

## Appeal History:

appealed to District Court No. [C96-320](#) (N. D. Iowa Aug. 16, 1996) (Melloy, J.)  
reversed and remanded to Bankruptcy Court Feb. 24, 1998  
hardship discharge entered Feb. 26, 1998

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# In the United States Bankruptcy Court

## for the Northern District of Iowa

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MICHAEL RAE WILLIAMS, RANDY LEE  
WILLIAMS  
Debtors.

Bankruptcy No. 93-11513KC  
Chapter 13

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### ORDER RE DEBTOR'S MOTION FOR HARDSHIP DISCHARGE

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This matter came on for hearing before the undersigned on July 30, 1996 on Debtor's Motion for Hardship Discharge, or in the Alternative, Motion to Modify Plan and Trustee's Motion to Dismiss. Debtors Michael and Randy Williams appeared with their attorney Webb Wassmer. Carol Dunbar appeared as Chapter 13 Trustee. After the presentation of evidence and argument, the Court took the matter under advisement. This is a core proceeding pursuant to 28 U.S.C. 157(b)(2)(A), (J), (O).

#### STATEMENT OF THE CASE

The amount due under Debtors' Plan confirmed in October 1993 now stands at \$4,448. A deficiency, however, of \$2,268.50 currently exists. Trustee moves for dismissal based on Debtors' material default in making plan payments Debtors resist dismissal and move for a hardship discharge under 1328(b). In the alternative, Debtors request modification of the plan to reduce payments and extend the life of the plan to 60 months.

#### FINDINGS OF FACT

Under their confirmed plan, Debtors were required to make monthly payments to the Trustee of \$139.00. Debtors assert that they can no longer afford these payments. According to Exhibit B, some of Debtors' living expenses have decreased while others have increased. Public assistance payments to Mrs. Williams have apparently decreased while her husband's income has slightly increased. Exhibit B indicates that Debtors' monthly expenses exceed their monthly income by approximately \$50.00.

Mrs. Williams suffers from a medical condition called familial polyposis which causes increased medical expenses. Debtors state that their failure to comply with their payment schedule is due to this medical condition. The Court notes that according to Schedules J and I on file at the time of plan confirmation, Mrs. Williams' only income was from food stamps, although she anticipated receiving

Social Security disability income in the future. This anticipated disability income has not yet been forthcoming.

Original plan payments commenced in October 1993. The plan has a term of 42 months. Unsecured creditors would have received no distribution if Debtors' estate had been liquidated under Chapter 7. To date, they have received no distribution under the Chapter 13 plan.

### HARDSHIP DISCHARGE

Debtors request discharge under 1328(b). That section states as follows:

- b. At any time after the confirmation of the plan and after notice and a hearing, the court may grant a discharge to a debtor that has not completed payments under the plan only if--
  - the debtor's failure to complete such payments is due to circumstances for which the debtor should not justly be held accountable;
  - the value, as of the effective date of the plan, of property actually distributed under the plan on account of each allowed unsecured claim is not less than the amount that would have been paid on such claim if the estate of the debtor had been liquidated under chapter 7 of this title on such date; and
  - modification of the plan under 1329 of this title is not practicable.

Debtors have the burden to prove that they meet the requirements of 1328(b). In re Nelson, 135 B.R. 304, 307 (Bankr. N.D. Ill. 1991); In re Schleppe, 103 B.R. 901, 903 (Bankr. S.D. Ohio 1989). The three subsections of 1328(b) are to be read in the conjunctive. In re Dark, 87 B.R. 497, 499 (Bankr. N.D. Ohio 1988). Thus, in order to qualify for a hardship discharge, Debtors must persuade the Court that they satisfy each subsection of 1328(b). Id. The granting of a hardship discharge is discretionary with the court. Id. at 498.

