REVIEW OF CASE LAW ADDRESSING FORM 122C-1, 122C-2, AND TRUSTEE RECOMMENDATIONS REGARDING THE CHAPTER 13 PLAN – CLEVELAND, OHIO

Presented by the Office of the Chapter 13 Trustee - Cleveland

BREAKING DOWN FORM 122C

122C-1, CALCULATION OF YOUR CURRENT MONTHLY INCOME AND CALCULATION OF COMMITMENT PERIOD

Distinction between Form 122A and Form 122C

Form 122A

Form 122A is used in Chapter 7 to calculate whether debtor(s) are eligible to file a Chapter 7 bankruptcy case. Form 122A-1 calculates debtor(s) current monthly income ("CMI") and then determines whether it is under or over the applicable median income. If debtor's CMI is over the median income, they must also complete Form 122A-2, the "Means Test Calculation" to determine whether, after performing this calculation, debtor has income to pay 25% of the unsecured, nonpriority debt. If debtor can pay 25% or more of the unsecured non-priority debt, there is a presumption that the debtor does not qualify for a Chapter 7 case. The presumption may be rebutted by special circumstances "such as a serious medical condition or a call or order to active duty in the Armed Forces, to the extent such special circumstances that justify additional expenses for adjustments of current monthly income for which there is no reasonable alternative". 11 U.S.C. §707(b)(2)(B).

Form 122C

Form 122C is used in Chapter 13 to calculate (1) whether the debtor must propose a 36 month or a 60 month plan and (2) if a 60 month plan is required, how much is the disposable income that must be paid to unsecured, nonpriority creditors. Disposable income as calculated by Form 122C-2 may also be rebutted with special circumstances. In addition, if there are changes in income or expenses, or if changes are virtually certain to occur after the petition date, those changes may be asserted as a basis to change the disposable income (Form 122C-2, Line 46).

Because Form 122A calculates whether a debtor can file Chapter 7 and Form 122C calculates the applicable commitment period and disposable income, then in a case that is converted from Chapter 7 to Chapter 13, a Form 122C-1 and Form 122C-2 generally must be filed.

<u>Form 122A-1 and Form 122C-1, Line 4: Household Income</u>

<u>The language in the form states:</u>
"**All amounts from any source which are regularly paid for household expenses of you or your dependents, including child support**. Include regular contributions from an unmarried partner, members of your household, your dependents, parents, and roommates. Do not include payments from a spouse. Do not include payments you listed on line 3."

Examples:

(a) Parent living with debtor pays for utilities
(b) Unmarried partner pays for half of the rent
(c) Roommate pays half of the rent and utilities
(d) Employer reimbursed expenses

If money comes from an outside, non-household member and is a gift in nature (compared to court ordered) then we will not ask for it to be included in the household income. A technical reading of the form says it should be included. There can always be a unique circumstance. We are not aware of any case law on this, but generally our policy.

<u>Case Law:</u>
<u>In re Anderson</u>, 444 B.R. 505, 509 (Bankr. W.D.N.Y. 2011). CMI includes any amount paid by the debtor's girlfriend for household expenses on a regular basis.

<u>In re Fitzgerald</u>, 418 B.R. 778, 784 (Bankr. D. Conn. 2009). Court refused to include non-filing roommate's total income as part of debtor's CMI. Court only included the amount of rent actually paid to Debtor by the roommate.

<u>In re Trimarchi</u>, 421 B.R. 914, 918 (Bankr. N.D. Ill. 2010) (*<u>citing</u>* *<u>In re Travis</u>*, 353 B.R. 520, 526 (Bankr. E.D. Mich. 2006). Grooming, clothing, basically everything other than the specified contribution to the household was otherwise personal to a non-spouse partner of the debtor. *Debtor may still claim household size of 2*.

<u>DeAngelis v. Holmes (In re Holmes</u>), 496 B.R. 765 (Bankr. M.D. Pa. 2013). Significant other living with debtor, only include significant others' contributions to the household expenses. The Court found it important that there was no legally binding relationship.

