

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION

IN RE:

Roland P. Coats,
Debtor.

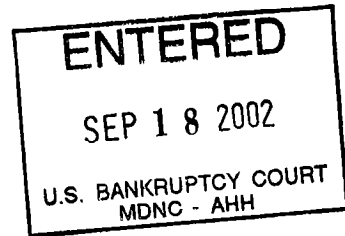
Case No. 01-80880C-7D

Pamela F. Coats,
Plaintiff,

v.

Roland P. Coats,
Defendant.

Adversary No. 01-9014



MEMORANDUM OPINION

This adversary proceeding came before the court for trial on May 9, 2002. The plaintiff appeared pro se and Clyde A. Wootton appeared on behalf of the defendant.

MATTER BEFORE THE COURT

This is a dischargeability action in which the plaintiff contends that obligations of the defendant under a separation agreement between the plaintiff and the defendant are nondischargeable. Having considered the evidence offered by the parties and the arguments submitted by or on behalf of the parties, the findings and conclusions of the court pursuant to Rule 7052 of the Federal Rules of Bankruptcy Procedure are hereinafter set forth.

JURISDICTION

The court has jurisdiction over the subject matter of this proceeding pursuant to 28 U.S.C. §§ 151, 157 and 1334, and the General Order of Reference entered by the United States District Court for the Middle District of North Carolina on August 15, 1984. This is a core proceeding within the meaning of 28 U.S.C. § 157(b)(2)(I) which this court may hear and determine.

FACTS

The plaintiff and the defendant were married in New York on October 22, 1988. The marriage was a second marriage for both parties. Both parties had children by their prior marriage, but no children were born during the marriage of the plaintiff and the defendant. Both parties were employed throughout the marriage.

On January 5, 1999, the plaintiff and the defendant borrowed \$43,000.00 from Travelers Bank. The loan from Travelers was secured by a mortgage on a residence owned by the parties located on Keese Mill Road, Paul Smiths, New York.

The plaintiff and the defendant separated on March 19, 1999, when the defendant moved from the residence. On September 3, 1999, the parties entered into a separation agreement. The separation agreement provides that the plaintiff may reside in the residence and obligates the defendant to pay the indebtedness owed to Travelers Bank. Following the execution of the separation agreement, the plaintiff continued to reside in the residence and the defendant made

payments to Travelers for some period of time.

In approximately August of 2000, the defendant moved from New York to North Carolina, where he now resides. On March 27, 2001, the defendant filed a Chapter 7 case in this court. Prior to filing the Chapter 7 case, the defendant had ceased making the monthly payments on the Travelers indebtedness. This adversary proceeding was filed on June 27, 2001. Plaintiff alleges in the complaint that the defendant's obligation to pay the indebtedness owed to Travelers in accordance with the separation agreement gives rise to a nondischargeable debt pursuant to § 523(a)(15).

DISCUSSION

Under § 523(a)(15), a debt not of a kind described in § 523(a)(5) and incurred in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other court order, is not dischargeable unless (a) the debtor lacks the ability to pay the debt from property or disposable income or (b) discharging the debt results in a benefit to the debtor that outweighs the detrimental consequences to the debtor's spouse, former spouse or child. The use of triple negatives in § 523(a)(15) makes the statutory language somewhat confusing. Nevertheless, it is clear that § 523(a)(15) speaks in the disjunctive. If the debtor lacks the ability to pay the debt from property or disposable income or discharging the debt would result in benefit to the debtor that outweighs the detrimental consequences to the debtor's spouse, then

the debt will be dischargeable.