The first subsection of 1328(b) requires that the circumstances leading to the debtor's failure to make payments be beyond the debtor's control. When confronted with a request for a hardship discharge under Chapter 13, bankruptcy courts have typically limited its application to catastrophic circumstances. Schleppe, 103 B.R. at 903. "A catastrophe denotes a great and sudden disaster. It bears the sense of being outside the control of those whom it hurts." In re Weaver, No. Y87-00327S, slip op. at 8 (Bankr. N.D. Iowa Dec. 7, 1990) (considering hardship discharge in Chapter 12 under 1228 (b), which is identical to 1328(b)). Reasons which are essentially economic do not generally support a hardship discharge under 1328(b). Nelson, 135 B.R. at 307. The circumstances must be "truly the worst of the awfuls -- something more than just the temporary loss of a job or a temporary physical disability." Id. (citation omitted). An unanticipated death precluding payments under a confirmed Chapter 13 plan has understandably been held to be such a catastrophic circumstance which is beyond the debtor's control to support granting a hardship discharge. In re White, 126 B.R. 542, 545 (Bankr. N.D. Ill. 1991).

A review of the few cases considering whether circumstances are beyond the debtor's control discloses that hardship discharges are rarely granted other than in the case of a debtor's death. In Nelson, the debtor's truck broke down, after which he could not find full time employment, and an unexpected expense occurred during a dispute with a bank. 135 B.R. at 307. In White, the debtors' loss of disability income which was committed to making car payments under the plan resulted in the

debtors being unable to make payments to unsecured creditors as required under the plan. 126 B.R. at 544. In Schleppi, the brokerage firm employing the debtor ceased business resulting in and fifty percent decrease in the debtor's income. 103 B.R. at 902. In all of these cases, the courts concluded that the debtors had failed their burden to prove that their inability to make plan payments was "due to circumstances for the debtor[s] should not justly be held accountable" under 1328(b)(1).

In contrast, courts have granted hardship discharges where a debtor or codebtor has died during the pendency of a Chapter 13 Plan. In In re Pecenka, No. 83-02223, slip op. at 1-2 (Bankr. N.D. Iowa Jan. 31, 1986), rev'd on other grounds, No. 86-2030 (N.D. Iowa Jan. 15, 1987), this Court granted a 1328 (b) discharge where the lengthy terminal illness and death of a codebtor dramatically reduced the ability of the surviving debtor to make plan payments. Another court determined that the debtor could not be held accountable for failure to complete payments when he died after paying \$5,174 of the \$5,600 required by his Chapter 13 plan. In re Graham, 63 B.R. 95, 96 (Bankr. E.D. Pa. 1986); see also In re Bond, 36 B.R. 49, 51 (Bankr. E.D.N.C. 1984) (stating that the death of debtor, who died of cancer leaving two minor children, was certainly beyond her control); In re McNealy, 31 B.R. 932, 934 (Bankr. S.D. Ohio 1983) (finding that a debtor's death is not a circumstance for which the surviving codebtor should be held accountable).

The second subsection of 1328(b) requires that unsecured creditors actually receive no less than they would have received in a Chapter 7 liquidation. This is a "best interests" test identical to that required for confirmation of a Chapter 13 plan in 1325(a)(4). White, 126 B.R. at 545; Schleppi, 103 B.R. at 904. Where unsecured creditors would receive no distribution in a Chapter 7 liquidation, any payment to them in a Chapter 13 plan satisfies this requirement. Nelson, 135 B.R. at 308.

The third prong of 1328(b) is the requirement that modification under 1329 is not practicable. Under 1329, the modified plan must meet the statutory requirements for confirmation and may not extend the life of the plan beyond five years after the first payment on the original plan was due. See Nelson, 135 B.R. at 308. Modification is not "practicable" if there is no source of income to fund the modified plan. Bond, 36 B.R. at 51. One court has held that this prong was not satisfied where circumstances changed soon after confirmation but the debtor waited to request relief until it was too late to modify the plan. Nelson, 135 B.R. at 308.

Applying the foregoing law to the facts of this case, the Court concludes that Debtors are not entitled to a hardship discharge under 1328(b). The type of difficulties in which Debtors find themselves are not the type of circumstances envisioned by 1328(b)(1) which would justify a hardship discharge. Mrs. Williams' medical condition, although distressing, is not a catastrophic circumstance. Mrs. Williams was not working and was seeking disability income at the time the Plan was confirmed. Increases in medical expenses and utility bills are essentially economic reasons which generally do not support a 1328(b) discharge.

Because the Court holds that Debtors have failed in their burden to satisfy the first prong of 1328(b), the Court need not address the second and third prongs. Under the record, the Court could conclude that Debtors have met the best interests test of subsection (2). It appears that unsecured creditors would have received no distribution had there occurred a Chapter 7 liquidation.

