

In the United States Bankruptcy Court

for the Northern District of Iowa

AMY M. BROWN and
FELTON L. BROWN

Debtor(s).

Bankruptcy No. X90-00788S

Chapter 7

Amy M. Brown and
Felton L. Brown

Plaintiff(s)

Adversary No. X90-0119S

vs.

DONALD H MOLSTAD Trustee

Defendant(s)

MEMORANDUM AND ORDER RE: STATUS OF ACCRUED WAGES AND APPLICATION TO TURN OVER FUNDS

The matters before the court are the trustee's objection to exemptions and the debtors' complaint to determine status of accrued wages and application to turn over funds. Trial was held on July 3, 1990 in Sioux City, Iowa. The court now issues its findings of fact and conclusions of law as required by Bankr. R. 7052. This is a core proceeding under 28 U.S.C. § 157(b)(2)(B) and (E).

FINDINGS OF FACT

Debtors filed their chapter 7 bankruptcy petition on May 2, 1990. At the time of the filing, Amy Brown (BROWN) was employed full time as a school teacher for the 1989-1990 school year. According to Brown's teaching contract, which took effect on August 30, 1989, her salary for the school year was \$18,566.00.

This salary was to be paid to her in twelve equal installments. Exhibit A. Brown was paid on approximately the 21st day of each month for pay periods running from the middle of the preceding month to the middle of the month in which she was paid. Her take-home pay from each monthly pay check was \$1,096.75. Brown also earned \$687.00 annually as the junior high girls, volleyball coach. Her coaching salary was also paid in equal monthly installments. Exhibit B. Brown's teaching and coaching salaries were both included in the one monthly check for \$1,096.75.

Brown's teaching contract required her to work for a term of 187 days, including 180 legally recognized school days and additional days as required by the Board of Education. Exhibit A. The parties stipulate that Brown had no employment responsibilities during the months of June, July and August.

On the date debtors filed bankruptcy, Brown was entitled to \$685.05 for work she had performed pre-petition. She received a pay check which included these pre-petition wages on May 21, 1990. The trustee has not received any portion of these prepetition wages.

On schedule B-4 of their bankruptcy petition, debtors claimed as exempt tax refunds valued in the amount of \$1,000.00 pursuant to I.C. § 627.6(9)(c). Debtors' 1989 federal income tax refund was \$909.87. There is no evidence before the court regarding any state tax refund.

On June 22, 1990, the debtors filed an amended B-4 schedule to list \$1,000.00 of Amy Brown's accrued wages as exempt. The trustee filed his objection to this exemption on June 27, 1990, arguing that because debtors received a post-petition tax refund exceeding \$1,000.00, they could not also claim Amy Brown's wages as exempt.⁽¹⁾ However, because the amendment to schedule B-4 and a complaint to determine the status of Brown's accrued wages were improperly filed in the same document, debtors were ordered to refile them as separate documents (Order of June 28, 1990). Debtors refiled their complaint to determine the status of accrued wages and an application to turn over funds on July 2, 1990, but they have yet to amend their B-4 schedule.

The trustee filed his answer to debtors' complaint on the date of the hearing. The trustee's complaint also contains a counterclaim against the debtors regarding a matter unrelated to Amy Brown's accrued wages.

Because Amy Brown's summer wages are needed for living expenses, debtors sought an emergency hearing regarding their complaint and the claim of exemptions. The litigants have requested that the court enter a final judgment regarding the debtors' complaint and application for turnover and that the court delay trial on the trustee's counterclaim to a later date.⁽²⁾ However, the court notes that because debtors have yet to properly amend their B-4 schedule, a ruling as to exemptions is premature. Creditors will be permitted to object to the debtors' amendment within 30 days of its filing. Bankr. R. 4003(b). The case is ripe for adjudication of how much of Brown's wages is property of the estate.

DISCUSSION

Status of Amy Brown's Accrued Wages

Trustee contends that Brown's June, July and August income represents accrued wages already earned by Amy Brown. Trustee argues that Amy Brown's teaching contract had been fully performed by the § 341 meeting of creditors, held on June 4, 1990, and thus Brown's summer income amounts to accrued summer vacation pay and constitutes property of the bankruptcy estate. The trustee also claims an interest in \$685.05 representing the payment of work performed by Amy Brown prior to May 2, 1990 and paid to her in her May, 1990 pay check. Finally, if the debtors amend their B-4 schedule and she claims as exempt \$1,000.00 of her accrued wages, then the trustee would seek the return of Amy Brown's interest in the debtors' 1989 tax refund.

