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Judicial Treatment of Charitable Donations in Bankruptcy Before and After the Religious Liberty and Charitable Contribution Protection Act of 1998

John J. Dyer*
Gregory Todd Jones**

I. INTRODUCTION

In seventeenth and eighteenth century England, courts protected creditors' rights by hanging uncooperative debtors.¹ In contrast, present day United States courts will not hang bankrupt debtors, but will protect them as well as their creditors' commercial interests.² This Article will focus on the judicial ramifications of one statutory protection that the federal government has given to debtors, the Religious Liberty and Charitable Donation Protection Act of 1998 (the "Donation Act"),³ and consider the influence that this protection has exerted on creditors' rights - an issue that is of significant import for practitioners in the areas of commercial law and bankruptcy.

Congress designed the Bankruptcy Code around two goals: allowing a debtor to obtain a fresh start, while at the same time treating creditors as fairly as possible.⁴ In 1978, when Congress reformed Chapter 13 of the Bankruptcy Code, it demonstrated concern for creditors' in-

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1. DOUGLAS G. BAIRD, *THE ELEMENTS OF BANKRUPTCY* 4 (1992).

2. Richard Collin Mangrum, *Tithing, Bankruptcy and the Conflict between Religious Freedom and Creditors Interests*, 32 CREIGHTON L. REV. 815, 818-19 (1999).

3. Religious Liberty and Charitable Donation Protection Act of 1988, Pub. L. No. 105-183, 112 Stat. 517 (codified at 11 U.S.C. § 548 (2004)).

4. Mangrum, *supra* note 2, at 819; *see also* Thomas M. Walsh, Note, *Religious Liberty and Charitable Donation Act of 1998: Putting the Fear of God into Bankruptcy Creditors*, 7 AM. BANKR. INST. L. REV. 235, 238-39 (1999) (stating that bankruptcy in the United States has a strong public policy of giving debtors a fresh start . . . [while] ensur[ing] the orderly distribution of a debtors assets to its creditors).

terests by requiring that debtors' plans be in the best interest of the unsecured creditors.⁵ Hence, bankruptcy courts frequently invalidated any Chapter 13 debtor's plan that included anything more than a nominal regular donation to a charity.⁶ Bankruptcy courts applied similar standards under Chapter 7 by refusing relief from debts resulting from a debtor's charitable donations.⁷

Although courts generally struck down debtors' charitable donations, in 1996, the Eighth Circuit ruled in favor of philanthropic debtors in *Christians v. Crystal Evangelical Free Church*.⁸ This case was seen as a major victory for charities, especially religious groups.⁹ There, the court held that a debtor's charitable gifts to his church could not be recovered by a bankruptcy trustee because of the Religious Freedom Restoration Act.¹⁰ However, the victory was short lived.

The Supreme Court announced its decision in *City of Boerne v. Flores*¹¹ one year after the first *Christians* decision was reported. In *Flores*, the Court held that the Religious Freedom Restoration Act was unconstitutional as applied to state law.¹² Interestingly, the *Flores* case did not deal with a church's receipt of money; rather, it was the result of a dispute between the Archbishop of San Antonio and the city government over the validity of a city ordinance that required the

5. C. Scott Pryor, *Tension Between the Trustee and the Tithes: Is P.L. 105-183 Absolution?*, 17 AM. BANKR. INST. J. 10, 36 (1999).

6. See generally *id.*; *In re Andrade*, 213 B.R. 765, 769 (Bankr. E.D. Ca. 1997) (recognizing that although a few courts have held that charitable donations were acceptable, that line of cases is the minority view and has been criticized) (citations omitted).

7. Oliver B. Pollack, *Be Just Before You're Generous: Tithing and Charitable Contributions in Bankruptcy*, 29 CREIGHTON L. REV. 527, 554 (1996) (citing *In re Sutliff*, 79 B.R. 151, 158 (Bankr. N.D.N.Y. 1987) (holding that the Chapter 13 and Chapter 7 standards for bankruptcy abuse by debtors were similar)). Pollack also notes, however, that a debtor who wishes to continue to make charitable contributions is better off filing for bankruptcy under Chapter 7 than under Chapter 13 because under Chapter 7 the debtors assets will be dispersed and the debt will be discharged quickly. *Id.* Therefore, the court will have less interest in the debtor's future income and budget. *Id.*

8. 82 F.3d 1407, 1417 (8th Cir. 1996) (holding that the Religious Freedom Restoration Act protects charitable donations from avoidance even if they are fraudulent), *vacated and remanded*, 141 F.3d 854 (8th Cir. 1998). It should be noted that although the Supreme Court vacated and remanded the Eighth Circuit's decision in *Christians* to be retried in light of the *City of Boerne v. Flores* opinion, the Eighth Circuit did not reverse its previous ruling. Pryor, *supra* note 5, at 35. The Eighth Circuit's decision upon remand supports the view that the *Flores* decision only affected state laws, and not bankruptcy law, which would indicate that *Christians* was still valid law despite the belief of many bankruptcy trustees otherwise. Walsh, *supra* note 4, at 249-50.

9. Walsh, *supra* note 4, at 249.

10. *Christians v. Crystal Evangelical Free Church*, 141 F.3d 854, 856 (8th Cir. 1998).

11. 521 U.S. 507 (1997).

12. *Id.* at 511.

church to obtain a building permit to enlarge the church in a historical district.¹³ The Court held that the church could not rely upon the Religious Freedom Restoration Act because it would be an unconstitutional burden on the states to invalidate a law which a state had passed with a showing of "a compelling [state] interest and . . . [which the state] adopted [using] the least restrictive means of achieving that interest"¹⁴ just because the law had a negligible effect upon a religious interest.¹⁵ It should be noted that the Court did not determine whether the Religious Freedom Restoration Act was unconstitutional as applied to federal law, i.e., the Bankruptcy Code.¹⁶

Concerned religious and charitable groups persuaded members of Congress that the *Flores* decision had a negative effect upon a debtor's right to donate money to charitable organizations.¹⁷ Congress quickly responded by passing the Donation Act.¹⁸ The Donation Act amended several provisions of the Bankruptcy Code (including 11 U.S.C. §§ 544, 548, 707, and 1325) in an effort to head off the perceived negative effect that the *Flores* decision would have on a bankrupt debtor's ability to make charitable donations.¹⁹

This Article will examine the effects that the Donation Act has *actually* had upon a debtor's ability to make charitable donations while petitioning for relief under various provisions of the Bankruptcy Code. First, it will offer a basic explanation of the general mechanics of each of the relevant bankruptcy provisions that will be discussed throughout the Article and of how a charitable contribution is normally analyzed under those provisions. Next, it will discuss how courts handled bankrupt debtors' charitable contributions before Congress passed the Donation Act. Third, it will analyze the different ways in which courts have interpreted the Donation Act since its enactment. Fourth, it will compare and contrast the ways in which courts have handled charitable donations by bankrupt debtors under the new law. The Article will conclude with a discussion about the actual effects, or lack thereof, that the Donation Act has had upon courts' treatment of debtors' charitable donations.

13. *Id.* at 512; see also Walsh, *supra* note 4, at 249.

14. *Flores*, 521 U.S. at 534. It should be noted that the Supreme Court did not expressly overturn the holding in *Christians*. See generally *id.*

15. *Id.*

16. See generally *Flores*, 521 U.S. 507 (1997) (determining the constitutionality with regard to a local law).

17. See 144 CONG. REC. H3999, H4000 (comments of Rep. Nadler) (stating that the Supreme Court's decision in *Flores* has left the Religious Freedom Restoration Act's ability to protect charitable donations by bankrupt debtors in doubt).

18. Walsh, *supra* note 4, at 250.

19. See 144 Cong. Rec. H3999-02, H4000, H4005 (1998).

II. BASIC MECHANICS OF RELEVANT BANKRUPTCY CODE PROVISIONS

To lay a foundation, Subsection A will describe the basic ideas behind Chapter 13 bankruptcy and the general functions of Bankruptcy Code provisions that normally control Chapter 13 cases affected by the Donation Act. Subsection B will discuss the basic concepts within Chapter 7 bankruptcy, the mechanics of the Bankruptcy Code provisions that normally govern Chapter 7 cases, and those provisions that were changed by the Donation Act. In addition, Subsection B will examine a Bankruptcy Code provision that was not changed by the Donation Act, but which often comes up in Chapter 7 bankruptcy cases and, as such, is relevant to the examination of courts treatment of charitable donations. Subsection C considers the effect of the Donation Act on provisions of the Bankruptcy Code commonly utilized in both Chapter 7 and Chapter 13 cases.

A. Chapter 13 Bankruptcy

Chapter 13 allows debtors to retain their assets when filing for bankruptcy, while simultaneously gaining the benefit of having their debts discharged.²⁰ Upon filing for relief under Chapter 13, debtors must submit several reports, called schedules, which describe their expected monthly income and their necessary monthly expenses.²¹ The bankruptcy trustee²² will then subtract the debtor's necessary monthly expenses from the debtor's monthly income, the difference of which is recognized as the debtor's disposable income.²³

A debtor must then agree to divert all of his disposable income into a bankruptcy fund or estate which is managed by the bankruptcy trustee, who will disperse the funds appropriately, according to a hierarchy of creditors.²⁴ Chapter 13 debtors must continue to pay creditors all of their disposable income for a designated amount of time, usually three to five years.²⁵

20. DOUGLAS G. BAIRD & THOMAS H. JACKSON, CASES, PROBLEMS AND MATERIALS ON BANKRUPTCY 907-08 (1985) (citing *Ravenot v. Rimgale* (*In re Rimgale*), 669 F.2d 426 (7th Cir. 1982)).