A. Burden of proof.

The first matter to be addressed is the burden of proof in an action brought pursuant to § 523(a)(15). The appropriate rule is one in which the burden of proof shifts. Initially, the plaintiff must file a timely adversary proceeding and must show a debt incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other qualifying matrimonial order. If the plaintiff satisfies this burden, the burden of proof then shifts to the defendant/debtor to show inability to pay the marital obligation. If the debtor can show inability to pay the marital obligation, then the examination stops and the debtor prevails in the dischargeability action. If the debtor fails to carry the burden regarding ability to pay, a majority of courts have concluded that the debtor then has the burden of showing that the benefits of a discharge for the debtor outweigh the detriment to the plaintiff if a discharge is granted. See e.g., In re Dexter, 250 B.R. 222, 224 (Bankr. D. Md. 2000); In re Craig, 196 B.R. 305, 308 (Bankr. E.D. Va. 1996). This court adopts the majority rule and will place the burden of proof upon the debtor both as to debtor's ability to pay as well as to whether the benefits of a discharge for the debtor outweigh the detriment to the plaintiff if a discharge is granted.

B. Debt not of a kind described in § 523(a)(5) that is incurred by the debtor in the course of a divorce or separation.

In the present case, the plaintiff relies upon paragraphs seven and fifteen of the separation agreement as establishing an obligation that is subject to § 523(a)(15). There is an issue as to whether the separation agreement does so because the agreement requires the debtor to make payments to Travelers Bank rather than to the plaintiff. Does this create an obligation from the defendant to the plaintiff for purposes of § 523(a)(15)? If not, the inquiry is ended because without some type of obligation or debt of her own owing from the defendant, the plaintiff has no basis for obtaining any relief under § 523(a)(15).

In deciding the nature and extent of the obligations arising out of a domestic relations order or separation agreement reference should be had to applicable nonbankruptcy law. See In re Gibson, 219 B.R. 195, 202 (6th Cir. BAP 1997); In re Carlisle, 205 B.R. 812, 816 (Bankr. W.D. La. 1997); In re Henson, 197 B.R. 299, 302-03 (Bankr. E.D. Ark. 1996). Therefore, in the context of a proceeding under § 523(a)(15), the bankruptcy court should look to applicable nonbankruptcy law in determining whether a debt has been incurred that satisfies the qualifying language of § 523(a)(15). See In re Gibson, 219 B.R. at 202. And, if under applicable nonbankruptcy law, a court order or separation agreement creates an obligation from the

debtor to the nondebtor spouse, then the debtor has incurred an obligation of the type required under § 523(a)(15) even though the court order or separation agreement may not include explicit hold harmless language. See In re Gibson, 219 B.R. 195 (6th Cir. B.A.P. 1998); In re Schmitt, 197 B.R. 312 (Bankr. W.D. Ark. 1996); In re Speaks, 193 B.R. 436 (Bankr. E.D. Va. 1995).

In the present case, the separation agreement was executed in New York by parties who were then residents of New York. The agreement specifically provides that it shall be construed and enforced in accordance with the laws of the State of New York. Therefore, the court should look to New York law in determining the nature and extent of the obligation imposed upon the defendant under the separation agreement. Both paragraphs seven and fifteen obligate the defendant to pay the mortgage indebtedness owed by the parties jointly to Travelers Bank. It may be that the separation agreement does not affect the liability of the plaintiff and the defendant to Travelers Bank. However, under New York law the order does have new legal consequences as between the plaintiff and the defendant regarding such third-party indebtedness. Once the separation agreement was signed, as between the plaintiff and the defendant, a joint obligation was converted into one in which the defendant became solely responsible for the third-party indebtedness with an obligation to indemnify the plaintiff. See Barax v. Barax, 667 N.Y.S.2d 733 (Sup. Ct., App. Div. 1998) (recognizing that husband's

stipulation to pay a joint debt gave rise to an enforceable claim by the wife); Van Vechten v. Van Vechten, 526 N.Y.S.2d 704 (Sup. Ct. 1988) (husband's agreement to pay a third-party indebtedness gave rise to obligation to reimburse the wife). Thus, under New York law, the effect of the separation agreement was to create a new obligation on the part of the defendant owing to the plaintiff. By offering the separation agreement into evidence, the plaintiff established the existence of an obligation not of the kind described in § 523(a)(5) that was incurred by the debtor in the course of a divorce or separation for purposes of § 523(a)(15).

