

In the United States Bankruptcy Court

for the Northern District of Iowa

SUZANNE LOUISE HALL*Debtor(s).*

Bankruptcy No. 98-01351-W

Chapter 7

GEORGE BRADLEY HALL*Plaintiff(s)*

Adversary No. 98-9125-W

vs.

SUZANNE LOUISE HALL

Defendant(s)

ORDER

On August 17, 1999, the above-captioned matter came on for trial pursuant to assignment. Plaintiff George Bradley Hall appeared by Attorney Michael Dunbar. Debtor/Defendant Suzanne Louise Hall appeared by Attorney Joseph Sevcik. Evidence was presented and the matter was taken under advisement pending briefs which were due September 1, 1999. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(I).

STATEMENT OF THE CASE

Plaintiff George Bradley Hall objects to discharge of a debt owed to him by his former spouse, Debtor Suzanne Louise Hall, as a result of a dissolution decree entered in Black Hawk County, Iowa District Court, on September 11, 1996. He relies on 11 U.S.C. §523(a)(15) which provides an exception to discharge for debts incurred by a debtor in the course of a dissolution proceeding. Mr. Hall seeks a determination that the outstanding portion of Debtor's obligation to him in connection with "Annie's Maid Rite" is nondischargeable.

FINDINGS OF FACT

Debtor/Defendant Suzanne Louise Hall and Plaintiff George Bradley Hall were married in 1980. On September 11, 1996, Debtor and Mr. Hall were granted a decree of dissolution. The dissolution decree granted Debtor full ownership of the couple's "Annie's Maid Rite" business, which the state court valued at \$75,000. In return for receiving full ownership of Annie's Maid Rite, the decree obligated Debtor to pay the sum of \$36,500 to Mr. Hall, a substantial portion of which remains unpaid. The dissolution decree also granted Debtor ownership of the couple's former residence. Mr. Hall, however, retained a lien in the residence in the amount of \$26,229, representing one-half of the equity that the Hall's had in their home at the time of the dissolution. Debtor listed the value of this home on her bankruptcy schedules at \$90,000, which is the same value the divorce court placed on the home in 1996.

In January, 1999, the bank holding the primary lien on the home foreclosed on the Hall residence. As part of an alleged oral agreement with Debtor, a friend of Debtor agreed to redeem the home for approximately \$40,000. The friend has also allegedly agreed to pay Debtor an additional \$45,000 to purchase the house. Mr. Hall was not a party to this agreement. No evidence supporting the existence of this agreement, other than oral testimony, was offered. Mr. Hall has not released his lien in the home.

Debtor is 39 years of age and has two years of college education. She testified that she has had medical problems including alcohol abuse and recent pancreatic surgery. She has primary care of the couple's three children, who were between the ages of twelve and seventeen years old at the time Debtor filed her Chapter 7 petition. Debtor and these three children reside at Debtor's parents' home. Debtor currently has no obligation to pay rent or utilities. In addition, Debtor has no obligation for an automobile other than normal maintenance and insurance expenses. Debtor is employed at a job earning \$8.00 per hour. Her after-tax income is approximately \$520 per pay-period, which amounts to \$13,520 per year, or \$1,126 per month. In addition, Debtor currently receives approximately \$500 per month in support from Mr. Hall through a withholding order.

After subtracting the expenses listed on Debtor's schedules relating to the maintenance of a home which she no longer incurs, Debtor lists the following monthly expenses: (1) \$400 for food; (2) \$75 for clothing; (3) \$10 for laundry; (4) \$25 for medical care; (5) \$85 for automobile maintenance; and (6) \$25 for auto insurance. These expenses total \$620 per month. Debtor testified that these expenses are accurate, with the exception of a claim that her clothing expenses have now increased to between three and four hundred dollars per month.

