as Jerry's, it is likely that the courts would permit Roberta's income to be included in the calculation of the debtor's income for purposes of eligibility under § 101(30).

2. The foreclosure action is pending, and they probably have to file quickly in order to prevent the foreclosure from going so far that it can not be upset. While the last day on which a petition may be filed to prevent the loss of the home may vary around the country, it is certainly true that action taken before the time an answer is due in the foreclosure proceeding would be timely in any jurisdiction to stay the foreclosure proceedings and protect the debtors' interest in the home.

Assuming that a Chapter 13 petition is timely filed, the claim of 1st Bank is undersecured. However, because this is their principal residence, under § 1322(b)(2), they may not modify the mortgage. Therefore, Jerry and Roberta can not strip down the mortgage to the present value of the house. However they may "cure and maintain" the mortgage by continuing to pay the \$1,200 monthly amounts due, and cure the default over a reasonable period.

3. The two car payments total \$1000 per month, with \$500 due monthly on the Cadillac lease and \$500 per month due on the Jeep purchase agreement. Focusing first on Jerry's car, the creditor is undersecured. Unlike home mortgages, auto loans are subject to cram down in Chapter 13. Therefore, the plan could provide for the payment of the \$16,000 secured claim over five years at the same 10% rate that currently is included in the contract. This would reduce the monthly payments by approximately one-fourth, so that Jerry's car payment would be about \$375 per month. This assumes, of course, that the court is willing to permit Jerry to maintain ownership of the Jeep rather than to require him to "trade down" to a less expensive vehicle. Given the nature of the business, however, it seems likely that you could convince the court to permit Jerry to keep the Jeep. He could carry supplies to the job sites and take prospective customers to lunch in the same vehicle.

The court may be less willing to authorize the continued leasing of a Cadillac for Roberta. The \$500 monthly lease payment arguably generated no equity for the estate in contrast to the monthly payments on Jerry's car. To that end, the court could find that the monthly expense on the Cadillac lease is excessive and not "reasonably necessary" for the debtor. Roberta's counterargument is that she needs a luxury automobile to conduct her business successfully. Certainly, her continued success as a real estate agent is essential to the success of the plan. Therefore, the court might permit the continuation of the Cadillac lease. A contingency plan might be considered which would involve the lease of a less expensive automobile for Roberta's use. In the event that a less expensive lease is obtained, it would increase the debtor's monthly disposable income available to fund the plan.

4. If the Crandalls are above-median debtors, their amounts reasonably necessary to be expended in computing disposable income under § 1325(b)(2) must be computed in accordance with the computation used for the means test of § 707(b)(2). The

problem does not give us enough information to make that determination, but if they are above-median debtors, disposable income would be computed by taking their total current monthly income (\$ 4,450) and subtract the applicable monthly expense amounts specified under the National Standards and Local Standards and their actual monthly expenses for the categories specified as Other Necessary Expenses issued by the IRS. They may also deduct the actual administrative expenses for the chapter 13, up to 10% of the projected plan payments, average monthly payments on account of secured debt, and expenses for payment of all priority claims.

If the Crandalls are not above-median debtors, the amount reasonably necessary to be expended is left to the discretion of the court. In all likelihood, the court would see the payments on the boat as not reasonably necessary. Therefore the debtors' disposable income would be increased by \$200 per month.

The other encumbered asset is the business equipment. Assuming that it is necessary to the operation of the business, the payments to the creditor on account of that property are permitted under § 1325(b)(2)(B). The payments are currently being made and the business is breaking even. The creditor is secured to the extent of \$14,000 and unsecured to the extent of \$1,000. Thus, even in a cramdown of the claim, there would be very little difference in the monthly payment on that asset.

Most of the other monthly payments would appear to be reasonably necessary for the support of the debtor and dependents of the debtor. Utilities, food, newspapers, haircuts, tithe, and insurance payments all are within the range of reasonable. Some courts might object to monthly cable TV bills, especially when a separate budget item for recreation is included. The recreation amount also could be attacked as too high. The courts also might be skeptical of a \$200 per month transportation budget. However, given the nature of the businesses involved, it would appear that some significant travel is required and the figure may be reasonable. The tithe is permitted under § 1325(b)(2)(A)(ii). The last budget item is the \$300 per month payment for miscellaneous college expense. It would not be surprising to find creditors objecting to those payments. Similarly, some courts probably would not permit those payments to continue. Others, however, find the payments reasonable and necessary, at least if the debtors' son is enrolled in a state university and is obtaining the lowest cost education available to him.

