

OCT 05 2009

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U.S. BKCY. APP. PANEL  
OF THE NINTH CIRCUIT

ORDERED PUBLISHED

UNITED STATES BANKRUPTCY APPELLATE PANEL  
OF THE NINTH CIRCUIT

In re:	)	BAP Nos.	WW-08-1311-MoJuH
	)		WW-08-1312-MoJuH
TIMOTHY SMITH and KARRIE A. SMITH,	)		WW-08-1313-MoJuH
	)	Bk. No.	07-43853-PBS
Debtors.	)		

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AMERICAN EXPRESS BANK, FSB;  
ROBERT D. MILLER, JR., Acting  
United States Trustee; DAVID  
M. HOWE, Chapter 13 Trustee,

Appellants,

v.

TIMOTHY SMITH and KARRIE A. SMITH,

Appellees.

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O P I N I O N

Argued and Submitted on May 19, 2009  
at Seattle, Washington

Filed - October 5, 2009

Appeal from the United States Bankruptcy Court  
for the Western District of Washington

Hon. Paul B. Snyder, Bankruptcy Judge, Presiding.

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Before: MONTALI, JURY and HOLLOWELL, Bankruptcy Judges.

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1 MONTALI, Bankruptcy Judge:

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3 In this case we decide an issue that has come before many  
4 courts throughout the country, but not before this Panel or the  
5 United States Court of Appeals for the Ninth Circuit. It is a  
6 problem that has vexed the bankruptcy bench and bar since the law  
7 was changed in 2005: may a debtor "deduct" secured debt payments  
8 not being paid because the property has been surrendered? We  
9 part company with several of our colleagues and conclude that  
10 debtors may not take those deductions.<sup>1</sup> Our conclusion is  
11 reinforced by a persuasive and compelling statement from our own  
12 court of appeals just a few weeks ago: "Ironic it would be indeed  
13 to diminish payments to unsecured creditors in this context on  
14 the basis of a fictitious expense not incurred by a debtor."  
15 Ransom v. MBNA Am. Bank (In re Ransom), 577 F.3d 1026, 1030 (9th  
16 Cir. 2009).

17 The chapter 13 trustee, the United States Trustee and an  
18 unsecured creditor objected to confirmation of debtors' chapter  
19 13<sup>2</sup> plan, arguing that debtors had failed to devote all of their  
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21 <sup>1</sup>In a separate opinion we are issuing concurrently with this  
22 one we reach a similar conclusion regarding attempted deductions  
23 from disposable income for payments not being made because the  
24 underlying property has been valued at zero, leaving any  
25 remaining claim no more than wholly unsecured. Yarnall v.  
Martinez (In re Martinez), No. NV-08-1332 (9th Cir. BAP Oct. 5,  
2009).

26 <sup>2</sup>Unless otherwise indicated, all chapter, section and rule  
27 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and  
28 to the Federal Rules of Bankruptcy Procedure, Rules 1001-9037, as  
(continued...)

1 "projected disposable income" to payment of unsecured creditors  
2 as required by section 1325(b) and that the plan was not proposed  
3 in good faith. In particular, in calculating their "projected  
4 disposable income," debtors deducted payments for collateral (two  
5 houses and a vehicle) which they were surrendering under their  
6 plan.

7 Holding that Congress removed the flexibility of courts to  
8 consider whether the expenses of above-median income debtors are  
9 "reasonably necessary" and that the fixed formula of the means  
10 test under section 707(b)(2) (as incorporated by section  
11 1325(b)(3)) permitted debtors to deduct payments that they were  
12 contractually obligated to make as of the petition date even  
13 though they intended to surrender the collateral, the bankruptcy  
14 court overruled the objections. All three objecting parties  
15 appealed.

16 Subsections (b)(2) and (b)(3) of section 1325, read  
17 together, provide that if an expense is not reasonably necessary  
18 for a debtor's and/or dependants' maintenance and support, it is  
19 not included in the calculation of disposable income. If the  
20 expense is reasonably necessary, and the debtor is an above-  
21 median income debtor, subsection (b)(3) requires the court to  
22 determine the amount in accordance with section 707(b)(2). In  
23 other words, subsections 1325(b)(2) and (b)(3) require a two-part  
24 inquiry.

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26 <sup>2</sup>(...continued)  
27 enacted and promulgated after the effective date of The  
28 Bankruptcy Abuse Prevention and Consumer Protection Act of 2005,  
Pub. L. 109-8, 119 Stat. 23 ("BAPCPA").



1 disclosed in their Form B 22A, except that Form B 22C included a  
2 chapter 13 administrative expense of \$89 a month.

3 In particular, both Form B 22A and Form B 22C showed a  
4 current monthly income of \$12,906 (for annual income of  
5 \$154,872), which all parties agree was in excess of the  
6 applicable state median income. Debtors deducted from this  
7 income monthly expenses of \$14,655, resulting in a negative  
8 monthly disposable income of -\$1,749.00. Debtors' expenses  
9 included \$7,185 in monthly payments on two houses and a vehicle  
10 which they proposed to surrender pursuant to section 4 of their  
11 chapter 13 plan. Because the resulting disposable income was a  
12 negative figure, Debtors did not propose a five-year plan but  
13 instead proposed a six-month plan with plan payments of \$889 a  
14 month, providing unsecured creditors a total of \$4,300.60 for a  
15 yield of approximately four percent.

16 If the payments on the surrendered property were not  
17 deducted, Debtors could claim a statutorily allowed housing  
18 allowance of \$1,245<sup>3</sup> and would have a positive monthly disposable  
19 income of \$4,191. In that event, Debtors could pay the scheduled  
20 unsecured debt<sup>4</sup> in full over 24 months (if all disposable income  
21 were applied to the plan each month) or in full over 60 months  
22 (if Debtors applied less than half of their disposable income to  
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24 <sup>3</sup>According to Debtors' opening brief, they are currently  
renting a house for \$2,100 a month.

