

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO

IN RE: *
*
ROBERT L. ADAMSON - and - * CASE NUMBER 01-42110
*
JENNIFER L. ADAMSON, * CHAPTER 13
*
Debtors. * HONORABLE KAY WOODS
*

ORDER OVERRULING MOTION TO MODIFY
DEBTORS' CONFIRMED CHAPTER 13 PLAN

On May 5, 2005, this Court held a hearing on the Motion to Modify Debtors' Confirmed Chapter 13 Plan filed by the United States of America (the "Motion to Modify Plan"), on behalf of its agency, the Internal Revenue Service (the "IRS"). Debtors Robert L. Adamson and Jennifer L. Adamson (the "Debtors"), through counsel, filed an Objection to Motion to Modify Debtors' Confirmed Chapter 13 Plan (the "Debtors' Objection"). Also before the Court is United States' Response to Debtors' Objection to Motion to Modify Debtors' Confirmed Chapter 13 Plan (the "IRS Response"). The Standing Chapter 13 Trustee filed a response listing all timely filed claims, including claimants' name, amount as filed, amount distributed to date on each claim and the balance to be paid if the claims were paid at one hundred percent (100%). The Standing Chapter 13 Trustee concludes that, if the Motion to Modify Plan were granted, an additional Seven Thousand Two Hundred Seventy-Five and 77/100 Dollars (\$7,275.77) would be due and owing to the plan.

This Court has jurisdiction over this matter pursuant to

28 U.S.C. § 1334. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A) and (L). The following constitutes the Court's findings of fact and conclusions of law pursuant to FED. R. BANKR. P. 7052.

BACKGROUND

Debtors filed a voluntary petition for Chapter 13 on May 22, 2001. On that same date, they filed a Chapter 13 plan. On July 11, 2001, the IRS filed an Objection to Confirmation of Debtors' Chapter 13 Plan, which objection was withdrawn on July 8, 2002. The Order Confirming Chapter 13 Plan was entered on July 16, 2002. Debtors amended their Summary of Schedules and Schedule F on September 22, 2003. Subsequently, on October 22, 2003, an Order Providing for Increased Payment and Extending the Term of the Plan was entered, which provided for an increase in the monthly payment from One Hundred Thirty-One Dollars (\$131.00) to Two Hundred Fifty Dollars (\$250.00) and an increase in the plan term from forty-eight (48) months to sixty (60) months.

On February 17, 2005, the IRS filed a Motion for Relief from Stay to setoff tax overpayment. This motion requested authority to setoff a tax overpayment (refund) for the year 1999 in the amount of One Thousand Five Hundred Twenty-Six Dollars (\$1,526.00) against the IRS claim. An order granting that unopposed motion was entered on March 22, 2005. On April 5, 2005, the IRS filed the Motion to Modify Plan, which is presently before

the Court.

THE MOTION TO MODIFY PLAN

The IRS brings this motion pursuant to 11 U.S.C. § 1329(a), which provides: "At any time after confirmation of the plan but before the completion of payments under such plan, the plan may be modified, upon request of the debtor, the trustee, or the holder of an allowed unsecured claim"

Debtors filed their 2001, 2002 and 2003 income tax returns claiming refunds in the amounts of Three Thousand Six Hundred Eighty Dollars (\$3,680.00), One Thousand Nine Hundred Forty-Eight Dollars (\$1,948.00) and Five Thousand One Hundred Twenty-Six Dollars (\$5,126.00), respectively (collectively, the "Tax Refunds"). The IRS argues that the Tax Refunds qualify as disposable income, pursuant to § 1325 of the Bankruptcy Code, and cites *Freeman v. Schulman (In re Freeman)*, 86 F.3d 478 (6th Cir. 1996), for that proposition. (See Motion to Modify Plan at ¶ 7.) The IRS maintains that, pursuant to § 1325(b)(1)(B), Debtors are required to pay all disposable income into the plan for the benefit of creditors holding allowed unsecured claims. As a consequence, the IRS argues that Debtors should be required to turn over the Tax Refunds to the Chapter 13 Trustee to increase the dividend to be paid to the holders of general unsecured claims. (See Motion to Modify Plan at ¶ 8.) The IRS further argues that the confirmed Chapter 13 Plan currently provides for a dividend to general

unsecured claim holders in the amount of twenty-five percent (25%), but that the inclusion of Debtors' Tax Refunds would increase the dividend to one hundred percent (100%) (see Motion to Modify Plan at ¶ 10), without extending the term of the plan.¹ The IRS has frozen Debtors' Tax Refunds while this motion is pending; thus, Debtors are not in possession of the Tax Refunds at this time. (See Motion to Modify Plan at ¶ 11.)