Prior to filing her petition for Chapter 7 relief, Debtor transferred ownership of the "Annie's Maid Rite" business to her sister and brother-in-law. Debtor's testimony regarding the value that the purchasers in this transaction gave was contradictory. At one point, Debtor testified that her brother-in-law assumed all liabilities for the business. However, at another point, Debtor indicated that she is still liable for tax liabilities resulting from the business. In addition, the business held a note in the amount of \$42,000 against Debtor's father. Neither Debtor, nor any other party, has liquidated this note.

Mr. Hall currently earns \$16.10 per hour doing seasonal work for an earth-moving company in Colorado. He collects unemployment benefits in the off-season. Although there is no evidence in the record regarding Mr. Hall's expected yearly income from this work, he has earned approximately \$20,000 to date this year. Other than his support obligation to Debtor, there is no evidence in the record regarding Mr. Hall's current expenses.

CONCLUSIONS OF LAW

The Bankruptcy Code excludes from discharge debts incurred pursuant to a divorce or separation that are not support obligations unless the debtor does not have the ability to pay the debt or the discharge of the debt would "result in a benefit to the debtor that outweighs the detrimental consequences" to the non-debtor spouse resulting from the discharge. 11 U.S.C. §523(a)(15)(1994). Specifically, §523(a)(15) provides:

- (a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt ...

(15) not of the kind described in paragraph (5) that is incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court of record, a determination made in accordance with State or territorial law by a governmental unit unless:

(A) the debtor does not have the ability to pay such debt from income or property of the debtor 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 a business, for the payment of expenditures necessary for the continuation, preservation, and operation of such business; or

(B) discharging such debt would result in a benefit to the debtor that outweighs the detrimental consequences to a spouse, former spouse, or child of the debtor....

11 U.S.C. §523(a)(15)(1994).

If a non-debtor spouse establishes that the debt in question arises from a property settlement pursuant to a divorce or separation decree, the burden of proof under §523(a)(15) shifts to the debtor to establish the elements of one of the exceptions outlined in §523(a)(15)(A) or (B). In re Moeder, 220 B.R. 52, 55-56 (B.A.P. 8th Cir. 1998).

Under §523(a)(15)(A), a debtor may discharge a property settlement obligation if failure to discharge the debt would "reduce the debtor's income below that necessary for the support of the debtor and the debtor's dependents." In re Anthony, 190 B.R. 433, 436 (Bankr. N.D. Ala. 1995) (citing H.R. Rep. No. 835, 103d Cong., 2nd Sess. 54 (1994), reprinted in 1994 U.S.C.C.A.N. 3363) . Courts have interpreted this standard as allowing a debtor to discharge a property settlement obligation only where the debtor is not able to make reasonable payments out of future income. It is not necessary that Debtor be able to make a present lump sum payment. In re Gamble, 143 F.3d 223, 226 (5th Cir. 1998) . Courts ordinarily decline to apply a straight budget analysis where a debtor's inability to pay is the result of the voluntary assumption of debt, the squandering of assets awarded to a debtor during a dissolution proceeding or a debtor's voluntary election to reduce the debtor's income. In re Greenwalt, 200 B.R. 909, 913 (Bankr. W.D. Wash. 1996) ; In re Crosswhite, 148 F.3d 879, 883 (7th Cir. 1998) .

At least one court has expressed skepticism as to a debtor's inability to pay where the debtor lived with the debtor's parents, incurred no obligation for rent or utilities, and presented no extraordinary circumstances. Anthony, 190 B.R. at 433. This skepticism is warranted given the burden of proof under §523 (a) (15) . Where a debtor lives with the debtor's parents, will presumably receive a discharge for most of the debtor's pre-bankruptcy expenses, and incurs no expenses for rent or utilities, the natural conclusion is that, even where the debtor's income is relatively modest, the debtor could pay a property settlement obligation. If the facts require a different conclusion, the burden is properly on the debtor to present evidence to establish such a result.

