UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
WESTERN DIVISION

In Re:	)	Case No. 04-34999
	)	
Keith Alan Verhoff	)	Chapter 7
Linda Sue Verhoff,	)	
	)	
Debtors.	)	JUDGE MARY ANN WHIPPLE

MEMORANDUM OF DECISION AND ORDER
REGARDING MOTION TO DISMISS

This case came before the court for hearing on the United States Trustee's ("UST") Motion to Dismiss [Doc. # 18] and Debtors' opposition [Doc. # 21]. The UST moves to dismiss Debtors' Chapter 7 case for substantial abuse pursuant to 11 U.S.C. § 707(b). He argues that Debtors have sufficient disposable income to fund a Chapter 13 plan and pay a significant portion of their unsecured debt.

The court has jurisdiction over this case pursuant to 28 U.S.C. §1334 and the general order of reference entered in this district. Proceedings to determine the dismissal of a case under § 707(b) are core proceedings that the court may hear and decide. 28 U.S.C. § 157(b)(1) and (b)(2)(A). Regardless of whether or not specifically referred to in this decision, the court has examined the submitted materials, weighed the credibility of the witnesses, considered all of the evidence, and reviewed the entire record of the case. Based upon that review, and for the following reasons, the UST's motion will be granted.

FACTUAL BACKGROUND

Debtors filed their Chapter 7 petition on June 15 2004. They are married and have three children, ages 12, 14, and 16 years. Debtor Keith Verhoff is 46 years old and is employed as a road construction equipment mechanic. Although he has worked for his current employer for only one year, he had worked for its predecessor company for the previous 16 years. There is no evidence to suggest that his current employment is anything but stable. Debtors' original Schedule I indicates that he earns monthly gross income of $5,913.74, which includes overtime pay of $1,675.44, and monthly net income of $3,704.48. However, Schedule I indicates that overtime hours are eliminated after the summer months. Keith Verhoff testified that, although he earned over $24,000 in overtime pay in

2004, he was the only mechanic on staff during that time period. Nine additional mechanics have since been hired and he anticipates only seasonal overtime being available. He testified that traditionally he earns approximately $8000 per year in overtime pay, which results in approximately $5,760 in additional take home pay per year.[1]

He also testified that his weekly pay varies depending on the amount of time worked that is designated as "road time" for which he is paid an additional $6.77 per hour. Debtors' exhibits 4 and 6, consisting of pay stubs setting forth his earnings for the weekly pay periods ending December 25, 2004, and January 22, 2005, respectively, both of which include only forty hours of pay, differ by approximately $91 in gross pay and $52 in net pay as a result of "road time" pay. He testified, however, that his net pay of $565 on January 22, 2005, will be one of his smallest paychecks for the year. Keith Verhoff further testified that he and his wife have received income tax refunds in the years 2003 and 2004 in the amount of approximately $2,200 and he expects a similar refund in 2005.

Debtor Linda Verhoff has worked at Blanchard Valley Hospital in Findlay, Ohio, for 10 years, with her current position coding coordinator. There is no evidence that her employment is not stable. She testified that Schedule I correctly reflects her gross monthly income of $3,645.83, and net monthly income of $2,107.23. She is paid twice a month. In addition to withholding taxes, her payroll deductions include contributions to her 401k plan of $76.92 per month and a flexible medical account of $208 per month, as well as deductions for life insurance and family health, vision, and dental insurance. Debtors' combined monthly net income, as set forth on Schedule I, and before any adjustments, equals $5,811.71.

Debtors' Schedule J indicates that their monthly expenses total $4,771.64. But at the hearing on the motion, Debtors acknowledged that this total should be reduced as a result of certain expenses being inadvertently double counted. Specifically, $115 designated as an expense for real estate taxes is also included in their home mortgage payment and $312 designated as an expense for health insurance is already deducted from Linda Verhoff's income on Schedule I. In addition, the court finds that an additional reduction of $100 with respect to medical and dental expenses is appropriate. Debtors list such expenses as averaging $420. But the check register report for the account from which all expenses are paid indicates

[1] Keith Verhoff's pay stubs indicate that withholding taxes represent approximately 28% of his earnings. Debtors' Exs. 4, 6. Thus, his anticipated overtime take home pay for the year is $5,760 ($8,000 x .72 = $5,760).

that their medical and dental expenses average only $320 per

month. (Debtors' Ex. 7, p. 12-13).