21. *Id.* at 907-12.

22. The bankruptcy trustee is the person who is charged by the bankruptcy courts with the responsibility of reviewing and overseeing the maintenance of the bankruptcy plan. *See id.* at 44-45.

23. *Id.* at 907-12.

24. *Id.*

25. 11 U.S.C. § 1322(d) (2003) (stating that courts may approve plans of up to three years and can approve plans of up to five years if the circumstances make such a plan necessary); *see* John B. Butler III, *A Chapter 13 Trustee Looks at Section 1325(b) of the Bankruptcy Code*, 63 AM.

1. A Look At 11 U.S.C. § 1325(b)²⁶

Section 1325(b) provides the requisite elements needed in order to qualify for disposable income.²⁷ Prior to the Donation Act's enactment, 11 U.S.C. § 1325(b)(2) defined disposable income as:

- [I]ncome which is received by the debtor and which is not reasonably necessary to be expended -
- (A) for the maintenance or support of the debtor or a dependant of the debtor . . . and
 - (B) if the debtor is engaged in business, for the payment of expenditures necessary for the continuation, preservation, and operation of such business.²⁸

This definition of disposable income gave the courts a considerable amount of discretion in determining what qualified as a reasonably necessary expense.²⁹ In an attempt to clarify whether a charitable donation was a reasonably necessary expense, the Donation Act amended § 1325(b)(2)(A) and:

[A]dd[ed] the words "including charitable contributions (that meet the definition of 'charitable contribution' under 548(d)(3)) to a qualified religious or charitable entity or organization (as that term is defined in § 548(d)(4)) in an amount not to exceed 15 percent [sic] of the gross income of the debtor for the year in which the contributions are made."³⁰

Although this amendment seems to have clarified the issue of whether charitable contributions can satisfy the demands of the § 1325(b) disposable income test, there are issues left unsettled that still give courts discretion over the matter.³¹

It should also be noted that although the disposable income test is a provision that is directly applicable in Chapter 13 cases, courts have applied its principles as a means of reaching a decision under other provisions of the Bankruptcy Code.³²

BANKR. L.J. 401, 413 (1989) (citing *In re Krull*, 54 B.R. 375, 377 (Bankr. D. Colo. 1985)) (commenting that at least one court has held that all disposable income to be paid to creditors for up to three years); Mindy L. Silver, Recent Development, *The Disposable Income Test: An Attempt Toward Uniformity*, 4 BANKR. DEV. J. 221 (1987).

26. 11 U.S.C. § 1325(b) (2002).

27. 11 U.S.C. § 1325(b)(2) (2002).

28. Silver, *supra* note 25, at 221 n.1 (quoting 11 U.S.C. § 1325(b) (West Supp. 1985)).

29. Butler, *supra* note 25, at 408-09.

30. COLLIER ON BANKRUPTCY 1325-57 (Alan N. Resnick et al. eds., 15th ed. 2003).

31. See *In re Buxton*, 228 B.R. 606 (Bankr. W.D. La. 1999) (holding that although Congress amended the 11 U.S.C. § 1325(b) disposable income test to allow some charitable contributions, the Code still imposes a reasonableness requirement on the donations).

32. See *In re Shimula*, 234 B.R. 240 (Bankr. D.R.I. 1999) (applying the § 1325 disposable income test to a § 707(b) substantial abuse analysis); *In re Laman*, 221 B.R. 379 (Bankr. N.D. Tex. 1998) (applying the § 1325(b) disposable income test to a Chapter 7 § 707(b) substantial abuse analysis); *Feldmann v. Feldmann* (*In re Feldmann*), 220 B.R. 138 (Bankr. N.D. Ga. 1998) (apply-

B. *Bankruptcy Under Chapter 7*

When a debtor files for Chapter 7 bankruptcy she will not be allowed to keep all of her assets. Instead her non-exempt assets³³ will be sold or liquidated by a bankruptcy trustee who will then distribute the proceeds to creditors according to bankruptcy regulations.³⁴

1. The Substantial Abuse Provision: 11 U.S.C. § 707

Section 707(b) states that when a petitioner seeking relief under Chapter 7 has primarily consumer debt, a court may act *sua sponte* or in response to a trustee's motion, and decide to dismiss a debtor's petition for bankruptcy relief if it finds that discharging the debt "would be a substantial abuse."³⁵ Bankruptcy courts use this power to disallow a debtor relief when the court determines that the debtor can afford to pay her debts out of future earnings.³⁶ However, § 707(b) does not include a clear indication that the ability to pay should be the determining factor in deciding whether granting a debtor relief would result in substantial abuse. Hence, not all courts will deny a claim for bankruptcy relief based solely on a debtor's ability to pay out future earnings.³⁷ Prior to the enactment of the Donation Act, the language of § 707(b) read as follows:

(b) After notice and a hearing the court, on its own motion or on a motion by the United States trustee, but not at the request or suggestion of any party in interest, may dismiss a case filed by an individual debtor under this chapter whose debts are primarily consumer debts if it finds that the granting of relief would be a substantial abuse of the provisions of this chapter. There shall be a presumption in favor of granting the relief requested by the debtor.³⁸

ing the § 1325(b) disposable income test to a § 523(a)(15) ability to pay analysis); *In re Smither*, 194 B.R. 102 (Bankr. W.D. Ky. 1996) (holding that the § 1325(b) disposable income test case law had been adopted by courts applying § 523(15)); *Lynn v. Diversified Collection Serv.* (*In re Lynn*), 168 B.R. 693 (Bankr. D. Ariz. 1994) (holding that the § 1325(b) definition of disposable income was applicable in making a § 523(a)(8) determination)).

33. When determining whether a piece of property is exempt or part of the bankruptcy estate, the trustee must first look to 11 U.S.C. § 541 to see if the asset fits into the federal bankruptcy laws' definition of property of the estate. BAIRD, *supra* note 1, at 38-45. If the asset is not correctly classified as property of the estate then the trustee cannot capture it. *Id.* If the asset is correctly classified as property of the estate under 11 U.S.C. § 541 then 11 U.S.C. § 522 mandates that the trustee must look to state and federal non-bankruptcy laws to see if there are any statutes which define the asset as exempt. *Id.* If there are any such statutes then the asset is exempt, if not the asset is non-exempt and can be liquidated by the trustee. *Id.*

34. BAIRD & JACKSON, *supra* note 20, at 44-45.

35. BAIRD, *supra* note 1, at 34.

36. *Id.*

37. *See id.*

38. 11 U.S.C. § 707(b) (West Group 1994).

The Donation Act amended § 707(b) to include the words “[i]n making a determination whether to dismiss a case under this section, the court may not take into consideration whether a debtor has made, or continues to make, charitable contributions.”³⁹ Following this amendment, courts were no longer allowed to consider a debtor’s charitable contributions in determining whether the debtor had an ability to pay creditors out of future earnings when conducting a § 707(b) substantial abuse analysis.⁴⁰

Under § 707(a) a court may dismiss a case “for cause” following notice to the debtor and a hearing.⁴¹ When making a determination of whether to dismiss a case for cause under § 707(a), courts have applied a totality of the circumstances test which allows a court to look at all of the circumstances surrounding the debtor’s bankruptcy and decide whether granting the debtor relief would be equitable.⁴² It is important to note that, unlike § 707(b), the Donation Act did not prohibit courts from considering a debtor’s charitable donations when deciding cases under § 707(a).⁴³ It is also important to note that there is no restriction preventing a party from filing a motion to dismiss under § 707(a) - unlike the § 707(b) motions to dismiss, which can only be raised by the court itself or by the bankruptcy trustee.⁴⁴ Thus, under § 707(a), a creditor may file a motion to dismiss for cause which will prompt the courts to apply roughly the same test as they would apply in a § 707(b) analysis, however, in the § 707(a) situation the courts will be able to consider the debtor’s charitable contributions.⁴⁵ The result of a dismissal under § 707(a) is the same as a dismissal under § 707(b); the debtor is denied discharge of their debts.

39. 11 U.S.C. § 707(b) (2003).

40. See generally RESNICK, *supra* note 30, at 1325-57.

41. 11 U.S.C. § 707(a) (2003). 707(a) states:

- (a) The court may dismiss a case under this chapter after notice and a hearing and only for cause, including -
- (1) unreasonable delay by the debtor that is prejudicial to creditors;
 - (2) nonpayment of any fees [or] and charges required under chapter 123 of title 28; and
 - (3) failure of a debtor in a voluntary case to file, within fifteen days or such additional time as the court may allow after filing of the petition commencing such case, the information required by paragraph (1) of section 521, but only on a motion by the United States trustee.

Id.

42. *In re Collins*, 250 B.R. 645, 654 (Bankr. N.D. Ill. 2000).