Section 523(a)(15)(B) does allow a debtor who could pay a property settlement obligation to nonetheless discharge that obligation if the debtor establishes that such a discharge would benefit the debtor more than it would harm the non-debtor spouse. 11 U.S.C. §523(a)(15)(B) (1994) . When determining whether a debtor has satisfied the burden under §523(a)(15)(B), courts analyze the totality of the circumstances. See In re Hill, 184 B.R. 750, 756 (Bankr. N.D. Ill. 1995) ; Gamble, 143 F.3d at 226 (same) . The most common factor courts use when analyzing the totality of the relative benefits and detriments to each spouse under §523(a)(15)(B) is each party's current and potential

income and expenses. See In re Molino, 225 B.R. 904 (B.A.P. 6th Cir. 1998); see also Vander Werf v. Barker (In re Barker), No. 97-9176-C, slip op. at 7-9 (Bankr. N.D. Iowa Apr. 7, 1998). A debtor does not satisfy the burden of proof under this analysis when the debtor fails to present evidence regarding the income and expenses of a non-debtor spouse. In re Stone, 199 B.R. 753, 785 (Bankr. N.D. Ala. 1996).

Courts look with skepticism on claims of hardship when debtor's financial position is due more to a voluntary decision or intentional manipulation than to circumstances beyond the debtor's control.⁽¹⁾ This is especially true under §523(a)(15) where Congress has expressed concern with a debtor's ability to discharge property settlement obligations. Although Congress enumerated two exceptions to the rule of nondischargeability, a debtor may not manipulate those exceptions by voluntarily reducing income or assets. Such an interpretation would encourage debtors to reduce their earning capacity and liquidate assets. Consequently, the Court must consider not only the relative burdens or benefits involved in discharging the debtor's property settlement obligation, but also whether those burdens are the result of voluntary conduct by the debtor.

Application of §523(a)(15)(A)

The parties stipulate that Mr. Hall's claim against Debtor is a property settlement obligation that arose as a result of a dissolution decree. Consequently, the burden of proof under §523(a)(15)(A) and (B) shifts to Debtor. In evaluating whether Debtor has met that burden of proof, the Court will examine various factors.

A. Income and Expenses

Debtor estimates that the payments on her obligation to Mr. Hall are \$350.00 a month. She calculates these payments by amortizing the principal obligation over ten years with interest at a rate of seven percent per annum, which are the same terms under which Debtor previously paid Mr. Hall. Debtor's current net after-tax pay is approximately \$520 every other week, which totals \$13,520 annually. Mr. Hall testified that his current child support obligation to Debtor, which she is collecting under a withholding order, is approximately five-hundred dollars per month. Debtor testified that her opportunity for advancement at her current job is limited. Her expenses are minimal. She currently lives with her parents and does not have automobile expenses, rent or utilities. Debtor's current monthly expenses total \$620 per month. Her total after-tax income is approximately \$1,626 monthly.

Thus, Debtor has over one-thousand dollars in disposable income. She testified that she remains personally liable for a tax obligation of "Annie's Maid Rite," but later testified that her brother-in-law assumed that liability in connection with his purchase of the business. Even considering this obligation, however, Debtor retains sufficient disposable income to pay her debt to Mr. Hall.

Debtor has expressed an understandable desire to move from her parents' home. There is no requirement in the Code that a debtor live with family members to minimize expenses. Nonetheless, when applying the provisions of the Code, the Court must evaluate the circumstances based on existing facts. To consider alternative circumstances would require the Court to base its holdings on hypothetical facts. Debtors are allowed a range of expenses based on their circumstances at the time examined. Section 523(a)(15)(A) does not mandate a fixed allowance for each debtor. Instead, §523(a)(15)(A) requires the Court to analyze the debtor's actual ability to pay the debt based on the debtor's actual, reasonably necessary expenses. Debtor's reasonably necessary expenses, as now before the Court, are \$620 per month.