25 <sup>4</sup>Debtors scheduled \$101,256.00 in unsecured debt. This  
26 debt, however, does not include whatever deficiency remains  
27 following surrender of the two houses and the vehicle. Debtors'  
28 schedule of unsecured nonpriority claims reflects five credit  
card debts and one medical bill.

1 the plan each month).

2 American Express Bank, FSB ("Amex"), the UST and the chapter  
3 13 trustee ("Trustee")<sup>5</sup> (collectively, "Appellants") objected to  
4 confirmation of Debtors' plan. They contended that if Debtors  
5 did not deduct payments for surrendered property when calculating  
6 their monthly disposable income, Debtors would be able to pay a  
7 100 percent dividend to all creditors.<sup>6</sup> Both the UST and Amex  
8 asserted that Debtors' plan was not proposed in good faith (thus  
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10 <sup>5</sup>Karla Forsythe was the chapter 13 trustee when the notice  
11 of appeal was filed; on February 24, 2009, we entered an order  
12 substituting successor trustee David M. Howe as appellant.

13 <sup>6</sup>In support of its objection, Amex attached three memorandum  
14 decisions issued by the bankruptcy court in August 2006, before  
15 the Ninth Circuit issued its decision in Maney v. Kagenveama (In  
16 re Kagenveama), 541 F.3d 868 (9th Cir. 2008). In those  
17 decisions, the court held that the means test under section  
18 707(b) is a historical gauge; even though a debtor may intend to  
19 surrender collateral, the underlying debt is "contractually due"  
20 on the petition date and could be included as an expense in the  
21 means test calculation. That said, the bankruptcy court held  
22 that the means test was just a "starting point in determining the  
23 amount of projected disposable income available to unsecured  
24 creditors." Reviewing the "projected disposable income" language  
25 of section 1325(b)(1), the bankruptcy court concluded that courts  
26 were required to employ a forward-looking analysis for both a  
27 debtor's income and for his or her expenses, and thus positive  
28 cash flow resulting from the surrender of collateral had to be  
allocated to the repayment of unsecured creditors.

24 Thereafter, the Ninth Circuit held in Kagenveama that  
25 "projected disposable income" is determined on a backward-looking  
26 basis. Instead, in calculating "projected disposable income," a  
27 court must use the "current monthly income" as defined in section  
28 101(10A), which requires consideration of historical facts: the  
debtor's income based on an average of what he or she earned over  
the six months preceding the petition date. Postpetition  
adjustments to income are not relevant.

1 violating section 1325(a)(3)) and that the deduction of expenses  
2 for surrendered collateral was contrary to Congress' intent in  
3 enacting BAPCPA. Trustee contended that section 1325(b)(2)  
4 requires a court to determine whether an expense is "reasonably  
5 necessary" and that section 1325(b)(3)'s incorporation of the  
6 means test calculation of section 707(b)(2) for determining the  
7 "amounts" of permissible expenses simply supplements section  
8 (b)(2) and does not replace or supersede it. The UST contended  
9 that section 707(b)(2)(A) does not permit the deduction of  
10 payments on debts secured by property surrendered or to be  
11 surrendered by Debtors.

12 On November 14, 2008, the bankruptcy court entered an order  
13 overruling Appellants' objections to confirmation and a  
14 memorandum decision setting forth its findings of fact and  
15 conclusions of law. See In re Smith, 401 B.R. 469 (Bankr. W.D.  
16 Wash. 2008). Amex and the UST filed timely notices of appeal on  
17 November 24, 2008, commencing BAP Nos. 08-1311 and 1312,  
18 respectively. Trustee's predecessor filed a notice of appeal on  
19 November 25, 2008, commencing BAP No. 08-1313.<sup>7</sup>

20 No order confirming Debtors' plan has been entered, so the  
21 order on appeal is interlocutory. On February 26, 2009, we sua  
22 sponte entered an order granting Appellants leave to appeal the  
23 interlocutory order overruling the objections to confirmation of  
24  
25

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26 <sup>7</sup>Trustee's appeal was timely under Rule 8002(a), which  
27 provides that if one party files a timely notice of appeal, "any  
28 other party" may file a notice of appeal within ten days of the  
first notice of appeal.

1 Debtors' chapter 13 plan.<sup>8</sup> We also allowed Debtors to file a  
2 joint brief for all three appeals.

3 The case was argued before us on May 19, 2009. On August  
4 14, 2009, the Ninth Circuit issued its Ransom decision.

5 **II. ISSUE**

6 In calculating their disposable income to be paid under  
7 their plans, may above-median income chapter 13 debtors deduct  
8 payments for collateral they are surrendering?

9 **III. JURISDICTION**

10 The bankruptcy court had jurisdiction under 28 U.S.C.  
11 § 157(b)(2)(L) and § 1334. We have jurisdiction under 28 U.S.C.  
12 § 158(a)(3), as we have granted leave to Appellants to appeal the  
13 interlocutory order overruling their objections to Debtors'  
14 chapter 13 plan.

15 **IV. STANDARD OF REVIEW**

16 The issue presented in these appeals is purely one of law  
17 and statutory construction; no factual dispute exists. "We  
18 review issues of statutory construction and conclusions of law,  
19 including interpretation of provisions of the Bankruptcy Code, de  
20 novo." Mendez v. Salven (In re Mendez), 367 B.R. 109, 113 (9th  
21 Cir. BAP 2007) (citing Einstein/Noah Bagel Corp. v. Smith (In re  
22 BCE W., L.P.), 319 F.3d 1166, 1170 (9th Cir. 2003)).

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23  
24 <sup>8</sup>In light of the significance of the issue presented by  
25 these appeals, we are concurrently issuing a certification for  
26 appeal of this interlocutory order to the Ninth Circuit, as we  
27 did recently in two other cases of first impression. Ransom v.  
28 MBNA Am. Bank (In re Ransom), 380 B.R. 809 (9th Cir. BAP 2007);  
Int'l Assn. of Firefighters, Local 1186 v. City of Vallejo (In re  
City of Vallejo), 408 B.R. 280, n.3 (9th Cir. BAP 2009).