43. *Id.*

44. 11 U.S.C. § 707(a), (b) (2003); *In re Collins*, 250 B.R. 645, 654 (Bankr. N.D. Ill. 2000).

45. *Collins*, 250 B.R. at 654.

C. *Generally Applicable Provisions of the Bankruptcy Code*

The provisions discussed below are commonly utilized in both Chapter 7 and Chapter 13 bankruptcy cases.

1. 11 U.S.C. § 548⁴⁶

Section 548 is the provision of the Bankruptcy Code which deals with fraudulent transfers of funds.⁴⁷ This provision allows a Chapter 13 bankruptcy trustee to reach back and avoid transfers of funds made by debtors within one year prior to the debtor filing for bankruptcy.⁴⁸ Prior to the enactment of the Donation Act, the relevant provisions of § 548 read as follows:

(a) The trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor, that was made or incurred on or within one year before the date of the filing of the petition, if the debtor voluntarily or involuntarily

(1) made such transfer or incurred such obligation with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made or such obligation was incurred, indebted; or

(2)(A) received less than a reasonably equivalent value in exchange for such transfer or obligation; and

(B)(i) was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation⁴⁹

The pre-amendment version of § 548, as quoted above, allowed courts to avoid both transfers that were actually fraudulent⁵⁰ and those that were constructively fraudulent, including donations made to charitable organizations.⁵¹ Section 548 handles actual and constructively fraudulent transfers separately.⁵² Section 548(a)(1)(A) demands evidence of actual intent to defraud creditors, while § 548(a)(1)(B) allows a trustee to avoid a transfer despite a lack of any evidence of actual intent to defraud creditors.⁵³

46. 11 U.S.C. § 548 (2003).

47. 11 U.S.C. § 548 (2003).

48. *See id.* § 548(a)(1).

49. *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 535 n.2 (1994) (quoting 11 U.S.C. § 548 (1988)).

50. *See* 11 U.S.C. § 548(a)(1).

51. *See* 11 U.S.C. § 548(a)(2); *see also* Steven Walt, *Generosity in Bankruptcy: The New Place of Charitable Contributions in Fraudulent Conveyance Law*, 32 *LOY. L.A. L. REV.* 1030-31 (1999) (stating that the unamended version of 11 U.S.C. § 548(a)(2) permitted a court to hold a donation as constructive fraud where a debtor did "not receive reasonably equivalent value" for the transfer).

52. 11 U.S.C. § 548 (2003).

53. Mangrum, *supra* note 2, at 815 n.2.

The Donation Act amended § 548 to prevent bankruptcy trustees from using it to avoid charitable donations made by insolvent debtors during the year before they filed for bankruptcy.⁵⁴ The amended 11 U.S.C. § 548 states:

(a)(2) A transfer of a charitable contribution to a qualified religious or charitable entity or organization shall not be considered to be a transfer covered under paragraph (1)(B) in any case in which

(A) the amount of that contribution does not exceed 15 percent of the gross annual income of the debtor for the year in which the transfer of the contribution is made; or

(B) the contribution made by a debtor exceeded the percentage amount of gross annual income specified in subparagraph (A), if the transfer was consistent with the practices of the debtor in making charitable contributions

(d)(3) In this section, the term “charitable contribution” means a charitable contribution, as that term is defined in section 170(c) of the Internal Revenue Code of 1986, if that contribution

(A) is made by a natural person; and

(B) consists of

(i) a financial instrument (as that term is defined in section 731(c)(2)(C) of the Internal Revenue Code of 1986); or

(ii) cash

(4) In this section, the term “qualified religious or charitable entity or organization” means

(A) an entity described in section 170(c)(1) of the Internal Revenue Code of 1986; or

(B) an entity or organization described in section 170(c)(2) of the Internal Revenue Code of 1986.⁵⁵

Although this amendment may protect constructively fraudulent transfers, it does not offer any protection for those transfers that are acts of actual fraud.⁵⁶

2. 11 U.S.C. § 544(b)

Section 544(b) grants bankruptcy trustees the power to avoid transfers made by debtors in violation of state laws.⁵⁷ The ability of trustees to avoid transfers under applicable state law is a significant power as it can allow a trustee to use the applicable state’s reach back period,

54. See CONG. REC. H3999-02, H4000 (1998) (statement of Mr. Nadler) (stating that “[t]his legislation would protect religious and charitable donations in bankruptcy proceedings by clarifying that they are not fraudulent transfers”); see also *Walt*, *supra* note 52, at 1030-31.

55. 11 U.S.C. § 548 (2003).

56. *Walsh*, *supra* note 4, at 259.

57. *Pryor*, *supra* note 5, at 36.

which is usually longer than the one year limit provided by § 548.⁵⁸ Prior to the enactment of the Donation Act, § 544 read as follows:

(b)The trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502 of this title or that is not allowable only under section 502(e) of this title.⁵⁹

The Donation Act amended § 544 to disallow a trustee the ability to use state laws to avoid transfers made before the debtor filed for bankruptcy.⁶⁰ The Donation Act's amendment of § 544 states in relevant part:

(b)(1) Except as provided in paragraph (2), the trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502 of this title or that is not allowable only under section 502(e) of this title.

(2) Paragraph (1) shall not apply to a transfer of a charitable contribution (as that term is defined in section 548(d)(3)) that is not covered under section 548(a)(1)(B), by reason of section 548(a)(2). Any claim by any person to recover a transferred contribution in the preceding sentence under Federal or State law in a Federal or State court shall be preempted by the commencement of this case.⁶¹

However, it has been argued that the amendment to § 544 is defective because it only disallows state law avoidance of transfers which are not covered by § 548(a)(1)(B), the constructive fraud provision of the statute, by virtue of the language of § 548(a)(2), the provision which creates an exception for charitable donations.⁶² The contention is that this statutory language is faulty because it allows a trustee the opportunity to make a reasonable argument that because § 544 limits its protection to only those transfers which would have been covered by § 548(a)(1)(B), i.e. those made within one year before the debtor filed for bankruptcy, the amended version of § 544 does not offer protection for transfers made earlier than one year before the debtor filed for bankruptcy from attack under state laws.⁶³ Thus, as Professor Walt indicates, if a state law has a five year reach back provision an unsecured creditor *may* be able to use that law to attack a transfer

58. Walsh, *supra* note 4, at 239 n.21 (noting that "New York[, for example,] has a six year reach back period").

59. 11 U.S.C. § 544(b) (West Group 1999).

60. See generally RESNICK, *supra* note 30, at 1325-57.

61. 11 U.S.C. § 544(b) (2003); see also Pryor, *supra* note 5, at 36 (noting that the Donation Act amended 11 U.S.C. § 544(b)).

62. Walt, *supra* note 52, at 1035.

63. *Id.* at 1035-37.

made by a debtor anytime between one and five years prior to filing for bankruptcy.⁶⁴

3. 11 U.S.C. § 523⁶⁵

Section 523 of the Bankruptcy Code provides that certain types of debt are non-dischargeable even if the debtor is granted relief via one of the Bankruptcy Code chapters.⁶⁶ Section 523 contains a lengthy list of debts that cannot be discharged, including debts for fraud, willful and malicious injury caused by the debtor, certain taxes, child support, divorce support, and student loans.⁶⁷ This section will focus on §§ 523(a)(8) and (15) which deal with student loans and divorce support payments, respectively.⁶⁸ Section 523(a)(8) provides that student loans are generally not dischargeable, however the court can make exceptions if payment of the debt would be an “undue hardship.”⁶⁹ The language providing this exception states that:

(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title [these are the provisions granting discharge from debt under Chapters 7, 11, 12, and 13 respectively] does not discharge an individual debtor from any debt

(8) for an educational benefit overpayment or loan made . . . by a governmental unit or nonprofit institution, or for an obligation to repay funds received as an educational benefit, . . . unless excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor’s dependents.⁷⁰

This statutory language has been interpreted by courts to demand that a debtor satisfy three elements in order to successfully claim that repayment of their student loans would result in an undue hardship.⁷¹ The elements are as follows: first, the debtor must be unable to repay the loan and maintain a base standard of living; second, there must be proof that the debtor’s financial condition will remain the same for a large portion of the repayment period; and third, there must be proof that the debtor has made a good faith attempt to repay the loan before filing for bankruptcy.⁷²

64. *Id.*

65. 11 U.S.C. § 523 (2003).

66. *See id.*

67. *Id.* at § 523 (a)(1),(2),(4) - (6),(8),(15).

68. 11 U.S.C. 523(a)(8), (15) (2003).

69. *Id.* at § 523 (a)(8).

70. *Id.*

71. *See* Educ. Credit Mgmt. Corp. v. McLeroy (*In re* McLeroy), 250 B.R. 872, 878 (Bankr. N.D. Tex. 2000); *See also* Wegrzyniak v. United States (*In re* Wegrzyniak), 241 B.R. 689, 691-92 (Bankr. D. Idaho 1999).

72. *See* McLeroy, 250 B.R. at 878; *see also* Wegrzyniak, 241 B.R. at 691-92.

