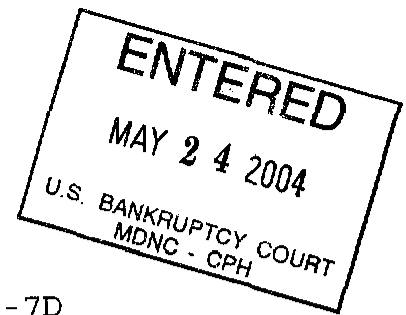


UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION



IN RE:

Ross L. Ulmer,

Debtor.

)
)
) Case No. 03-83209C-7D
)
)
)

ORDER

This case came before the court on April 8, 2004, for hearing on whether this Chapter 7 case should be dismissed pursuant to § 707(b) of the Bankruptcy Code. The Debtor appeared at the hearing with his attorney, Neil M. O'Toole. Appearing on behalf of the Bankruptcy Administrator was Robyn C. Whitman. Having considered the evidence offered by the parties and the matters of record in this case, the court has concluded that this case should be dismissed pursuant to § 707(b) of the Bankruptcy Code based upon the following findings of fact and legal conclusions.

FACTS

This voluntary Chapter 7 case was filed by the Debtor on October 24, 2003. The Debtor has a Doctorate degree in clinical psychology and is employed by Westat, Inc. in Durham, North Carolina. The Debtor currently earns \$5,959.00 per month or \$71,508.00 per year not including annual bonus. In 2003 the Debtor earned \$73,770.00, in 2002 earned \$96,036.00, and in 2001 earned \$105,889.00. The Debtor is single and has no dependents.

The schedules filed by the Debtor reflect secured indebtedness totaling \$147,809.00. The secured debt consists of \$127,860.00

secured by a residence valued at \$135,000.00, and \$19,949.00 secured by a 1999 Lexus RX 300 SUV. In his Schedule F the Debtor listed unsecured indebtedness totaling \$56,694.94 consisting mostly of credit card indebtedness.

The personal property listed by the Debtor in Schedule B includes his wearing apparel (\$500.00), jewelry (\$25.00), household furnishings and miscellaneous items (\$1,550.00), a pool table (\$1,000.00), the 1999 Lexus (\$19,573.00) and interests in retirement plans and a 401(k) valued at \$41,111.00. In his claim for property exemptions the Debtor claimed essentially all of his property as exempt property. The Debtor thus seeks to retain all of his property without paying one cent to his creditors.

On December 23, 2003, a sua sponte order was entered directing that a hearing be held for a determination as to whether this case should be dismissed pursuant to § 707(b) of the Bankruptcy Code on the grounds that the granting of relief in this case would be a substantial abuse of the provisions of Chapter 7 of the Bankruptcy Code. The hearing pursuant to such order was held on April 8, 2004. The evidence consisted of the Debtor's testimony, documentary exhibits offered by the parties and the schedules and other matters of record in this case.

LEGAL CONCLUSIONS AND DISCUSSION

Under § 707(b), the court "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." This provision represents an attempt to strike a balance between allowing debtors a fresh start and stemming abuse of consumer credit by providing the bankruptcy court with a means of dealing equitably with the situation in which a debtor seeks to take unfair advantage of his or her creditors through the use of Chapter 7. See In re Green, 934 F.2d 568, 570 (4th Cir. 1991). Section 707(b) should be applied in a manner in which a truly needy debtor is allowed a fresh start, while denying a head start to the abusers. See In re Rodriguez, 228 B.R. 601, 603 (Bankr. W.D. Va. 1999).

The first requirement in order for § 707(b) to be applicable is that the debts of the debtor be primarily consumer debts. Under § 101(8) of the Bankruptcy Code a consumer debt is a "debt incurred by an individual primarily for a personal, family, or household purpose". A debt "not incurred with a profit motive or in connection with a business transaction" is considered consumer debt for purposes of § 707(b). In re Kestell, 99 F.3d 146, 149 (4th Cir. 1996). In the present case, the debts consist of a mortgage related to the purchase of Debtor's residence, secured indebtedness related to the purchase of a personal vehicle and credit card and other unsecured personal, family or household indebtedness that was not incurred for a profit motive or in connection with a business transaction. Debtor's debts therefore are primarily, if not

entirely, consumer debts incurred by an individual, thus satisfying the first requirement under § 707(b).

