

**UNITED STATES BANKRUPTCY COURT
For the Southern District of Iowa**

In re:	:	Case No. 02-06762-rjh-7
MICHAEL JAMES GALE and	:	
CYNTHIA DENISE GALE,	:	
	:	
Debtors.	:	Chapter 7
	:	

**ORDER—TRUSTEE'S MOTION TO DISMISS CASE
AND OBJECTION THERETO**

On June 4, 2003, the court held a hearing on the United States Trustee's Motion to Dismiss Case and Debtor's objection thereto. Attorney Jerrold Wanek represented Debtors Michael J. Gale and Cynthia D. Gale. Assistant United States Trustee James L. Snyder represented the United States Trustee, Habbo Fokkena. At the conclusion of the hearing, the court took the matter under advisement. The court considers the matter fully submitted.

The court has jurisdiction of these matters pursuant to 28 U.S.C. §§ 157(b)(1) & 1334 and order of the United States District Court for the Southern District of Iowa pursuant to 28 U.S.C. § 157(a). This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A) and (O). Upon review of the pleadings, evidence, and arguments of counsel, the court now enters its findings and conclusions pursuant to Fed. R. Bankr. P. 9014 and 7052.

FINDINGS OF FACT

1. Michael J. Gale and Cynthia D. Gale (hereinafter collectively, Debtors) filed a joint voluntary petition for chapter 7 bankruptcy relief on December 12, 2002.

2. Debtors scheduled five secured creditors holding claims amounting to \$271,871.85. GMAC has a claim for \$9,000.00 secured by a 2000 Saturn SL2, which Debtors valued at \$6,5000.00. GMAC has a claim for \$24,000.00 secured by a 2000 Chevy Silverado valued at \$17,000.00. Home Eq has a claim for \$34,700.00 secured by a second lien on Debtors' home valued at \$236,900.00. Homeside Lending has a claim for \$187,810.53 secured by a first lien on Debtors' home. Premier Credit has a claim for \$16,361.32 secured by a 1999 GMC Jimmy valued at \$10,000.00.

3. Debtors scheduled thirty-one creditors holding \$49,910.20 in unsecured claims. Of the unsecured claims, none were identified as business debt. Debtors indicated that they had no creditors holding unsecured priority claims.

4. Debtors' scheduled claims are primarily consumer in nature.

5. Debtors scheduled four dependants. Their ages are 10, 11, 13, and 22 years.

6. Michael Gale has been employed as a teacher by the Des Moines Public School System for eighteen years. He scheduled gross monthly income of \$3,575.38 or approximately \$42,904.56 yearly; a support payment of \$2,300.00; deductions of \$1,023.53 and \$166.10 for payroll taxes and social security and for Des Moines Teacher Retirement plan respectively, giving him a monthly income of \$4,685.75.

7. Cynthia Gale scheduled gross monthly income of \$2,656.37 for a yearly amount of approximately \$31,876.00. From this amount, \$520.66 is withheld for payroll taxes and social security, leaving net monthly take home pay of \$1,650.20.

8. Debtors scheduled total combined monthly income of \$6,335.96.

9. Debtors supplied wage statements upon request by the United States Trustee (hereinafter UST). From Michael's statement, UST calculated his gross annual income

from employment as \$50,939.35. This amount included income from teaching, coaching, and a teacher compensation program. UST calculated Michael's gross monthly income to be \$4,244.95, and after deductions for taxes, social security, Medicare, retirement, and union dues, his net monthly income to be \$3,092.44. Michael's gross monthly income will drop by \$250.00 in the near future because of reduced coaching opportunities.

10. Based on her wage statement, UST calculated Cynthia's gross annual income to be \$28,649.92 and her monthly gross income to be \$2,387.49. Deductions for taxes, social security, and Medicaid left her with a monthly net income of \$1,975.18. Cynthia has changed employers since filing for bankruptcy protection; however, no evidence was offered to show that her income has changed significantly.

11. Debtors raise and care for three adopted children. The children have special needs and qualify for state assistance. Debtors receive \$11,200.00 annually for each child to assist in their support. Accordingly, Debtors receive additional income of \$33,600.00 per year, or \$2,800.00 per month.

12. UST calculates Debtors' combined net monthly income as \$7,868.00. UST acknowledges that this amount will decline somewhat based on Michael's decreased coaching compensation.

