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Introduction

Title 11 of the United States Code (the “Bankruptcy Code”) provides a fresh start to the “honest but unfortunate debtor.”¹ Chapter 7 therefore permits a debtor to “discharge their outstanding debts in exchange for liquidating their nonexempt assets and distributing them to their creditors.”² Dismissals in chapter 7 are governed by section 707 of the Bankruptcy Code.³ Section 707(a) governs all chapters of bankruptcy filings and applies when adequate “cause” is shown.⁴

There is currently a circuit split regarding whether a debtor’s lack of good faith constitutes cause for dismissal under section 707(a). Under section 707(a), a case may only be dismissed for cause after notice and hearing.⁵ Section 707 does not define “cause,” offering only a non-exhaustive list of what may constitute cause. This includes unreasonable delay, nonpayment of fees, and failure to file required information on motion of the U.S. Trustee.⁶ As a result, bankruptcy courts are given significant discretion when asked to determine whether there

¹ Janvey v. Romero, 883 F.3d 406, 410 (4th Cir. 2018) (internal quotation marks omitted).

² *Id.* at 401.

³ Perlin v. Hitachi Capital America Corp. (*In re Perlin*), 497 F.3d 364, 370 (3d Cir. 2007).

⁴ 11 U.S.C. § 707(a) (2018).

⁵ *Id.*

⁶ *Id.*

is cause to dismiss under section 707.⁷ This is a fact-based inquiry.⁸ Courts have found cause to dismiss, for example, where the administration of the estate would require the Trustee to operate the debtor's business in violation of federal law, or where the dismissal would further the judicial economy without harm to either the debtor or their creditors.⁹

This article explores the circuit split surrounding whether a debtor's lack of good faith is cause for dismissal under section 707(a). Part I analyzes the approaches of the various circuits, beginning with the majority view established by the Sixth Circuit in *In re Zick* that bad faith is grounds for dismissal. Part II analyzes case law on the issue of bad faith dismissals out of lower courts within the Second Circuit, which has not yet heard the issue. The article concludes with a finding that the Second Circuit is likely to follow the Sixth Circuit's approach in *Zick* and accept a debtor's bad faith as grounds for dismissal under section 707(a) in cases of egregious misconduct.

Discussion

I. The Circuit Split

A. *The Third, Fourth, Fifth, Sixth, Eighth, and Eleventh Circuits Have Adopted Bad Faith as Grounds for Dismissal Under Section 707(a).*

The majority view is that a debtor's lack of good faith constitutes grounds for dismissal under section 707(a).¹⁰ This approach has been adopted by the Third, Fourth, Fifth, Sixth, Eighth and Eleventh Circuits.¹¹ A bankruptcy court's decision to dismiss for cause is reviewed on

⁷ *In re Nash Eng'g Co.*, 619 F.Supp.3d 268, 272 (D. Conn. 2022).

⁸ *Id.*

⁹ See 6 COLLIER ON BANKRUPTCY § 707.03 (Alan N. Resnick & Henry J. Sommer Eds., 16th ed. 2009).

¹⁰ *Id.*

¹¹ See *Kruger v. Torres*, 812 F.3d 365, 370 (5th Cir. 2016); *In re Piazza*, 719 F.3d 1253, 1262 (11th Cir. 2013); *Perlin v. Hitachi Capital America Corp. (In re Perlin)*, 497 F.3d 364, 367 (3d Cir. 2007); *Janvey v. Romero*, 883 F.3d 406, 412 (4th Cir. 2007); *In re Tamecki*, 229 F.3d 205, 206 (3d Cir. 2000); *Huckfeldt v. Huckfeldt (In re Huckfeldt)*, 39 F.3d 829, 832 (8th Cir. 1994); *In re Zick*, 931 F.2d 1124, 1126 (6th Cir. 1991).

appeal for abuse of discretion, factual findings are reviewed for clear error, and legal conclusions are reviewed de novo.¹²

The Sixth Circuit was first to hold that bad faith was cause for dismissal in *In re Zick*.¹³ In *Zick*, the debtor filed a petition for relief under chapter 7 of the Bankruptcy Code only days after a monetary judgment in favor of his former employer was entered against him, which judgment he sought to have discharged.¹⁴ His employer moved to dismiss asserting the petition had been filed in bad faith.¹⁵ The motion was granted by the bankruptcy court.¹⁶ It reasoned that Zick had intentionally reduced creditors in the case down to one, failed to make any lifestyle adjustments or efforts to repay the mediation award, and had clearly filed in response to the award.¹⁷