The remaining issue is whether granting the Debtor in this case a Chapter 7 discharge pursuant to § 727 would involve a "substantial abuse" of the provisions of Chapter 7. There is no statutory definition of "substantial abuse" to aid in this determination. Various tests or rules for determining "substantial abuse" have been developed by the courts. However, the rule cited most frequently in the Fourth Circuit is the one adopted in In re Green, 934 F.2d 568 (4th Cir. 1991). In Green the court declined to adopt a per se rule under which a debtor's ability to pay his debts, standing alone, justifies a § 707(b) dismissal. Instead, while specifically recognizing that the debtor's ability to pay is the primary factor to be considered, the court ruled that "the substantial abuse determination must be made on a case-by-case basis, in light of the totality of the circumstances." Id. at 573. The court then provided the following examples of the circumstances or factors to be considered: (1) whether the bankruptcy petition was filed because of sudden illness, calamity, disability or unemployment; (2) whether the debtor incurred consumer credit in excess of his ability to pay; (3) whether the debtor's family budget is excessive or unreasonable; (4) whether the schedules and statement of financial affairs reasonably and accurately reflect true financial condition; and (5) the ability of the debtor to pay

his or her creditors; and (6) whether the petition was filed in good faith. See id. In making this evaluation, the court must accept and give effect to the presumption in favor of granting Chapter 7 relief that Congress included in § 707(b). See id.

The petition in the present case was not filed because of sudden illness, calamity, disability or unemployment. The evidence did show that in 2002 the Debtor lost a second job which resulted in a significant reduction in his income. While this reduction in income created some financial stress for the Debtor, it appears that his failure to reduce consumer spending after learning of this reduction was the predominant factor in the filing of this case in October of 2003.

For several years prior to 2000, the Debtor worked as a clinical director at the Butner Adolescent Center and at the same time had a second, part-time teaching position at Duke University. During this period the Debtor's annual income was approximately \$63,000.00 per year, consisting of \$42,000.00 per year from Butner and \$21,000.00 from Duke University. In 2000 the Debtor's employment changed when he accepted a position at Westat, Inc. at a salary of \$62,000.00 per year, while continuing to teach at Duke University. During 2001 the Debtor had annual earnings of \$105,889.00, consisting of \$64,924.00 from Westat and \$40,965.00 from Duke. In 2002 the Debtor had earnings of \$96,036.00 consisting of \$68,174.00 from Westat and \$27,862.00 from Duke.

However, in 2002 the Debtor learned that his part-time teaching position at Duke would no longer be available. The result was that the Debtor experienced a drop in income during 2002 of some \$9,800.00, when his income went from \$105,889.00 to \$96,036.00. However, in 2003 the Debtor received a raise and a bonus at Westat, earning \$73,770.00 during 2003. The Debtor also received a tax refund of \$4,749.00 in 2003 from his 2002 tax return. This case was filed on October 24, 2003, approximately a year after the loss of the part-time job at Duke University and at a time when the Debtor was receiving a salary of \$5,626.40 per month at Westat.

Notwithstanding the loss of his part-time job, the Debtor continued to incur and increase his consumer debt. In October of 2002, shortly after the Debtor learned of the loss of his teaching position, the Debtor incurred consumer debt of some \$24,000.00 when he purchase a 1999 Lexus SUV. As a result of this transaction, the Debtor became obligated to make payments of \$447.00 per month. In early 2003, at a time when Debtor knew that he no longer had the part-time job at Duke, the Debtor purchased a pool table at a price of \$1,000.00. The Debtor continued to make frequent ATM withdrawals of cash which apparently were used primarily to fund expenses related to playing pool and attending pool tournaments. The Debtor also continued to use his credit cards after he lost the part-time job and increased the amount of his credit card debt in doing so. Under the foregoing circumstances, the court finds that

the first of the Green factor weighs against the Debtor.