C. Whether the Debtor has the ability
to pay the § 523(a)(15) obligation.

A majority of courts have concluded that an appropriate test for determining whether a debtor lacks the ability to pay within the meaning of § 523(a)(15) is the "disposable income test" that also applies in chapter 13 cases and is found in § 1325(b) of the Bankruptcy Code. See e.g., In re Campbell, 198 B.R. 467, 473 (Bankr. D.S.C. 1996). For purposes of § 1325(b) and § 523(a)(15), disposable income means income received by the debtor that is not reasonably necessary to be expended for the maintenance or support of the debtor or dependents 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. See In re Hesson, 190 B.R. 229 (Bankr. D. Md. 1995).

The cases are not uniform regarding the appropriate date for determining whether the debtor has the ability to pay the marital debt. The dates which have been utilized by various courts that have considered the issue include the date of the filing of the case, the date of the filing of the adversary proceeding, and the date of the trial. The court has concluded that the better rule is for the determination to be made as of the date of the trial and that is the date which will be utilized in the present case. Although a debtor's disposable income is measured as of the time of trial, a determination of a debtor's ability to pay for purposes of § 523(a)(15)(A) does not consist of simply looking at a "snapshot" of his financial abilities at that time. See In re Huddelston, 194 B.R. 681, 687-88 (Bankr. N.D. Ga. 1996). Rather, the court should examine the totality of the debtor's financial circumstances. See In re Cleveland, 198 B.R. 394, 398 (Bankr. N.D. Ga. 1996); In re McGinnis, 194 B.R. 917, 920 (Bankr. N.D. Ala. 1996); In re Smither, 194 B.R. 102, 107 (Bankr. W.D. Ky. 1996) (rather than snapshot, court should consider prospective earning capacity). The circumstances that the court should consider include (1) the debtor's disposable income as measured at the time of trial; (2) the presence of more lucrative employment opportunities that might enable the debtor fully to satisfy the divorce-related obligations; (3) the extent to which the debtor's burden of debt will be lessened in the near term; and (4) the extent to which the debtor previously has made a good faith

effort to fully employ toward satisfying the debt in question. Cleveland, 198 B.R. at 398; Huddelston, 194 B.R. at 688. If an examination of these broader considerations reveals an ability to pay the marital obligation, the debtor may not avail himself of the "safe harbor" embodied in § 523(a)(15)(A). See Cleveland, 198 B.R. at 398. See also In re Straub, 192 B.R. 522, 528-29 (Bankr. D.N.D. 1996); In re Florio, 187 B.R. 654, 657 (Bankr. W.D. Mo. 1995).

With these guidelines in mind, the next question to be determined in the present case is whether the defendant carried the burden of proving that he does not have the ability to pay such debt from income or property of the defendant not reasonably necessary to be expended for the maintenance or support of the defendant or a dependent of the defendant, within the meaning of § 523(a)(15)(A). This question must be answered in the negative.

The defendant is a federal employee employed in the Federal Prison System. He was so employed before moving to North Carolina and has continued in such employment since moving to North Carolina. His employment is stable and has been marked by regular, periodic pay increases. Although the defendant accepted a reduction in pay in order to transfer to North Carolina, he nevertheless has had sufficient income to pay the Travelers indebtedness as he agreed to do in the separation agreement. During 1999 the defendant's income was \$38,592.00 per year. By 2001 his annual income had increased to \$44,311.00. At the time of the hearing his annual income was

\$46,314.00. It was incumbent upon the defendant to show that he lacked the disposable income to make the payments to Travelers in accordance with the separation agreement. Defendant failed to make such a showing. The defendant has no minor children or other dependents and the evidence failed to show that his reasonable and necessary expenses are or have been such that he lacks the financial ability to pay indebtedness owed to Travelers Bank.