Although Debtor's lifestyle is by no means extravagant, §523(a)(15)(A) only provides an exception where the debtor has the inability to pay, it does not require that the debtor be afforded an extravagant lifestyle, or even a lifestyle equivalent to other debtors. Debtor has supplied the Court with no specific evidence showing expenses that render her unable to pay her obligation to Mr. Hall. On this record, Debtor currently has one-thousand dollars in disposable income each month. This renders her capable of paying a \$350 monthly obligation.

B. Debtor's Ability to Retire Her Obligation to Mr. Hall

Evidence presented at trial indicates that the couple's former residence is under an oral agreement for sale at a price yielding nearly \$45,000 of equity to Debtor. Mr. Hall is not a party to the agreement, nor has Mr. Hall released his lien on the home. In addition, the purchaser of the property does not appear to have agreed to pay Mr. Hall any part of the purchase price. However, because a lien on real property is generally enforceable against future purchasers, Mr. Hall may still enforce his lien against the purchasers of the home.

Debtor mistakenly deducts Mr. Hall's lien from the equity she will receive from the sale. (Def.'s Br. at 1). Because the agreement to sell is between Debtor and the purchaser, and because the purchaser has not agreed to pay Mr. Hall any portion of the purchase price, Debtor will presumably receive the full \$45,000 of the agreement. If so, Debtor will receive sufficient equity from the sale to retire her obligation to Mr. Hall.

Debtor testified as to her desire to use the proceeds from the sale of the home to purchase a new home and maintains a desire not to return to the couple's previous home. Debtor's desire to purchase a new home is understandable. If the Court were to allow Debtor to discharge her debt to Mr. Hall on this basis, however, it would have the effect of increasing the support obligations the state court has already imposed upon Mr. Hall. Debtor cannot escape her burden of showing that she is unable to pay her obligation to Mr. Hall by asking this Court to approve purchases with money she owes Mr. Hall. If Debtor is in need of additional support from Mr. Hall, her remedy lies with the state court in an action to modify Mr. Hall's support obligation, not with this court in the determination of whether Debtor's obligation to Mr. Hall is dischargeable.

C. The Abandonment of a Substantial Asset

Prior to filing her Chapter 7 petition, Debtor voluntarily transferred the entire ownership of the "Annie's Maid Rite" business to her sister and brother-in-law. In addition to the value of the operation as a going concern, the business held a \$42,000 note against Debtor's father which was never collected. Debtor received no cash as a result of the sale of the "Annie's Maid Rite." The evidence was unclear as to whether Debtor's brother-in-law assumed Debtor's tax liability in return for the business. Nonetheless, the maximum value Debtor received for the "Annie's Maid Rite" was \$15,000. Prior to the transfer of the business to Debtor's sister and brother-in-law, Debtor's father contacted a realtor who declined to list the property because he did not feel the prospects of a sale were high. The realtor was unaware of the \$42,000 note, however. (Cortright Dep. at 27). Mr. Hall had expressed a strong interest in retaining ownership of the business in the dissolution proceedings. Neither Debtor nor any member of her family, however, contacted Mr. Hall to ask whether he would be willing to purchase the business.

This transfer, whereby Debtor practically gifted an asset of potentially substantial value to a relative for little or no consideration without first contacting a known, interested buyer, does not appear to be an arm's length transaction. It is true that Debtor's father contacted a real estate professional who

declined to list the business. It is also true, however, that Debtor's father himself valued this business at \$75,000 during Debtor's dissolution proceedings less than three years previously.

While it is possible that the business declined in value since the dissolution proceedings, as some evidence tends to indicate, Debtor's brother-in-law is apparently able to operate the business at a profit. It is highly unlikely, therefore, that the business, even if it has depreciated in value, had no value. Moreover, the fact that Debtor transferred the property to a relative without contacting a known interested buyer and without collecting a \$42,000 note against another relative are sufficient to establish that this transaction was not one at arm's length and was not intended to maximize value.