Debtors have succeeded in meeting the requirement 1328(b)(3), that modification is not practicable, and for the same reasons will be denied their alternative request for relief, i.e. modification of the amount of payments and the term of the plan. Under 1329, modified plans must meet the requirements of confirmation contained in 1325(a). One of the requirements is that secured creditors receive the value of their secured claim. 11 U.S.C. 1325(a)(5)(B). Another requirement is that Debtors be able to

make all the payments under the plan. 11 U.S.C. 1325(a)(6). These requirements must be met within five years after the first payment was due under the original plan, in this case by October 1998.

Exhibit B shows that Debtors have no funds remaining after monthly expenses with which to fund a plan. The amount of \$2,268.50 remains due. Debtors' confirmed plan indicates that this amount is dedicated to paying a secured claim. In order to pay that amount by October 1998, Debtors must be able to make monthly payments of more than \$60.00. Under the record as presented, this is not feasible. Therefore, modification of the plan under 1329 is denied.

### DISMISSAL

Section 1307(c)(6) states that the court may dismiss a Chapter 13 case, "for cause, including . . . [a] material default by the debtor with respect to a term of a confirmed plan." Failure to make payments to the trustee under a confirmed plan may be considered a material default. In re Belanger, 60 B.R. 656, 656-57 (Bankr. D.R.I. 1986); In re Olson, No. L90-00423W, slip op. at 7-8 (Bankr. N.D. Iowa Oct. 14, 1994) (granting dismissal where debtors failed to make payments for over a year and their current employment situation made completion of the plan unlikely). Some authorities do not consider simple failure to make payments under the plan an automatic ground for dismissal. In re Howell, 76 B.R. 793, 795 (Bankr. D. Or. 1986); In re Ford, 78 B.R. 729, 762 (Bankr. E.D. Pa. 1987); In re Black, 78 B.R. 840, 842 (Bankr. S.D. Ohio 1987). Whether missed payments constitute a "material default" must be determined on a case-by-case basis. Black, 78 B.R. at 842; In re Green, 64 B.R. 530, 530 (9th Cir. BAP 1986).

Dismissal under 1307(c)(6) is a matter of the Court's discretion. White, 126 B.R. at 546. Generally, dismissal is appropriate when efforts to cure a default are unsuccessful and the plan cannot be modified to make it feasible for completion. Id.

The Court concludes that dismissal for material default is appropriate in this case. Debtors have paid less than one-half of the amount now due under their confirmed plan. They do not appear to be able to cure this deficiency now or anytime in the foreseeable future. As discussed above, modification of the plan is not feasible. The missed payments constitute a "material default" under 1307(c)(6) making dismissal appropriate.

**WHEREFORE**, Debtor's Motion for Hardship Discharge, or in the Alternative, Motion to Modify Plan is DENIED.

**FURTHER**, Trustee's Motion to Dismiss is GRANTED.

**SO ORDERED** this 8th day of August, 1996.

Paul J. Kilburg  
U.S. Bankruptcy Judge

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**In the United States District Court**

**for the Northern District of Iowa**

## Cedar Rapids Division

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MICHAEL RAE WILLIAMS and  
RANDY LEE WILLIAMS OPINION and  
ORDER

Appeal No.C96-320

*Debtor(s)-Appellants.*

Bankruptcy No. [93-11513KC](#) Chapter 13

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### APPEAL

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This matter is before the Court as an appeal from the Bankruptcy Court's Order Denying Motion for Hardship Discharge, filed October 18, 1996. The Williams filed a voluntary Chapter 13 bankruptcy petition on September 10, 1993. The payment plan provided that the Williams would make monthly payments of \$139.00. On June 6, 1996, the Chapter 13 Trustee filed a motion to dismiss based on failure to make payments pursuant to the plan. The Williams filed a motion for hardship discharge pursuant to 11 U.S.C. §1328(b) or, in the alternative, a motion to modify the plan. The basis for the hardship discharge was Michael Williams' medical condition and the increased medical expenses associated with her condition. Those increased expenses cause the Williams' monthly expenses to exceed their income by \$50. The Williams requested either reduced payments or an extended time in which to make the payments.