5. In a hypothetical Chapter 7, the debtors likely could exempt all of their property with the exception of the \$4,000 equity in the ski boat and the \$14,000 of IRAs. In some states, even these items might be exemptible. In any event, the most that creditors would appear to be able to receive in a Chapter 7 case would be \$18,000 (IRA-\$14,000, Ski Boat-\$4,000 equity). A quick scan of the debtors' income and expenses indicates that they would be able to meet the best interest of creditors test without too much difficulty.

6. Under §1322(a)(2), the plan must pay priority claims in full in the absence of an agreement by the creditor to less favorable treatment. In this case, the debtors owe at least \$29,000 of priority taxes to the IRS. The State income tax claim is more than three years old for purposes of § 507, so it is not a priority claim. Nevertheless, the debtors' plan would have to pay at least \$29,000 to the IRS in order to meet the requirements of § 1322(a)(2). Moreover, the Chapter 13 trustee's fee would also be an administrative expense claim that must be paid in full under the plan. Assuming a ten percent fee, the debtor would have to pay approximately \$33,000 over the life of the plan to pay \$29,000 to the IRS. In a 36-month plan, the debtors would be paying slightly more than \$900 per month into the plan just to cover the priority claims. If the plan is stretched out to 60 months (as required for an above-median debtor), however, the minimum monthly payment is reduced to approximately \$550 per month. The debtors' budget as initially set out indicates a monthly surplus of \$500. This would be insufficient even to meet the minimum required payment for a 60 month plan. However, if the \$200 monthly boat payment is removed from the debtors' list of expenses, then they would have disposable income of approximately \$700 per month. This would be enough to fund a 60 month plan, but it would be insufficient to fund a 36 month plan. If the debtors cram down the claims secured by the Jeep, they could add another \$125 per month to their disposable income. This would bring them closer to the amount necessary to pay the priority claims with 36 months. Nonetheless, they would have to find some additional assets to complete those payments. The additional assets could be obtained through the liquidation of the ski boat and the transfer of the \$4,000 of equity directly to the IRS. Similarly, the debtors could use some of the funds currently in IRAs to pay off the priority claims of the IRS and the Chapter 13 trustee. Additionally, Ward Worker also has a priority claim under § 507(a)(3), and he would have to be paid in full during the life of the plan. Finally, although it is not a priority claim, the mortgage arrearage of approximately \$6,000 must be paid within a reasonable time under the plan. Thus, the "must pay" debts total approximately \$40,000 (IRS - \$29,000; Worker - \$8,000; Mortgage arrearage - \$6,000; trustee fee \$3,600). Given all of these expenses, it seems likely that the debtors will have to reduce their expenses further in order to increase their disposable income. The two candidates for expense reduction are Roberta's car lease and the debtors' son's monthly college expenses. If Roberta can "trade down" to a less expensive car, the debtors can save a significant amount monthly. Furthermore, if the son's education is put on hold, or he is able to obtain his own funds for his educational expenses, then \$300 per month can be added to the debtors' disposable income. It might be necessary to add these additional funds to the debtors' plan in order to obtain confirmation from the bankruptcy court.

7. Jerry is facing prosecution under the bad check law pursuant to the criminal complaint filed by Cleenze, Inc. There is some possibility that the claim could become specifically non-dischargeable if a criminal restitution obligation is created that would meet the exception to discharge provisions now set out in § 1328(a)(3). Thus, the debtor might propose special treatment under their plan for the Cleenze, Inc. debt.

The problem with this extra special treatment of the Cleenze claim, of course, is that the debtors are running out of money. The additional expense of the potentially non-dischargeable debt totals \$3,000. It might require that the debtors liquidate the IRAs in order to meet the minimum funding necessary to pay the IRS, Ward Worker, the mortgage arrearage, the trustee's fee, and the bad check debt. The bad check debt could be classified separate from other unsecured claims and paid in full. The IRS claim is, as noted above, a priority claim that must be paid in full. However, even if the debtors are able to propose a plan with all of these provisions, one could anticipate an objection from unsecured creditors to the classifications proposed as well as to the good faith of the plan generally. The courts are not generally very favorably disposed to Chapter 13 plans that are undertaken largely to pay the IRS. Recent decisions denying confirmation of Chapter 13 plans as thinly veiled attempts to evade tax obligations (particularly interest on the taxes) are illustrative. Nevertheless, since the debtors are paying all of their disposable income into the plan for probably five years, the court may be willing to confirm the debtors' plan. The alternative under Chapter 7 would be to lose all of their nonexempt assets and have a number of claims excepted from the discharge. Furthermore, under Chapter 7 they would not be able to strip down the home mortgage which would leave the home subject to the entire \$127,000 balance owing to First Bank. Given these grave consequences following from a Chapter 7 as opposed to a Chapter 13 proceeding, the court should confirm the debtors' Chapter 13 plan.