THE DEBTORS' OBJECTION

Debtors have objected to the Motion to Modify Plan, arguing that the *Freeman* case is distinguishable from their situation. Debtors argue that the IRS has the burden of showing that there has been "a substantial change in Debtors' ability to pay since the con-firmation hearing and that the prospect of the change had not already been taken into account at the time of confirmation." (See Debtors' Objection at 2.) Debtors further argue that if any creditor should have anticipated potential Tax Refunds, it is the IRS. Debtors cite *In re Flennory*, 280 B.R. 896 (Bankr. S.D. Ala. 2001), for the proposition that modification of a Chapter 13 plan is not warranted on account of the debtor's receipt of a tax refund because the creditor was not surprised by such receipt and should have anticipated that a tax refund might have been paid to the debtor.

Debtors further argue that the "disposable income" test

¹The term of the plan is already 60 months and cannot be further extended.

does not require Chapter 13 debtors to ensure that all of their actual disposable income will be paid into a plan, but rather merely requires that a plan provide for payment of all projected disposable income of the debtors, calculated at the time of confirmation of the plan. (See Debtors' Objection at 2-3.)

Moreover, Debtors assert that the Tax Refunds are reasonably necessary for the maintenance and support of themselves and their dependents. Debtors argue that since confirmation of the plan, Mrs. Adamson is no longer employed and has lost income of Eight Hundred Forty-Eight Dollars (\$848.00) a month; Debtors received permission to purchase a vehicle and now have a monthly car payment in the amount of Three Hundred Dollars (\$300.00); and their son is enrolled at The University of Akron, thus resulting in Two Thousand Dollars (\$2,000.00) per month in educational expenses. (See Debtors' Objection at 3.)

THE IRS RESPONSE

The IRS questions Debtors' assertion that the Tax Refunds are "reasonably necessary to be expended for the maintenance and support of Debtors and their dependents[.]" (See IRS Response at ¶ 5.) The IRS specifically notes that, although Debtors received permission to incur post-petition (and post-confirmation) debt to purchase a car and now have a monthly car payment in the approximate amount of Three Hundred Dollars (\$300.00), such debt was incurred without relying on the Tax Refunds to make those

payments. The IRS also notes that, despite the assertion that Mrs. Adamson is unemployed, Debtors have not sought to reduce the amount of their monthly payments to the Trustee. The IRS states that Debtors are making the Two Thousand Dollars (\$2,000.00) per month college education expense without the use of the Tax Refunds. Debtors also have not objected to the proof of claim filed by the IRS in this proceeding. (Id.)

ANALYSIS

Despite the IRS' reliance on *Freeman*, that case is not dis-positive with respect to the issue before the Court. In *Freeman*, the debtor had moved to amend a confirmed Chapter 13 plan, to exempt the tax refund that was larger than the debtor had anticipated. The confirmed Chapter 13 plan had included a semi-monthly payment of One Hundred Fifty-Eight and 50/100 Dollars (\$158.50) and, in addition, payment into the plan of "all income tax refunds due to the debtors for a three-year period." *Freeman*, 86 F.3d at 479. The Sixth Circuit Court of Appeals analyzed whether income that was "exempt" came within the definition of projected disposable income, as set forth in § 1325(b). The court held that:

"Disposable income" under section 1325 is to be interpreted broadly in this Circuit. In this case, as a factual matter, the debtor had specifically identified that tax refunds should go to the plan and made no argument that the funds were needed for "maintenance and support" of the debtor or her dependents. The income therefore qualifies as "projected disposable

income" under section 1325. Situations may arise where a debtor did not specifically list tax refunds for inclusion in the plan and those situations would need to be examined on a case-by-case basis to decide whether a tax refund arising from pre-petition income qualified as "projected disposable income."

Id. at 481 (emphasis added).

In the present case, Debtors' confirmed Chapter 13 plan did not specifically identify that tax refunds should go to the plan. Additionally, the Tax Refunds in question are for 2001, 2002 and 2003, two years of which are wholly post-petition (2002 and 2003) and one of which is partially post-petition (2001) since Debtors filed their Chapter 13 petition in May 2001.