D. Whether the Benefit of a Discharge
to Defendant Outweighs the Resulting
Detriment to Plaintiff.

Section 523(a)(15)(B) embodies a balancing test in which the court weighs the respective interest of the debtor in a fresh start against the interest of the debtor's spouse. If the benefit of a discharge to the debtor outweighs the resulting detriment that will be suffered by the spouse, then the indebtedness is dischargeable. This balancing test must be applied on a case-by-case basis and involves an examination of the totality of the circumstances involved in each case. In applying the balancing test, the court should review the financial status of the debtor and the spouse and compare their relative standards of living to determine the true benefit of the debtor's possible discharge against any hardship the former spouse and children would suffer as a result of the debtor's discharge. If, after making this analysis, the debtor's standard of living would be greater than or approximately equal to the spouse's standard of living if the debt is not discharged, then the debt

should be nondischargeable under § 523(a)(15)(B). On the other hand, if the debtor's standard of living will fall materially below the spouse's standard of living if the debt is not discharged, then the debt should be discharged under § 523(a)(15)(B). In re Molino, 225 B.R. 904 (6th Cir. B.A.P. 1998).

The cases that have applied the balancing test have identified various factors which should be considered. E.g., In re Taylor, 199 B.R. 37, 41 (Bankr. N.D. Ill. 1996) (the amount and nature of the debt sought to be discharged, the conduct of the parties, and the income and expenses of the parties); In re Campbell, 198 B.R. 467, 475 (Bankr. D.S.C. 1996) (the income and expenses of both parties, whether the nondebtor spouse is jointly liable on the debts, the number of dependents, the nature of the debts, the reaffirmation of any debts and the nondebtor spouse's ability to pay); In re Craig, 196 B.R. 305, 309 (Bankr. E.D. Va. 1996) (the income and expenses of both parties, whether the nondebtor's spouse is jointly liable on the debts, the number of dependents, the nature of the debts, the reaffirmation of any debts, and the nondebtor spouse's ability to pay). One of the most comprehensive list of factors for consideration is found in In re Smither, 194 B.R. 102, 111 (Bankr. W.D. Ky. 1996), where the court offered the following non-exclusive list of factors: (1) the amount of debt involved, including all payment terms; (2) the current income of the debtor, the objecting spouse and their respective spouses; (3) the current expenses of the

debtor, the objecting spouse and their respective spouses; (4) the current assets, including exempt assets of the debtor, the objecting spouse and their respective spouses; (5) the current liabilities, excluding those discharged by the debtor's bankruptcy of the debtor, the objecting spouse and their respective spouses; (6) the health, job skills, training, age and education of the debtor, the objecting spouse and their respective spouses; (7) the dependents of the debtor, the objecting spouse and their respective spouses, their ages and any special needs which they may have; (8) any changes in the financial conditions of the debtor and the objecting spouse which may have occurred since the entry of the divorce decree; (9) the amount of debt which has been or will be discharged in the debtor's bankruptcy; (10) whether the objecting creditor is eligible for relief under the Bankruptcy Code; and (11) whether the parties have acted in good faith in the filing of the bankruptcy and the litigation of the § 523(a)(15) issues.

In some respects, the parties in the present case stand on an equal footing regarding the effect of discharging the defendant's obligations under the separation agreement. Thus, neither party has any assets from which their living expenses or the Travelers indebtedness can be paid and there is similarity between the parties as to age and education. Neither party is any longer indebted to Travelers Bank, the plaintiff having obtained a discharge in an earlier bankruptcy case in New York and the defendant having obtained

a discharge in this court. However, there are other factors which make it clear that this is not a case in which the debtor's standard of living will fall below that of the plaintiff if the marital debt is not discharged. To the contrary, the evidence reflects that even without a discharge of the marital indebtedness, the defendant's standard of living nonetheless will remain substantially higher than that of the plaintiff.