The Bankruptcy Court held a hearing on both motions and entered an order on August 8, 1996, granting the motion to dismiss. The Court held that the Williams' increased medical expenses did not rise to the level of "catastrophic circumstances" that the Court believed necessary in order to consider a hardship discharge. The Court also found that modification of the plan was not feasible.

### Discussion

The standard for this Court's review of a bankruptcy court's ruling is well settled:

The Eighth Circuit Court of Appeals has stated the standard of review for decisions of the bankruptcy court with remarkable consistency and succinctness. The court of appeals sits as a second court of review, applying the same standards of review as the district court. In re Roso, 76 F.3d 179, 180 (8th Cir. 1996); In re Rine & Rine Auctioneers, Inc., 74 F.3d 848, 851 (8th Cir. 1996). Thus, both the court of appeals and the district court review the bankruptcy court's conclusions of law *de novo* and its factual findings for clear error. In re Be-Mac Transp. Co., Inc.,

83 F.3d 1020, 1025 (8th Cir. 1996); In re Brown, 82 F.3d 801,804 (8th Cir. 1996); In re Molitor, 76 F.3d 218, 219 (8th Cir. 1996); In re Roso, 76 F.3d at 180; In re Rine & Rine Auctioneers, Inc., 74 F.3d at 851.

Manufacturer's Bank & Trust Co. v. Hoist, 197 B.R. 856, 857 (N.D. Iowa 1996). In this case, the pertinent provision is 11 U.S.C. §1328(b), which provides the authority for a hardship discharge as follows:

At any time after the confirmation of the plan and after notice and a hearing, the court may grant a discharge to a debtor that has not completed payments under the plan only if-

- (1) the debtor's failure to complete such payments is due to circumstances for which the debtor should not justly be held accountable;
- (2) the value, as of the effective date of the plan, of property actually distributed under the plan on an account of each allowed unsecured claim is not less than the amount that would have been paid on such claim if the estate of the debtor had been liquidated under Chapter 7 of this title on such date; and
- (3) modification of the plan under §1329 of this title is not practicable.

11 U.S.C. §1328(b). The debtors must establish the existence of all three subsections in section 1328 (b) before the court will consider whether the debtors qualify for a hardship discharge. See In re Guentert, 206 B.R. 958, 961 (Bankr. W.D. Mo. 1997); In re Nelson, 135 B.R. 304, 307 (Bankr. N.D. III. 1991).

The first subsection of §1328(b) requires "circumstances for which the debtor should not justly be held accountable." This language has usually been interpreted to require the presence of catastrophic circumstances, the "truly worst of the awfuls-something more than just the temporary loss of a job or temporary physical disability." See, e.g., Nelson, 135 B.R. at 307 (quoting K. Lundin, Chapter 13 Bankruptcy, §9.18 at 9-26 (1990)). It is clear that the death of a debtor is one circumstance which constitutes such a catastrophic circumstance. See In re White, 126 B.R. 542, 545 (Bankr. N.D. III. 1991)(citing cases); In re Graham, 63 B.R. 95 (Bankr. E.D. Pa. 1986)(hardship discharge granted due to death of debtor); In re Bond, 36 B.R. 49 (Bankr. E.D.N.C. 1984)(same). It is unclear, however, what circumstances beyond death constitute a catastrophic circumstance, or whether courts must find the existence of a catastrophic circumstance in order to consider a hardship discharge. See, e.g., In Re Edwards, 207 B.R. 728, 729-30 (Bankr. N.D. Fla. 1997)(discussing issue). The paucity of cases discussing the first subsection and the misinterpretation of several cases citing this subsection have complicated the issue.