The second factor mentioned in Green also weighs against the Debtor because the evidence established that the Debtor incurred consumer debt in excess of his ability to pay. After Debtor was aware that he no longer had a part-time job and that his income was going to be less than before, he continued to incur consumer debt which was beyond his ability to pay, given the debt he previously had amassed and the reduction in his income. Such additional debt involved the purchase of the Lexus which created a new, continuing obligation of \$447.00 per month, as well as continued use of credit cards which increased the level of his credit card debt at a time when he was aware that his income had been reduced as a result of the loss of his part-time job.

Whether Debtor's proposed family budget is excessive or unreasonable is closely related to whether the Debtor has the ability to repay, and requires consideration of Debtor's Schedule I and Schedule J which set forth the income and expenses included in Debtor's budget. According to Schedule I as amended in court, the Debtor had gross monthly income of \$5,626.40 when this case was filed. However, Debtor admits that his income has increased and that at the time of the hearing had gross income of \$5,959.00 per month and net income of \$3,701.00 per month. Thus, for purposes of the § 707(b) evaluation Debtor has net income of \$3,701.00 per month. Moreover, Debtor's employment history at Westat reflects

that Debtor can expect to receive regular, periodic pay increases and annual bonuses while he remains employed with Westat.

Debtor's Schedule J sets forth the expenses which he listed when this case was filed. In determining whether a Chapter 7 case should be dismissed as a substantial abuse of Chapter 7, it is appropriate for the court to consider whether the expenses claimed by a debtor can be reduced significantly without depriving the debtor of adequate food, clothing, shelter and other necessities of life. See In re Engskow, 247 B.R. 314, 317 (Bankr. M.D. Fla. 2000). The expenses that may be reviewed in making such an analysis include the mortgage payments or rent paid by the debtor for housing. See id. (budget was "extravagant and unreasonable" based upon the amount included for mortgage payments and utilities); In re Smith, 229 B.R. 895, 899 (Bankr. S.D. Ga. 1997) (mortgage payment of \$1,695.00 was not reasonable); In re Carlton, 211 B.R. 468, 473 (Bankr. W.D.N.Y. 1997) (residence rental of \$3,000.00 per month for a family of four was unreasonable and excessive).

The Debtor has itemized monthly living expenses in Schedule J that total \$3,301.00. The expenses listed by the Debtor include a monthly housing cost of \$1,389.00, consisting of a monthly mortgage payment of \$1,289.00 and home maintenance of \$100.00 per month. This \$1,389.00 monthly expense enables the Debtor to live in a three bedroom residence situated on a two-acre lot which he is

purchasing, and to build equity in the home. Given that Debtor's family consists of only himself, the court concludes that such a large monthly housing expense is excessive and unreasonable for an individual seeking a Chapter 7 discharge. See In re DeRosear, 265 B.R. 196, 218 (Bankr. S.D. Iowa 2001) ("While the sentimental reason underlying the Debtors' desire to continue living in their current homestead may be understandable, it does not justify permitting them to erase an otherwise manageable debt load via a Chapter 7 proceeding."). As a result, in deciding whether the Debtor has the ability to repay, this excessive monthly expense should be reduced by at least \$389.00 per month and such reduction treated as being available for payment to creditors.

Another item of expense listed in Schedule J which should be reduced is the \$150.00 for medical expenses. According to the Debtor he participates in a flex-spending program in which pre-tax deductions from his salary are made by his employer. These deductions are returned to the Debtor and are available to the Debtor to pay his medical expenses rather than Debtor having to pay the expenses from his net salary.

The current expenditures claimed by the Debtor in Schedule J also include the sum of \$391.00 per month for payment on Debtor's educational loans. Although nondischargeable, the educational loans are unsecured debts that stand on the same footing as any other unsecured debt in the context of a § 707(b) analysis of a

debtor's ability to pay. Accordingly, in evaluating Debtor's ability to repay, the educational loans will be included as unsecured debts along with Debtor's credit card debt, and the \$391.00 will be treated as being available for use in repaying such debt. In summary, the court finds that the Debtor's family budget is excessive and unreasonable to the extent of the foregoing items. Hence, this factor, too, weighs against the Debtor. In reaching this conclusion, the court has considered Debtor's testimony that some of the expenses listed in Schedule J are understated. However, Debtor has never amended Schedule J. And, having heard and evaluated Debtor's testimony that, in effect, sought to impeach his own Schedule J, such testimony was discounted based upon a lack of credibility.

