

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

IN RE:) CHAPTER 13
)
ANITRA LARAI MYLES) CASE NO. 05-92125-MHM
)
Debtor)

**ORDER SUSTAINING OBJECTION TO CONFIRMATION
AND CLAIMED EXEMPTIONS**

This adversary proceeding is before the Court on the Chapter 13 Trustee's objection to confirmation of Debtor's plan (the "Plan") and on the Chapter 13 Trustee's objection to Debtor's exemptions. The confirmation objection of the Chapter 13 Trustee ("Trustee") asserts that the Plan should be amended to treat future tax refunds as disposable income; to provide that any tax refunds received by Debtor for years ending December 31, 2005, December 31, 2006, and December 31, 2007 be paid into Debtor's Chapter 13 plan funds; and to direct the Internal Revenue Service ("IRS") to remit payments for those three years directly to Trustee. Trustee's objection to Debtor's exemptions also contends that the amount of the tax refunds Debtor claims as exempt exceeds the amount allowed by Georgia law. At the confirmation hearing, the parties were given the opportunity to submit post-hearing briefs in support of their arguments regarding the treatment of future tax refunds. This matter is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(L), and the Court has jurisdiction over it pursuant to 28 U.S.C. § 157 and 28 U.S.C. § 1334. For the reasons stated below, Trustee's objection to confirmation and objection to Debtor's exemptions are sustained.

Trustee filed an objection to confirmation of Debtor's plan May 4, 2005. In response to Trustee's objection, Debtor amended Schedule B¹ June 1, 2005², to add future income tax refunds for the years 2005, 2006, and 2007 in the amount of \$5,000. At the same time, Debtor also amended Schedule C to claim an exemption of \$5,000 in the tax refunds. Subsequently, before expiration of the deadline for objecting to Debtor's exemptions, Trustee filed a Supplemental Objection to Confirmation alleging that Debtor's claimed exemptions exceed the amount allowed under O.C.G.A. § 44-13-100(a)(6). Trustee also asserts that any proceeds from future tax refunds should be paid into the plan as disposable income. Debtor contends that future tax refunds are neither property of the estate nor disposable income. This dispute presents two issues: (1) whether future tax refunds are exempt property and, if they are exempt property, (2) whether future tax refunds are disposable income and therefore must be included in the analysis of disposable income provided for in § 1325(b)(1)(B).

¹ Bankruptcy Rule 1007 requires a debtor to file a statement of financial affairs, a schedule of assets and liabilities, a schedule of claimed exemptions, a schedule of current income and expenditures, and a schedule of executory contracts and unexpired leases (the "Schedules"). Standard forms are promulgated for the Schedules

² Debtor's statement of exemptions (Schedule C) is ambiguous. Is each year's tax refund estimated to be \$5,000.00, or is the total of all three years' refunds estimated to be \$5,000.00? A review of the originally-filed Schedule C showed a federal income tax refund of \$1,700 (received?) for 2004 with none shown for the state; however, Debtor's amendment to Schedule B eliminated any refund for 2004 due to an anticipated liability therefor. Tax claims filed by the IRS and the State of Georgia Department of Revenue after the parties' briefs were filed indicate a more complex picture of tax possibilities than the original or amended Schedules reflect; among other possibilities, if those claims are not objected to, successfully, Debtor may have no actual refunds for any of the three years, 2005-2007, in which event this issue may become moot. In any event, it appears more likely that the aggregate 2005-2007 tax refunds, if any, will not exceed \$5,000.

May Future Tax Refunds Be Claimed as Exempt Property?

Section 522 permits a debtor to exempt certain assets from reach of her creditors.

Although § 522(b) specifies the type of property that a debtor may exempt, subsection (b) also allows states to “opt out” of this federal exemption scheme and to enact state exemption provisions. Georgia has opted out of the federal exemptions and codified state bankruptcy exemptions under O.C.G.A. § 44-13-100(a), which lists the specific exemptions to be allowed to its Georgia residents who are also under bankruptcy court jurisdiction. Section 44-13-100(a)(6) provides:

In lieu of the exemption provided in Code Section 44-13-1, any debtor who is a natural person may exempt, pursuant to this article, for purposes of bankruptcy, the following property –

. . . (6) The debtor's aggregate interest, not to exceed \$ 600.00 in value plus any unused amount of the exemption, not to exceed \$ 5,000.00, provided under paragraph (1) of this subsection, in any property[.]