One case that is often cited as requiring catastrophic circumstances is In re Dark, 87 B.R. 497 (Bankr. N.D. Ohio 1988). See, e.g., In re Fennig, 174 B.R. 475,478 (Bankr. N.D. Ohio 1994)(citing Dark).<sup>(1)</sup> However, as a federal bankruptcy court recently pointed out, the Dark court did not base its denial of hardship discharge on an absence of catastrophic circumstances. Edwards, 207 B.R. at 730 (analyzing Dark). Instead, the Dark court denied the debtor's hardship discharge because the debtor had failed to establish the second subsection of section 1328(b)-not the first subsection. *Id.* at 499 ("Thusly, having failed to satisfy the requirements of §1328(b)(2), the Debtor's motion for a hardship discharge is hereby denied."). When discussing whether the debtor was unable to satisfy the *first* subsection, which is the section from which courts have often interpreted a catastrophic circumstances requirement, the Dark court simply said that the debtor's "unsubstantiated and conclusory statements regarding an inability to fund a plan [were] insufficient." *Id.* at 498. Similarly, courts often cite In re Schleppe, 103 B.R. 901 (Bankr. S.D. Ohio 1989) as one of the main cases requiring catastrophic circumstances, but even Schleppe did not base its denial of discharge on the debtor's failure to establish catastrophic circumstances. 103 B.R. at 904 (parties conceded that the debtor's failure to complete payments as provided by the plan was due to circumstances for which he should not justly be held accountable).<sup>(2)</sup>

In contrast to Dark and Schleppe, In re White, 126 B.R. 542 (Bankr. N.D. III. 1991), held that the first subsection had not been satisfied and referred to a necessity of showing catastrophic circumstances. 126 B.R. at 546-47. Although the White court referred to a catastrophic circumstances requirement, it

did not elaborate on what constituted such circumstances. See Edwards, 207 B.R. at 730 (discussing White). The White court went on to find that:

[Debtor's] hardship is far less than permanent or totally disabling. The nature, extent, and degree of severity of [Debtor's] chronic low back pain are not of such permanence and hardship to constitute the proper characterization as catastrophic in light of the judicial gloss interpreting section 1328(b).

White, 126 B.R. at 546.

The court deciding In re Nelson reached the same conclusion. There, the court ruled that the debtors' loss of their truck, inability to find full time employment, and an unexpected expense of \$1118 were not circumstances that warranted a hardship discharge. Nelson, 135 B.R. at 307. The court explained that these circumstances were economic and "not the type of catastrophic events

such as death or disability which prevent a debtor, through no fault of his or her own, from completing payments pursuant to a plan of reorganization." *Id.* The court also noted that the debtors did not contend that either of them suffered from a disability which prevented them from

working, that the events which prevented them from making payments had occurred prior to their previous modification of the plan, and that those events should have been brought to the court's attention at that time. *Id.*

One of the most recent cases analyzing whether section 1328(b) requires a finding of catastrophic circumstances is In Re Edwards, 207 B.R. 728 (Bankr. N.D. Fla. 1997). There, the court found that circumstances less serious than catastrophic could sometimes warrant a hardship discharge. Edwards, 207 B.R. at 730-31. In explaining why it found an insufficient legal basis for requiring catastrophic circumstances, the court noted that the language of section 1328(b)(1) does not require such a standard and that the "limited extent of the discharge received under section 1328(b)" does not justify such an "exacting" standard. *Id.* The court reasoned that "to deny a debtor who has made every effort to comply with a Chapter 13 plan the benefits of any discharge in bankruptcy when, despite his best efforts, economic circumstances prevent him from

completing his payments would punish that debtor for attempting to repay his creditors under Chapter 13 in the first place." *Id.* Based on this interpretation of section 1328(b), the court applied the following test:

Where a debtor is unable to complete payments under a Chapter 13 plan due to economic circumstances that did not exist nor were foreseeable at the time of confirmation of the plan, where those circumstances are beyond the debtor's control, and where the debtor has made every effort to overcome those circumstances but is unable to complete his plan payments, then I think the requirement of §1328(b)(1) has been met.

*Id.* at 731. Using this reasoning, the Edwards court granted a hardship discharge to a debtor who had lost his business, experienced depression requiring medication, and suffered the breakup of his marriage. *Id.* at 729, 731.

Legislative history supports the Edwards court's opinion that situations less serious than catastrophic could sometimes satisfy section 1328(b)(1). The legislative history accompanying section 1328(b) lists, as an example of circumstances for which debtors should not justly be held accountable, "family illness or accidents with attendant medical bills...severe enough that modification is impracticable ....



"H.R. Rep. No. 595, 95th Cong., 2nd Sess., at 125, *reprinted in* 1978 U.S. Code Cong. & Admin. News 5963, 6086.