13. Debtors' Schedule J, Current Expenditures of Individual Debtors, lists the following monthly expenses:

Home mortgage payment.....	\$1854.00
Second mortgage payment.....	434.00
Property taxes.....	440.00
Homeowner's or renter's insurance.....	68.00
Home maintenance.....	100.00
Electricity and heating fuel.....	213.00
Water and sewer.....	99.00
Telephone.....	150.00

Cellular phones	120.00
Cable television.....	100.00
Food	600.00
Clothing.....	200.00
Laundry and dry cleaning	60.00
Medical and dental expenses	150.00
Transportation (not including car payments).....	160.00
Recreation	200.00
Charitable contributions.....	40.00
Life insurance.....	40.00
Auto insurance	213.00
Auto installment payment	588.00
Second auto installment payment	705.50
Parent Plus College Loan.....	107.64
Overdraft charges.....	50.00
<u>Miscellaneous expenses</u>	<u>50.00</u>
Total monthly expenses	\$6,742.14

12. Direct expenses for Debtors' home, including two mortgage payments, property taxes, and homeowners insurance, total \$2,728.00. These expenses were included in Debtors' mortgage payments. Debtors have not made the mortgage payments since October 2002, and they are surrendering their home. Cynthia has been actively searching for alternative housing, and she testified that the cost would be between \$1,500.00 and \$1,700.00 per month. At the time of the hearing, Debtors had not obtained replacement housing.

13. Debtors incur expenses for service for four telephones. They have two lines going into their home, and two cellular phones with identical service plans. Debtors originally obtained one line for use by their adult daughter and son-in-law. Debtors retained the line to give them telephone access while the other line was used for Internet access. The children access the Internet for school projects.

DISCUSSION

UST filed a motion to dismiss Debtors' bankruptcy case pursuant to 11 U.S.C. §707(b) and contends that allowing Debtors to proceed under chapter 7 would result in a substantial abuse of the provisions of the chapter. UST argues that Debtor has sufficient disposable income to repay their unsecured consumer debt. In the motion, UST claims Debtors have understated their income and overstated their expenses. UST proposes adjustments to their calculations and stated expense. Using the adjusted figures UST argues that Debtors could generate monthly disposable income of \$3,903 for a total of \$140,508.00 of disposable income over the course of a 36-month hypothetical chapter 13 plan. Such sum represents 281.52% of their total unsecured debt.

Debtors dispute UST's conclusions and calculations. They contend that the scheduled expenses filed with the court are accurate and reasonable. They argue that raising three special needs children necessitate additional expenses and that the support payments are used to pay for those additional expenses. Therefore, any disposable income calculation by UST is illusory. Debtors argue that their disposable income is minimal and granting them relief under chapter 7 would not be an abuse of its provisions.

Section 707(b) was enacted in 1984 in response to Congress's perception that an increasing number of unneedy debtors were using chapter 7 to escape paying consumer debts. In re Walton, 866 F.2d 981, 982-83 (8th Cir. 1989). After amendments in 1986 and 1998, § 707(b) now provides:

(b) After notice and a hearing, 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 this chapter whose debts are primarily consumer debts if it finds that the granting of relief would be a substantial abuse of the provisions of this chapter. There shall be a presumption in favor of granting the relief

requested by the debtor. In making a determination whether to dismiss a case under this section, the court may not take into consideration whether a debtor has made, or continues to make, charitable contributions (that meet the definition of "charitable contribution" under section 548(d)(3)) to any qualified religious or charitable entity or organization (as that term is defined in section 548(d)(4)).

11 U.S.C. § 707(b) (2001).

In order to prevail on a motion to dismiss, UST must show that Debtors' debts are primarily consumer in nature, and that granting chapter 7 relief would result in substantial abuse of the provisions of the chapter. In re Praleikas, 248 B.R. 140, 143 (Bankr. W.D. Mo. 2000).

The Bankruptcy Code does not define "substantial abuse." In interpreting the term, the Eighth Circuit holds that the essential inquiry is "whether the debtor's ability to repay creditors with future income is sufficient to make the Chapter 7 liquidating bankruptcy a substantial abuse of the Code." Fonder v. United States, 974 F.2d 996, 999 (8th Cir. 1992). See also U.S. Trustee v. Harris, 960 F.2d 74, 77 (8th Cir. 1992); In re Walton, 866 F.2d at 984-85. While the Circuit Court does not adopt a wide ranging "totality of the circumstances test," Harris, 960 F.2d at 77, the court may consider a variety of factors. See In re Walton, 866 F.2d at 983- 85 (courts not foreclosed *inter alia* from considering future income and inability to pay alone might not shield a debtor from dismissal under § 707(b)); see also In re Woodward, 265 B.R. 179, 187-88 (Bankr. S.D. Iowa 2001) (courts may consider additional relevant factors to determine that § 707(b) dismissal is proper). However, a debtors' ability to fund a chapter 13 plan is the primary factor to be considered. In re Walton, 866 F.2d at 985 (citing with approval the Ninth Circuit's analysis in Zolg v. Kelly (In re Kelly)), 841 F.2d 908, 914-15 (9th Cir. 1988).