1 **V. DISCUSSION**

2 A. Overview

3 Section 1325(b)(1)(B) provides that if a trustee or  
4 unsecured creditor objects to confirmation of a chapter 13 plan,  
5 the court may not approve the plan unless, as of its effective  
6 date, the plan "provides that all of the debtor's projected  
7 disposable income to be received in the applicable commitment  
8 period beginning on the date that the first payment is due under  
9 the plan will be applied to make payments to unsecured creditors  
10 under the plan." 11 U.S.C. § 1325(b)(1)(B).

11 In Kagenveama, the Ninth Circuit held a debtor's "projected  
12 disposable income" for the purposes of section 1325(b)(1)(B) is  
13 the debtor's "disposable income" as defined in subsection (b)(2)  
14 "projected out over the 'applicable commitment period.'" Kagenveama,  
15 541 F.3d at 872. The Ninth Circuit specifically  
16 rejected the chapter 13 trustee's argument that section  
17 1325(b)(1)(B) requires a forward-looking determination of  
18 "projected disposable income."<sup>9</sup> Id. at 873-74. The Ninth

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19  
20 <sup>9</sup>Since Kagenveama's issuance, four other courts of appeal  
21 have rejected its reasoning and holding. In particular, the  
22 Seventh Circuit held in In re Turner, 574 F.3d 349 (7th Cir.  
23 2009), that a chapter 13 above-median income debtor could not  
24 deduct as an expense his mortgage payments on property that he  
25 intended to surrender. In reaching its holding, the Seventh  
26 Circuit refused to apply a mechanical calculation that considers  
27 expenses that exist on the petition date, noting that such a  
28 mechanical test is appropriate for determining eligibility to  
proceed under particular chapters.

Since the object of a Chapter 13 bankruptcy is to  
balance the need of the debtor to cover his living  
(continued...)

1 Circuit also rejected the argument that the "disposable income"  
2 calculation of section 1325(b)(2) was a presumptive starting  
3 point which could be supplemented by evidence of future or actual  
4 "finances of the debtor." Id. at 874, overruling Pak v. eCast  
5 Settlement Corp. (In re Pak), 378 B.R. 257, 267 (9th Cir. BAP  
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7  
8 <sup>9</sup>(...continued)

9 expenses against the interest of the unsecured  
10 creditors in recovering as much of what the debtor owes  
11 them as possible, we cannot see the merit in throwing  
12 out undisputed information, bearing on how much the  
13 debtor can afford to pay, that comes to light between  
14 the submission and approval of a plan of  
15 reorganization. Sometimes as in this case the  
16 creditors will benefit from the new information. But  
17 in other cases it will be the debtor . . . . The use of  
18 the later date, which is consistent with the statutory  
19 language though not compelled by it, is more sensible.

20 Id. at 355. See also Nowlin v. Peake (In re Nowlin), 576 F.3d  
21 258 (5th Cir. 2009) (holding that "projected" disposable income  
22 permits consideration of "reasonably certain" future events and  
23 stating that the Ninth Circuit emphasized the modified definition  
24 of "disposable income" without recognizing the independent  
25 significance of the word "projected"); Hamilton v. Lanning (In  
26 re Lanning), 545 F.3d 1269 (10th Cir. 2008), petn. for cert.  
27 filed, 77 U.S.L.W. 3449 (Feb. 3, 2009) (Supreme Court has  
28 requested briefing by the Solicitor General on the petition (129  
S.Ct. 2820)) (holding that the starting point for calculating a  
chapter 13 debtor's projected disposable income is presumed to be  
debtor's current monthly income, subject to showing of  
substantial change in circumstances); Coop v. Frederickson (In re  
Frederickson), 545 F.3d 652, 659 (8th Cir. 2008), cert. denied,  
129 S.Ct. 1630 (2009) (holding that the means test is only a  
starting point for determining a chapter 13 debtor's disposable  
income). "[T]he final calculation can take into consideration  
changes that have occurred in the debtor's financial  
circumstances as well as the debtor's actual income and expenses  
as reported on Schedules I and J." Frederickson, 545 F.3d at  
659.

1 2007).

2 Section 1325(b)(2) defines "disposable income" as the  
3 debtor's current monthly income less the amounts reasonably  
4 necessary to be expended for, inter alia, the support of the  
5 debtor and his or her dependents. 11 U.S.C. § 1325(b)(2).<sup>10</sup>  
6 Section 1325(b)(3), however, restricts the ability of a  
7 bankruptcy court to determine the "amounts reasonably necessary  
8 to be expended" when the debtor has an above-median income.<sup>11</sup>

9  
10 <sup>10</sup>Section 1325(b)(2) provides:

11 (2) For purposes of this subsection, the term "disposable  
12 income" means current monthly income received by the debtor  
13 (other than child support payments, foster care payments, or  
14 disability payments for a dependent child made in accordance  
15 with applicable nonbankruptcy law to the extent reasonably  
16 necessary to be expended for such child) less amounts  
17 reasonably necessary to be expended --

18 (A) (i) for the maintenance or support of the debtor  
19 or a dependent of the debtor, or for a domestic  
20 support obligation, that first becomes payable  
21 after the date the petition is filed; and

22 (ii) for charitable contributions (that meet the  
23 definition of "charitable contribution" under  
24 section 548(d)(3) to a qualified religious or  
25 charitable entity or organization (as defined in  
26 section 548(d)(4)) in an amount not to exceed 15  
27 percent of gross income of the debtor for the year  
28 in which the contributions are made; and

(B) if the debtor is engaged in business, for the  
payment of expenditures necessary for the continuation,  
preservation, and operation of such business.

<sup>11</sup>Section 1325(b)(3) provides:

(continued...)

1 For a debtor with above-median income, "amounts reasonably  
2 necessary to be expended under paragraph (2) . . . shall be"  
3 calculated in accordance with section 707(b)(2)(A) and (B). 11  
4 U.S.C. § 1325(b)(3). Section 707(b)(2) is the chapter 7 "means  
5 test" provision, and subsection (b)(2)(A)(iii) provides that the  
6 debtor's average monthly payments on account of secured debts  
7 shall be calculated as the sum (then divided by 60) of

8 (I) the total of all amounts scheduled as contractually  
9 due to secured creditors in each month of the 60 months  
10 following the date of the petition; and

11 (II) any additional payments to secured creditors  
12 necessary for the debtor, in filing a plan under  
13 chapter 13 of this title, to maintain possession of the  
14 debtor's primary residence, motor vehicle, or other  
15 property necessary for the support of the debtor and  
16 the debtor's dependents, that serves as collateral for  
17 secured debts[.]

