UNITED STATES BANKRUPTCY COURT
DISTRICT OF VERMONT

In re:
In re Michael E. French
Debtor.

Filed & Entered
On Docket
03/04/05

Chapter 13 Case
 # 01-10603

Appearances: *Michael Palmer, Esq.*
Middlebury, VT
Attorney for Debtor

Robert DiPalma, Esq.
Burlington, VT
Attorney for Creditor Suggitt

MEMORANDUM OF DECISION
APPROVING STIPULATION WITH MODIFICATION AND GRANTING IN PART BOTH THE DEBTOR'S MOTION TO REFINANCE AND THE CREDITOR'S MOTION TO MODIFY PLAN

On December 27, 2004, the Debtor filed a motion seeking approval of this Court to refinance his homestead in order to pay his remaining plan payments in full, in the sum of $16,523.00 (doc. # 115)("Motion to Refinance"). Maureen Suggitt, one of his creditors, filed an objection to the Motion to Refinance (doc. # 116) and a second motion to modify the Debtor's chapter 13 plan (doc. # 117) (the "Motion to Modify"). In the Motion to Modify, creditor Suggitt argues that both the Debtor's current chapter 13 plan and the proposed payoff of the plan fail to comply with § 1325(b)(1)(B)[1] by not allocating all of the Debtor's disposable income to his plan for distribution to his creditors. In an effort to avoid litigation of this issue and reduce legal costs, the Debtor and the chapter 13 Trustee reached an agreement and filed a stipulation that purports to resolve their outstanding disputes over the Motion to Refinance and the Motion to Modify (docs. ## 124 and 126)(the "Stipulation"). Because the objecting creditor did not accept the Stipulation as a resolution to the outstanding motions and asserted that there were genuine issues still in dispute, the Court held an evidentiary hearing on both the Motion to Modify and the Motion to Refinance on February 25, 2005.

Based upon the voluminous record in this case, the evidence presented at the recent hearing, and in the exercise of this Court's equitable powers, the Court approves the Stipulation on condition that the amount paid to creditors through the refinance is increased. To the extent the Debtor is able to perform the Stipulation so modified, the Court will grant in part both the Motion to Refinance and the Motion to Modify. If the Debtor is not able to perform the Stipulation with this modification and wishes to remain in chapter 13, then the Court will schedule a continued hearing on the Motion to Modify.

[1] Unless indicated otherwise, all statutory references contained herein are to the United States Bankruptcy Code.

PROCEDURAL BACKGROUND

The Debtor filed a petition for relief under chapter 7 on April 24, 2001 (doc. # 1). On August 15, 2002, the Debtor's case was converted to one under chapter 13 (doc. # 44). After several contested confirmation hearings, the Debtor's plan was approved on October 8, 2003 (doc. # 112). The confirmed plan required the Debtor to make payments of $826.15 per month for 48 months (Id.). The memorandum of decision entered on May 30, 2003, held that creditor Maureen Suggitt had not persuaded the Court that the Debtor should be deprived of an opportunity to reorganize under chapter 13 and also found that in light of the evidence presented certain conditions would be attached to such a reorganization effort (doc. # 89). Most notably, the Court required the Debtor to file quarterly reports detailing his income and indicated that it would entertain a motion to modify the plan if the Trustee or Ms. Suggitt believed on the basis of these reports that the Debtor had sufficient disposable income to warrant an increase in the plan payments (doc. #89, at pp. 9-10).

JURISDICTION

The Court has jurisdiction over this case and these two motions pursuant to 28 U.S.C. §§ 157(b)(2)(A), (L) and 1334.

DISCUSSION

Creditor Suggitt's argument that the Debtor should be required to pay more than he proposes under the Motion to Refinance is based primarily upon two assertions: first, that the Debtor enjoyed a substantial increase in income during calendar year 2004 and notwithstanding the special caveats attached to the confirmation of his plan, the Debtor has not shared any part of this increased income with his creditors to date; and second, that it is fair and reasonable to project that the Debtor's disposable income, as that term is defined under § 1325(b)(2), over the course of the plan would be higher than the sum the Debtor is offering to pay to cash out the plan now. The Stipulation provides that if the Debtor is permitted to refinance his homestead and pay the plan in full at this time, that he would increase the figure set forth in the Motion to Refinance ($16,523) by $9,913.80. The Stipulation states that this increase reflects the amount the Debtor would pay if the Debtor modified his plan to increase the term of the plan from 48 months to 60 months, and hence increases the total to be paid into the plan by an amount equal to 12 additional payments of $826.15 (docs. ## 124 and 126, p. 2, ¶ 1). Creditor Suggitt rejects this offer on the ground that the creditors in this case are entitled to all of the Debtor's disposable income during the life of the plan and this proposal falls short of paying all of the Debtor's disposable income to his creditors.