O.C.G.A. § 44-13-100(a)(6). Debtor’s Amended Schedule C identifies the following property exempted pursuant to § 44-13-100(a)(6):

- (1) checking account in the amount of \$50;
- (2) savings account in the amount of \$600; and
- (3) future federal tax refunds for years 2005, 2006, and 2007 in the amount of \$5,000. Debtor’s claimed exemptions under O.C.G.A. § 44-13-100(a)(6) exceed the \$5,600 cap by \$50. Therefore, Trustee’s objection to the claimed exemptions has merit, to the extent of \$50.

Is Exempt Property Disposable Income?

Section 1325(b)(1)(B) provides that “[i]f a trustee . . . objects to the confirmation of the plan, then the court may not approve the plan unless . . . 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). Section 1325(b)(2) defines disposable income 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). Finally, disposable income must be “projected.” 11 U.S.C. § 1325(b)(1)(B); *Freeman v. Schulman*, 86 F.3d 478, 481 (6th Cir. 1996). In this case, three years’ tax refunds are specifically identified by Debtor in amended Schedules B and C. Identification of the income in Debtor’s schedules is sufficient to establish “projected income.” *Cf. Freeman, supra* (holding that identification of the tax refunds in the plan was sufficient to establish “projected disposable income”).

Case law is split as to whether exempt property may be treated as disposable income. The majority of courts addressing the issue hold that exempt property must be included in the disposable income analysis under § 1325(b)(1)(B). *Stuart v. Koch*, 109 F.3d 1285 (8th Cir. 1997) (Workers compensation benefits); *Taylor v. U.S.*, 212 F.3d 395 (8th Cir.), *cert. denied*, 531 U.S. 1010, 121 S. Ct. 564, 148 L. Ed. 2d 484 (2000) (income from ERISA plan); *Freeman v. Schulman*, 86 F.3d 478, (6th Cir. 1996) (tax refund); *In re Gebo*, 290 B.R. 168 (Bankr.M.D.Fla. 2002)(J. Paskay)(Workers’ compensation benefit);

Hagel v. Drummond, 184 B.R. 793 (B.A.P. 9th Cir. 1995) (Social Security disability benefits). The majority view generally holds that by its plain language § 1325(b)(2) is not limited to consideration of property of the estate and that exempt property may be considered in applying the disposable income test.³

A minority of courts hold that exempt property should not be included in the disposable income analysis. *In re Graham*, 258 B.R. 286 (Bankr.M.D.Fla. 2001)(personal injury settlement); *In re Hunton*, 253 B.R. 580 (Bankr.N.D.Ga. 2000)(J. Drake)(exempt personal injury settlement proceeds); *In re Ferretti*, 203 B.R. 796, 800 (Bankr.S.D.Fla. 1996)(exempt personal injury settlement proceeds); *In re Baker*, 194 B.R. 881, 884-85 (Bankr.S.D.Cal. 1996)(exempt insurance proceeds were not projected disposable income because proceeds did not come in the form of a stream of payments); *In re Kerr*, 199 B.R. 370 (Bankr.N.D.Ill. 1996)(proceeds from the sale of exempt real estate); *In re Tomasso*, 98 B.R. 513, 515-16 (Bankr.S.D.Cal. 1989)(exempt personal injury settlement proceeds).

Several of the opinions decided by bankruptcy courts in this circuit have relied upon the case of *Gamble v. Brown (In re Gamble)*, 168 F.3d 442, 443 (11th Cir. 1999) for their conclusion that exempt property should not be included included in the disposable income analysis of §1325. In *Gamble*, the Chapter 13 debtors had claimed an exemption in the net sales proceeds of real property, but the bankruptcy court ordered the debtors to turn over the net proceeds to the Chapter 13 trustee. *Id.* at 443-44. Thereafter, the bankruptcy court denied the debtors' "Motion Requesting Turnover of Exempt Property,"

³ "Property of the estate" is a defined and often-used term in the Bankruptcy Code. *See* 11 U.S.C. §541 and §1306. If Congress had intended to limit the disposable income test to property of the estate, it could have done so.

stating that the proceeds must be preserved until the conclusion of the bankruptcy case. *Id.* at 444. The Eleventh Circuit reversed, finding that the bankruptcy court's holding conflicted with its holding in *Hall v. Finance One of Georgia, Inc. (In re Hall)*, 752 F.2d 582 (11th Circuit 1985), which held that "once the debtor lists property as exempt from the estate, and neither the trustee nor the creditors object during the 30-day period [provided under § 522(l)], the property no longer belongs to the estate and the debtor 'may use it as its own.'" *In re Hall*, 752 F.3d at 584. See also *Taylor v. Freeland & Kronz*, 503 U.S. 638, 112 S.Ct. 1644 (1992), which held that a late-filed objection to a debtor's exemptions was invalid, even if the claimed exemption lacked statutory support.