The Sixth Circuit affirmed the bankruptcy court's dismissal, holding that "cause" was not limited to the examples set forth in section 707(a)–(c).¹⁸ While chapter 7 does not have an explicit good faith filing requirement, the circuit court found good faith was an implied requirement because it is "inherent in the purposes of bankruptcy relief."¹⁹ Bankruptcy protections are not intended to "assist those who, despite their own misconduct, are attempting to preserve a comfortable standard of living at the expense of their creditors."²⁰ As such, a case may be dismissed for lack of good faith.²¹ The court noted that bad faith dismissals should be used only in "egregious cases that entail concealed or misrepresented assets and/or sources of income, and excessive and continued expenditures, lavish life-style, and intention to avoid a large single

¹² *Janvey*, 883 F.3d at 412.

¹³ *In re Zick*, 931 F.2d at 1126.

¹⁴ *Id.*

¹⁵ *Id.*

¹⁶ *Id.* at 1128.

¹⁷ *Id.*

¹⁸ *In re Zick*, 931 F.2d at 1126.

¹⁹ *Id.* at 1129 (quoting *In re Jones*, 114 B.R. 917, 913 (N.D. Ill. 1991)).

²⁰ *Id.*

²¹ *Id.* at 1129.

debt based on conduct akin to fraud, misconduct, or gross negligence.”²² Nonetheless, the court found no abuse of the bankruptcy court’s discretion in dismissing Zick’s petition.²³ The Sixth Circuit’s holding in *Zick* set the framework for the majority view among the circuits.

In *In re Tamecki*, the Third Circuit followed the *Zick* court’s reasoning by permitting bad faith dismissals under 707(a).²⁴ The Trustee sought dismissal for lack of good faith when the debtor claimed his home equity as an exemption knowing he would soon become entitled to it during an upcoming divorce proceeding.²⁵ The bankruptcy court found the debtor “failed to disprove his bad faith” once the issue had been raised and dismissed.²⁶ The district court affirmed.²⁷ Citing *Zick*, the Third Circuit also affirmed, holding a bad faith dismissal appropriate where the debtor “fails to demonstrate his good faith in filing” by a “showing of honest intention.”²⁸ Once good faith was brought into question, the burden shifted to the debtor to prove good faith in filing.²⁹ Despite the shifting of burden, the *Tamecki* court noted that bad faith should not be inferred lightly.³⁰ Evidence that the debtor acquired vast debt just prior to the filing of his petition and during the pendency of his divorce was “sufficiently questionable to warrant good faith scrutiny.”³¹

The Third Circuit further expanded its holding in *In re Perlin*, holding that a debtor’s income may be considered by a bankruptcy court while assessing the debtor’s good faith.³² The Third Circuit found it was “within the sound discretion of the bankruptcy court to consider a

²² *Id.*

²³ *Id.*

²⁴ *In re Tamecki*, 229 F.3d 205, 205–06 (3d Cir. 2000).

²⁵ *Id.* at 206.

²⁶ *Id.* at 207.

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.*

³⁰ *Id.* at 207–08.

³¹ *Id.* at 208.

³² *Perlin v. Hitachi Capital America Corp. (In re Perlin)*, 497 F.3d 364, 367 (3d Cir. 2007).

debtor's monthly income and expenses together with any other factors relevant to a debtor's good faith in filing for bankruptcy."³³ The *Perlin* court acknowledged that Congress did not intend a debtor's ability to repay to constitute cause for dismissal.³⁴ However, the court was unwilling to "read the history as prohibiting a bankruptcy court from considering a debtor's substantial income and expenses" when evaluating good faith.³⁵ This would require bankruptcy courts to ignore the debtor's economic reality.³⁶ Though, a bankruptcy court's ultimate finding of bad faith may not be exclusively or primarily based on the debtor's ability to repay, as this would undercut congressional intent.³⁷ The remainder of circuits in the majority — the Fourth, Fifth, and Eleventh — have held consistently with *Zick* that a debtor's lack of good faith constitutes grounds for dismissal under section 707(a).³⁸

In *In re Huckfeldt*, the Eighth Circuit took a modified, more "narrow [and] cautious" approach to *Zick*.³⁹ While some conduct that provides cause to dismiss could be characterized as "bad faith conduct," the Eighth Circuit held that a section 707(a) analysis was "better conducted under the statutory standard, 'for cause.'"⁴⁰ Bad faith dismissals under section 707(a) therefore should "be limited to extreme misconduct falling outside the purview of more specific Code

³³ *Id.*

³⁴ *Id.* at 372.