Although § 523 was not amended by the Donation Act,⁷³ it is relevant to this discussion because bankrupt debtors have attempted to use the Donation Act in order to seek protection for their charitable donations, while at the same time claiming that their student loans should not be excepted from discharge under the undue hardship provision of § 523(a)(8).⁷⁴ In addition, 11 U.S.C. § 523(a)(15)(A) provides an exception from the general rule that debt incurred as part of divorce or separation is non-dischargeable.⁷⁵ However, to qualify for the exception the debtor must show that he cannot pay the debt because after paying all of his reasonably necessary expenses, he does not have enough income left over to pay the debt.⁷⁶ Section 523(a)(15)(A) states that a debt resulting from a divorce is not dischargeable, unless the debtor does not have the ability to pay such debt from income or property of the debtor not reasonably necessary to be expended for the maintenance or support of the debtor or a dependent of the debtor.⁷⁷ Again, although the Donation Act did not amend § 523(a)(15)(A), debtors have tried to use the Donation Act to protect their charitable donations by asking the court to include their donations as an expense that is reasonably necessary for their support.⁷⁸

III. JUDICIAL TREATMENT OF CHARITABLE DONATIONS IN BANKRUPTCY

A. *Before the Donation Act*

This section will examine the facts and holdings of bankruptcy cases where the debtor had made or planned to make charitable donations prior to the Donation Act.

1. Charitable Contribution Cases under § 1325(b)

In *Zaleski*,⁷⁹ the Bankruptcy Court for the District of North Dakota held that a debtor's Chapter 13 plan could not be confirmed because it violated § 1325(b)(2).⁸⁰ In *Zaleski* the debtors presented a plan which contained several expenses, including a monthly charitable donation of \$65.00, that the court found to be excessive and in violation of the

73. 11 U.S.C. § 523 (2003).

74. See *McLeroy*, 250 B.R. 872; see also *Wergzyniak*, 241 B.R. at 693.

75. 11 U.S.C. § 523(a)(15)(A) (2003).

76. See *id.*

77. *Id.*

78. See *Dennison v. Hammond (In re Hammond)*, 236 B.R. 751, 760 (Bankr. D. Utah 1998).

79. *In re Zaleski*, 216 B.R. 425 (Bankr. D.N.D. 1997).

80. *Id.* at 432-33.

spirit of § 1325(b)(2).⁸¹ The court specifically stated that the charitable donation could not reasonably be classified as necessary for the family's maintenance.⁸² The court lumped the charitable donations in with expenses such as unspecified recreation and an unidentified dental plan, thus indicating that charitable contributions were to be given no special treatment.⁸³

Likewise, in *Saunders*,⁸⁴ the Bankruptcy Court for the District of Massachusetts held that a debtor's plan could not be confirmed because the plan included a \$400.00 monthly donation to their church.⁸⁵ The court held that it would be inappropriate to allow a person to donate money to a church when the same donation to a non-religious group would be a violation of § 1325(b).⁸⁶ The court reasoned in reaching its conclusion that bankrupt debtors do not have a right to tithe - stating that "[a]bsent the most unusual circumstances, one's religion ought not to affect one's legal rights or duties or benefits."⁸⁷

Conversely, in 1989 the Bankruptcy Court for the District of Connecticut held that a bankrupt debtor's charitable contribution to his church was a "reasonably necessary expenditure" within the meaning of § 1325(b)(1)(B).⁸⁸ In the *Bien*⁸⁹ case, the debtor filed for relief under Chapter 13.⁹⁰ The bankruptcy trustee objected under § 1325(b)(1)(B) because the trustee believed that the debtor's plan did not distribute all of the debtor's disposable income to the creditors.⁹¹ The debtor's plan claimed a monthly income of \$2,732.08 and monthly expenses of \$2,621.48.⁹² The debtor planned to pay his creditors \$85.00 per month out of the \$110.60 difference between his income and expenses.⁹³ The trustee's primary objection was that \$391.65 of the debtor's monthly expenses went to the Mormon church as a tithe.⁹⁴ The parties stipulated that, although tithing was not re-

81. *Id.* at 432 (noting that \$200.00 per month for wear and tear on a leased car and \$416.00 per month for a new truck were also excessive and that the truck expense was "an absurd luxury bordering on the lifestyles of the rich and famous").

82. *Id.*

83. *See id.*

84. *In re Saunders*, 215 B.R. 800 (Bankr. D. Mass. 1997).

85. *Id.* at 802-03.

86. *Id.* at 803.

87. *Id.* (citing *Bd. of Educ. v. Grumet*, 512 U.S. 687 (1994)) (O'Connor, J., concurring in part and in judgment).

88. *In re Bien*, 95 B.R. 281, 282 (Bankr. D. Conn. 1989).

89. *Bien*, 95 B.R. at 281.

90. *Id.* at 281.

91. *Id.*

92. *Id.*

93. *Id.* at 281.

94. *See Bien*, 95 B.R. at 281.

quired of all members of the Mormon church, only tithing members may participate fully in the church's activities.⁹⁵ The court held that religion is fundamental for many people and that the Mormon Church was a fundamental part of the debtor's life in this case.⁹⁶ Hence, because the church required the debtor to tithe before it would allow him to participate fully in the church, the charitable donation was not disposable income under § 1325(b)(2)(A).⁹⁷ Thus, for this court the determinative factor was that the debtor actually received something tangible for his money.⁹⁸

2. Charitable Contribution Cases under § 707

In *Laman*,⁹⁹ the Bankruptcy Court for the Northern District of Texas held that it would be a substantial abuse of the bankruptcy system to allow a debtor to discharge his debt under Chapter 7 because the court found that the debtor did have the ability to pay his creditors without resorting to Chapter 7 liquidation.¹⁰⁰ The court reasoned that when determining whether a debtor had an ability to pay his debt, the correct test would be to determine if the debtor could afford to pay a significant dollar amount, irrespective of percentage, to unsecured creditors through such a Chapter 13 . . . plan.¹⁰¹ The fact that the court found a number of expenses, including a monthly charitable donation of at least \$200.00 that is not allowed under § 1325(b)(2)(A), supported its conclusion that the debtors, had they applied for Chapter 13 relief, could have supported themselves and paid their creditors sufficiently.¹⁰²

Likewise in *Lee*,¹⁰³ the court dismissed the debtors' Chapter 7 petition under § 707(b) where the debtor planned to begin donating \$350.00 per month to his church after he filed for bankruptcy.¹⁰⁴ The court held that the debtor's charitable donations should be included as part of his disposable income, and that therefore the debtor had the

95. *Bien*, 95 B.R. at 281-82 (noting that any non-full tithing members of the Mormon church may not attend services nor pray in the central church in Salt Lake City nor can those members hold a Temple Recommend nor be called to serve in offices of responsibility within the church).

96. *Id.* at 283.

97. *See id.* at 283.

98. *See id.*

99. *In re Laman*, 221 B.R. 379 (Bankr. N.D. Tex. 1998).

100. *Id.* at 383.

101. *Id.* at 383-84.

102. *See id.* at 382-83 (noting that in addition the charitable donation the debtors had other excessive expenses such as \$120.00 per month for dry cleaning, \$267.00 per month in telephone bills and \$500.00 per month for clothes).

103. *In re Lee*, 162 B.R. 31 (Bankr. N.D. Ga. 1993).

104. *Id.* at 32; *see also* Pollak, *supra* note 9, at 557.

ability to repay his creditors.¹⁰⁵ The court then found that under the circumstances it would have been a substantial abuse of the bankruptcy system to allow the debtor's claim to proceed and dismissed the claim under § 707(b).¹⁰⁶

3. Charitable Contribution Cases under § 548

The Bankruptcy Court for the District of Kansas avoided charitable contributions under § 548 in the *Newman* case.¹⁰⁷ There, the debtors were an elderly husband and wife who had made monthly donations to their church in the year prior to filing for bankruptcy.¹⁰⁸ The court held that the debtors did not receive reasonably equivalent value for \$2,442.22 of the \$2,457.72 total amount transferred to the church during the year before they filed.¹⁰⁹ The strength of the debtors' religious beliefs was found irrelevant in determining whether the debtors had received equivalent value for their donations.¹¹⁰ Instead, the court decided to focus on any economic or tangible benefits that the debtors may have received in exchange for their money; the court subsequently found that the debtors had received no such benefits.¹¹¹ In articulating its reasons for avoiding the donations, the court noted that 400 years ago those who created the bankruptcy laws from which our Bankruptcy Code was developed decided, for policy reasons, that certain transactions should be recoverable by creditors without any evidence of fraud.¹¹²

Conversely, the Bankruptcy Court for the Northern District of Georgia returned the exact opposite verdict on nearly identical facts in the *Moses* case.¹¹³ There the court refused to avoid the debtors' transfers, which totaled \$4,733.50, because it felt that the debtors had received reasonably equivalent value in exchange for their donations.¹¹⁴ In its reasoning, the court actually stated that the debtors did not receive anything tangible in exchange for their contributions, but held that they did receive some return on their money in the form of counseling and the benefit of the heat and air conditioning provided

105. *In re Lee*, 162 B.R. 31, 32 (Bankr. N.D. Ga. 1993); see also Pollak, *supra* note 9, at 557.