The ability to fund a chapter 13 plan is determined by a calculation of the debtors' disposable income. Stuart v. Koch (In re Koch), 109 F.3d 1285, 1289 (8th Cir. 1997). "Disposable income" is defined as income not reasonably necessary for the support of the debtor, the debtor's dependents, or the debtor's business. Id. citing 11 U.S.C. § 1325(b)(2).

In this case, Debtors do not dispute UST's assertion that their debts are primarily consumer debts. A review of their schedules shows various unsecured claims identified as credit card debt, but none of the secured or unsecured claims are identified as business debt. No evidence was introduced at the hearing to indicate that any of the debts listed in the schedules were acquired for the purpose of obtaining a profit. Accordingly, the court finds that UST has met this element as required by § 707(b).

For purposes of a § 707(b), the ability to maintain a hypothetical chapter 13 plan is measured by evaluating the debtor's financial condition. In re Koch, 109 F.3d at 1288. "The essential inquiry is whether the debtor's ability to repay creditors with future income is sufficient to make the [c]hapter 7 liquidating bankruptcy a substantial abuse of the Code." Fonder v. United States, 974 F.2d 996, 999 (8th Cir. 1992).

At the outset, the court finds that Debtors' calculation of income is at best inaccurate and at worst is a blatant attempt to mislead the trustee, UST, and the court. Debtors scheduled Michael's monthly gross income as \$3,575.38. Multiplying this number by twelve months yields a yearly income of just over \$42,904.56. However, Michael's wage statement of December 20, 2002 (Exh. D), shows year to date compensation of \$50,939.35. Debtors' statement of financial affairs shows his income from teaching and coaching to be \$52,000.00 for the year 2002. Debtors filed their schedules on December 12, 2002, so this is not a case of extrapolating from incomplete information. Debtors had year to date income

information for at least eleven months. Further, their statement of financial affairs shows Adoption Subsidy Payments of \$33,600.00 each year for the years 2000-2002. Debtors scheduled this income as \$2,300.00 per month, however, \$33,600.00 divided by twelve months yields \$2,800.00 per month. Debtors offered no credible explanation for these discrepancies in their calculations.

UST's calculations of income are based on wage statement provided by Debtors. The court finds these calculations to be accurate and will base its disposable income analysis on UST's income figures. Accordingly, the court finds that Michael's net monthly take home pay is \$3,092.00 (numbers rounded to the next lowest whole dollar), and Cynthia's net take home pay is \$1,975.00. Together they take home \$5,067.00 per month from their jobs.

Debtors argue that the adoption subsidy should not be included in their disposable income. They argue that the money is provided for the support of their special needs children. They contend that expenses for their additional needs consume the subsidy payment making it "a wash." The court disagrees.

Debtors have cited no authority for excluding the subsidy from the disposable income analysis, nor have they cited authority providing that the subsidy is exempt property. Regardless, even exempt property can be included in a disposable income analysis. See e.g. Taylor v. United States (In re Taylor), 212 F.3d 395 (8th Cir. 2000) (holding that the fact that income from a pension fund is exempt does not preclude including it in a disposable income analysis).

The subsidy is intended to provide for the children's support. Support necessarily includes food, shelter, and clothing. To the extent that the subsidy funds are used for

these basic expenses, Debtors' income from other sources is available to pay unsecured creditors. Accordingly, the subsidy payment should be included in the disposable income analysis, and Debtors combined net monthly income is \$7,867.00 ($\$5,067.00 + \$2,800.00 = \$7,867.00$).

Debtors scheduled monthly expenditures of \$6,743.00 (rounded up to the next dollar). UST argues that Debtors have overstated their expenses and suggests adjustments. However, taking Debtors expenses as scheduled leaves them with monthly disposable income of \$1,124.00. Over the course of a three-year chapter 13 plan, they would contribute \$40,464.00 ($1124 \times 36 = 40,464.00$). Said amount represents approximately 81% of their unsecured debt before administration fees. Over five years, Debtors could contribute \$67,440.00 or 135% of their unsecured debt before administration fees. Accordingly, even without considering UST's adjustments, the court finds that Debtors have the means to fund a chapter 13 plan.