Keith Verhoff also testified that, after reviewing their summary check register report, he realized that certain expenses were under-reported on their Schedule J. Specifically, he testified that their house payment increased by $17 and their car insurance increased by $57 as a result of one daughter getting her driver's license. In addition, he testified that transportation expenses actually averaged $462 per month rather than $285 as originally indicated, expenses for recreation, clubs and entertainment, newspapers, and magazines averaged $220 rather than $120, and expenses for the children's school fees, lunches and activities averaged $460 per month rather than $300. Debtors' check register report, however, does not support the $160 increase in expense for the children's school fees, lunches and activities but instead indicates that such expenses average approximately $300 as originally indicated on their Schedule J. With these modifications to Debtors' scheduled expenses, their monthly expenses total $4,595.

Debtors own no non-exempt assets. They are current on the mortgage payments on their home, which is valued at $144,000 and is subject to first and second mortgages totaling approximately $131,099. Debtors stipulated, and their schedules indicate, that their debts are primarily consumer debts. Their unsecured nonpriority debts total $81,029, almost all of which consists of credit card debt. No major medical expenses, unemployment, or other unexpected financial crisis precipitated their bankruptcy filing. Rather, the fact that several creditors filed lawsuits against them, notwithstanding the fact that they had sought the assistance of a credit management company to negotiate with these creditors, was the precipitating factor in filing their Chapter 7 petition.

LAW AND ANALYSIS

Section 707(b) provides as follows:

> After notice and a hearing, the court, on its own motion or on a motion by the United States trustee, . . . 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.

11 U.S.C. § 707(b). Viewed in light of the court's ability to raise the substantial abuse issue sua sponte, it appears that the presumption in favor of granting relief under Chapter 7 is something other than simply a

rule regarding the burden of production and burden of proof. *In re Kelly*, 841 F.2d 908, 917 (9th Cir. 1988). It is "in reality a caution and a reminder to the bankruptcy court that the Code

and Congress favor the granting of bankruptcy relief, and that accordingly 'the court should give the benefit of any doubt to the debtor and dismiss a case only when a substantial abuse is clearly present.'" *Id.* (citation omitted); 4 Alan N. Resnick, et al., *Collier on Bankruptcy* ¶ 15th ed. 2003); *see also In re Krohn*, 886 F.2d 123, 128 (6th Cir. 1989) (referring to the presumption found in § 707(b) as a "statutory preference" in favor of granting relief).

Debtors have stipulated that their debts consist primarily, if not entirely, of consumer debts. Thus, the first prerequisite for dismissal under § 707(b) has been satisfied. The second prerequisite requires a finding that the granting of relief under Chapter 7 would be a substantial abuse.

The Bankruptcy Code does not define "substantial abuse." Instead, its meaning was left to be determined by the courts. The amendment that added subsection (b) to § 707 was enacted in 1984 in response to an increasing number of bankruptcies being filed by people perceived to be non-needy debtors. *Krohn*, 886 F.2d at 126 (quoting S. Rep. No. 65, 98th Cong., 1st Sess. 53, 54 (1983)). The legislative history indicates that the amendment "was intended to uphold 'creditors' interests in obtaining repayment where such payment would not be a burden." *In re Laury-Norvell*, 157 B.R. 14, 16 (Bankr. N.D. Ohio 1993) (quoting S. Rep. No. 65, 98th Cong., 1st Sess. 53, 54 (1983)). While courts that have addressed the issue have developed various formulations for analyzing whether the filing of a debtor's petition rises to the level of "substantial abuse," *see In re Attanasio*, 218 B.R. 180 (Bankr. N.D. Ala. 1998) (providing an exhaustive discussion of the various standards employed), this court is bound by the approach set forth by the Sixth Circuit in *Krohn*.