Despite the realtor's decision not to list the property, the fact that Debtor transferred the business to a relative for little or no consideration, that Debtor's father had recently valued the business at \$75,000, and that Debtor did not contact Mr. Hall about purchasing the property, despite his known interest, are sufficient to convince this Court that any inability Debtor has to pay her obligation to Mr. Hall is due, at least in part, to a manipulation of her finances. Gamble, 143 F.3d at 226. If the Court were to conclude otherwise, the effect would be to require Mr. Hall to subsidize a gift, in the amount of \$30,000, to Debtor's family. Although an honest but unfortunate debtor is entitled to a fresh start, Congress, through §523(a)(15), has expressed an intention that the courts analyze property settlement obligations with particular scrutiny before a debtor receives a completely fresh start. Debtors are not allowed to manipulate their finances through gifts to family members in order to create an artificial inability to pay property settlement obligations. Section 523(a)(15)(A) provides an exception to the general nondischargeability rule for property settlements where a debtor lacks the ability to pay, not where a debtor simply lacks the desire to pay.

Debtor has failed to satisfy her burden of proof under §523(a)(15)(A) and therefore cannot discharge her obligation to Mr. Hall. Debtor has not proven a lack of disposable income sufficient to pay her debt to Mr. Hall. The transaction involving the sale of the house and the transfer of the business both compel this Court to conclude that Debtor is attempting to artificially manipulate her finances to present a more sympathetic financial picture. Therefore, Debtor cannot discharge her property settlement obligation under §523(a)(15)(A) .

Application of §523(a)(15)(B)

The parties stipulate that the obligation at issue is a property settlement obligation. Therefore, the burden of proof under §523(a)(15)(B) rests with Debtor to establish that the benefit to her in discharging this obligation is greater than the detriment such discharge will cause Mr. Hall. Neither Debtor nor Mr. Hall have extravagant lifestyles. Nonetheless, because Debtor has not provided the Court with evidence regarding Mr. Hall's expenses or precise net annual earnings, she has failed to carry her burden under §523(a)(15)(B) .

When determining the relative benefits and detriments of the parties, the Court must focus on the totality of the circumstances. This inquiry includes an analysis of the relative income and expenses of the parties. The inquiry must also examine any voluntary decisions the debtor made that increase the detriment to the debtor. Debtor lives with her parents, has no car or home payment and has approximately \$1,626 of total monthly income. After subtracting Debtor's expenses, she has approximately one-thousand dollars per month in disposable income.

Mr. Hall on the other hand earns \$16.10 per hour doing seasonal work for an earth-moving company and has earned approximately \$20,000 this year. Debtor presented no evidence regarding Mr. Hall's expenses. Debtor did not address §523(a)(15)(B) in the Brief her counsel supplied to the Court. The

Court has no basis to compare the relative detriments and benefits of discharge by comparing the expenses and income of the parties as it did in Barker, slip. op. at 7. As a result, Debtor has failed to carry her burden of proof under §523(a)(15)(B) by failing to provide sufficient evidence to the Court regarding: 1) Mr. Hall's expenses, and 2) any extraordinary circumstances on her part to offset the one-thousand dollars of monthly disposable income that she currently has available. See Stone, 199 B.R. at 784-85 (providing that the debtor must present evidence of the income and expenses of the non-debtor spouse to carry the debtor's burden of proof under §523(a)(15)(B)).

Even if Debtor had presented sufficient evidence for the Court to compare the relative expenses of the parties, she can substantially reduce the burden of paying Mr. Hall by retiring the debt with the proceeds of her sale of the couple's former home. Assuming Mr. Hall has ordinary and reasonable expenses, the benefit to Debtor in discharging any remaining obligation, given Mr. Hall's similarly modest salary and Debtor's nearly one-thousand dollars per month in disposable income, is much smaller than the detriment such discharge would impose upon Mr. Hall.