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18 <sup>11</sup>(...continued)

19 (3) Amounts reasonably necessary to be expended under  
20 paragraph (2), other than subparagraph (A)(ii) of paragraph  
21 (2), shall be determined in accordance with subparagraphs  
22 (A) and (B) of section 707(b)(2), if the debtor has current  
23 monthly income, when multiplied by 12, greater than--

24 (A) in the case of a debtor in a household of 1 person,  
25 the median family income of the applicable State for 1  
26 earner;

27 (B) in the case of a debtor in a household of 2, 3, or  
28 4 individuals, the highest median family income of the  
applicable State for a family of the same number or  
fewer individuals; or

(C) in the case of a debtor in a household exceeding 4  
individuals, the highest median family income of the  
applicable State for a family of 4 or fewer  
individuals, plus \$575 per month for each individual in  
excess of 4.

1 11 U.S.C. § 707(b) (2) (A) (iii).

2 B. The Bankruptcy Court's Decision

3 In a thorough and reasoned decision, the bankruptcy court  
4 analyzed whether, in light of Kagenveama, section 1325(b) and  
5 section 707(b) permit an above-median income chapter 13 debtor,  
6 when calculating disposable income to be paid under a plan, to  
7 deduct payments on secured debt even though the debtor does not  
8 intend to make such payments in the future. The bankruptcy court  
9 held that section 1325(b) (3) supersedes -- not supplements --  
10 subsection (b) (2) when debtors have above-median incomes:

11 As with "disposable income," the term "amounts  
12 reasonably necessary to be expended" appears only twice  
13 in § 1325; once in § 1325(b) (2) and then in  
14 § 1325(b) (3). If the Court were to require an  
15 additional requirement that the expense also be  
16 necessary for a debtor's "maintenance or support," it  
would likewise render as surplusage the clear direction  
in § 1325(b) (3) as to how "amounts reasonably necessary  
to be expended" shall be determined.

17 Smith, 401 B.R. at 474.

18 There is certainly a temptation to affirm the bankruptcy  
19 court's thoughtful decision. The court interprets Kagenveama as  
20 requiring symmetry such that if we look backward to calculate  
21 income, we should not look forward to measure expenses.<sup>12</sup> The  
22 court equates doing otherwise with using two sets of books to  
23 account for a company's finances.<sup>13</sup> But we ultimately disagree

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24 <sup>12</sup>See Smith, 401 B.R. at 474 ("After Kagenveama, it would  
25 also be inconsistent to apply a backward-looking approach to  
26 income, yet adopt a forward-looking approach in determining  
expenses[.]").

27 <sup>13</sup>Id. (applying a backward-looking approach to income but a  
28 (continued...))

1 with this reasoning because good accounting practices have  
2 nothing to do with the doctrine of *stare decisis* or with the  
3 familiar rules of statutory construction.

4 C. The Dicta of Kagenveama

5 It goes without saying that we must follow binding precedent  
6 in our circuit, as the bankruptcy court felt it must. We do not  
7 read Kagenveama as binding precedent with respect to the  
8 calculation of expenses under sections 1325(b)(2) and (b)(3).  
9 Consequently, we are bound only by the Supreme Court's directive  
10 to follow the plain meaning of the words of a statute unless they  
11 lead to an absurd result.<sup>14</sup>

12 The issue before the Ninth Circuit in Kagenveama did not  
13 involve either the determination of what are proper expenses  
14 (under section 1325(b)(2)) or the measurement of them (under  
15 section (b)(3)). Its only meaningful allusion to expenses to be  
16 deducted from income is a passing reference to those two  
17 subsections, without any analysis:

18 The revised "disposable income" test uses a formula to  
19 determine what expenses are reasonably necessary. See  
11 U.S.C. § 1325(b)(2)-(3). This approach represents a

20  
21 <sup>13</sup>(...continued)  
22 forward-looking approach to expenses "would be similar to having  
a business employ two different accounting systems").

23 <sup>14</sup>U.S. v. Ron Pair Enterprises, Inc., 489 U.S. 235, 242  
24 (1989) (plain meaning of legislation should be conclusive, except  
25 in rare cases in which literal application of statute will  
26 produce result demonstrably at odds with intention of its  
27 drafters; in such cases, intention of drafters, rather than  
28 strict language, controls); Lamie v. U.S. Trustee, 540 U.S. 526,  
534 (2004) (when statute's language is plain, sole function of  
courts, at least where the disposition required by statute's text  
is not absurd, is to enforce statute according to its terms).

1 deliberate departure from the old "disposable income"  
2 calculation, which was bound up with the facts and  
3 circumstances of the debtor's financial affairs. In re  
4 Winokur, 364 B.R. 204, 206 (Bankr. E.D. Va. 2007); In  
5 re Farrar-Johnson, 353 B.R. 224, 231 (Bankr. N.D. Ill.  
6 2006) (stating that "[e]liminating flexibility was the  
7 point: the obligations of [C]hapter 13 debtors would be  
8 subject to clear, defined standards, no longer left to  
9 the whim of a judicial proceeding") (internal  
10 quotations omitted).

11 Kagenveama, 541 F.3d at 874 (emphasis added).<sup>15</sup>

12 If those brief statements even rise to the level of dicta,  
13 they are still not binding on us because there is absolutely no  
14 analysis of whether sections 1325(b)(2) and (b)(3) operate as  
15 one, albeit redundantly, or in sequence, with (b)(3) operative  
16 only if (b)(2) triggers it. More specifically, there is no  
17 analysis or discussion whether or how the subsections operate to

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18 <sup>15</sup> Elsewhere in the opinion, in two footnotes, the  
19 subsections are cited:

20 Disposable income is defined as "current monthly income  
21 received by the debtor . . . less amounts reasonably  
22 necessary to be expended[.]" 11 U.S.C. § 1325(b)(2). . . .  
23 Section 1325(b)(3) requires that if a debtor's annualized  
24 current monthly income is greater than the median family  
25 income of similarly-sized households, then "amounts  
26 reasonably necessary to be expended" are determined in  
27 accordance with § 707(b)(2).