Debtors argue that Amy Brown's summer teaching wages are not accrued wages, and therefore are not an asset of the bankruptcy estate. Rather, it is argued that Brown's contract is executory and wages earned by her after the filing of her bankruptcy petition do not constitute property of the estate.

The court must determine what portion of Brown's wages constitutes property of the bankruptcy estate under 11 U.S.C. 541(a). Section 541 broadly defines property of the estate to include "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a)(1). However, 11 U.S.C. § 541(a)(6) excludes from the estate earnings from services performed by an individual after the commencement of the case. Section 541(a)(6). See Matter of Hellums, 772 F.2d 379, 381 (7th Cir. 1985); Staats v. Meade (In re Meade), 84 B.R. 106, 108-9 (Bankr. S.D. Ohio 1988).

At the time of bankruptcy, Amy Brown was still obligated by her contract to teach for approximately one month, therefore her teaching contract was executory. Personal service contracts are not generally assignable by either party unless the contract so provides or the other party consents to or ratifies the assignment. Orkin Exterminating Co. v. Burnett, 259 Iowa 1218, 146 N.W.2d 320, 327 1966). Therefore, in Iowa, a bankruptcy trustee is prohibited from assuming or assigning a debtor's personal service contract. 11 U.S.C. § 365(c)(1)(A). However, that the trustee cannot assume Brown's contract does not necessarily eliminate his right to Brown's accrued wages under the contract.

Among the debtor's legal interests which are considered to be part of the bankruptcy estate are his choses in action and claims against third parties existing as of the commencement of the case. Rau v. Ryerson (In re Ryerson), 739 F.2d 1423, 1425 (9th Cir. 1984). These choses in action and claims include rights of action based on contract. Id. at 1425. To the extent that the debtor had a contract right for wages that vested prepetition, her claim for wages is property of the estate. "[W]here a personal service contract has been fully performed by the debtor, the accrued right of the debtor becomes property of the estate and may be used, assumed or assigned by the trustee." In re Scanlon, 10 B.R. at 247.

Where a personal service contract has been only partially performed by the debtor, the accrued right to wages earned prepetition becomes property of the estate. See Clark v. First City Bank (Matter of Clark), 891 F.2d 111, 115 (5th Cir. 1989).

Consequently, the court should not focus on whether debtor's personal service contract is executory. It must rather focus on the extent to which rights to payment under the contract vested as a result of performance which took place prepetition. "Where the right to receive wages in the future is coupled with an interest at the time the petition is filed, it is clear that the right to those wages belongs to the trustee." In re Scanlon, 10 B.R. at 248. See First National Bank of Mercer County v. Rankin (In re Rankin), 102 B.R. 439, 441 (Bankr. W.D. Pa. 1989) (debtor's insurance renewal commissions on policies sold prior to bankruptcy were part of bankruptcy estate); Boyle v. Stefurak (In re Sloan), 32 B.R. 607, 611 (Bankr. E.D.N.Y. 1983) (debtor's share of a finder's fee paid post-petition was property of the estate where debtor essentially fulfilled his obligations prior to bankruptcy); In re Scanlon, 10 B.R. at 247 (real estate commission received post-petition was property of the estate where debtor fully performed his part of the contract prepetition); In re Marshburn, 5 B.R. 711, 713-14 (Bankr. D. Colo. 1980) (post-petition termination payments were property of the estate where essentially no post-petition obligations were required of the debtor to receive the payments.)