A comparison of the income and expenses of the parties reveals that the defendant's income, both from the standpoint of gross income and net income, is significantly greater than that of the plaintiff. The plaintiff's current employment is at a medical facility where she works as a registrar, registering and admitting patients. Her income is less than the defendant's current income of \$46,314.00. At the same time, the plaintiff's living expenses are at least as great as the defendant's. Moreover, the plaintiff is responsible for the expenses of a minor child from a previous marriage who is a member of the plaintiff's household.

The fact that the plaintiff is not personally liable for the Travelers debt is offset by the fact that such debt is secured by a mortgage on the residence where the defendant agreed that the plaintiff could continue to live. Thus, while the plaintiff will not have to pay the Travelers debt if the defendant fails to do so, she stands to lose her home because the Travelers debt is secured by a mortgage on the property. The separation agreement reflects that

both parties contemplated and agreed that the plaintiff could continue to live in the residence and that the defendant would pay the Travelers mortgage so that she could do so. If defendant's obligation to do so is discharged, the detrimental consequences to the plaintiff will heavily outweigh the benefit to the defendant because the plaintiff and her daughter will be without the home the defendant agreed to provide or the ability to recover from the defendant the money to provide a replacement home.

Additionally, this is a case in which the defendant's financial condition has improved as a result of several increases in income, while that of the plaintiff has diminished. Moreover, looking to the future, the defendant's income is much more stable than that of the plaintiff and the likelihood of continuing increases in income are much greater for the defendant than for the plaintiff.

In summary, based upon the totality of the circumstances of this case, the court concludes that the benefit to the debtor of discharging his obligation to pay the indebtedness owed to Travelers Bank does not outweigh the detrimental consequences to the plaintiff that would result from discharging such obligation. It follows that, pursuant to § 523(a)(15) of the Bankruptcy Code, the defendant's obligation to the plaintiff to pay the Travelers indebtedness is not dischargeable.

The only remaining matter is to quantify the amount of the nondischargeable indebtedness. Because of the limited evidence

offered regarding damages, the only damages established by the plaintiff is the value of her one half interest in the residence which she will lose as a result of the defendant's breach of the separation agreement by not making the payments to Travelers. The record reflects that as a result of defendant's default, Travelers is proceeding with foreclosure against the jointly-owned residence. The foreclosure will result in the plaintiff losing her half interest in the residence. According to defendant's sworn schedules, the value of the residence is \$45,000.00. This means that plaintiff's loss and defendant's resulting obligation to plaintiff is \$22,500.00. Such obligation constitutes an indebtedness that falls within the ambit of § 523(a)(15) and hence is not dischargeable.

CONCLUSION

In accordance with the foregoing findings and conclusions, a judgment will be entered contemporaneously with the filing of this memorandum opinion adjudging that the defendant is indebted to plaintiff in the amount of \$22,500.00 and that such indebtedness is nondischargeable pursuant to § 523(a)(15) of the Bankruptcy Code.

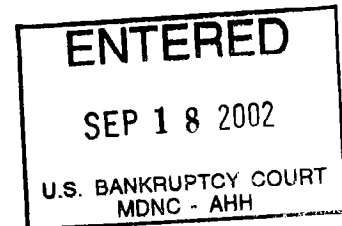
This 16th day of September, 2002.

William L. Stocks

WILLIAM L. STOCKS
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION

IN RE:)
)
Roland P. Coats,) Case No. 01-80880C-7D
)
Debtor.)
)
_____)
)
Pamela F. Coats,)
)
Plaintiff,)
)
v.) Adversary No. 01-9014
)
Roland P. Coats,)
)
Defendant.)
)



JUDGMENT

In accordance with the memorandum opinion filed contemporaneously herewith, it is ORDERED, ADJUDGED AND DECREED that the defendant is indebted to the plaintiff in the amount of \$22,500.00 and that such indebtedness is nondischargeable pursuant to § 523(a)(15) of the Bankruptcy Code.

This 16th day of September, 2002.

William L. Stocks

WILLIAM L. STOCKS
United States Bankruptcy Judge