

In the United States Bankruptcy Court

for the Northern District of Iowa

DAVID RUSTIGE and
DENISE RUSTIGE

Bankruptcy No. 98-01227F

Debtor(s).

Chapter 7

ORDER RE: MOTION TO DISMISS

The matter before the court is the court's own motion to dismiss this case for substantial abuse under 11 U.S.C. § 707(b). Hearing was held October 21, 1998 in Sioux City. John F. Schmillen appeared for the United States Trustee. Maynard M. Mohn represented the debtors. The following constitutes the court's findings of fact and conclusions of law as required by Fed.R.Bankr.P. 7052. This is a core proceeding under 28 U.S.C. § 157(b)(2)(O).

Findings of Fact

David Rustige and Denise Rustige filed a Chapter 7 bankruptcy petition on April 27, 1998. The Rustiges live on an acreage near Dolliver, Iowa. They have no dependents.

David Rustige is 46 years old. He has been employed for the last seven years by Building Centers in Estherville, Iowa as a driver, counter salesman and yard man. He works a 30-hour week at \$7.25 per hour for gross pay of \$217.50 per week. He has customarily been laid off from Building Centers for some time in the winter months. His gross income from Building Centers was \$7,804 in 1996 and \$7,940 in 1997. Exhibits I, J. For the past seven years, David has also been self-employed in construction work. He does various home remodeling jobs. At the time of filing, David had monthly gross income of \$1,187 from his jobs and \$147 from unemployment compensation. His net income was \$1,030 per month. Trustee's Exhibit 1, Schedule I. At the hearing on the motion, David claimed his present net monthly income is \$842.34. Debtors' Exhibit B.

Denise Rustige is 44 years old. She is employed as a clerical worker at Spirit Lake Medical Center in Spirit Lake, Iowa. Her monthly gross wage is \$1,369. Exhibit 1. She has deductions of \$219 for taxes, \$316 for insurance, and \$34 for a medical account.⁽¹⁾ The medical account may be used to pay medical bills. Denise receives a permanent disability payment from Orange County in the amount of \$1,579. Exhibit B. Rustiges' Schedule I shows total net monthly income of \$3,397 at the time of filing. Exhibit 1. They say their current income is \$3,255.34 per month. Exhibit B.

Rustiges' Schedule J shows monthly expenses of \$3,682 at the time of filing. Exhibit 1. They say their expenses are now \$3,752.75. Exhibit B. Their expenses include the following items:

Rent	\$200.00
------	----------

Electricity and heating fuel	165.00
Telephone	105.00
Water softener	40.00
Home maintenance	100.00
Food	762.25
Clothing	175.00
Laundry	40.00
Medical	251.00
Transportation	427.50
Recreation	50.00
Renter's insurance	25.00
Life insurance	50.00
Auto insurance	125.00
Auto payment	581.00
Pickup payment	556.00
Personal items	100.00

Exhibit B.

Since 1990, Rustiges have rented their home from a brother-in-law. For the first six months of the tenancy, they paid \$200 cash rent. Since then, in lieu of cash rent, they have been required to spend an average of \$300 per month on building materials to improve the home. The expense items of \$200 for rent and \$100 for home maintenance represent the expense of \$300 for building materials under the agreement with the landlord. On October 1, 1998, the parties reduced their agreement to writing. Exhibit E.

Denise Rustige has had medical problems. In 1997 she had surgery to remove a tumor from her thyroid. The medical expense item of \$251 is the monthly average amount not covered by insurance in 1997. Denise is scheduled for spinal fusion surgery in February 1999. David estimated the cost not covered by insurance would be \$3,000 to \$5,000.

Rustiges' estimate of food expense is the average monthly amount spent in 1997 at grocery stores, plus an allowance of \$200 per month for eating lunch in restaurants on workdays. The personal expense of \$100 is based on their average monthly expense in 1997 for hair and nail care.

Rustiges calculated their transportation expense at 19.5 cents per mile using rates allowed by the Internal Revenue Service. See Exhibit K, CCH tax guide (standard mileage rate is 31.5 cents, less 12 cents for depreciation). David drives 15 miles one way to his job in Estherville. Spirit Lake, where Denise works, is 30 miles away from their home. They drive a total of approximately 34,000 miles annually. From the total auto expense figure, they subtracted and listed separately the monthly expense for auto insurance. David estimates their actual expense for fuel is about \$200 per month.