Form 122C-1, Line 13: Marital Adjustment

The language in the form states:
"This deduction is for the non-filing spouse's income that is not "regularly paid for the household expense of you or your dependents, such as payment of the spouse's tax liability or the spouse's support of someone other than [debtor] or [debtor's] dependents."

Note: The drafting of the form presumes all NFS income is contributed, and then allows for deductions for items that are purely personal to the NFS. This is consistent with case law. *In re Tapply,* 652 B.R. 124 (Bankr. Mass. 2023); *In re Montalto*, 537 B.R. 147 (Bankr. E.D.N.Y. 2015). The presumption is that all of the NFS's income is used for household expenses and the burden of proof is on the debtor to prove otherwise. An exception to the rule is if the NFS lives in a separate household. *In re Tapply*, *Id.*

Courts look to the nature of the debt or expense, and not to who is legally liable for it, to make the determination. If NFS signs a contract for private tuition for children, the tuition is still a household expense even though debtor not obligated on the contract. *In re Persaud,* 486 B.R. 251, 262 (Bankr. E.D.N.Y. 2013), *citing In re Rable*, 445 B.R. 826, 829 (Bankr. N.D. Ohio 2011); *Montalto, Id.,* at 149; *Tapply , Id.* at 130.

Expenses that are not household expenses:

- Student loan expenses. *In re Hamilton -Conversano*, 2017 LEXIS 3282 (Bankr. E.D. N. Carolina 2017).

- Income tax debt that arises from a joint tax return is not solely a NFS debt and cannot be adjusted out. *In re Jackson*, 2020 LEXIS 2207, Case No. 19-41723 Bankr. N.D. Texas, Ft. Worth Div., May 4, 2020). Therefore, it should follow that tax deductions and insurance costs are probably household in nature and not purely personal to the extent that the amount covers other people in the household.

- Repayment of a retirement loan by NFS should undergo the same scrutiny as NFS credit card debt (see below).

Expenses that are household expenses:

- College tuition for children is a household expense even if paid for by NFS and NFS insisted on said payment. *In re Persaud, Id.*

- Children's dance lessons. *Tapply, Id.*

- It is uncontroverted that a NFS's credit cards, loan consolidation, or other expense for which the NFS is the sole legal obligor, but used to pay for household expenses, cannot be adjusted out as a marital expense.

Issues the Trustee will watch for:

- Putting NFS car in Form 122C-2 as a vehicle deduction rather than in marital adjustment in 122C-1 if IRS standard allowance is higher than actual expense.

- NFS uses credit card for vehicle expenses and also puts NFS vehicle expense as marital deduction.

- NFS boosting 401(k) deductions significantly right before case is filed.

- NFS retirement loan repayment when used for household expenses.

What number goes in the Form 122C-1 Marital Adjustment Line?

The amount to be entered as the marital adjustment is the total marital adjustment amount divided by 60 months. Not the entire current monthly payment.

Example:

NFS car note. Payoff amount $6,600. Monthly payment amount $586.40. Marital Adjustment Amount is $6,600 / 60 = $110.

Same analysis for NFS retirement loans and credit card debt. To the extent it is an allowable marital adjustment item, the proper amount is the balance owed divided by 60, not the current monthly payment amount.

Line 16b: Household Size

Prevailing law uses the Economic Unit theory: "household" is defined as all individuals who act as a single economic unit with the debtor, or in other words, those the debtor financially supports and those who financially support the debtor. *In re Skiles*, 504 B.R. 871 (Bankr. N.D. OH 2014). The *Skiles* opinion also states that a voluntarily unemployed or underemployed person "usually should be excluded from debtor's 'household'".

In re Versace, Case 16-05593-HB (Bankr. S.C. 2017)
Debtor paid money to help support her adult daughter, granddaughter, and father but she did not live with them. Under Economic Unit, she could not include them in her household size.

In re Ford, 509 B.R. 695 (Bankr. Idaho 2014)
Debtor had no legal obligation to support ex-spouse's stepson. However, he did have a legal obligation to support their daughter. As a practical matter, he treated the children the same, they visited together, and he supported them both. Debtor could not include the stepson as part of the household – he was gratuitously giving the support. No showing they were economically entwined and no legal obligation.