In *Krohn*, the court held that "substantial abuse can be predicated upon either lack of honesty or want of need." *Id.* at 126. The court set forth a totality of the circumstances test to determine whether the debtor is "merely seeking an advantage over his creditors, or instead is 'honest,' in the sense that his relationship with his creditors has been marked by essentially honorable and undeceptive dealings, and whether he is 'needy' in the sense that his financial predicament warrants the discharge of his debts in exchange for liquidation of his assets." *Id.* The UST does not allege that Debtors lacked honesty in their relationships with their creditors. Indeed, Debtors tried to work with their creditors through a credit

counseling entity that Mr. Verhoff found on the internet, and were essentially ripped off to the tune of more than $3,000.

The UST asserts instead that Debtors are not "needy" such that discharge of their debts is warranted. One of the primary factors to be considered when determining whether a debtor is needy "is his ability to repay his debts out of future earnings." *Id.* Indeed, "that factor alone may be

sufficient to warrant dismissal for substantial abuse." *Id.* The Sixth Circuit explained that "a court would not be justified in concluding that a debtor is needy and worthy of discharge, where his disposable income permits liquidation of his consumer debts with relative ease." *Id.* Other factors to be considered include "whether the debtor enjoys a stable source of income, whether he is eligible for adjustment of his debts through Chapter 13 of the Bankruptcy Code, whether there are state remedies with the potential to ease his financial predicament, the degree of relief obtainable through private negotiations, and whether his expenses can be reduced significantly without depriving him of adequate food, clothing, shelter and other necessities." *Id.* at 126-27.

In order to determine whether a debtor has the ability to pay, courts often evaluate whether the debtor has sufficient disposable income to fund a Chapter 13 plan. *Behlke v. Eisen (In re Behlke)*, 358 F.3d 429, 435 (6th Cir. 2004). "Disposable income" is defined as "income which is received by the debtor and which is not reasonably necessary to be expended . . . for the maintenance or support of the debtor or a dependent of the debtor. . . ." 11 U.S.C. § 1325(b)(2).

In this case, Debtors' original Schedules I and J, without making the modifications discussed above, show a positive balance of approximately $1,000 after their listed monthly expenses are paid. If this amount were applied monthly to payment of their debt of $81,029 over three years, Debtors would be able to repay slightly over 44 percent of their unsecured debt. If applied over a five-year period, they could repay approximately 74 percent of their unsecured debt.

Debtors contend, however, that certain adjustments to their originally listed income and expenses are required. The UST cites *In re Pier*, 310 B.R. 347 (Bankr. N.D. Ohio 2004), for the proposition that Debtors are bound by the information provided in their Schedules I and J and may not now attempt to amend those schedules. While *Pier* holds that debtors cannot "purge themselves of prior misconduct by simply amending their bankruptcy petition," it recognizes that bankruptcy schedules may be amended when

mistakes or omissions contained therein are made inadvertently. *Id.* at 357-58. One consideration in determining whether the mistake or omission was inadvertent is whether the debtor had a motive to provide the misinformation. *Id.* In this case, Debtors had no motive to over-estimate their monthly income while under-estimating their expenses and the UST alleges no misconduct that they might be attempting to correct.

Nevertheless, even a conservative estimate of Debtors' income and the fairly generous estimate of expenses results in considerable disposable income with which Debtors could repay a significant and meaningful portion of their debt. Keith Verhoff testified that his weekly net pay of

$565 on January 22, 2005, which includes no overtime pay, represents one of his smallest paychecks he expects for the year. This amount translates into monthly take-home pay of approximately $2,448. Although Linda Verhoff reports monthly take-home pay of $2,107 on Schedule I, that amount reflects a payroll deduction of $76 as her contribution to her 401k plan. That expenditure is not necessary for the maintenance or support of Debtors or their dependents. *See Behlke*, 358 F.3d at 435-36 (applying in the context of a § 707(b) motion the reasoning in *Harshbarger v. Pees (In re Harshbarger),* 66 F.3d 775 (6th Cir. 1995), that it would be unfair to creditors to allow debtors "to commit part of their earnings to the payment of their own retirement fund while at the same time paying their creditors less than a 100% dividend."). In addition, her payroll deductions include $104 to her flexible medical account. This amount is used to pay with pre-tax dollars for the medical expenses, at least in part, that are listed as expenses on Schedule J, resulting in the expense being double-counted also as a deduction from her pay. As she is paid twice per month, Linda Verhoff's monthly net pay, after being adjusted for the flexible medical account and 401k contribution, is $2,467.