28 Kagenveama, 541 F.3d at 872 n.1.

BAPCPA replaced the old definition of what was "reasonably  
necessary" with a formulaic approach for above-median  
debtors. 11 U.S.C. § 1325(b)(3). This formula  
significantly changed the way in which "disposable income"  
is calculated.

Id. at 873 n.2.

1 determine deductible expenses.<sup>16</sup>

2 It is true that figuring out "projected disposable income"  
3 necessarily involves consideration of proper expenses to subtract  
4 from "current monthly income". But the court in Kagenveama was  
5 struggling with the competing views about how to define  
6 "projected" with respect to the "income" half of the equation and  
7 was not addressing whether the deducted expenses were necessary  
8 for the debtor's support.<sup>17</sup>

9 Thus, while Kagenveama directs us to "look backward" to  
10 define the income to be projected throughout the applicable  
11 commitment period, it did not address the definition of expenses  
12 or the measurement of them. Simply put, the opinion does not  
13 direct how courts are to calculate the "disposable" portion of  
14 "projected disposable income" (income minus expenses x temporal  
15

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16 <sup>16</sup>V.S. ex rel. A.O. v. Los Gatos-Saratoga Joint Union High  
17 School Dist., 484 F.3d 1230, 1232 n.1 (9th Cir. 2007) ("we are  
18 not bound by a holding 'made casually and without analysis, ...  
19 uttered in passing without due consideration of the alternatives,  
20 or where it is merely a prelude to another legal issue that  
21 commands the panel's full attention ...'"), quoting United States  
22 v. Johnson, 256 F.3d 895, 915 (9th Cir. 2001); see also Pakootas  
23 v. Teck Cominco Metals, Ltd., 452 F.3d 1066, 1082 (9th Cir. 2006)  
(quoting Johnson, holding that statements made without a  
24 deliberate consideration of the issues presented are not binding  
25 and may be re-visited).

26 <sup>17</sup>In holding that "projected disposable income" is the same  
27 as "disposable income," the Ninth Circuit relied on Anderson v.  
28 Satterlee (In re Anderson), 21 F.3d 355, 357 (9th Cir. 1994)  
(pre-BAPCPA case, determining the debtor's "disposable income"  
and then projecting that sum into the future for the required  
duration of the plan). This is how the court defined the term  
"projected" within the phrase "projected disposable income."



1 period of three or five years = amount to be paid to unsecured  
2 creditors). For this reason the opinion does not bind us to a  
3 rule of how to determine the expenses that must be applied to the  
4 income side of the equation, nor does it compel us to impose a  
5 symmetry that neglects the reality of the case before us, viz.,  
6 that Debtors decided that they did not need their extra vehicle  
7 or their two houses. We violate nothing by applying an  
8 interpretation of the statutory scheme that teaches that if an  
9 item is not necessary for a debtor's support or maintenance, a  
10 debtor cannot engage in the fiction of pretending to pay for it.

11 We apply the words of the statute even though doing so  
12 leaves us with a backward looking definition of projected  
13 disposable income (because of Kagenveama) and a definition of  
14 expenses which (because of the plain wording of the statute)  
15 takes into account financial realities occurring post-petition  
16 and incorporated into a debtor's chapter 13 plan.<sup>18</sup> Without  
17 citing Kagenveama anywhere in its opinion, the Ransom court

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18  
19 <sup>18</sup>While this may be labeled a "forward-looking" approach to  
20 expenses, it is actually consideration of "a fixed debt that we  
21 know will disappear before the Chapter 13 plan is approved."  
22 Turner, 574 F.3d at 356. As Judge Posner stated in Turner:

23 [B]ankruptcy judges must not engage in speculation  
24 about the future income or expenses of the Chapter 13  
25 debtor. That would unsettle and delay the Chapter 13  
26 process as well as exaggerate how accurately a person's  
27 economic situation in five years can be predicted. But  
28 in this case there is no speculation; all that is at  
issue is a fixed debt that we know will disappear  
before the Chapter 13 plan is approved.

Id.

1 quoted our Panel's thinking on this very point:

2       However, in making that calculation [what debtors can  
3       afford to pay their creditors], what is important is  
4       the payments that debtors actually make, not how many  
5       cars they own, because the payments that debtors make  
6       are what actually affect their ability to make payments  
7       to their creditors.

8 Ransom, 577 F.3d at 1030 (emphasis added).

9 D. Two-Part Analysis of Sections 1325(b) (2) and (b) (3)

10       Under the statute, a debtor may deduct from income those  
11       expenses reasonably necessary "for the maintenance or support of  
12       the debtor or a dependent of the debtor." 11 U.S.C.

13 § 1325(b) (2) (A) (i).<sup>19</sup> Thus, we read sections 1325(b) (2) and  
14 (b) (3) in sequence, as follows: if an expense is not reasonably  
15 necessary for the debtor's and/or dependants' maintenance and  
16 support, the inquiry ends at section 1325(b) (2) as there is no  
17 "amount" to determine in section 707(b) (2) via section  
18 1325(b) (3). Stated otherwise, there is no corresponding amount  
19 to subtract from the income component to get to what is  
20 "disposable" for the above-median income debtor.

21       If the expense is reasonably necessary for the debtor's  
22 and/or dependants' maintenance and support, then section  
23 1325(b) (3) requires the court to determine the amount in  
24 accordance with section 707(b) (2).<sup>20</sup> In other words, sections

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25 <sup>19</sup>Section 1325(b) (2) (B) adds a deduction from current  
26 monthly income for necessary expenses for a debtor engaged in  
27 business.