The Court also considers, as part of the totality of the circumstances, the Debtor's voluntary prepetition transfer of assets that will contribute in large part to any detriment Debtor may suffer by having to pay her debt to Mr. Hall. The Court must scrutinize the detriment a debtor will incur where such detriment is due in part to the debtor's voluntary reduction of assets or income. Debtor could have substantially mitigated any detriment the retention of this obligation will cause her by offering to sell the "Annie's Maid Rite" to Mr. Hall in satisfaction of all or part of the obligation. Instead, Debtor gave the business to her sister and brother-in-law without contacting Mr. Hall, a known interested buyer. More importantly, Debtor could have retired her entire obligation to Mr. Hall by collecting the \$42,000 note that the business held against her father. Just as a debtor may not voluntarily quit employment and claim a burden, Molino, 225 B.R. at 909, neither may a debtor voluntarily gift away substantial assets and claim a burden. Although the Court need not ultimately determine whether the circumstances of this transfer are sufficient by themselves to deem a property settlement obligation nondischargeable, the circumstances of the transaction are sufficiently attenuated from an arm's length transaction to be a relevant factor under the totality of the circumstances.

The totality of the circumstances establishes the following: 1) neither party lives an extravagant lifestyle; 2) Mr. Hall earns an income that is modestly higher than Debtor's; 3) Mr. Hall lives on his own; 4) Debtor lives with her parents and has presented no evidence of extraordinary expenses; 5) Debtor will receive nearly \$45,000 from the sale of her home; 6) Debtor transferred a business that Mr. Hall had previously expressed an interest in purchasing and that the divorce court valued at \$75,000 to her sister and brother-in-law for little or no consideration without first contacting Mr. Hall to ask whether he would be interested in purchasing the business; and 7) Debtor failed to collect on a \$42,000 note against her father that the business held. Given these circumstances, Debtor has failed to carry her burden of showing to the Court that she would enjoy a benefit greater than Mr. Hall's detriment if she discharged this debt.

CONCLUSION

The burden of proof under §523(a)(15) is properly shifted to Debtor because the obligation is a property settlement obligation incurred as the result of a dissolution proceeding. Debtor has failed to satisfy her burden under §523(a)(15)(A) by failing to demonstrate an inability to pay the debt. Debtor has similarly failed to carry her burden under §523(a)(15)(B) by failing to demonstrate that under the totality of the circumstances, her burden in not discharging her obligation to Mr. Hall is greater than Mr. Hall's burden would be if such debt were discharged. Therefore, Debtor's property settlement obligation to Mr. Hall is nondischargeable pursuant to 11 U.S.C. §523(a)(15).

WHEREFORE, for all the reasons set forth herein, the obligation owing to George Bradley Hall by Suzanne Louise Hall arising out of the parties' dissolution, and relating to ownership of the business known as "Annie's Maid Rite" is nondischargeable pursuant to 11 U.S.C. §523(a)(15).

FURTHER, judgment shall enter accordingly.

SO ORDERED this 16th day of September, 1999.

Paul J. Kilburg
Chief Bankruptcy Judge

1. Compare Hill, 184 B.R. at 756 (discharging property settlement, despite the recognition that such discharge would likely force the non-debtor spouse into a Chapter 7 filing herself, where the debtor's inability to pay the property settlement was due to a modest income level that was beyond his control and where the debtor did not have any extravagant expenses); with Gamble, 143 F.3d at 225-6 (refusing to discharge a debtor's property settlement obligation, despite non-debtor spouse's net worth of nearly \$500,000, where the debtor had more education and a slightly higher income than the non-debtor spouse and where the debtor had "manipulated his finances" by paying an alleged \$100,000 dischargeable debt to his father and by concealing his new spouse's contributions to the household income); and Molino, 225 B.R. at 909 (specifically listing good faith as a relevant factor under the §523(a)(15)(B) analysis and refusing to discharge a property settlement obligation where the debtor's lack of income was due to his voluntary decision not to work for pay but instead to volunteer his services at a local bar).