Making an analysis of a debtor's ability to pay under § 707(b), of course, involves examining the debtor's future income and future expenses. See Green, 934 F.2d at 572 (exploring "the relation of the debtor's future income to his future necessary expenses" is part of § 707(b) analysis); In re Krohn, 886 F.2d 123, 126 (6th Cir. 1989); Waites v. Braley, 110 B.R. 211, 214-15 (E.D. Va. 1990). This is particularly true where, as in the present case, the debtor has stable income.

As a general rule, the ability to pay is measured by assessing how much disposable income a debtor would be able to pay his or her unsecured creditors under a three to five year Chapter 13 plan.

DeRosear, 265 B.R. at 203-04. The debtor's disposable income is determined in accordance with the definition contained in § 1325(b)(2) of the Bankruptcy Code using income and expense figures that are reasonable and accurate. Id. at 204. Many courts base the ability to pay determination upon the percentage of unsecured debt that could be repaid by the debtor in a Chapter 13 case. The percentages regarded as reflecting an ability to pay have varied from case to case. See In re Norris, 225 B.R. 329, 332 (Bankr. E.D. Va. 1998). However, "the essential inquiry remains whether the debtor's ability to repay creditors with future income is sufficient to make the Chapter 7 liquidating bankruptcy a substantial abuse." DeRosear, 265 B.R. at 204.

In the present case, the Debtor's current net income is \$3,701.25 per month. For the reasons previously discussed, the \$3,301.00 in current expenditures claimed by the Debtor in Schedule J should be reduced by \$930.00. These adjustments yield net monthly income of \$3,701.25 and net monthly expenses of \$2,371.00, leaving at least \$1,330.25 per month for payments to creditors. Thus, if the Debtor were in a Chapter 13 case and submitted only a 36 month plan, a total of \$47,884.00 would become available for distribution under a Chapter 13 plan. There are no taxes or other priority debt in this case and the unsecured debt is listed at \$56,694.94. After taking into account the trustee fees and costs related to a Chapter 13, it appears that the Debtor could

pay a dividend in excess of 75% to his unsecured creditors if he were willing to proceed under Chapter 13 with a three-year plan, rather than seeking a Chapter 7 discharge. With a longer plan, the Debtor, of course, could pay a substantially higher dividend to his creditors. This constitutes an ability to pay that, under the totality of the circumstances of this case, is sufficient to render this case abusive for purposes of § 707(b).

A further factor to be considered is whether the Debtor's schedules and statement of financial affairs reasonably and accurately reflect Debtor's true financial condition. As discussed above, Debtor's schedules include some unreasonable items involving Debtor's expenses and Debtor failed to list accurately his income. Otherwise, there was no showing that the schedules do not accurately reflect Debtor's true financial condition. Hence, this factor did not carry much weight in the court's conclusion that this case should be dismissed pursuant to § 707(b).

The last factor that will be discussed is whether this case was filed in good faith. In Green the court concluded that § 707(b) was intended to provide a tool for dismissing a Chapter 7 case "when 'the total picture is abusive.'" Green, 934 F.2d at 572. However, neither bad faith nor fraud is an element required for a finding of substantial abuse. Id. This case arguably involves an effort to take unfair advantage of creditors through the use of Chapter 7, in light of Debtor's ability to substantially

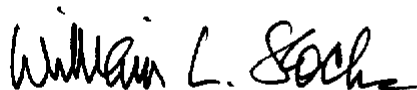
repay his creditors if he were willing to do so. However, even if the good faith factor is resolved in Debtor's favor, the other circumstances of the case are such that the granting of Chapter 7 relief in this case nonetheless would involve a substantial abuse of the provisions of Chapter 7.

CONCLUSION

Having considered the totality of the circumstances presented by this case, the court concludes that the granting of Chapter 7 relief in this case would be a substantial abuse of the provisions of Chapter 7 and that this case, therefore, should be dismissed under § 707(b) of the Bankruptcy Code.

IT IS SO ORDERED.

This 21st day of May, 2004.

A handwritten signature in black ink, appearing to read "William L. Stocks", is written over a horizontal line.

WILLIAM L. STOCKS
United States Bankruptcy Judge