28 <sup>20</sup>This is because section 1325(b) (2) begins "For purposes of  
this subsection, the term 'disposable income' means . . . ."  
(continued...)

1 1325(b) (2) and (b) (3) require a two-step inquiry.

2 Turning to the facts before us, the debtors found their two  
3 houses and one vehicle so unnecessary to their maintenance and  
4 support they surrendered them to the lenders. They made that  
5 decision, not the court. Thus they had no payments to make. As  
6 in Ransom in a situation having precisely the same economic  
7 effect (no lien at all there; no secured debt to pay here), the  
8 court's words are instructive:

9 As did our BAP, we decide this issue not on the  
10 IRS's manual, but instead on the statutory language,  
11 plainly read, which we believe does not allow a debtor  
12 to deduct an "ownership cost" (as distinct from an  
"operating cost") that the debtor does not have. An  
"ownership cost" is not an "expense"--either actual or  
applicable--if it does not exist, period.

13 577 F.3d at 1030 (citation and internal quotation marks omitted).

14 The bankruptcy court believed that Kagenveama requires a  
15 bankruptcy court to apply a "snapshot" petition-date analysis in  
16 calculating both prongs of disposable income: expenses and  
17 income. In other words, the bankruptcy court felt it could not  
18 consider post-petition events in determining whether expenses are  
19 reasonably necessary for the maintenance and support of debtors  
20 and their dependants. We disagree because, as noted, the clear  
21 language of section 1325(b) (2) requires the expenses to be  
22 reasonably necessary for the support and maintenance. In In re  
23 Martinez, we are holding that payments for collateral that has  
24 been stripped of its value are not necessary for support and  
25 maintenance.

26 \_\_\_\_\_  
27 <sup>20</sup> (...continued)

28 Then subsection (b) (3) begins "Amounts reasonably necessary to be  
expended under paragraph (2) shall be determined . . . ."

1           So too, here. Items that a debtor has surrendered or  
2 intends to surrender are not necessary for his or her support or  
3 maintenance. The concepts -- surrender and necessity -- are  
4 mutually exclusive of one another. Phantom payments for the  
5 surrendered item are not reasonably necessary for a debtor's  
6 support and maintenance.

7           Section 1325(b)(2) therefore requires the court to look at  
8 the necessity of the expense as determined by the debtor on a  
9 real-time, forward-looking basis, while section 1325(b)(3) --  
10 which incorporates section 707(b) -- requires a static,  
11 backwards-looking inquiry, since 707(b) itself requires such an  
12 analysis. See, e.g., Morse v. Rudler (In re Rudler), 576 F.3d 37  
13 (1st Cir. 2009). Here, section 1325(b)(3) does not come into  
14 play, so we are not bound by a backwards-looking inquiry.

15           This interpretation is consistent with the plain language of  
16 the statute. The Ninth Circuit in Kagenveama acknowledged that  
17 when a statute's language is plain, the court should enforce it  
18 according to its terms. Kagenveama, 541 F.3d at 872. To the  
19 extent that sections 1325(b)(2) and (b)(3) are ambiguous, this  
20 interpretation avoids an absurd result and is consistent with the  
21 intent of the statute's drafters.

22           Purely historical expenses which will never be paid under or  
23 outside of the plan (phantom expenses) cannot be reasonably  
24 necessary for a debtor's support or maintenance. To include them  
25 in the calculation of disposable income ignores the different  
26 functions of sections 1325(b)(2) and (b)(3). Subsection (b)(2)  
27 is keyed to what the debtor determines to be necessary; once that  
28 is done, as here, subsection (b)(3) governs the amounts of these

1 expenses, not the determination of whether such expenses are  
2 necessary in the first place.

3 To prove the point that sections 1325(b)(2) and (b)(3) are  
4 not conjoined, but perform different functions and must be  
5 considered in sequence, consider the situation (admittedly not  
6 the case before us)<sup>21</sup> of an above-median income debtor engaged in  
7 business.<sup>22</sup> If section 1325(b)(3) governed what expenses are  
8 deductible, as opposed to the amount of those expenses, chapter  
9 13 debtors engaged in business could not deduct business expenses  
10 as those expenses are not specifically found in section 707(b)(2)  
11 (and thus not incorporated by section 1325(b)(3)), even though  
12 section 1325(b)(2)(B) otherwise permits the deduction of business  
13 expenses. Thus we are sent to discover the allowable expenses  
14 from the Internal Revenue Service.<sup>23</sup>

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15  
16 <sup>21</sup>The dissent refers to our "reliance" on this hypothetical.  
17 That is not the case. As noted in the text, we simply look to an  
18 analogous situation under the statute to bolster our view of the  
19 issue before us.

20 <sup>22</sup>Disposable income is current monthly income less amounts  
21 reasonably necessary to be expended "if the debtor is engaged in  
22 business, for the payment of expenditures necessary for the  
23 continuation, preservation, and operation of such business." 11  
24 U.S.C. § 1325(b)(2)(B). See Drummond v. Wiegand (In re Wiegand),  
25 386 B.R. 238 (9th Cir. BAP 2008).

26 <sup>23</sup>In Wiegand, we held that a chapter 13 debtor engaged in  
27 business may not deduct business expenses for the purposes of  
28 calculating current monthly income, but that such expenses are to  
be deducted from the current monthly income when calculating  
"disposable income." In so holding, we noted that Form B 22C --  
which is the form for calculating section 707(b)'s means test --  
is "directly at odds with" section 1325(b)(2)(B). Id. at 241 and  
243. Kagenveama does not address the conflicts between section  
(continued...)

1 Relying on the Internal Revenue Service's handbook does not  
2 provide the answer after all, because it offers no specific  
3 dollar amounts for business expenses. We necessarily circle back  
4 to what the debtor claims as necessary expenditures, subject to  
5 any party-in-interest challenging the reasonableness of them.  
6 Even the debtor in Wiegand claimed specific amounts as proper;  
7 the quarrel there was not whether they were proper deductions,  
8 but when they should be subtracted.