The Lack of Reliable Schedules and Income / Expense Projections

Although it is generally a simple mathematical computation to project disposable income during the remaining term of a confirmed plan, it is not so in this case. The Debtor's income fluctuates substantially from year to year, and from the record of this case, it appears that even the Debtor is unable to predict his future income. Additionally, as was made abundantly clear at the hearing, this Debtor is likewise unable to predict his annual expenses and unable to live within the projection of expenses he files with the Court. Although the Debtor has filed several Schedules I and J over the course of this case, which the Court and creditors should have been able to rely upon, it is clear from the record (including the Debtor's testimony at the most recent hearing) that the Debtor's actual spending has exceeded that which he projected in the filed schedules. The Court has already addressed allegations of this Debtor's good faith in connection with the confirmation of the plan (see doc #112) and the revelation that the Debtor's actual expenses are so far out of line with the filed Schedule J opens the specter of good faith anew. Moreover, with such unreliable filings before it, the Court must either disregard the testimony of actual spending and make a determination on the instant motions based upon the documents the Debtor filed under penalty of perjury, or conduct a further hearing to assess the Debtor's good faith performance to date and ability to fulfill his obligations going forward under chapter 13. The Court's assessment is that it would be impossible to compute projected disposable income in this case or evaluate the Debtor's good faith without an extensive evidentiary hearing and painstaking analysis of all of the Debtor's expenses – both from the date of the confirmation order through the present and those for the future. The Court is persuaded that to engage in such hearings would result in substantial attorneys' fees, may not provide any more reliable information than is before it at this time, and ultimately is not likely to serve the interest of any party in this case. Therefore, the Court concludes that it is in the best interest of all parties in interest to permit the Debtor to pay off the plan early, provided he pays a sum which appears to be the reasonable equivalent of the disposable income his creditors are entitled to under the confirmed plan. Thus, the Court will address the instant motions and Stipulation based upon the record before it, notwithstanding the absence of reliable income and expense projections.

It is unfortunate that the evidence presented at the hearing did little to elucidate a determination of the Debtor's projected disposable income which is the central question presented by both pending motions and the basis of the Stipulation. The Debtor filed amended Schedules I and J at 3:10 P.M. on February 24, 2005, less than 24 hours before the subject hearing**.** This gave both the Court and creditor Suggitt precious little time to analyze this new information prior to the hearing. Although many of the figures on Schedule J have been amended, the new Schedule J is only materially different from its most recently filed predecessor to the extent it includes additional expenses for alimony (in the amount of $2,500 per month) and child support (in the amount of $ 832 per month). There are also a few other *de minimus* changes resulting from the Debtor's recent separation from his wife. The Debtor's expenses on this newly filed Schedule J (doc #125), including the alimony and support expenses, is $9,306.93; if these expenses are backed out, the total expenses reflected would be $5,974.93. The expenses reflected on the Schedule J that was before the Court prior to last week (doc # 51) was $6,996.41. Thus, this new Schedule J is not substantively controversial; but for the marital obligations, it shows an overall reduction in expenses.