Although *Gamble* did not address 1325(b), the court in *In re Graham*, 258 B.R. 286 (Bankr.M.D.Fla. 2001), interpreted *Gamble* as prohibiting the bankruptcy court from including exempt property in the disposable income analysis. The *Graham* court stated that "if a debtor's claimed exemption is established under § 522(l) through expiration of the Rule 4003(b) period without objection, then § 522(c), *Taylor* and *Gamble* operate to prevent a bankruptcy court from treating such exempt property as 'disposable income' under § 1325(b)." 258 B.R. at 292-93. Similarly, in *Hunton*, 253 B.R. 580 (Bankr.N.D.Ga. 2000), the court held that where the debtor claimed an exemption in the personal injury claim and no one objected, the settlement proceeds did not constitute disposable income. 253 B.R. at 582-83. "To subject the Debtors' exempt settlement proceeds to the claims of creditors, by treating the proceeds as 'disposable income,' would conflict with this Court's reading of *Gamble*." *Id.* at 582.

Other cases, however, have not read *Gamble* so broadly. In the case of *In re Gebo*, 290 B.R. 168 (Bankr.M.D.Fla. 2002)(J. Paskay), the court sustained the trustee's objection to the debtor's proposed chapter 13 plan. 290 B.R. at 170-71. In *Gebo*, the trustee raised an "informal" (oral) objection to confirmation at the confirmation hearing. *Id.* at 168-69. The trustee contended that the proceeds resulting from settlement of the debtor's worker compensation claim should be devoted to funding the plan as disposable income in accordance with § 1325(b)(1)(B). *Id.* at 169. The trustee failed to object to the debtor's claim of exemption in the settlement proceeds within the time for objections fixed by Rule 4003(b). *Id.* Nevertheless, the court held that the settlement proceeds received by the debtor postpetition were disposable income for purposes of confirmation of the Chapter 13 plan. *Id.* at 170. Moreover, the court held that its findings did not conflict with the court's holding in *Gamble*:

A close analysis of facts involved in *Gamble* leaves no doubt that the holding of *Gamble* is less than persuasive to serve as controlling authority of the precise and discrete issue present in the instant case. *Gamble* did not involve the question of whether the debtor's exempt property should be included in considering the "disposable income test" when considering the confirmability of a chapter 13 plan. The holding of the court in *Gamble* was nothing more than the undisputable principle which is: once property is allowed as exempt, it is no longer property of the estate and the debtor *cannot be forced to use those funds to satisfy the claims of creditors*. This conclusion is not opposite to the view of the majority that exempt property may be considered when applying the "disposable income test" in a chapter 13 case.

The court in *Gebo* went on to explain that, because of the substantial differences in Chapter 7 and Chapter 13, inclusion of exempt property as "disposable income" is appropriate.

In sum, this Debtor has a choice and can elect to seek relief under chapter 7 and keep the funds allowed as exempt, or seek relief under chapter 13 and use its liberal and remedial provisions to save the family home from loss through foreclosure sale. But if that is the Debtor's choice, it is unfair and grossly inequitable and smacks of bad faith to immunize exempt funds by excluding them from the "disposable income test."

As did the court in *Gebo*, the undersigned believes *Gamble* should be limited to the facts and issues before the *Gamble* court – facts and issues which differ from those before this court in the instant case. The holding in *Gamble* may certainly be reconciled with the conclusion of the majority of courts holding that exempt property must be included in the disposable income analysis under § 1325(b)(1)(B).

It is this court's experience that some debtors use over-withheld funds, returned annually in the form of a tax refund, as a pseudo-savings account or emergency fund, sometimes for the purpose of providing a cushion for the various expected and unexpected expenses which are difficult to project as easily as a tax refund, and sometimes to provide cash for vacations or other purchases. The amount of an individual's tax refund is within the control of the individual: the number of an individual's tax exemptions (claimed on the W-4 form provided to the employer) can be decreased so that the individual's net pay increases; or the number of tax exemptions can be increased to artificially decrease net income and thus provide a hidden savings account (albeit without interest) which produces income after the tax return is filed. In fact, an individual can designate a specific amount to be withheld, rather than leave it to the employer's calculation based on the number of exemptions claimed.