However, where post-petition earnings are attributable to services performed by the individual debtor after the commencement of the bankruptcy case, the earnings are excluded from the bankruptcy estate by 11 U.S.C. § 541(a)(6). See Matter of Clark, 891 F.2d 111, 114-15 (5th Cir. 1989), aff.g. In re Clark, 100 B.R. 317 (E.D. La. 1989) (because football player had ongoing obligations under his player contract, salary payments received post-petition were not property of the estate); Cissell v. Zahneis (In re Zahneis), 78 B.R. 504, 505-6 (Bankr. S.D. Ohio 1987) (real estate commission not property of the estate where post-petition payments were dependent on the continuance of a contractual relationship and efforts on the part of the debtor after his filing for bankruptcy); Vogel v. Palmer (In re Palmer), 57 B.R. 332, 335-6 (Bankr. W.D. Va. 1986) (debtor's post-petition year end bonus was not property of the estate where debtor had no right to the bonus when his bankruptcy case commenced).

The court must focus on the debtor's right to payment as of the date of the bankruptcy filing. If the debtor's right to payment is contingent on continued performance of contract obligations, the post-petition income is compensation for post-petition services and does not constitute property of the estate. However, where the debtor's right to post-petition payment is not contingent upon any future obligation on the part of the debtor, the earnings must be considered part of the bankruptcy estate under § 541(a)(1).

In the case at bar, debtors concede that Amy Brown has no continuing obligations under her teacher's contract. In fact, upon completion of the school year, the debtors moved to Florida. The debtors' attorney argues that if Amy Brown returns to teach in the fall, she will need to begin preparing for fall classes and to attend teach workshops. However, Brown's teaching contract does not require the performance of any duties upon the completion of the school year:

Should the first party [Brown] fail or refuse to enter upon or complete such [teaching] duties, either in whole or in part, or should full performance by said teacher be prevented or should this contract be terminated for any cause, then wages shall be paid pro rata only for the time actually taught.

Exhibit A. (Emphasis added.)⁽³⁾

Because Brown's summer wages are based on time actually taught, she became entitled to receive her entire salary upon completion, of her teaching duties. Any Brown could have quit her job on June 2 and still have been entitled to all of her summer wages. The fact that debtors have moved and, according to their attorney, are not likely to return for the trial regarding the trustee's counterclaim, indicates that Brown has effectively vacated her teaching position. In any event, it is clear to the court that Amy Brown fulfilled all of her teaching obligations as of June 2, 1990, and therefore her summer wages from the end of the school year through the completion of the contract year were earned and fully accrued as of June 2, 1990.

Although Amy Brown's wages had accrued as of June 2, not all of these wages accrued prior to the filing of her bankruptcy petition. Had Brown quit her job on the day of bankruptcy, her salary would have been reduced pro rata by

the amount of teaching days she failed to perform. Therefore, wages earned by Brown between May 2, 1990 and June 2, 1990 were clearly post-petition wages and fall outside of the bankruptcy estate. 11 U.S.C. § 541(a)(6). In addition, because a portion of the wages earned by Brown are paid to her over the course of the summer, her postpetition services also increased the amount of summer wages due to her. Including May 2, 1990 and not including June 2, 1990, Brown taught 23 days post-petition. Had Amy Brown not worked these 23 days, she would only have been entitled to 87% of her salary under her 1989-90 teaching contract (157 days actually taught divided by 180 legally recognized teaching days = 87%). Brown's monthly take-home pay is \$1,096.75, and she has or will receive postpetition pay checks in May, June, July and August. Therefore, her take-home pay under her 1989-90 teaching contract is \$13,161.00, and her take-home pay for May through August will total \$4,387.00. Had Brown not worked the 23 teaching days following her filing, she would have been entitled only to a total net 1989-90 salary of \$11,450.07 (87% x \$13,161.00). Therefore, Brown's postpetition earnings total \$1,710.93. Consequently, the court finds that \$1,710.93 of the wages paid Brown after May 2, 1990 is not property of the estate and cannot be withheld by the case trustee.⁽⁴⁾

At the time of her bankruptcy petition, Amy Brown had a claim for wages accrued as a result of her teaching services through the date of filing. Therefore, had Brown quit her job on May 2, 1990, she would have had a claim against her employer for pro rata payment of her salary for the 157 days actually taught. To the extent that Brown had fulfilled her obligations under the contract as of the date of bankruptcy, her claim against her employer for wages accrued through that date constitutes property of the estate. Amy Brown's take-home pay for May, June, July and August will total \$4,387.00 (\$1,096.75 monthly take-home pay X 4 months). Therefore, the court finds that Brown's accrued prepetition wages totaling \$2,627.07 (\$4,387.00 - \$1,710.93) constitute property of the bankruptcy estate.