Debtors' combined monthly net pay, with no overtime included, totals $4,915. Their monthly expenses, modified as set forth in this opinion, total $4,595, providing them with disposable income of $320 per month. This amount, however, includes neither overtime nor anticipated tax refunds. Although the court accepts Keith Verhoff's testimony that his overtime will be significantly reduced in the future, he still expects to earn approximately $8,000 per year in overtime pay, providing an additional after tax income of approximately $5,760. Debtors have also received yearly income tax refunds of approximately $2,200 in 2003 and 2004 and anticipate receiving a similar refund in 2005. There being no indication that Debtors have otherwise adjusted their tax withholdings, and considering the ages of their three dependent children,

the court finds similar refunds may be anticipated over the next several years. Thus, Debtors' tax refunds, together with Keith Verhoff's overtime pay, will provide an additional $7,960 per year. If this amount, together with their monthly disposable income of $320 is applied to payment of their unsecured debt of $81,029 over a period of three years, creditors will receive $35,400 or approximately a 43 percent dividend. If those amounts are applied to payment of their debt over a period of five years, creditors will receive $59,000 or nearly 72 percent of the amount they are owed.

In determining whether granting relief to Debtors would be a substantial abuse of Chapter 7 in light of their ability to repay such a significant portion of their debt, the court also considers the

fact that Debtors appear to enjoy stable employment. Linda Verhoff has been employed at her present job for ten years and, although her husband has worked for his present employer for only one year, he is a skilled mechanic who was employed by its predecessor for the previous sixteen years. There is no evidence that Debtors are in danger of losing their jobs. In addition, Debtors are eligible for adjustment of their debts under Chapter 13 of the Bankruptcy Code. Both of these factors weigh against Debtors being granted relief under Chapter 7.

Finally, the court considers the fact that Debtors not only can reduce their expenses beyond the few adjustments discussed earlier in this opinion, but are also likely to receive income greater than the conservative calculation set forth above. With respect to additional income, the court's calculation does not include additional pay Keith Verhoff sometimes receives for "road time." Linda Verhoff also received a $2,000 gross raise from 2003 to 2004. With respect to expenses, Debtors' total life insurance expense appears excessive. The parents' potential death and loss of income with which to support the children can justifiably be insured against for the benefit of their children should tragedy occur. But Linda Verhoff also testified that they make elective premium payments on life insurance policies for the children, who have no income to insure or replace.

The court also finds Debtors' entertainment expense of $220 and the expense for their children's lunches and activities of $300 per month, according to their summary check register, and $460 per month according to Keith Verhoff's testimony, to be excessive in light of the debt they owe their creditors. It is undeniably difficult to say no to children. And the Verhoffs obviously permit their children to engage in a brimming slate of extra-curricular activities. But the Sixth Circuit has shown in *Krohn,* 886 F.2d at 128

(noting the option of "good, old fashioned belt tightening"), and more recently in *Behlke* that it clearly expects that debtors must sometimes make difficult financial and lifestyle choices when faced with unpaid creditors who have financed them in the past.

On these facts, the court finds that Debtors can make significant repayment of their debt without depriving them or their dependents of adequate food, clothing, shelter and other necessities.
While "there is no 'cutoff' or bright-line test under which an ability to pay a certain percentage over a three-to-five year period would or would not be substantial abuse regardless of other circumstances," *Behlke*, 358 F.3d at 438, having considered the totality of the circumstances, the court finds that any presumption in favor of granting relief is overcome and concludes that granting Debtors a discharge in this case would be a substantial abuse of the provisions of Chapter 7.

THEREFORE, for the foregoing reasons, good cause appearing,

IT IS ORDERED that the United States Trustee's motion be, and hereby is, **GRANTED**. Debtors are granted thirty (30) days from the date of this order to file a motion to convert to a Chapter 13 case or the case will be dismissed.

Mary Ann Whipple
United States Bankruptcy Judge

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