106. See *In re Lee*, 162 B.R. 31, 43 (Bankr. N.D. 1993).

107. *Newman v. Midway S. Baptist Church (In re Newman)*, 183 B.R. 239, 242-43 (Bankr. D. Kan. 1995).

108. *Id.* at 243-44.

109. *Id.* at 243, 246.

110. *Id.* at 246.

111. *Id.*

112. *Id.* at 245.

113. See *Moses v. Chapel Hill Harvester Church, Inc. (In re Moses)*, 59 B.R. 815 (Bankr. N.D. Ga. 1986).

114. *Id.* at 816, 818-19.

by the church during its services.¹¹⁵ Also, the court took note of the fact that there was no indication of fraudulent intent on the part of the debtors,¹¹⁶ a factor that the *Newman* court would declare irrelevant.¹¹⁷

4. Charitable Contribution Cases under § 523

In *Lynn*,¹¹⁸ the Bankruptcy Court for the District of Arizona held that a debtor's charitable donations were an inappropriate expense under § 523(a)(8).¹¹⁹ There, the court considered whether her charitable donations were a "necessary expense for [her] maintenance and support . . . [which should] be omitted from [her] 'disposable income.'"¹²⁰ The court then held that because the debtor did not receive services from her church in exchange for her donations, the donations could not be characterized as a necessary living expense.¹²¹ The court concluded that the debtor's student loans were non-dischargeable.¹²²

In *Feldmann*,¹²³ the Bankruptcy Court for the Northern District of Georgia held that a debtor was not eligible for a discharge of his divorce related debt under § 523(a)(15).¹²⁴ In reaching this conclusion, the court had to determine whether the debtor had sufficient disposable income to pay the debt.¹²⁵ The court applied the disposable income test of § 1325(b) in its analysis.¹²⁶ Using § 1325(b) guidelines, the court looked to the debtor's claimed expenses, including his monthly donation to the University of Washington Boosters.¹²⁷ In its discussion of why the charitable contribution was not allowed, the court noted that the debtor had "no right to more discretionary in-

115. *Id.* at 818-19.

116. *Id.* at 819-20.

117. See *Newman v. Midway S. Baptist Church (In re Newman)*, 183 B.R. 239, 245 (Bankr. D. Kan. 1995).

118. *Lynn v. Diversified Collection Serv. (In re Lynn)*, 168 B.R. 693 (Bankr. D. Ariz. 1994).

119. *Id.* at 700. The debtor held "strong religious beliefs" that compelled her to donate ten percent of her income to the church. *Id.* at 696.

120. *Id.* at 697. The court expressly used the definition of disposable income found in § 1325(b)(2) of the Bankruptcy Code. *Id.* at 697 n.6.

121. *Id.* at 700. The court also noted that the debtors' church had express provisions that allowed members to cease donating in circumstances where the member is impoverished and that the debtor would not lose any privileges for failing to donate. See *id.*

122. *Id.* at 700.

123. *Feldmann v. Feldmann (In re Feldmann)*, 220 B.R. 138 (Bankr. N.D. Ga. 1998).

124. *Id.* at 144-45.

125. *Id.* at 145.

126. *Id.* at 144.

127. *Id.* at 145. The court also scrutinized the debtors' claims of \$25.00 per month for football tickets, \$350.00 per month for his 401K plan, and \$100.00 per month for recreation which did not include many items such as cable or dining which were accounted for under other expense categories. *Id.*

come than other debtors merely because [he] wish[ed] to use some of it to make charitable contributions."¹²⁸ The court then held that if one took all of the excess expenses that had been filtered out of the debtor's plan by the § 1325(b) disposable income test and added them together, the debtor would have at least \$500.00 per month of disposable income and a satisfactory ability to pay the debt.¹²⁹ Therefore, his Chapter 7 claim was dismissed under § 523(a)(15).¹³⁰

IV. CHARITABLE CONTRIBUTION CASES AFTER THE DONATION ACT

This Section will discuss how courts have interpreted charitable donations after the Donation Act on a provision by provision basis.

A. *A Look at Cases under § 1325(b)*

In the *Cavanagh*¹³¹ case, the Bankruptcy Court for the District of Montana held that the debtor's charitable donations were protected by the Donation Act and denied the trustee's motion to deny confirmation of the debtor's plan under § 1325(b)(2)(A).¹³² The debtors in *Cavanagh* submitted a plan to the trustee in which they claimed to have a monthly gross income of \$3,333.33 and monthly expenses of \$2,259.00.¹³³ The trustee took exception to the debtor's plan because it included a monthly charitable donation to the Mormon Church of \$234.00 which constituted a little more than seven percent of the debtor's monthly gross income.¹³⁴ The court held that the plain language of the Donation Act allows a debtor to shield up to fifteen percent of his gross income from attack under § 1325(b)(2)(A) if the debtor contributes the income to a charitable organization.¹³⁵ Because the debtor's donation only equaled about seven percent of his gross income, the donation was unavoidable.¹³⁶ The court also held that it was irrelevant that one of the debtors only recently joined the Mormon Church because, in the court's view, Congress did not make

128. *Id.* (quoting *In re Griffith*, 209 B.R. 823, 828 (Bankr. N.D.N.Y. 1996)).

129. *Feldmann*, 220 B.R. at 145.

130. *Id.* at 146-47.

131. *In re Cavanagh*, 242 B.R. 707 (Bankr. D. Mont. 2000).

132. *Id.* at 708.

133. *Id.* at 709.

134. *Id.* (noting that the \$234.00 monthly donation was not included in the debtor's original petition for bankruptcy, it first appeared on an amended petition which was filed as part of an addendum that the debtors submitted in response to the trustee's objections to their original petition).

135. *Id.* at 710-11.

136. *See Cavanagh*, 242 B.R. at 711.

any distinction between new contributions and “pre-petition contributions.”¹³⁷

Likewise, in *Bottelberghe*,¹³⁸ the court held that a debtor’s charitable donations were not in violation of § 1325(b).¹³⁹ The creditors in *Bottelberghe* took exception to the debtor’s plan, under which they would be paid only \$225.00 per month for fifty-five months, because of several of the debtor’s claimed expenses, including the debtor’s \$30.00 monthly donation to charities.¹⁴⁰ The court held that nearly all of the expenses, including the charitable contribution, were not questionable.¹⁴¹ However, although the charitable contribution was challenged under § 1325(b), the court did not make any mention of the Donation Act’s amendments, which specifically deal with charitable donations. Therefore, it was unclear whether the court validated the charitable contribution simply because it conformed with the statute, or first applied a reasonableness test, similar to the test articulated by the court in *Buxton*,¹⁴² before determining that the donation conformed with the provisions of § 1325(b).¹⁴³

In contrast, the Bankruptcy Court for the Western District of Louisiana held that the Donation Act did not protect a debtor’s charitable donations from a trustee’s § 1325(b) motion to deny confirmation.¹⁴⁴ In *Buxton*, the debtors were husband and wife who filed for relief under Chapter 13.¹⁴⁵ The debtors submitted a bankruptcy plan in which they claimed to earn a monthly net income of \$3,024.16 and to have \$2,702.00 of monthly expenses, of which \$280.00 per month would be donated to the debtors’ church.¹⁴⁶ Under the debtors’ plan they would submit \$330.00 per month¹⁴⁷ to the bankruptcy trustee for

137. *Id.* at 712.

138. *In re Bottelberghe*, 253 B.R. 256 (Bankr. D. Minn. 2000).

139. *Id.* at 264.

140. *Id.* at 259, 264.

141. *Id.* at 264 (noting that the court lumped the \$30.00 monthly charitable donation in with other expenses that the creditors claimed to be excesses such as \$200.00 per month for dental care, monthly pet expenses of \$16.00, a \$136.00 monthly life insurance premium, \$300.00 per month for clothes, and other similar expenses).

142. See discussion *infra* notes 145-153 and accompanying text.

143. *In re Bottelberghe*, 253 B.R. at 263-64 (finding that although the court did not confirm the debtors’ plan it did so because the debtor did not supply the court with sufficient information regarding his income to allow the court to do so).

144. See *In re Buxton*, 228 B.R. 606, 610 (Bankr. W.D. La. 1999).

145. *Id.* at 606.

146. *Id.* at 607.

147. *Id.* (noting, however the debtors’ plan called for a submission of only \$322.00 per month for the first two months).

distribution to creditors over a period of fifty-eight months.¹⁴⁸ The court held that the debtor's plan did not meet the requirements of § 1325(b)(2)(A) because, even after the Donation Act's amendment, the provision still demanded that all of the debtor's expenses be "reasonably necessary."¹⁴⁹ The court held that because Congress left the reasonably necessary language in 11 U.S.C. § 1325(b)(2)(A), it intended the courts to hold all debtors' transfers to that standard, regardless of whether or not they were donations to charitable organizations.¹⁵⁰ According to the court, the debtors' donations were not reasonably necessary for his maintenance and under the circumstances¹⁵¹ the debtors' plan could not withstand the trustee's § 1325(b) motion requesting that the plan not be confirmed.¹⁵²

Similarly, in *McDonald*,¹⁵³ the Bankruptcy Court for the Southern District of Florida held that a husband and wife's monthly charitable donation was not a reasonably necessary expense under § 1325(b).¹⁵⁴ The *McDonald* debtors submitted a Chapter 13 bankruptcy plan which included a \$320.00 monthly donation to their church.¹⁵⁵ The court did not mention the Donation Act amendments of § 1325.¹⁵⁶ Instead, the court recognized that the goal of Chapter 13 was to ensure that creditors recovered the maximum amount possible and held that allowing a debtor's charitable donations to his church to be classified as a necessary expense under § 1325 would impair the achievement of that goal.¹⁵⁷

148. *Id.* at 607 (noting that under this plan unsecured creditors would only receive \$225.00 of the \$7,500.00 that the debtors owed).