Rustiges are making installment payments on two vehicles, a 1998 Chevrolet Blazer and a 1998 Chevrolet 3/4 ton 4 x 4 pickup truck. The pickup is a Silverado model with a V-8 engine, automatic transmission, 4-wheel drive, air conditioning, power windows, power door locks, cruise control and

tilt wheel. The Blazer has an LS trim package, 4-wheel drive, power steering, power windows, power door locks, power driver seat, cruise control, tilt wheel, luggage rack and CD player.

The vehicles were purchased March 31 and April 6, 1998. The purchase price of the 1998 pickup was approximately \$27,478. The price for the Blazer was \$28,570. Rustiges scheduled the vehicles as having these values on the date of their filing. Exhibit 3, Schedule B. The vehicles were financed through General Motors Acceptance Corporation on a 60-month payment schedule at \$580.92 per month for the Blazer and \$556.41 per month for the pickup. Exhibit A. The payments are based on interest rates of 4.9% and 6.9%, respectively. On June 25, 1998, Rustiges filed agreements to reaffirm both contracts with GMAC. Id. They have kept current with payments.

The auto dealer took Rustiges' 1986 pickup and 1988 Pontiac Bonneville in trade. Rustiges had had the pickup for seven years, and the Bonneville six years. The pickup had about 215,000 miles; it used oil. The Bonneville had about 166,000 miles. Both vehicles had transmission problems. Neither was encumbered. The Bonneville did not have 4-wheel drive. Rustiges expect repair expenses on the new vehicles to be significantly lower; insurance and registration costs are higher. Registration is \$68 for the pickup, a special farm rate, and \$268 for the Blazer.

Rustiges scheduled a total of \$58,977 in secured debt to GMAC, and a \$731 priority tax claim. Exhibit 2, Schedules D, E. All their unsecured debt, a total of \$40,072, is for credit card purchases for personal use. Id., Schedule F. David Rustige uses the pickup 30 to 40 percent of the time for his construction business.

Other than the two vehicles, debtors scheduled the following property: cash and bank accounts, \$200; household goods, \$1,500; art prints and compact discs, \$225; clothing, \$600; a wedding ring; three firearms, \$155; term life insurance policies; Denise's disability payments; and accrued wages and tax refunds. Exhibit 3, Schedule B. All property was claimed exempt except \$25 in a bank account and the compact discs valued at \$25. Id., Schedule C.

Rustiges have not filed amended Schedules I and J. They first contacted an attorney about filing bankruptcy in February 1998.

Discussion

On July 1, 1998, the court filed its own motion to dismiss the debtors' Chapter 7 case for substantial abuse. The U.S. Trustee supported the motion orally at the hearing. Section 707(b) of the Bankruptcy Code provides that:

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 [chapter 7] whose debts are primarily consumer debts if it finds that the granting of relief would be a substantial abuse of the provisions of [chapter 7]. There shall be a presumption in favor of granting the relief requested by the debtor.

11 U.S.C. § 707(b). The Rustiges' debts are primarily consumer debts. Their case is subject to the provisions of § 707(b).

Section 707(b) was added to the Bankruptcy Code in 1984 as a way to promote fairness to creditors by reducing the use of Chapter 7 relief by unneedy debtors. Stuart v. Koch (In re Koch), 109 F.3d

1285, 1288 (8th Cir. 1997); In re Walton, 866 F.2d 981, 983 (8th Cir. 1989). "Substantial abuse" is not a defined term. The primary factor for determining substantial abuse is the "debtor's ability to pay his debts when due as determined by his ability to fund a chapter 13 plan." Walton, 866 F.2d at 984-85 (quoting Zolg v. Kelly (In re Kelly), 841 F.2d 908 (9th Cir. 1988)); United States Trustee v. Harris, 960 F.2d 74, 76 (8th Cir. 1992).

The Eighth Circuit has declined to adopt the "totality of circumstances" approach. Harris, 960 F.2d at 77. A debtor's "substantial ability to pay creditors *standing alone* warrants dismissal of a Chapter 7 petition for substantial abuse." In re Koch, 109 F.3d at 1288; accord Harris, 960 F.2d at 76. This approach does not create a mandatory Chapter 13 provision. Debtors may still choose whether to file a Chapter 13 petition. Koch, 109 F.3d at 1290. A Chapter 7 discharge is a privilege, not a right. In re Carlton, 211 B.R. 468, 478 n.9 (Bankr. W.D.N.Y. 1997).