FORM 122C-2 CALCULATION OF YOUR DISPOSABLE INCOME

Line 43 - Special Circumstances

Special circumstances are determined on a case-by-case basis. The code section allowing for special circumstances to rebut a means test issue is 11 U.S.C. §707(b)(2)(B)(i): "such as a serious medical condition or a call or order to active duty in the Armed Forces, to the extent such special circumstances that justify additional expenses or adjustments of current monthly income for which there is no reasonable alternative."

The language in the form states:
"**Deduction for special circumstances.** If special circumstances justify additional expenses and you have no reasonable alternative, describe the special circumstances and their expenses. You must give your case Trustee a detailed explanation of the special circumstances and documentation for the expenses."

The prevailing reason for denial of special circumstances is debtors' failure to provide detailed explanation and documentation. The Courts often do not address the merits of the claim due to failure to meet the "explanation and documentation" requirements.

The Court needs information to allow it to determine whether an expense is "reasonable and necessary" or just a "lifestyle" choice. *In re Greer*, 2011 Bankr. LEXIS 5633 (Bankr. E.D. Cal. 2011).

Cigarettes

No case law found on allowance of cigarettes as special circumstance. If used by NFS, can be marital adjustment. *In re Anderson*, Bankr. LEXIS 989 (Bankr. N.D. Michigan 2020).

In an under-median case, and thus not a 122C-2 special circumstance situation, Judge Morgenstern-Clarren looked at the overall budget and ruled that the debtor had made sacrifices in her spending to accommodate the cigarette expense. *In re Short*, 2008 Bankr. LEXIS 3940, Case No. 08-11224 (Bankr. N.D. Ohio September 11, 2008).

Retirement

Debtor's desire to eventually retire is not a special circumstance. *In re Walker*, 2019 Bankr. LEXIS 3481 (Bankr. N.D. Ga. 2019).

Repayment of a retirement loan could be a special circumstance depending on the reason for taking the loan. *In re Cribbs*, 387 B.R. 324, 327-330 (Bankr. S.D. Ga. 2008).

Age by itself and the "mere desire for retirement" is not a special circumstance. *In re Anderson*, 444 B.R. 505, 508 (Bankr. W.D.N.Y. 2011).

Antenuptial Agreement

Antenuptial Agreement between husband and wife, which they did not adhere to is not a special circumstance. *In re Stocker*, 399 B.R. 522 (Bankr. M.D. Fla 2008).

Storage Unit, unreimbursed work expenses, college, student loan payments

Expenses for a storage unit, unreimbursed expenses for food while debtor's husband is traveling for work, living expenses of debtor's adult child while away at college, and student loan payments, do not qualify as special circumstances. *In re Patterson*, 392 B.R. 497, 504 (Bankr. S.D. Fla. 2008).

Voluntary lifestyle changes - marriage

Post-petition marriage and decrease in work hours are not special circumstances. *In re Hernandez*, No. 08-31588, 2008 Bankr. LEXIS 3609 (Bankr. N.D. Ohio 2008).

Purchase of vehicle

Deduction for NFS to finance a new vehicle in the future is not a special circumstance. *In re Henderson*, 2023 Bankr. LEXIS 2377 (Bankr. N.D. Ga. 2023)

Pet expenses

In re Chambers, 2022 Bankr. LEXIS 717 (Bankr. M.D. Fl. 2022). Pet expense okay as special circumstances.

In re Crow, 2012 Bankr. LEXIS 6149 (Bankr. E.D. Ca. 2012). Pet expenses are not special circumstances.

Medical Marijuana

In re Andrick, 604 B.R. 577 (Bankr. N.D. Colorado 2019). Medical marijuana is not a special circumstance.

Housekeeping help and lawncare expenses

Housekeeping help and lawncare expenses are not special circumstances for a family with small children and both parents work full time jobs. *In re Jackson*, 2020 LEXIS 2207 (Bankr. N.D. Texas 2020) (also not a marital adjustment). *See also In re Everhart*, 604 B.R, 565 (Bankr. N.D. Texas 2019) (lawncare is not a special circumstance, but high transportation costs, utilities and insurance were allowed as special circumstances once debtors proved the costs and the Court determined there was no reasonable alternative as moving was more expensive than accepting these expenses).