Debtor contends that her future tax refunds are not disposable income because she will need the funds to support herself and her minor children. To support her argument

Debtor cites *In re McCray*, 172 B.R. 154 (Bankr.S.D.Ga. 1994). The *McCray* court concluded that the confirmation order should not be modified in regard to disposable income except in extraordinary circumstances. *Id.* The court did recognize, however, that exempt property could be considered disposable income. *Id.* at 156. The *McCray* court further explained that in determining whether income is “disposable income” pursuant to § 1325(b)(1)(B), the bankruptcy court must consider the totality of the circumstances. *Id.* at 157. Determinations of the reasonableness of the debtor’s budget and the minimum level of expense necessary for, among other things, housing, food, and clothing should be determined on a case by case basis. *Id.* The *McCray* court found that the tax refunds in that case did not constitute a substantial change in the debtor’s circumstances sufficient to justify disturbing a confirmed Chapter 13 plan. *Id.* at 158.

Debtor shows that her Schedules do not include an allocation for food expense. Debtor argues that future tax refunds are necessary for her maintenance and support and thus is not disposable income. At the confirmation hearing, however, Debtor’s attorney stated that Debtor pays rent to live with her mother, who in turn uses the money to buy food for the household. Debtor has not made any representations that her mother is no longer so willing or that her mother has demanded additional rent to cover such expenses. Therefore, Debtor has failed to meet her burden of showing that the tax refunds are necessary for her maintenance or support. (See *In re Ehret*, 238 B.R. 85 (Bankr.D.N.J. 1999) (“The party objecting to confirmation bears the initial burden of presenting evidence that the proposed plan does not include all disposable income, but the ‘ultimate burden’ then shifts to the debtor to show compliance with the requirements of section 1325(b)(1)(B).”).

The income from Debtor's future tax refunds must be included in the disposable income analysis. "The fact that [the income] is exempt from the reach of creditors does not preclude a bankruptcy court from finding that the [the income] is also disposable income for purposes of Chapter 13." *Taylor v. U.S.*, 212 F.3d 395 (8th Cir. 2000). To hold otherwise would encourage an unscrupulous debtor to conceal funds from the Chapter 13 estate and to circumvent the disposable income test by simply withholding more income taxes than required by law and recovering tax refunds after confirmation of the plan. See *Midkiff v. Stewart*, 342 F.3d 1194, 1201 (10th Cir. 2003). The use of exempt income for personal expenses unburdens non-exempt income which then becomes available for payment into the plan. The purpose of Chapter 13 is to provide creditors with maximum recovery, while leaving the debtor with enough money to pay living expenses. *In re Minor*, 177 B.R. 576, 281 (Bankr.E.D.Tenn. 1995). In this way, the debtor's fresh start is protected by the retention of non-disposable income, as opposed to the retention of exempt assets under Chapter 7. *In re Tolliver*, 257 B.R. at 100.

In his objection to confirmation, Trustee contends the Debtor's Chapter 13 plan should be amended to require that any federal tax refunds Debtor receives for calendar years 2005, 2006, and 2007 be paid directly by the IRS into Debtor's Chapter 13 plan, whose funds are administered by Trustee. Debtor's projected disposable income must be paid into the plan. See 11 U.S.C. § 1325(b)(1)(B). Debtor's projected disposable income in this case will be calculated including the projected tax refunds that she will receive during the term of the plan. Debtor is not, however, required to pay over the exempt income, *Gamble v. Brown*, 168 F.3d 442, 444 (11th Cir. 1999), although she may choose to do so. *Bibb County DFACS v. Hope (In re Hammonds)*, 729 F. 2d 1391 (11th Cir. 1984). Accordingly, it is hereby

ORDERED that the Chapter 13 Trustee's objection to Debtor's exemptions is sustained to the extent of the \$50 by which they exceed the amount allowed under Georgia law. It is further

ORDERED that Trustee's Objection to Confirmation is sustained and confirmation is denied without prejudice. It is further

ORDERED that Debtor may file an amended Chapter 13 plan within 20 days of the entry of this Order. Debtor's amended Chapter 13 plan must include a plan payment based on projected disposable income calculated including the projected tax refunds that she will receive during the term of the plan. Debtor need not provide for the tax refunds to paid directly to the Chapter 13 Trustee for distribution under her plan although she may choose to do so rather than paying an increased monthly plan payment. If no such amended plan is filed within the time allowed, this case may be dismissed without further order or notice.

IT IS SO ORDERED, this 8th day of March, 2006.



MARGARET H. MURPHY
UNITED STATES BANKRUPTCY JUDGE