149. *In re Buxton*, 228 B.R. at 610.

150. *Id.* at 610.

151. *Id.* at 611 (finding it unreasonable, even under a discretionary spending allowance, to grant the debtor permission to donate \$280.00 per month to a church while only paying \$330.00 per month into the bankruptcy repayment plan).

152. *Id.*

153. *In re McDonald*, 232 B.R. 818 (Bankr. S.D. Fla. 1999).

154. *Id.* at 820.

155. *Id.* at 819.

156. *Id.*

157. *Id.* at 820. Interestingly, the court adopted the reasoning of *In re Andrade*, 213 B.R. 765, 770 (Bankr. E.D. Cal. 1997), *rev'd*, 141 F.3d 1407 (8th Cir. 1998) in reaching its decision. *Id.* at 820. The court in *Andrade* held that charitable contributions are never reasonably necessary expenses, but that all debtors are given a small amount of discretionary income and that a debtor could choose to spend his discretionary funds on his favorite charity, but he could not ask for additional discretionary funds because he donates his original allowable portion to charity. *Andrade*, 213 B.R. at 770-71. The *McDonald* court's adoption of this reasoning is interesting because the *Andrade* decision was overturned by the Ninth Circuit in 1998. *In re Andrade*, 141 F.3d 854 (8th Cir. 1998).

B. *Charitable Contribution Cases under Section 707*

In *Smihula*,¹⁵⁸ the Bankruptcy Court for the District of Rhode Island granted a trustee's section 707(b) motion to dismiss a debtor's Chapter 7 petition for relief where the debtor planned to make a monthly charitable donation of \$700.00 per month.¹⁵⁹ Of particular significance was the fact that the debtors' charitable donation was found only on the amendment to their original bankruptcy petition.¹⁶⁰ Their original petition contained nothing in charitable contributions.¹⁶¹ The court noted that this sudden generosity would destroy almost all of the debtors' disposable income given that the debtors claimed \$4,189.00 of monthly income and \$3,251.00 worth of monthly expenses *before* they filed the amended petition containing the charitable donations.¹⁶² Under the amended petition, the debtors' disposable income would drop from \$838.00 per month to only \$138.00 per month.¹⁶³ The debtors' claimed that the amended version of § 707(b) prohibited the court from using § 548(a)(1)(A) to characterize their donations as actually fraudulent.¹⁶⁴ The court disagreed and found the debtors' sudden decision to make large monthly donations on the eve of filing for bankruptcy dispositive in finding the donations as actually fraudulent.¹⁶⁵ Once the court recharacterized the donations as actually fraudulent transfers under § 548(a)(1)(A), it was free to consider the donation as part of the debtor's monthly disposable income when conducting its "ability to pay analysis" under § 707(b).¹⁶⁶ The court then concluded that, including the \$700.00 of donations, the debtors had sufficient disposable income to demonstrate an ability to pay their debts without depriving themselves of necessities.¹⁶⁷ The court then held that because the debtors had an ability to pay their creditors, granting their petition for relief under Chapter 7 would be a substantial abuse of the bankruptcy system under 11 U.S.C. § 707(b).¹⁶⁸

158. *In re Smihula*, 234 B.R. 240 (Bankr. D. R.I. 1999).

159. *Id.* at 241.

160. *Id.*

161. *Id.*

162. *Id.* at 241, 243.

163. *In re Smihula*, 234 B.R. at 243.

164. *Id.* at 243.

165. *Id.* at 242-43 (noting that in the legislative history of the Donation Act Congress expressed the opinion that sudden generosity, even if it fits within the percentage of income parameters permitted by the Donation Act, will be considered a "badge of fraud").

166. *See id.* at 243.

167. *Id.*

168. *Id.*

Similarly, in *Collins*,¹⁶⁹ the Bankruptcy Court for the Northern District of Illinois avoided the Donation Act by dismissing a debtor's Chapter 7 petition under § 707(a) as a bad faith filing.¹⁷⁰ The debtor in *Collins* was a zealous philanthropist who donated \$30,000.00 to charity the year before he filed for bankruptcy and claimed that he planned to donate at least that much during the next year.¹⁷¹ The court applied the totality of the circumstances test to the creditors' § 707(a) motion to dismiss the filing for cause.¹⁷² However, before applying this test the court was careful to note that bad faith under § 707(a) was different from bad faith § 707(b) in two ways.¹⁷³ First, § 707(a) allows creditors to challenge bankruptcy petitions, and second, § 707(a) allows courts to consider charitable contributions.¹⁷⁴ The court then applied the totality of circumstances test and held that the most heavily weighted circumstance was the debtor's ability to pay his creditors.¹⁷⁵ The court found that the debtor clearly had an ability to pay his creditors based on the total value of his assets, including the value of those assets he had earmarked for charitable donations.¹⁷⁶ The court also looked at factors such as whether the debtor was willing to change his lifestyle, whether his filing was motivated solely by financial gain, and whether he had made any attempt to pay his debts in the past; the court found that the debtor failed each of these tests.¹⁷⁷ The court then held that, based on these conclusions, the debtor had filed for bankruptcy in bad faith and dismissed his claim for cause under § 707(a).¹⁷⁸

C. Charitable Contribution Cases under Sections 548 and 544

In *Jackson*,¹⁷⁹ the Bankruptcy Court for the District of New Jersey held that a debtor's charitable donation could not be allowed under § 548(a)(1)(B).¹⁸⁰ The court noted that because the parties had stipulated that the donation of \$20,000.00, which constituted about sev-

169. *In re Collins*, 250 B.R. 645 (Bankr. N.D. Ill. 2000).

170. *Id.* at 654.

171. *Id.* at 653.

172. *Id.*

173. *Id.* at 654.

174. *Id.*

175. *Id.*

176. *See Collins*, 250 B.R. at 654. The court noted that the debtor held over \$2,300,000.00 in life insurance funds and pension funds and found that he could pay if he were inclined and that it was immaterial that those assets were unreachable by a court. *See id.*

177. *Id.* at 654-55.

178. *See id.* at 655.

179. *Jackson v. Church of Manalapan, Inc. (In re Jackson)*, 249 B.R. 373 (Bankr. D.N.J. 2000).

180. *Jackson*, 249 B.R. at 378.

enty-four percent of the debtor's income, exceeded the fifteen percent maximum allowable amount of donation to income under § 548(a)(2)(A), the only issue in the case was whether the donation fit within the parameters of § 548(a)(2)(B).¹⁸¹ Thus, the court had to decide whether the donation was consistent with the debtor's prior practices.¹⁸² The court held that the \$20,000.00 donation did not match the debtor's prior practices even though he had donated \$14,546.00, \$15,610.00, and \$7,545.00 in 1995, 1996, and 1997 respectively.¹⁸³ The court then held that because the donation was not consistent with the prior practices that it was a constructively fraudulent transfer, and therefore avoidable by the bankruptcy trustee under § 548(a)(1)(B).¹⁸⁴

In *Zohdi*,¹⁸⁵ the Bankruptcy Court for the Middle District of Louisiana also avoided a debtor's charitable donation under § 548(a)(2)(A).¹⁸⁶ The debtor donated \$10,000.00 to Louisiana State University during the twelve months preceding his filing a petition for bankruptcy.¹⁸⁷ The court found that this donation exceeded fifteen percent of the debtor's annual income by \$3,450.00.¹⁸⁸ The court then looked to the text of 11 U.S.C. § 548(a)(2) and noted that the plain meaning of the text only protected individual transfers that did not exceed fifteen percent of a debtor's income. If a transfer did in fact exceed fifteen percent, then the entire donation was subject to attack as a constructively fraudulent conveyance under § 548(a)(1)(B).¹⁸⁹ The debtor argued that this plain meaning analysis achieved an absurd result because it would allow one cent to be the cause for avoidance of a transfer of thousands of dollars.¹⁹⁰ The court responded that it was not a judicial function to correct a lack of foresight on the part of Congress and that when there was a conflict between statutory wording and Congressional intent, the plain meaning of the statute would control.¹⁹¹

181. *Id.* at 375-77.

182. *See id.* at 377.

183. *See id.* at 374-75. The court partially based its refusal to find the 1998 donation consistent with those of prior years not only because the amount was greater, but because the debtor did not provide the court with proof of the debtors' income during those years that would have enabled the court to make a percentage analysis. *See id.*

184. *Id.* at 378.

185. *Zohdi v. La. State Univ. Found. (In re Zohdi)*, 234 B.R. 371 (Bankr. M.D. La. 1999).

186. *Id.* at 373.

187. *Id.*

188. *Id.*

189. *Id.* at 375.