³⁵ *Id.*

³⁶ *Id.* (citing *In re Goulding*, 79 B.R. 874, 876 (Bankr. W.D. Mo. 1987)).

³⁷ *Id.* at 374.

³⁸ See *Janvey v. Romero*, 883 F.3d 406, 412 (4th Cir. 2007) (Fourth Circuit holding that dismissal for debtor's bad faith is the "most helpful in preventing serious abuses of the bankruptcy process," but limiting its application to "cases of real misconduct"); *Kruger v. Torres*, 812 F.3d 365, 370 (5th Cir. 2016) ("Every bankruptcy statute since 1898 has incorporated literally, or by judicial interpretation, a standard of good faith for the commencement, prosecution, and confirmation of bankruptcy proceedings." (quoting *Little Creek Dev. Co. v. Commonwealth Mortg. Co. (In re Little Creek Dev. Co.)*, 779 F.2d 1068, 1071 (5th Cir.1986)); *In re Piazza*, 719 F.3d 1253, 1262 (11th Cir. 2013) ("Considering bankruptcy courts may sanction litigants for filing documents with 'any improper purpose,' as well as 'tak[e] any action . . . necessary or appropriate . . . to prevent an abuse of process,' we see no reason why prepetition bad faith should not constitute an adequate or sufficient reason for dismissal.") (internal citations omitted).

³⁹ See *Huckfeldt v. Huckfeldt (In re Huckfeldt)*, 39 F.3d 829, 832 (8th Cir. 1994).

⁴⁰ *Id.*

provisions.”⁴¹ The *Huckfeldt* court expressed concern that a bad faith inquiry may be weaponized by courts against debtors “whose values do not coincide precisely with those of the court.”⁴²

B. The Ninth Circuit Has Not Adopted Bad Faith as Grounds for Dismissal Under Section 707(a).

The Ninth Circuit is the only circuit declining to hold that a lack of good faith constitutes cause to dismiss under section 707(a). In *In re Padilla*, the Ninth Circuit held that bad faith “as a general proposition” does not constitute cause.⁴³ While highlighting that there is undoubtedly cause to dismiss for a debtor’s bad faith in chapters 11 and 13, the Ninth Circuit noted that a plan under chapter 11 or 13 may not be confirmed *unless* it has been proposed in good faith.⁴⁴ In contrast, there is no explicit good faith requirement for a discharge in chapter 7.⁴⁵ The court also reasoned that a chapter 7 liquidation does not involve an ongoing debtor-creditor relationship after discharge, therefore chapter 7 “should be available to any debtor willing to surrender all of its nonexempt assets, regardless of whether the debtor's motive in seeking such a remedy was grounded in good faith.”⁴⁶

II. Courts Within the Second Circuit Have Generally Accepted Bad Faith as Grounds for Dismissal Under Section 707(a).

While the Second Circuit has not yet ruled on the issue, courts within the circuit have held that a petition may be dismissed under section 707(a) for the debtor’s lack of good faith.⁴⁷ Courts throughout the circuit have developed different factors bankruptcy courts may consider in

⁴¹ *Id.*

⁴² *Id.* (citations omitted).

⁴³ 222 F.3d 1184, 1991 (9th Cir. 2000).

⁴⁴ *Id.* at 1192–93.

⁴⁵ *Id.* at 1193.

⁴⁶ *Id.* (citations omitted).

⁴⁷ See *In re Murray*, 543 B.R. 484, 491 (Bankr. S.D.N.Y. 2016) (“Many courts, including this one, have recognized that cause for dismissal . . . may result from circumstances not specifically mentioned in the Code—whether for bad faith or circumstances falling short of bad faith but nevertheless representing an inappropriate use of the Code.”).

evaluating if a debtor acted in bad faith. For example, the Bankruptcy Court for the Eastern District of New York in *In re Blumenberg* listed the following six factors as relevant:

(1) The debtor's manipulations having the effect of frustrating one particular creditor; (2) The absence of an attempt to pay creditors; (3) The debtor's failure to make significant lifestyle changes; (4) The debtor has sufficient resources to pay substantial portion of debts; (5) The debtor inflates expenses to disguise financial well-being; (6) The debtor is overutilizing protections of the Bankruptcy Code to the conscious detriment of creditors.⁴⁸

The Bankruptcy Court for the Eastern District of New York added the following seven additional factors in *In re Lombardo*:

(1) The debtor reduced his creditors to a single creditor in the months prior to The filing of the petition; (2) The debtor filed in response to a judgment, pending litigation or collection action; there is an intent to avoid a large single debt; (3) The unfairness of the use of Chapter 7; (4) The debtor transferred assets; (5) The debtor is paying debts to insiders; (6) The debtor failed to make candid and full disclosure; (7) The debts are modest in relation to assets and income; and (8) There are multiple bankruptcy filings or other procedural “gymnastics.”⁴⁹