In considering Debtors' scheduled expenses, UST points out that Debtors have not made mortgage payments since October 2002, and they intend to surrender their home. Therefore, their actual monthly expenses have been reduced by \$2,728.00. Cynthia testified that she had been searching for suitable rental housing in the \$1,200.00 to \$1,700.00. Using the upper end as a reasonable expense reduces Debtors' monthly housing costs by \$1,028.00.

UST also suggests that Debtors' monthly food expense is low for a family of five. He would budget an additional \$400.00. UST would accept at face value Debtors' contention that Michael's gross income will decline by \$250.00 per month due to less income from coaching. Using the above adjustments, Debtors' monthly income would be

\$7,617.00 ($\$7,867.00 - \$250.00 = \$7,617.00$, said calculation credits the entire \$250.00 to net income without considering tax), their monthly expenses would be ($\$6,743.00 - \$1,028.00 + \$400.00 = \$6,115.00$), and their monthly disposable income would be \$1,502.00. In a hypothetical chapter 13, Debtors could contribute \$54,072.00 over three years or 108% of their unsecured debt before administrative expenses.

Further, the court agrees with UST that other expenses are unreasonable or unreasonable in amount. Such expenses include the two telephone lines, two identical cellular phone packages, the overdraft expense, and the vehicle expense. However, as UST has demonstrated, Debtors have the ability to fund a 100% plan without reducing these expenses. Therefore, the court will not address the proposed adjustments in further detail.

Finally, UST urges the court to adopt the Department of Labor's "Consumer Expenditures in 2001" separately or in combination with "Issues in Labor Statistics – Spending Patterns of High-income Households" to establish what he terms an objective standard to be used in the determination of the reasonableness of expenses. Essentially, UST is asking for a bright line test under which any expenses scheduled by debtors that exceed the published average would be per se unreasonable. The court declines to establish such a test.

The court appreciates the difficulty under which UST must make determinations of whether to bring motions to dismiss based on substantial abuse. The court likewise appreciates the detailed analysis which UST provides concerning income and expenses, and gives due weight to his proposals and conclusions. It is also willing to receive the above-mentioned publications as evidence of national averages.

However, the court is reluctant to establish such a test based on averages. A finding of substantial abuse is a determination not to be made lightly, and each debtor's case presents unique factors to be considered. What is a reasonable expense or amount in one case may be unreasonable in another. The averages that UST proposes the court to use in establishing a test are just that, averages. By definition, the numbers are calculated from a range, some greater and some lesser. However, there is no basis for determining that some and not others are reasonable amounts.

The court acknowledges that it has determined reasonable amounts for certain expenses. For instance, a general determination of food expenses per person. However, in those cases, Debtors did not present credible evidence of their food expense; generally, they testified that their scheduled amount was an approximation or a best guess as to how much they spent. Nothing prevents debtors from establishing actual expenses through documentation.

In short, the court is unwilling to limit its discretion in making factual determinations of reasonableness. It is particularly unwilling to substitute published averages, which are dated by months and sometimes years, for hard evidence and its own judgment. The court encourages UST to continue his practice of submitting analysis and support of his conclusions, but the court declines to adopt his proposed standard.

In conclusion, the court finds that UST has sufficiently demonstrated that Debtors have the means to fund a chapter 13 plan. Accordingly, UST has overcome the statutory presumption for granting the requested relief. Allowing Debtors to proceed with their chapter 7 case will result in a substantial abuse of the provisions of this chapter. UST's motion to dismiss will be granted. However, the court will stay the execution of its order for

fifteen days to provide the Debtors with the opportunity to convert their case if they so choose.

ORDER

IT IS ACCORDINGLY ORDERED as follows:

- 1) The United States Trustee's Motion to Dismiss is SUSTAINED.
- 2) Debtors Michael J. Gale and Cynthia D. Gale's chapter 7 case is DISMISSED pursuant 11 U.S.C. §707(b).
- 3) The execution of this order is hereby stayed for fifteen (15) days from the date of its entry to permit Debtors to take such actions as required to convert their case to another chapter, should they so choose.
- 4) Failure on the part of Debtors to take affirmative action within said fifteen (15) day period of time will cause the order dismissing the case to be entered without further notice and hearing.

Date: _____

RUSSELL J. HILL
U.S. BANKRUPTCY JUDGE