190. *Zohdi*, 234 B.R. at 381-82.

191. *Id.* at 381.

However, not all courts arrive at the conclusion articulated by the *Zohdi* court. The Bankruptcy Court for the Northern District of Oklahoma upheld a debtor's charitable donation under §§ 548(a)(2) and 544(b) in the *Witt*¹⁹² case without considering whether the donation was in excess of fifteen percent of her annual income.¹⁹³ In *Witt* the debtor donated \$6,800.00 to a religious charity during the year prior to her filing for bankruptcy and had donated at least that amount to the same group for each of the four years prior to the year in contest.¹⁹⁴ The court found that, according to the Donation Act's amendments to §§ 544 and 548, her prior consistent donation practices were dispositive in this case.¹⁹⁵ Thus, the debtor's charitable donation was not avoided.¹⁹⁶

D. Charitable Contribution Cases under § 523

In *McLeroy*,¹⁹⁷ the Northern District of Texas Bankruptcy Court disallowed the debtors' petition to discharge student loans because the court found that if the debtors' charitable donations were included as part of their disposable income, they would have the ability to pay their debts without enduring any undue hardship (as is required for student loan relief by § 523(a)(8)).¹⁹⁸ The court held that Congress did not amend any of the provisions of § 523 when it passed the Donation Act; therefore, it did not effect the court's analysis under § 523(a)(8), even if the donation would be permitted by other sections of the Bankruptcy Code under the Donation Act's amendments.¹⁹⁹ The court then held that the debtors were not automatically allowed to include their donations as "appropriate expense[s] under the undue hardship test."²⁰⁰ The court examined the debtors' proposed \$490.00 monthly donation under normal appropriate expense standards and held that the donation should be included as part of their disposable income for the undue hardship analysis.²⁰¹ Furthermore, the court determined that the inclusion of the donation as part of the debtors'

192. *Witt v. Grace Fellowship, Inc. (In re Witt)*, 231 B.R. 92 (Bankr. N.D. Okla. 1999).

193. *Id.* at 100.

194. *See id.* at 95.

195. *Id.* at 99-100. The applicable law that the court ruled on in the § 544 challenge was federal law, rather than state law, hence the court could use the same analysis for both the § 548 and § 544 challenges. *Id.*

196. *Id.*

197. *Educ. Credit Mgmt. Corp. v. McLeroy (In re McLeroy)*, 250 B.R. 872 (Bankr. N.D. Tex. 2000).

198. *Id.* at 883.

199. *See id.* at 877-78.

200. *Id.* at 880.

201. *See id.* at 875, 882-83.

disposable income would allow them to repay their debts without suffering any undue hardship.²⁰²

This line of reasoning was followed by the District of Idaho Bankruptcy Court in *Ritchie*.²⁰³ There, the debtors planned to donate \$315.00 (or 18.8%) of their \$1671.78 monthly income to their church.²⁰⁴ The debtors contended that their donations should be allowed as a necessary living expense and that they had diverted income from other areas in order to afford the monthly donations.²⁰⁵ Before the court made a determination about the donations, it accepted the rest of the debtors' budget for all other expenses as satisfactory.²⁰⁶ Then the court followed the reasoning of the *McLeroy* court and held that because Congress did not amend § 523(a)(8) to shield charitable donations from a court's consideration when determining whether a debtor could pay his debts without suffering an undue hardship, Congress did not intend to provide the protection for those attempting to discharge their student loan debts.²⁰⁷ The court also found the fact that Congress had amended § 523(a)(8) in other ways during the legislative session in which the Donation Act was passed, was particularly probative towards showing that Congress did not intend to exclude charitable donations from consideration as disposable income under § 523(a)(8).²⁰⁸ The court then took the amount of disposable income that the debtors claimed under their original budget and added the amount of the donations, to arrive at a sum of \$600.00 per month of income that the debtors could use to pay their student loans.²⁰⁹ The court then concluded that the debtors had more than enough income to repay their student loans.²¹⁰

However, the court in *Lebovits*²¹¹ arrived at an opposite conclusion when analyzing a charitable contribution under Section 523(a)(8). There, a debtor petitioned to discharge his student loans while main-

202. *Id.*

203. *Ritchie v. Student Loan Fund of Idaho, Inc. (In re Ritchie)*, 2000 WL 1683314 (Bankr. D. Idaho 2000).

204. *See id.* at *1, *3.

205. *Id.* at *4.

206. *Id.* at *3.

207. *Id.* at *5-6.

208. *Id.* at *6 (stating that in 1998 Congress removed the provision of § 523(a)(8) that allowed for the discharge of student loan debts that had become due seven years or more before the debtor filed for bankruptcy).

209. *Ritchie*, 2000 WL 1683314 at *6.

210. *Id.*

211. *Lebovits v. Chase Manhattan Bank (In re Lebovits)*, 223 B.R. 265 (Bankr. E.D.N.Y. 1998).

taining a \$60.00 per month donation to his church.²¹² The court's discussion of the Donation Act was limited to its taking note that the debtors were allowed to donate up to fifteen percent of their gross income to charity.²¹³ The court then concluded that the \$60.00 donation was well within the fifteen percent maximum provided for by the Donation Act, and therefore the charitable contribution was allowed as a necessary expense.²¹⁴ The court went on to imply that it would have allowed the debtor to donate any amount as long as it did not exceed fifteen percent of the debtor's gross income.²¹⁵

In *Wegrzyniak*,²¹⁶ the Bankruptcy Court for the District of Idaho reached a similar result by refusing to consider nominal charitable donations under § 523(a)(8),²¹⁷ rather than implicitly adopting the fifteen percent allowance into § 523(a)(8) as the court did in *Lebovits*.²¹⁸ In *Wegrzyniak*, the debtor sought relief from her student loan debt while planning to donate \$30.00 per month to charity.²¹⁹ The court expressed some concern over whether it had discretion to consider the charitable donations after the Donation Act.²²⁰ Nevertheless, the court went on to hold that the donations were satisfactory under § 523(a)(8) not because of any protections provided by the Donation Act, but because the amount of the donations were small enough to be considered inconsequential in light of the other expenses.²²¹

However, in *Hammond*,²²² the court held that a Chapter 7 debtor could not discharge the costs associated with his divorce under § 523(a)(15)(A) because he had expenses, including monthly charitable donations of about \$400.00 per month, which the court found to be unnecessary for his support.²²³ In determining that Congress did not intend for the Donation Act to effect § 523(a)(15)(A), the court utilized the "negative pregnant rule of statutory construction,"²²⁴ which

212. *Id.* at 273.

213. *Id.*

214. *Id.*

215. *See id.*

216. *Wegrzyniak v. United States (In re Wegrzyniak)*, 241 B.R. 689 (Bankr. D. Idaho 1999).

217. *See id.* at 693-94.

218. *See Lebovits v. Chase Manhattan Bank (In re Lebovits)*, 223 B.R. 265, 273 (Bankr. E.D.N.Y. 1998).

219. *Wegrzyniak*, 241 B.R. at 693-94.

220. *See id.*

221. *Id.* (stating that the court felt that the donation amounts could have been spread among the other expense amounts without pushing them above a satisfactory level under § 523(a)(8), hence the total amount of expenses, including the charitable donations, were acceptable in the court's eyes).

222. *Hammond v. Hammond (In re Hammond)*, 236 B.R. 751 (Bankr. D. Utah 1998).

223. *Id.* at 760, 767-68.

224. *Id.* at 767-68.

called for the court to contrast the express statutory statement of § 1325(b)(2)(A) with congressional silence on the same matter in § 523(a)(15)(A).²²⁵ The court then held that the silence in § 523 indicates that Congress intended the charitable contributions protections to apply only to those sections which Congress actually amended.²²⁶ The court then held that the debtor's charitable donation should have been included in his disposable income and, as a result, the debtor had sufficient funds to provide for his maintenance and support while paying his debt.²²⁷

V. ANALYSIS OF THE EFFECT THAT THE DONATION ACT HAS HAD ON JUDICIAL TREATMENT OF CHARITABLE CONTRIBUTIONS IN BANKRUPTCY

This Section will examine some of the differences—or the lack thereof—in the way in which courts have treated charitable donations under the provisions of the Bankruptcy Code that have been examined in the preceding sections of this Article.

A. Cases under 11 U.S.C. § 1325(b)

Prior to the enactment of the Donation Act, courts generally held that charitable donations were unreasonable expenses unless they were of a very small amount or the debtor received something in return for his donation.²²⁸ The fact that the *McDonald* and *Buxton* courts applied these requirements to charitable donations after the enactment of the Donation Act is evidence that Congress did not succeed in eliminating them.²²⁹

Further, many courts used disposable income tests that were identical in substance to the § 1325(b) test under other provisions of the Bankruptcy Code before the Donation Act's passage,²³⁰ and have

225. See *id.* at 767.

226. *Id.* at 767-68.

227. *Id.* at 768.

228. See *In re Zaleski*, 216 B.R. 425 (Bankr. D.N.D. 1997); *In re Saunders*, 215 B.R. 800 (Bankr. D. Mass. 1997); *In re Bien*, 95 B.R. 281 (Bankr. D. Conn. 1989).