9 Under our two-prong analysis of sections 1325(b)(2) and  
10 (b)(3), a court can permit an above-median income debtor to  
11 deduct necessary business expenses permitted by section  
12 1325(b)(2) when calculating disposable income. If, however,  
13 section 1325(b)(3) and section 707(b)(2) govern the determination  
14 of whether such expenses are necessary (as opposed to governing  
15 the amount of the expenses), section 1325(b)(2)(B) is rendered  
16 meaningless because there are no business expenses to deduct.

17 The foregoing illustrates the error of assuming that  
18 mechanical determinations of section 707(b)(2)(A)&(B) must be  
19 applied for above-median income debtors regardless of their  
20

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21 <sup>23</sup>(...continued)  
22 1325(b)(2)(B) and Form B 22C.

23 We suggested that above-median debtors should refer to the  
24 Internal Revenue Standards for "Other Necessary Expenses" as  
25 specified in the Internal Revenue Service Financial Analysis  
26 Handbook. Wiegand, 386 B.R. at 243 n.11. That resource lists as  
27 likely business expense items "Unsecured debts", with an example  
28 given as "[p]ayments required for the production of income such  
as payments to suppliers and payments on lines of credit needed  
for business . . . ." Int. Rev. Man. Financial Analysis  
Handbook, § 5.15.1.10 (available at <http://www.irs.gov/irm/>).

1 actual reasonably necessary expenses, whether for personal or  
2 business purposes.

3 In the case before us, Debtors cannot have it both ways.  
4 Once they determine that certain assets secured by liens are not  
5 necessary, and they surrender those assets, the corresponding  
6 debts disappear from section 1325(b) (2) and there is no need to  
7 resort to section 1325(b) (3) and its dispatch to the mechanical  
8 formulas of section 707(b) (2) (A)&(B). The dissent suggests that  
9 we have restored to the bankruptcy court the pre-BAPCPA  
10 discretion to decide what are reasonable expenses. Not so - the  
11 debtors made the decision about what assets they retained and  
12 what assets they surrendered. Under our analysis the role of the  
13 bankruptcy court is simply to hold them to the consequences of  
14 their decision.

15 For the foregoing reasons we disagree with the decision of  
16 the bankruptcy court.

#### 17 **VI. CONCLUSION**

18 For the foregoing reasons, we REVERSE.

19  
20 HOLLOWELL, J., dissenting,

21 Under the guise of a plain meaning statutory analysis, the  
22 majority holds that § 1325(b) (2) and (b) (3) must be read  
23 sequentially, thereby arriving at a "common sense" result which  
24 only permits an above median-income debtor to use the means test  
25 to calculate expenses after the debtor demonstrates the expense  
26 is reasonably necessary. While I sympathize with the majority's  
27 desire to achieve a common sense result, I cannot agree with its  
28 contorted statutory analysis.

1 Section 1325(b)(3) provides that when a debtor has an above-  
2 median income, the reasonably necessary expenses to be deducted  
3 from current monthly income ("CMI") "shall be" calculated in  
4 accordance with § 707(b)(2)(A) and (B), otherwise known as the  
5 means test. 11 U.S.C. § 1325(b)(3) (emphasis added). The word  
6 "shall" is mandatory. Therefore, for the above-median income  
7 debtor, expenses must be calculated under § 707(b)(2). In re  
8 Farrer-Johnson, 353 B.R. 224 (Bankr. N.D. Ill. 2006).

9 Presumably, Congress believed the inclusion of the means  
10 test into the calculation of an above median-income debtor's CMI  
11 was the mechanism through which debtors would meet BAPCPA's goals  
12 of ensuring debtors repay creditors the maximum they can afford  
13 and reducing judicial discretion and non-uniformity. See  
14 Marianne B. Culhane & Michaela M. White, Catching Can-Pay  
15 Debtors: Is the Means Test the Only Way, 13 Am. Bankr. Inst. L.  
16 Rev. 665, 677-683 (2005); Maney v. Kagenveama (In re Kagenveama),  
17 541 F.3d 868, 875 (9th Cir. 2008); In re Alexander, 344 B.R.  
18 742, 747-48 (Bankr. E.D.N.C. 2006) (Congress acted intentionally  
19 when it inserted the means test into the calculation of chapter  
20 13 payment plans).

21 The Ninth Circuit, in Kagenveama, declined to "override the  
22 definition and process for calculating disposable income under  
23 § 1325(b)(2)-(3) as being absurd" even if it produced a less  
24 favorable result for unsecured creditors. 541 F.3d 868, 875 (9th  
25 Cir. 2008). In contrast, the Ninth Circuit recently determined,  
26 in Ransom v. MBNA Am. Bank (In re Ransom), 577 F.3d 1026 (9th  
27 Cir. 2009) that in order to reach a result consistent with  
28 BAPCPA's goal of ensuring that debtors repay creditors as much as



1 possible, § 707(b)(2)(A)(ii)(I) could only be interpreted to  
2 “apply” expense standards in cases where debtors in fact pay such  
3 expenses.

4 Of course, as the majority notes, the somewhat inconsistent  
5 holdings of Kagenveama and Ransom are not binding as to the  
6 resolution of this case since they did not address the issue  
7 presented here on appeal. However, I part with the majority’s  
8 contention that the Kagenveama court’s statutory analysis and  
9 discussion about how projected disposable income should be  
10 calculated was “made casually and without analysis,” and can be  
11 dismissed as mere dicta. Instead, I believe the statutory  
12 analysis undertaken by the Ninth Circuit in Kagenveama provides  
13 important guidance for the interpretation of § 1325(b)(2) and  
14 (b)(3).

15 In Kagenveama, the Ninth Circuit was confronted, as we are  
16 here, with interpreting a subsection of § 1325(b) that contains  
17 an imbedded definition in a following subsection. It did not  
18 read the sections sequentially. Rather, the court held that the  
19 definition of “disposable income” in § 1325(b)(2) gave meaning to  
20 the phrase “projected disposable income” in § 1325(b)(1)(B). 541  
21 F.3d at 873. The Kagenveama court refused to “de-couple  
22 ‘disposable income’ from the ‘projected disposable income’  
23 calculation simply to arrive at a more favorable result for  
24 unsecured creditors, especially when the plain text and precedent  
25 dictate[d] the linkage of the two terms.” Id. at 875.