Egregious conduct is not a required element of a substantial abuse dismissal. Harris, 960 F.2d at 76. Inability to pay, however, will not prevent such dismissal in a case of bad faith. Id. (quoting In re Kelly, 841 F.2d at 914-15); In re Veenhuis, 143 B.R. 887, 888-89 (Bankr. D. Minn. 1992).

The facts of this case sufficiently rebut the presumption that Rustiges should receive relief under Chapter 7. The Rustiges' case combines the elements of ability to pay and bad faith. They have sufficient income to fund a Chapter 13 plan that would make substantial payments on their debts. They have masked their ability to pay creditors with a schedule of excessive expenses. Moreover, they have used the bankruptcy system as a means to acquire two luxury vehicles.

Ability to fund a plan is determined by analyzing disposable income in a hypothetical Chapter 13 case. Koch, 109 F.3d at 1288-89. Income from exempt sources is included in disposable income. Id. at 1289. Disposable income is "income ... which is not reasonably necessary to be expended ... for the maintenance or support of the debtor or a dependent of the debtor; and ... if the debtor is engaged in business, for the payment of expenditures necessary for the continuation, preservation, and operation of such business." 11 U.S.C. § 1325(b)(2).

Rustiges have no dependents. Their monthly allowance of \$762 for food, \$175 for clothing and \$100 for personal items appear double the amount that would be reasonable for two debtors in bankruptcy. Their employment does not require them to eat in restaurants. Neither one needs special clothing for work. Their allowances for telephone and recreation are generous. Rustiges claim their current expenses exceed income by \$497.41. Reduction of food, clothing and personal care expenses alone would give them disposable income.

Rustiges spend a total of \$1,137.33 each month on installment payments for their vehicles. They apparently have the ability to make the payments despite the anticipated costs of Denise's surgery. By reaffirming their debt with GMAC, Rustiges committed themselves to making auto payments totaling \$67,102.47. Their attorney made declarations that the agreements would not pose an undue hardship on the Rustiges. Exhibit A. They have made all the payments since entering into the contracts.

Rustiges explained the circumstances of their purchase of the new vehicles. Both of their older vehicles were having mechanical problems and would need to be replaced in the near future. Rustiges did not have money for a down payment and believed they would not be able to obtain financing after they filed bankruptcy. David's remodeling work requires a vehicle large enough to haul materials to jobs. Rustiges considered reliability and safety when deciding what vehicles to buy. They live on a gravel road which receives low priority for snow removal in the winter. In the past they have lost work from being snowed in.

Rustiges said they looked at other cars. They offered Exhibit C as an example of the payments they would have been making if they had obtained a used car loan from a bank. The example is based on the purchase of two-year-old vehicles of the same models and with the same features as the vehicles they actually purchased. It assumes financing a 20% down payment at 15.5% interest and the balance of the purchase price at 8.9% interest over 54 months. In the hypothetical, the total payments were \$461.79 for the Blazer, and \$465.27 for the pickup. Exhibit D, the rate sheet for auto loans from Northwest Federal Savings Bank, shows that a loan for the purchase of a car more than two years old requires a larger down payment and accrues interest at a higher rate. Rustiges said they decided to purchase new vehicles because the payments were not that much higher than for used vehicles, and because new vehicles are covered by extended warranties.

In addition to the \$1,137 for auto payments, Rustiges have budgeted \$427.50 for other transportation costs and \$125 for auto insurance, for a total of \$1,689.50 per month for auto expenses. This amount, 52% of their net income, is excessive and unreasonable.

Rustiges contend they are unable to fund a Chapter 13 plan. This argument assumes they had only two options when they contemplated bankruptcy relief: filing a Chapter 13 petition while keeping their old vehicles, or filing under Chapter 7 and buying the two new vehicles. They say it is not realistic to assume their old vehicles would have lasted much longer. Since they had to replace the vehicles, they argue, they no longer have disposable income to devote to a plan.

The court does not fault Rustiges for their desire to have reliable transportation. The court will assume for this discussion that they needed to replace both vehicles at the same time. Rustiges have not made a convincing argument, however, that their purchase of two new luxury vehicles was a reasonable expense. They had other options. By their own figures they could have reduced their monthly auto payments by \$200 by purchasing two-year-old vehicles. Exhibit C. Moreover, they might have purchased less expensive models or vehicles without such luxury features as power doors and a CD player. They might have leased vehicles. They might have financed older vehicles either through a bank or a car dealer.