229. See *In re McDonald*, 232 B.R. 818 (Bankr. S.D. Fla. 1999); *In re Buxton*, 228 B.R. 606 (Bankr. W.D. La. 1999).

230. See *Feldmann v. Feldmann (In re Feldmann)*, 220 B.R. 138 (Bankr. N.D. Ga. 1998) (applying the § 1325(b) disposable income test to a § 523(a)(15) ability to pay analysis); *In re Smither*, 194 B.R. 102 (Bankr. W.D. Ky. 1996) (holding that the § 1325(b) disposable income test case law had been adopted by courts applying § 523(15)); *Lynn v. Diversified Collection Serv. (In re Lynn)*, 168 B.R. 693 (Bankr. D. Ariz. 1994) (holding that the § 1325(b) definition of disposable income was applicable in making a § 523(a)(8) determination).

continued to do so after the enactment of the Donation Act.²³¹ This is curious because it is apparent that not all courts feel compelled to adjust their interpretation of what constitutes disposable income under these other provisions despite the fact that Congress has explicitly changed them. The *McLeroy* case is particularly interesting because it holds that the *Lynn* case is the guiding precedent for charitable contributions under § 523(a)(8).²³² However, while *Lynn* explicitly adopts the disposable income test of § 1325(b),²³³ the *McLeroy* court disregards the changes that Congress made to § 1325(b) with the Donation Act.²³⁴ If § 1325(b) is really the standard, should not the courts incorporate Congress' changes into their analysis, or are the courts free to apply the 1995 version of § 1325(b) as opposed to the current version?

The Donation Act appears to have stripped courts of some discretion over whether to include a charitable contribution that is less than fifteen percent of the debtor's gross income as part of the debtor's disposable income under § 1325.²³⁵ However, some courts are still applying the § 1325(b) reasonableness test to charitable contributions and have maintained discretion over whether to include charitable donations as disposable income when analyzing them under other provisions of the Bankruptcy Code.²³⁶

B. *Donation Act's Influence under § 707*

The Donation Act's amendment to § 707 was an attempt to protect certain charitable contributions from *sua sponte* attacks by the court and from attacks initiated by a bankruptcy trustee claiming substantial abuse.²³⁷ However, as demonstrated by the *Smihula* court, Congress did not succeed in preventing courts from using § 548(a)(1)(A) to recharacterize the charitable donations as actually fraudulent transfers.²³⁸ Once a court recharacterizes a donation as fraudulent, it is no longer protected by the Donation Act's amendments to § 707(b).²³⁹ Thus, the court may evaluate the charitable donation according to

231. See *Educ. Credit Mgmt. Corp. v. McLeroy (In re McLeroy)*, 250 B.R. 872 (Bankr. N.D. Tex. 2000); *In re Smihula*, 234 B.R. 240 (Bankr. D.R.I. 1999) (applying the § 1325(b) disposable income test to a § 707(b) substantial abuse analysis).

232. *McLeroy*, 250 B.R. at 877.

233. See *supra* Section II.A.4.

234. See *McLeroy*, 250 B.R. at 877.

235. See *supra* sections III.A.1, IV.A.

236. See *supra* sections III.A.2-4, IV.A.2-4.

237. See *supra* section II.B.

238. See *supra* section IV.B.

239. See *id.*

standards that are no different than those used by the courts before the Donation Act.²⁴⁰

In addition, the Donation Act did not amend § 707(a), which allows creditors to challenge bankruptcy petitions.²⁴¹ As shown by the *Collins* court, charitable donations may be used to show that a debtor filed for bankruptcy in bad faith when a court considers a creditor's motion to dismiss for cause under § 707(a).²⁴² Thus, a proactive creditor may still defeat a debtor's bankruptcy petition if she believes that she can show the debtor filed in bad faith—even if she must use the debtor's charitable donations as evidence of this bad faith.²⁴³

C. *Donation Act's Influence on Cases under § 548*

The amendment to § 548 was an attempt to shield charitable donations from being characterized as constructively fraudulent, while preserving the courts' ability to avoid those transfers that could fairly be characterized as actually fraudulent.²⁴⁴ The *Witt* case demonstrates that this amendment has been partially successful because there the court refused to avoid a transfer, in light of the Donation Act, which was similar to a transfer that the *Newman* court avoided as constructively fraudulent just four years earlier.²⁴⁵

However, the Donation Act cannot claim a total success in amending § 548 because of the confusion that *Zohdi* court demonstrated. The question of whether a donation that exceeds fifteen percent of debtor's gross income is avoidable in its entirety or only to the extent that it exceeds the fifteen percent maximum still remains unanswered.²⁴⁶ Also, as demonstrated by the *Jackson* court, there is no definition in the Donation Act's amendments which clearly state what constitutes a prior consistent practice.²⁴⁷ In *Jackson*, the court avoided a transfer which was clearly inconsistent in both amount and percentage of debtor's income.²⁴⁸ However, in making its determination the court relied only on a dictionary definition of consistency,

240. Compare *In re Smihula*, 234 B.R. 240, 243 (Bankr. D.R.I. 1999), with *In re Lee*, 162 B.R. 31, 38 (Bankr. N.D. Ga. 1993).

241. See *supra* sections II.B., IV.B.

242. See *In re Collins*, 250 B.R. 645, 654 (Bankr. N.D. Ill. 2000).

243. See *id.*

244. See 144 CONG. REC. H3999-02, H4000 (June 3, 1998) (statement of Rep. Gekas).

245. Compare *Witt v. Grace Fellowship, Inc. (In re Witt)*, 231 B.R. 92, 99-100 (Bankr. N.D. Okla. 1999), with *Newman v. Midway S. Baptist Church (In re Newman)*, 183 B.R. 239, 242-43 (Bankr. D. Kan. 1995).

246. See *supra* section IV.C.

247. *In re Jackson*, 249 B.R. 373, 377 (Bankr. D.N.J. 2000).

248. *Jackson*, 249 B.R. at 377.

which provides no bright line guidance for courts to use in close cases.²⁴⁹

D. *Donation Acts' Influence on § 523 Cases*

While Congress did amend § 523 in 1998, it did not do so with the Donation Act. Therefore, Congress did not provide any explicit protection for charitable contributions under this section.²⁵⁰ However, that did not prevent debtors from attempting to import the Donation Act's protection into § 523 cases.²⁵¹ Courts have generally refused to recognize that § 523 analysis was changed in any way by the Donation Act,²⁵² and as a result there has been little change in case results after the Donation Act.²⁵³

This has created confusion. For instance, the *Lebovits* case demonstrates that a court may take the fact that Congress made an attempt to protect charitable donations in other parts of the Bankruptcy Code as congressional indication that courts should allow a broader portion of charitable donations.²⁵⁴ On the other hand, some courts have viewed the lack of change in § 523 as an indication that Congress' intent was that analysis under § 523 should not be changed by the Donation Act.²⁵⁵

VI. CONCLUSION

Charities pressured Congress in response to a perceived vulnerability that they felt was promulgated by the Supreme Court's decision in *Boerne*.²⁵⁶ Congress responded by passing the Donation Act,²⁵⁷ which at first seemed to be cause for concern for creditors and counsel that protect creditors' rights. However, the Donation Act has not pre-

249. *See id.*

250. *See supra* section IV.D.

251. *See id.*

252. *See id.*

253. *See id.*

254. *See id.* It should be noted that the debtor in *Lebovits* was making charitable contributions in amounts similar to those of the debtor in *Wegrzyniak*, which the *Wegrzyniak* court held to be *de minimus*. *Wegrzyniak*, 241 B.R. at 694. Also, the *Lebovits* court did not give any reason for why the Donation Act should apply in § 523 cases aside from the possibility that Congress was implying leniency for charitable donations. *See id.* Also the *Lebovits* court did not give any reason for why the Donation Act should apply in § 523 cases aside from the possibility that Congress was implying leniency for charitable donations. *See In re Ritchie*, 2000 WL 1683314, at *5 (Bankr. D. Idaho 2000).

255. *Educ. Credit Mgmt. Corp. v. McLeroy (In re McLeroy)*, 250 B.R. 872, 882 n.14 (Bankr. N.D. Tex. 2000).

256. *See supra* section I.

257. *See id.*

vented courts from applying old standards of reasonableness to a debtor's gifts.²⁵⁸ Nor has it prevented courts from using other parts of the Bankruptcy Code to recharacterize the debtor's donations into something that will remove it from the Donation Act's safe harbor.²⁵⁹ The Donation Act also contains ambiguity in areas such as what constitutes a prior consistent practice and what should happen to a donation that exceeds fifteen percent of the debtor's gross income.²⁶⁰

Given these inconsistencies, there has been little net gain for charities in terms of the types of transfers that will be allowed after the Donation Act, and little corresponding increase in threat to the rights of commercial creditors. Courts are using roughly the same standards, and charities are left with nearly the same concerns in far too many cases for the Donation Act to be considered a blow to organizations that provide credit to consumers as well as to many small businesses. Deft navigation through the maze of loopholes and gaps in statutory construction that Congress left in its collection of amendments can place creditors on ground essentially level with the ground that they stood on before the Donation Act came to be.

258. *See supra* section IV.A.

259. *See supra* section V.A,B.

260. *See* section V.C.