Like *Zick*, courts within the Second Circuit have found that bad faith dismissals should be exercised only in egregious cases.⁵⁰

As such, courts within the second circuit regularly decline to dismiss a chapter 7 petition on bad faith grounds. For example, in *In re Nash Engineering Co.*, the District Court in Connecticut held that the bankruptcy court had abused its discretion in dismissing the debtors’ petition as one filed in bad faith.⁵¹ In *In re Nash Eng’g Co.*, the debtor filed for chapter 7 after ceasing operations due to asbestos products liability.⁵² The bankruptcy court dismissed the

⁴⁸ *In re Blumenberg*, 263 B.R. 704, 715 (Bankr. E.D.N.Y. 2001) (quoting *In re Griffieth*, 209 B.R. 823 (Bankr. S.D.N.Y. 1996)).

⁴⁹ *In re Lombardo*, 370 B.R. 506, 512 (citing *In re O’Brien*, 328 B.R. 669, 675 (Bankr. W.D.N.Y. 2007)) (noting that the presence of a single factor is insufficient on its own to support dismissal).

⁵⁰ See *In re Chovev*, 559 B.R. 339, 345 (Bankr. E.D.N.Y. 2016) (“[T]here is general consensus that the standard for finding bad faith under § 707(a) is stringent, and ‘is generally utilized only in those egregious cases . . .’”) (citations omitted).

⁵¹ *In re Nash Eng’g Co.*, 619 F. Supp. 3d 268, 272 (D. Conn. 2022).

⁵² *Id.* at 270.

petition as one filed in bad faith, proffering two reasons.⁵³ First, under 28 U.S.C. § 157(b)(2)(B) contingent or unliquidated personal injury tort claims are not core proceedings and therefore could not be liquidated or estimated for purposes of distribution in a Chapter 7 case.⁵⁴ Second, the case “lacked a legitimate bankruptcy purpose.”⁵⁵

On appeal, the District Court held a bad faith dismissal was improper because the debtor had in fact provided a legitimate bankruptcy purpose.⁵⁶ As demonstrated by *In re Nash Eng’g Co.*, a bankruptcy court does not have unlimited discretion and the standard for dismissal on the grounds of bad faith is an “exacting standard.”⁵⁷

Conclusion

It is generally accepted by the majority of bankruptcy courts that a chapter 7 petition may be dismissed for cause due to the debtor’s bad faith conduct.⁵⁸ While the issue has not yet been heard by the Second Circuit, most courts throughout the circuit have adopted the holding in *Zick*.⁵⁹ However, this is limited to only “egregious misconduct” of the debtor.⁶⁰ This strict standard protects debtors from the concerns raised by the Eighth and Ninth Circuits by ensuring that petitions are not dismissed for a debtor’s ability to repay alone or due to conflicting values between the debtor and the bankruptcy court.⁶¹ Debtors also receive protections from a district court’s ability to review a bankruptcy court’s decision to dismiss for an abuse of discretion. This

⁵³ *Id.* at 271.

⁵⁴ *Id.* at 272–73.

⁵⁵ *Id.* at 273–74.

⁵⁶ *In re Nash Eng’g Co.*, 619 F. Supp. 3d at 273 (D. Conn. 2022) (“[T]he case has a legitimate bankruptcy purpose—primarily, to maximize the property available to satisfy creditors and to promote equitable distribution of debtor assets.”).

⁵⁷ *See In re Chovev*, 559 B.R. 339, 345 (Bankr. E.D.N.Y. 2016) (holding that, while movant asserted several *Lombardo* factors were present, they failed to show the debtor’s misconduct “[was] so egregious as to fall within the ‘bad faith’ standard”).

⁵⁸ *In re Zick, In re Zick*, 931 F.2d 1124, 1129 (6th Cir. 1991).

⁵⁹ *In re Chovev*, 559 B.R. at 345.

⁶⁰ *Id.*

⁶¹ *See In re Huckfeldt*, 39 F.3d 829, 832 (8th Cir. 1994); *In re Padilla*, 222 F.3d 1184, 1992 (9th Cir. 2000).

allows a district court to reverse and remand a case where a bankruptcy court has found cause, but the debtor's conduct has not met the purview of "egregious."⁶²

⁶² See *In re Nash Eng'g Co.*, 619 F.Supp.3d 268, 276 (D. Conn. 2022).