The amount of Rustiges' disposable income in a hypothetical Chapter 13 plan depends largely on the amount they may reasonably budget for auto and transportation expenses. It is not the court's task to propose a budget for them. A reasonable figure, however, would be significantly lower than the amount Rustiges say they now spend, and would enable them to pay a substantial amount of their unsecured debt. For example, if they reduced their total auto expenses to \$1,189 per month, they would have \$500 available for monthly plan payments, or a total of \$18,000 in a three-year plan.

A debtor's ability to fund a Chapter 13 plan is often stated as a percentage of the total unsecured debt that disposable income would pay over three years. See Koch, 109 F.3d at 1287 (listing percentage calculations in Eighth Circuit § 707(b) cases). The Eighth Circuit has not set a minimum percentage amount that will satisfy the requirement that abuse be "substantial." In two cases, disposable income of less than \$500 per month was sufficient. See Harris, 960 F.2d at 77 (debtors with \$421.25 disposable income, case dismissed for abuse); Walton, 866 F.2d at 985 (same result for debtors with \$497 per month). Other courts have found abuse when the estimated repayment rate under a plan is less than 50 percent. See, e.g., In re Gomes, 220 B.R. 84, 88 (9th Cir. BAP 1998) (no threshold percentage required to find abuse; no basis to find 43% repayment in three years too low to dismiss); In re Laman, 221 B.R. 379, 383 (Bankr. N.D. Tex. 1998) (debtor had ability to pay 25% of \$88,895 credit card debt in three years); see also In re Carlton, 211 B.R. 468, 477 (Bankr. W.D.N.Y. 1997) (one measure of ability to fund plan is ability to pay "significant dollar amount, irrespective of percentage" to unsecured creditors). The analysis should not be a rigid mathematical calculation. A

debtor could manipulate a mechanical test by incurring more debt prepetition. The court finds and concludes that, if Rustiges allotted reasonable amounts for food, clothing, personal and auto expenses, they would have disposable income of approximately \$500 per month to devote to a plan. This amount is significant enough to make their Chapter 7 filing a substantial abuse of the bankruptcy system.

Rustiges' purchase of two new luxury vehicles on the eve of bankruptcy is an indicator of bad faith. See In re Veenhuis, 143 B.R. 887, 889 (Bankr. D. Minn. 1992) (factors that indicate bad faith include tying up value in expensive exempt assets); In re Grant, 51 B.R. 385, 393-94 (Bankr. N.D. Ohio 1985) (extravagant expenses incurred shortly before filing petition give debtor a "head start" rather than "fresh start"). The court does not doubt that Rustiges needed to have reliable transportation, which probably meant they needed to replace their vehicles. The vehicles they chose, however, were more luxurious as well as more reliable. They had not purchased their prior vehicles new. The older vehicles did not have the power equipment that the new ones have; the Bonneville did not have 4-wheel drive. Rustiges purchased the new vehicles when they knew they would be filing a bankruptcy petition. They anticipated discharging approximately \$40,000 of unsecured debt. They greatly improved their position at the expense of their creditors.

Devotion of large amounts of money to reaffirm the purchase of a luxury item, while discharging all unsecured debt, is an abuse of the bankruptcy system. In re Nelson, No. 97-03710S, slip op. at 6 (Bankr. N.D. Iowa March 5, 1998), aff'd, 223 B.R. 349 (8th Cir. BAP 1998).

IT IS ORDERED that the petition of David Rustige and Denise Rustige will be dismissed effective November 30, 1998 unless prior to that date debtors elect to convert to a case under Chapter 13.

SO ORDERED THIS 17th DAY OF NOVEMBER 1998.

William L. Edmonds
Chief Bankruptcy Judge

I certify that on I mailed a copy of this order to debtors, Maynard Mohn, David Sergeant, and the U.S. trustee.

1. Debtors first showed the medical account as a deduction from David's paycheck. Exhibit 1. They now show it as Denise's deduction. Exhibit B. Debtors did not subtract the \$34 in the calculation of her net income. The error is offset by an expected increase in her wages that is not shown in Exhibit B. Denise expects to receive a three percent raise in the near future, which would give her additional gross income of \$40 per month.