The more troubling newly disclosed information came into the record via the Debtor's testimony. At the evidentiary hearing, the Debtor testified and submitted documentary evidence to support that his actual expenditures during the calendar year 2004 bore virtually no resemblance to the operative Schedule J for 2004 on which all parties and the Court were relying when the plan was confirmed. For example, the Debtor's Schedule J reflected a home maintenance (repairs and upkeep) expense of $204.48 per month. According to the Debtor's testimony and the evidence submitted, in 2004 the Debtor spent $3,652.78 to replace windows in his home, spent $1,821.00 for lawn and driveway maintenance and has additional entries that might well be categorized as home maintenance. Based upon the Debtor's testimony, the Debtor actually spent approximately $456.15 per month for window replacement and lawn / driveway maintenance alone. That amount is more than twice what the operative Schedule J projected. Additionally, the Debtor's Schedule J in effect for 2004 projected monthly business expenses of approximately $397.28. According to the Debtor's testimony, in 2004 the Debtor paid $1,658.00 toward the school tuition of his sales assistant, $1,100 for a business computer, $3,254.33 in country club dues (which the Debtor's counsel described as a business expense), and additional miscellaneous business expenses of $8,324.34. Based upon the Debtor's testimony, the actual amount he spent on business related expenses per month in 2004 was $1,194.72, three times that which appears on the operative Schedule J. Based upon this evidence, the Court is persuaded that it would not be prudent to rely on the various Schedules J which the Debtor has filed in this case as accurate reflections of the Debtor's actual expenses. Additionally, this evidence raises serious questions regarding the reasonableness of the Debtor's expenditures during the term of the plan. Since disposable income is defined by § 1325(b)(2) as "income which is received by the debtor and which is not reasonably necessary to be expended" we would need to ascertain the reasonableness of the 2004 expenditures in order to reach a determination of whether the Debtor devoted all of his disposable income from 2004 to the plan. The record is woefully lacking for such a determination at this time.

The picture is not much different with regard to the Debtor's income. The Debtor testified in 2003 that he expected to have a poor year in 2004 since much of his 2003 income from out of the ordinary sources and he would not earn similar income in 2004. However, like the budget projections, this prediction turned out to be erroneous. The Debtor's income in 2004 was $206,442 – $125,000 more than he had earned in 2003. Therefore, the Court finds based upon the evidence presented at the hearing that the Debtor is not able to project reliably either his income or his expenses. While the Court finds this disturbing and a reasonable basis for the creditor's concerns about good faith, the Court finds it also provides additional impetus for permitting the Debtor to refinance his homestead property and pay off the plan early.

<u>The Debtor's Obligation to Satisfy the Requirements of § 1325(a)</u>

Before we address the computation of the amount due to creditors it is necessary to scrutinize whether the Debtor's proposal comports with the requirements of chapter 13 of the Bankruptcy Code. The Stipulation provides for a lump sum payments which is calculated on the hypothetical premise that the Debtor would pay $826.15 per month over the remaining term of the plan if the refinance is not permitted. However, the amended Schedule J which was filed contemporaneously with the Stipulation shows that the Debtor has only about $111 per month of disposable income. How can the Debtor pay $826 per month if he has disposable income of only $111 per month? Certainly, if the Debtor were proposing an amended payment plan with $826 per month payments, then, based upon this Schedule J, the Court would have to deny confirmation of the amended plan under § 1325(a)(6); on its face it simply is not feasible. The Court treats the application to pay the plan early as the procedural equivalent of a motion to modify plan. Hence, in order to approve the refinance, the Court must find that the proposed one-time lump payment of the plan via the refinance meets the criteria of § 1325 because it is essentially a modified plan. See 11 U.S.C. §1329. The Debtor must get over the feasibility hurdle. Fortunately, we will have absolute assurance of feasibility if the Debtor obtains the requisite sum from the refinance. Even though it does not appear that based upon the current record the Stipulation is feasible as presented, the Court will find it meets the requirements of §§ 1325(a) and 1329 and approve the refinance if the Debtor modifies it as set forth herein and is able to produce the requisite sum during the month of April 2005.

As a corollary to this analysis of how the refinance proposal satisfies the elements of confirmation, though, we must consider whether the Debtor is in compliance with chapter 13 if he does not refinance. The Court finds that if the Debtor is not able to consummate the modified Stipulation, then the record before the Court makes clear that current plan is not feasible and unless the Debtor amends the plan the Court will have no choice but to consider dismissal of the case.

<u>The Computation of Amount Due To Creditors</u>

The Stipulation sets forth a proposal that the Debtor make a payment, from funds he would obtain through a refinancing, as if his plan were extended by twelve months, to a sixty-month term. If this motion were granted and the plan paid, it would eliminate the need to revisit the questions of the Debtor's true disposable income for calendar year 2004, the Debtor's projected disposable income for the remaining term of the plan, and whether the Debtor has proceeded in this case in good faith. This appears to be in the best interest of all parties. Thus, the Court finds the proposal made by the Debtor and Trustee, to pay off the plan with a sum equal to the Debtor's projected disposable income over sixty-month term, to be a sound and fair approach to resolving the issue. However, there is one component that the Debtor has omitted in his projection, namely the impact of the $2,500 per month alimony expense during what would be the 5th year of the plan. That is the essence of the modification the Court will require in order to approve the Stipulation.