26 I agree with the courts that find the most natural reading  
27 of § 1325(b)(3) “commands the application of Section 707(b)(2)(A)  
28 and (B) to determine the meaning of the amounts ‘reasonably

1 necessary to be expended' " under § 1325(b) (2). In re Burbank,  
2 401 B.R. 67, 73 (Bankr. D.R.I. 2009) (citing In re Quigley, 391  
3 B.R. 294, 299 (Bankr. N.D. W.Va. 2008)). Because § 1325(b) (3)  
4 contains the definition of "amounts reasonably necessary to be  
5 expended," it must be read to give meaning to what is to be  
6 deducted by an above median-income debtor in order to determine  
7 disposable income. The bankruptcy court correctly analyzed  
8 § 1325(b) (2) and (b) (3):

9       As with "disposable income," the term "amounts  
10       reasonably necessary to be expended" appears only twice  
11       in § 1325; once in § 1325(b) (2) and then in  
12       § 1325(b) (3). If the Court were to require an  
13       additional requirement that the expense also be  
14       necessary for a debtor's "maintenance or support," it  
15       would likewise render as surplusage the clear direction  
16       in § 1325(b) (3) as to how "amounts reasonably necessary  
17       to be expended" shall be determined.

18 In re Smith, 401 B.R. 469, 474 (Bankr. W.D. Wash. 2008).

19       As another court noted, "§ 1325(b) (3) states that the  
20       amounts determined to be reasonably necessary under § 1325(b) (2)  
21       shall be determined in accordance with § 707(b) (2) (A) and (B)--  
22       period. The term 'reasonably necessary' in § 1325(b) (3) is not  
23       superfluous--it is the very term that this section defines. For  
24       that reason, . . . courts may [not] conduct a separate  
25       'reasonably necessary' analysis beyond § 707(b) (2)." In re Van  
26       Bodegom Smith, 383 B.R. 441, 448 (Bankr. E.D. Wis. 2008)  
27       (ultimately holding that payments on surrendered collateral are  
28       not "scheduled as contractually due" under § 707(b) (2) (A) (iii) (I)  
and, therefore, cannot be deducted in a debtor's means test  
calculation).

      I do not agree that § 1325(b) (2) and (b) (3) should be read  
sequentially and am unswayed by the majority's reliance on a

1 hypothetical situation of an above-median income debtor engaged  
2 in business to support its contention that this is the correct  
3 way to read the statute. Section 707(b)(2)(A)(ii) provides that  
4 a "debtor's monthly expenses shall be the debtor's applicable  
5 monthly expense amounts specified under the National Standards  
6 and Local Standards, and the debtor's actual monthly expenses for  
7 the categories specified as Other Necessary Expenses issued by  
8 the [IRS]. . . ." 11 U.S.C. § 707(b)(2)(A)(ii)(I).

9 Business expenses are considered Other Necessary Expenses as  
10 specified in the IRS Financial Analysis Handbook. Drummond v.  
11 Wiegand (In re Wiegand), 386 B.R. 238, 243 n.11 (9th Cir. BAP  
12 2008); In re Arnold, 376 B.R. 652, 654-55 (Bankr. M.D. Tenn.  
13 2007). The IRS Financial Analysis Handbook provides for expenses  
14 that are necessary for production of income: "[i]f the taxpayer  
15 substantiates and justifies the expense, the minimum payment may  
16 be allowed. The necessary expense test of health and welfare  
17 and/or production of income must be met. . . ." Int. Rev. Man.  
18 Fin. Analysis Handbook, § 5.15.1.10 (available at  
19 <http://www.irs.gov/irm/>). Therefore, an above-median income  
20 debtor engaged in business may deduct his or her actual Other  
21 Necessary Expenses (via § 1325(b)(3)'s reference to  
22 § 707(b)(2)(A)) as long as those expenses are substantiated and  
23 necessary. As a result, business expenses do not require a  
24 separate determination of necessity in § 1325(b)(2) as the  
25 majority asserts. Section 1325(b)(2)(B) is not rendered  
26 meaningless but continues to apply to below-median income debtors  
27 who have business expenses.

28 The statutory analysis put forth by the majority, which

1 reads § 1325(b) (2) and (3) sequentially, essentially adds  
2 language to § 1325(b) (3) to read "after it is determined the  
3 expense is reasonably necessary, then the amounts reasonably  
4 necessary to be expended shall be determined in accordance with  
5 § 707(b) (2)." Such a strained analysis also reads out the  
6 "reasonably necessary" language in calculations under  
7 § 707(b) (2) (A) for Other Necessary Expenses.

8 I cannot join my colleagues in an interpretation that upends  
9 the statutory inclusion of the means test in chapter 13,  
10 reverting back to the pre-BAPCPA judicial discretion as to what  
11 expenses of a debtor are reasonably necessary. See Kagenveama,  
12 541 F.3d at 874 (deliberate departure from the pre-BAPCPA  
13 disposable income calculation was so that debtors would "be  
14 subject to clear, defined standards, no longer left to the whim  
15 of a judicial proceeding" (citation omitted)). The majority  
16 contends the discretion of the bankruptcy court, under its  
17 analysis, is only to hold debtors to the consequences of their  
18 decisions about what assets they retain or surrender; however,  
19 the reality of the majority's interpretation of the statute is  
20 that bankruptcy courts will have the discretion to make  
21 determinations about what expenses are "reasonably necessary."

22 While I sympathize with the majority's desire for a common-  
23 sense solution to the problem created by incorporating the means  
24 test into the chapter 13 above median-income debtor's calculation  
25 of disposable income, I do not believe it is the role of the  
26 judiciary to remedy outcomes that do not comport with our view of  
27 common sense. See Id. at 875 ("If the changes imposed by BAPCPA  
28 arose from poor policy choices that produced undesirable results,

1 it is up to Congress, not the courts, to amend the statute." ).

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