B. Amy Brown's Claim of Exemption in Accrued Wages

Amy Brown intends to amend her schedules to list \$1,000.00 of accrued wages as exempt pursuant to Iowa Code § 627.6 (9) (c). The debtors have already claimed \$1,000.00 of their state and federal tax refunds as exempt. Iowa Code § 627.6 (9) (c) permits a debtor to claim as exempt up to \$1,000.00 in accrued wages and state and federal tax refunds. Therefore, an individual cannot claim more than \$1,000.00 of accrued wages and tax refunds as exempt.

In order to claim a \$1,000.00 exemption in her accrued wages, Amy Brown cannot claim any of her tax refunds as exempt. Her spouse is permitted to claim as exempt only a share of the debtors' income tax refund in proportion to the amount of the income tax withheld from his wages; he cannot claim any portion of his spouse's share of their income tax refund as exempt. In re Hornby, X90-00207S, slip op. at 3-4 (Bankr. N.D. Iowa, July 16, 1990). Therefore, the debtor must choose whether she intends to claim as exempt \$1,000.00 of her accrued wages, in which case she must turn over her share of the 1989 income tax refund to the trustee, or whether she intends to claim as exempt a combination of her accrued wages and income tax refunds totaling \$1,000.00. To the extent that the combination of Amy Brown's interest in tax refunds and prepetition wages claimed as exempt exceeds \$1,000.00, a trustee's objection to exemptions would be upheld.

CONCLUSION

Amy Brown's income from her 1989 income tax refund and her May, June, July and August teaching wages total \$5,214.98. Brown received her May, 1990 teaching paycheck in the amount of \$1,096.75 and her portion of debtors' 1989 federal income tax return, which the parties stipulate was \$827.98. Therefore, Amy Brown has received \$1,924.73 in cash, none of which has been turned over to the trustee. Brown has yet to receive her June, July and August paychecks, which will total \$3,290.25. Brown is entitled to claim a \$1,000.00 exemption in prepetition accrued wages and income tax refunds pursuant to Iowa Code 627.6(9)(c) and she is entitled to \$1,710.93 in wages accruing postpetition which do not constitute property of the estate. Therefore Amy Brown would be entitled to receive \$786.20 from her June, 1990 paycheck (\$2,710.93 postpetition wages and exempt property -\$1,924.73 cash received). The trustee would be entitled to the remainder of Brown's June, July and August paychecks, or \$2,504.05.

ORDER

IT IS ORDERED that \$1,710.93 of wages paid Amy Brown after May 2, 1990 do not constitute property of the estate.

Brown's postpetition wages in the amount of \$2,676.07 accrued prior to bankruptcy and therefore constitute property of the estate.

IT IS ORDERED that there being no just reason for delay, judgment shall enter accordingly.

IT IS FURTHER ORDERED that Amy Brown shall have 30 days to amend her claims of exemption. Final hearing as to any amended claim and objections thereto and final trial of the trustee's counterclaim and plaintiff's turnover claim as these are contained in this adversary proceeding will be set by the clerk of court. The clerk is to set status conference for the latter part of August, 1990.

SO ORDERED ON THIS 31st DAY OF JULY, 1990.

William L. Edmonds
Chief Bankruptcy Judge

1. Iowa Code § 627.6(9)(c) permits debtors in bankruptcy to claim as exempt the debtor's interests in accrued wages and in state and federal tax refunds as of the date of the filing of the bankruptcy petition not to exceed \$1,000.00 in the aggregate.

2. F.R.C.P. 54(b), which applies to bankruptcy adversary proceedings pursuant to Bankr. R. 7054(a), permits the court to "direct the entry of a final judgment as to one or more but fewer than all of the claims . . . only upon an express determination that there is no just reason for delay and upon express direction for the entry of the judgment."

3. The court notes that Brown's contract also states that its terms, conditions and provisions are subject to and may be modified by a 1989-1990 master contract between the Sergeant Bluff-Luton Education Association and the Sergeant Bluff-Luton Community School District. However, this master contract was not introduced into evidence and the court has no knowledge of its contents.

4. This case was argued by the trustee on the basis of take-home pay.