Whether or not the "catastrophic circumstances" standard is required by section 1328(b), virtually every court discussing the requirements of section 1328(b) agrees that the proffered reason for failure to comply with a plan must be more than just the temporary loss of a job or temporary physical disability. Both the statutory language and legislative history support this standard.

In this case, when finding that Mrs. Williams' situation did not warrant a hardship discharge under section 1328(b)(1), the Bankruptcy Court noted the following:

The type of difficulties in which Debtors find themselves are not the type of circumstances envisioned by §1328(b)(1) which would justify a hardship discharge. Mrs. Williams' medical condition, although distressing, is not a catastrophic circumstance. Mrs. Williams was not working and was seeking disability income at the time the Plan was confirmed. Increases in medical expenses and utility bills are essentially economic reasons which generally do not support a §1328(b) discharge.

In re Williams, Bankr. No. 93-11513KC, at 4 (Bankr. N.D. Iowa 1996). In making such a finding, the Bankruptcy Court was correct in noting that economic reasons have prevented the Williams from making payments as required by their plan. However, the Court did not acknowledge that the Williams' financial problems resulted from Mrs. Williams' medical condition, surgical procedures, and associated medical costs. Mrs. Williams' situation is not a case where the cost of her medication simply increased. Instead, Mrs. Williams has familial polyposis, which is a rare, inherited condition in which the mucosa of the colon is covered with polyps. See Doc. #3, Brf. of Debtors-Appellants, at 12 (discussing Mrs. Williams' condition in detail). Because of her polyposis, Mrs. Williams had to undergo a total colectomy, which is the removal of the colon and the installation of a pouch to collect waste products. See Doc. #3, at 12 n.6. As a result, she must now purchase medical supplies to enable her to function without her colon.<sup>(3)</sup>

Mrs. Williams' colectomy and resulting increased medical costs constitute more than a temporary physical disability. She has permanently lost her colon and cannot function without the necessary medical supplies. Compared to chronic low back pain, which failed to satisfy the first prong of section 1328(b) in White, the nature, extent, and degree of severity of Mrs. Williams' condition are more far reaching. Compare White, 126 B.R. at 546. Because the economic circumstances resulting from her colectomy were not foreseeable at the time the plan was confirmed, because those circumstances are beyond Mrs. Williams' control, and because she has made every effort to overcome them but is unable to complete the plan payments, see Edwards, 207 B.R. at 730, the requirement of section 1328(b)(1) has been met. The Bankruptcy Court therefore erred in finding that Mrs. Williams' medical condition and resulting increased medical expenses did not constitute "circumstances for which the debtor should not justly be held accountable." 11 U.S.C. §1328(b)(1).

Although the Bankruptcy Court did not find that the Williams had satisfied the first prong of section 1328(b), the Bankruptcy Court did find that the Williams had satisfied section 1328(b)'s other two prongs. The Bankruptcy Court found that the Williams had met the best interests test of section 1328(b)(2). The Court also found that section 1328(b)(3) was satisfied because the Williams' unsecured creditors would have received no distribution had a Chapter 7 liquidation occurred. These findings, in conjunction with this Court's conclusion that the Bankruptcy Court erred in finding that the Williams had not satisfied section 1328(b)(1), establish that the Williams were entitled to a hardship discharge pursuant to 11 U.S.C. §1328(b).



Accordingly, **It Is Ordered:**

This case is remanded to the Bankruptcy Court. The Bankruptcy Court is hereby ordered to enter a hardship discharge for the Williams.

Done and so ordered this 23<sup>rd</sup> day of February, 1998.

Michael J. Melloy  
Chief Bankruptcy Judge

UNITED STATES DISTRICT COURT

1. Fennig analyzes a hardship discharge requested pursuant to 11 U.S.C. §1228(b), which is identical to the language in 11 U.S.C. §1328(b).
2. The Schleppi court did indicate, however, that if the parties had not conceded that debtor's change of employment, divorce, and resulting court-ordered child support and insurance payments were beyond his control, the court would not have found compliance with the first subsection. 103 B.R. at 904.
3. The record shows that Debtors' medical expenses increased from \$50, at the time the Plan was approved, to \$270 at the time of Debtors' motion for hardship discharge.

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