The Debtor made his first plan payment on September 18, 2002. As a forty-eight month plan, the last plan payment would therefore be due in August 2006. If we compute the payment due to creditors assuming this were a 60-month plan, as the Stipulation proposes, the last payment under the plan would be due in August 2007. Since the plan payments are $826.15 a month, the one year "extension" offered in the Stipulation yields creditors $9,913.80 more than was proposed in the Motion to Modify.

However, under the Separation Agreement between the Debtor and Ms. French, the Debtor's monthly expenses will be reduced by $2,500 prior to the expiration of that 60-month period. The Separation Agreement requires the Debtor to pay Ms. French $2,500 per month from January 2005 until no later than December of 2006.[2] This would yield an additional $20,000 for the plan payoff (based upon the additional $2,500 in disposable income that will be available to the Debtor from January 2007 until August 2007). Although creditor Suggitt argues that the Debtor's disposable income in 2004 was more than $40,000 greater than the amount the Debtor paid into the plan, as noted above, the record before the Court is insufficient for the Court to make a determination on the Debtor's disposable income in 2004. Therefore, the Court deems it appropriate, and in the best interest of creditors, to approve the Stipulation without further hearing if the Debtor increases the amount offered in the Stipulation by $20,000, to account for the short-term duration of the alimony obligation.

Rationale for Approval of a Modified Stipulation

As a court of equity and without specific figures upon which it can rely, the Court reaches this determination out of deference to the right of the unsecured creditors to be paid all of the Debtor's disposable income in exchange for the Debtor obtaining the super-discharge of chapter 13, and being mindful of the fact that the distribution to unsecured creditors in this case has been reduced substantially as a result of attorney's fees incurred in litigation during the pendency of this case – most of which would not have been necessary if the Debtor had filed accurate, reliable schedules. Under the confirmed plan, the unsecured creditors are to receive a dividend of 7.53%, or $17,261.77 (doc. # 112). It is important to note that this reflects litigation in the case prior to confirmation resulted in legal fees due to the Debtor's attorney in the amount of $18,788.43

[2] According to the Debtor's testimony, he began making payments to Ms. French under the Separation Agreement in November of 2004 rather than in January 2005. Thus, it would appear that the Debtor's obligations under the Separation Agreement could terminate as early as October 2006. However, for purposes of the present analysis, and in light of the fact that the Debtor is not obligated under the Bankruptcy Code to pay his disposable income for 60 months, the Court will presume that the Debtor's support obligations could continue as long as December 2006.

(Id.). The total amount available under the plan is $36,050.20, and roughly half of which was required to be allocated to attorney's fees. If the Debtor increases the amount he proposed to pay creditors in the Motion to Refinance by $ 29,913.80 (as opposed to the $9,913.80), the creditors benefit in three substantial ways. First, the creditors could reasonably attribute a portion of this sum to the amount they might have received as a result of the Debtor's increased income in 2004. Second, the creditors are then less penalized by the extraordinary litigation expenses in the case. Third, in this way the Debtor and creditors more equally share the burden of the legal fee expenses, rather than the creditors having to bear that entire expense. For all of these reasons, the Court finds that the Stipulation would be fair and reasonable, and most likely result in a total distribution to creditors equal to the Debtor's disposable income over the term of the plan, if the amount paid from the refinance is adjusted upward by $20,000.

CONCLUSION

Therefore, the Court approves the Stipulation (docs. ## 124 and 126) if the Stipulation is modified such that the amount the Debtor pays into the plan upon refinance is increased by $20,000, for a total payment to creditors of $46,436.80, and the Debtor tenders this sum to the Trustee during the month of April 2005. If the Debtor is not able or willing to increase the Stipulation by this amount, then the Debtor must either file an amended plan, a motion to modify and reliable Schedules I and J, that meet all the criteria of §§ 1325(a) and 1329 or face dismissal of the case.

The Court sustains the objection of creditor Suggitt, grants the Motion to Modify and grants the Motion to Refinance, to the extent set forth herein.

The Court will enter an Order effectuating this memorandum of decision and setting forth the specific requirements and time frames for proceeding with this case.

This memorandum constitutes the Court's findings of fact and conclusions of law.

March 4, 2005
Rutland, Vermont

Colleen A. Brown
United States Bankruptcy Judge