Debtors rely, in part, on the *Flennory* case, which requires that there be some threshold requirement of change in circumstance before creditors can compel modification of a confirmed Chapter 13 plan. In *Flennory*, the bankruptcy court noted that income and expenses of a debtor may fluctuate weekly or monthly, but that § 1329 was designed to permit modification of a plan due to changed circumstances of the debtor that were unforeseen at the time of confirmation. In the *Flennory* case, the debtor had listed his income as One Thousand Two Hundred Dollars (\$1,200.00) per month. The court held that an income tax refund in the amount of Three Thousand Four Hundred Forty-Seven Dollars (\$3,447.00) did not amount to a substantial change in his ability to pay and, thus, did not permit modification of the plan.

The Sixth Circuit Bankruptcy Appellate Panel has concluded that a change in the debtor's financial circumstances is not required to modify a confirmed plan. "Although the court may properly consider changed circumstances in the exercise of its discretion, § 1329 does not contain a requirement for unanticipated or substantial change as a prerequisite to modification." *Ledford v. Brown (In re Brown)*, 219 B.R. 191, 195 (6th Cir. B.A.P. 1998).

The Ninth Circuit Bankruptcy Appellate Panel also has declined to hold that a change of debtor's circumstances must be substantial and unanticipated in order to require modification to a confirmed plan, pursuant to § 1329(b). The Ninth Circuit stated:

Although a party has an absolute right to request modification between confirmation and completion of the plan, modification under § 1329 is not without limits. . . . Furthermore, § 1329(b)(1) protects the parties from unwarranted modification motions by ensuring that the proposed modifications satisfy the same standards as required of the initial plan. See, 11 U.S.C. §§ 1322(a), 1322(b) and 1323(c). Like the initial plan, modifications must be proposed in good faith. 11 U.S.C. § 1325(a)(3). Finally, the circumstances of the debtor's changed financial situation can then be considered in exercise of the court's discretion.

Powers v. Savage (In re Powers), 202 B.R. 618, 622 (B.A.P. 9th Cir. 1996). See also, *In re Witkowski*, 16 F.3d 739, 746 (7th Cir. 1994) ("In sum, the clear and unambiguous language of § 1329 negates any threshold change in circumstances requirement and clearly demonstrates that the doctrine of res judicata does not apply.").

Thus, Debtors did not accurately set forth the applicable standard for determining if the Motion to Modify Plan should be granted in arguing that the IRS bears the burden of establishing a change in their ability to pay the plan since confirmation.

Since the IRS is not required to show that there has been an unanticipated change in Debtors' financial circumstances in order to bring the Motion to Modify Plan, the question then becomes, what must the IRS establish in order to prevail on its motion? The IRS postulates that the confirmed Chapter 13 plan must be modified because the Tax Refunds "qualify as disposable income" (see Motion to Modify Plan at ¶ 7), however, § 1325 of the Bankruptcy Code refers to "projected disposable income," not "disposable income."

[A] court may not approve the plan unless, as of the effective date of the plan--

. . .

(B) the plan provides that all of the debtor's projected disposable income to be received in the three-year period beginning on the date that the first payment is due under the plan will be applied to make payments under the plan.

11 U.S.C. § 1325(b)(1)(B). Accordingly, the issue becomes whether, at the time the plan was confirmed, the Tax Refunds were "projected disposable income to be received in the three-year period beginning on the date that the first payment is due under the plan." Debtors filed their original Chapter 13 plan on May 22, 2001. The plan was amended pursuant to Court order on October 22, 2003 to increase

both the plan payment amount and the length of the plan period.

The Bankruptcy Court for the Southern District of Ohio held in *In re Bass*, 267 B.R. 812 (Bankr. S.D. Ohio 2001), that the disposable income test in § 1325 did not require a Chapter 13 debtor to insure that all of its disposable income would be paid into the plan, but only that all projected disposable income of a debtor, as calculated at the time of confirmation, would be devoted to a plan. In *Bass*, there were four consolidated appeals of the trustee's objections to confirmation of proposed Chapter 13 plans. All four plans proposed a monthly plan payment that was equal to the difference between the total combined monthly income reflected on Schedule I and the total monthly expenses reflected on Schedule J. The trustee did not dispute that all disposable income would be applied to the plans if the assumptions used by the debtors to draft the plans proved to be correct, but, based on her experience, the trustee believed that the debtors might receive unanticipated income not reasonably necessary for their maintenance or support. Such unanticipated income might include "wage increases, tax refunds, inheritances, gifts, lottery proceeds, insurance proceeds, proceeds from causes of action, or proceeds from the sale of property." *Id.* at 814. Consequently, the trustee encouraged the use of a form plan and filed objections to the plan if the form language was not included. The court found that one of the issues for it to decide was "whether § 1325(b)(1)(B) requires actual or

projected disposable income." *Id.* The court noted that this issue had been decided by the Ninth Circuit Court of Appeals in *In re Anderson*, 21 F.3d 355 (9th Cir. 1994), which held:

[The trustee's] argument has a fatal flaw: § 1325(b)(1)(B) does not require debtors to [assure that all actual disposable income will be paid over the first thirty-six months of the plan]. Instead, § 1325(b)(1)(B) requires provision for "payment of all projected disposable income" as calculated at the time of confirmation, and we reject the Trustee's attempt to impose a different, more burdensome requirement[.]

Bass, 267 B.R. at 817. The *Bass* court noted that the Eighth Circuit had held to the contrary, but concluded that *Anderson* reflected the better statutory analysis.

The *Bass* court further noted:

Judge Lundin notes the following problems if § 1325(b) is construed as requiring actual disposable income: Courts that have required the debtor to project future wage increases, no matter how uncertain, do not offer a balancing methodology for projecting decreases in income and do not suggest how the debtor will project future increases in expenses

Id. at 818.

The problems noted by Judge Lundin are reflected here. Debtors argue that the Tax Refunds are reasonably necessary for the maintenance and support of themselves and their dependents, citing the loss of employment by Mrs. Adamson, and post-confirmation increase in expenses in the form of a new car payment and college tuition. If this Court were to grant the Motion to Modify Plan,

it is likely that Debtors would file yet another motion to modify the plan to decrease plan payments based upon the decrease in income and increase in expenses. Indeed, the IRS, in questioning whether the Tax Refunds are reasonably necessary for the support of Debtors, notes that Debtors have not sought a decrease in plan payments. This Court does not believe that Debtors' failure, to date, to seek a decrease in plan payments abrogates the argument that they need the Tax Refunds for their current support.

A similar argument was made by Judge Harris in denying the IRS' motion to modify a confirmed Chapter 13 plan on the grounds that the IRS had failed to include a detailed description of the proposed modification. *In re Breeden*, 304 B.R. 318 (Bankr. N.D. Ohio 2003).

Does the IRS's proposed modification permit the debtors to make other changes in their projected disposable income as a result of changes in their incomes and/or expenditures that are separate from an adjustment of withholding taxes? Does it matter if these other changes could have been anticipated prior to confirmation? While the turnover of a tax refund or an adjustment to the debtors' tax withholding may perhaps constitute acceptable means to achieving one of the modifications permitted under section 1329(a)(1), (2), or (3), a detailed description of the proposed modification is a critical prerequisite to the Court's determination whether the proposed modification meets the requirements of section 1329 and applicable case law.

Id. at 322. The court also wondered: "are the debtors entitled to adjust expenses or make other changes in their schedules to

reflect a more accurate, current estimate of their projected disposable income for the remainder of their time under Chapter 13" *Id.* at 323.

This Court believes that, absent authority from the Sixth Circuit Court of Appeals, *Bass* provides a good analysis of actual ver-sus projected income. This Court holds that Debtors are only required to devote projected disposable income at the time of confirmation. As a consequence, the Tax Refunds,² which were not accounted for in Debtors' confirmed Chapter 13 plan, do not serve as a basis to require modification of that confirmed plan. Even if the Court were to consider the Tax Refunds within Debtors' projected disposable income, the Court would also have to consider Debtors' post-confirmation loss of income and increased expenses. This analysis would require recalculation of Debtors' income and expenses, which are not presently before the Court. The basis for the Court's decision rests solely on a determination that projected disposable income at the time of confirmation did not include the Tax Refunds. Accordingly, this Court denies the Motion to Modify Plan.

IT IS SO ORDERED.

²Although the Tax Refunds appear to be large for the amount of income identified by Debtors, there has been no allegation or showing that Debtors have deliberately had more money withheld as taxes than needed in order to limit their monthly income and receive in a large refund.

HONORABLE KAY WOODS
UNITED STATES BANKRUPTCY JUDGE

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Order was placed in the United States Mail this _____ day of May, 2005, addressed to:

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