Pool maintenance

Pool maintenance might be a special circumstance because it requires specialized knowledge and a pool's maintenance is required for health and safety. *In re Jackson*, 2020 LEXIS 2207 (Bankr. N.D. Texas 2020).

Student Loan payment

Student loan payments are not special circumstances. *In re Vaccariello,* 375 B.R. 809 (Bankr. N.D. Ohio 2007) (cited by many courts and a majority position). If non-dischargeability is a basis for special circumstances, then fraud claims, willful and malicious injuries, drunk driving and tax debt, etc. would all be special circumstances.

A NFS refusal to make funds available for the bankruptcy

A NFS refusal to make funds available for the bankruptcy is not a special circumstance. *In re Tapply*, 652 B.R. 124 Bankr. Mass. 2023).

Homeowners or condominium association fees

Homeowners or condominium association fees are not special circumstances. *In re Growth*, 2018 Bankr. LEXIS 2189, Case 17-30264 , (Bankr. E.D. Wisconsin July 25, 2018). These fees are common and ordinary and thus included in the standards. If debtor had shown a disability resulting in a need to live where the HOA fees are typically high, then could be allowed. Court disregarded debtor's argument that she had no reasonable alternative but to pay the fees. Court said must first show she had a special circumstance and then look to see if a reasonable alternative.

Expenses for long commutes to work

In re De Lara, 2019 Bankr. LEXIS 4147 (Bankr. N.D. Cal. 2019). Long commute to work includes bridge tolls and parents to 3 children that needed to be driven to their activities. The examples given by Congress of a serious medical condition or call to active duty are situations that are beyond the debtor's control. Court ruled against the Debtor: (a) burden of proof is on the debtor; (b) she failed to itemize her expenses or provide documentation of her expenses; (c) she did not explain why costs could not be mitigated by carpooling or mass transit; (d) she did not explain why her calculation using IRS $0.58 per mile rate for tax deduction was an appropriate measure of her costs. Court was looking for better documentation.

"The fact that the money is actually spent does not automatically make the expense necessary and reasonable." The debtors must show the Court that the expenses are reasonable and necessary, beyond the debtor's control, there is no reasonable alternative and are not just "lifestyle" choices. *In re Greer*, 2011 Bankr. LEXIS 5633 (Bankr. E.D. Cal. 2011).

Medical conditions are compelling:

Courts typically find "special circumstances" that justify additional expenses where disorders, illnesses or disabilities render the person needing support unable to work or that require a debtor to pay expenses for medical treatment. *See, e.g.*, *In re Chabre*, 531 B.R. 875, 879 (Bankr. M.D. Fla. 2015) (allowing the debtor's additional expenses as special circumstances where the debtor supported relatives with "chronically poor health" and "disabilities that prevent their employment"); *In re Davis*, 2011 Bankr. LEXIS 4493, (Bankr. N.D. Tex. 2011) (allowing the debtors' $300 savings expense as a special circumstance for the wife's treatment for malignant melanoma); *In re*

Edwards, 2010 Bankr. LEXIS 823, (Bankr. E.D.N.C. 2010) (allowing a debtor's additional expenses as special circumstances where she suffered a severe stroke rendering her "totally disabled" and "unable to live without constant medical care"); *In re Haman*, 366 B.R. 307, 315 (Bankr. D. Del. 2007) (allowing the debtor to pay as co-signor on her son's nondischargeable student loan debt as a special circumstance where son's medical condition rendered him unable to make the payments).

Debtors must have concrete evidence rather than opinion or conjecture.

In re Behne, 575 B.R. 893 (Bankr. Neb. 2017). Debtor paid utilities for his adult daughter and her two small children to provide her a safe and secure home so that she would not resume drinking and lose her employment. These special circumstances were disallowed because debtor failed to offer medical evidence of daughter's conditions and evidence that his financial support provided what she needed to stay sober and remain employed. *See, e.g., In re Delunas,* 2007 Bankr. LEXIS 803 (Bankr. E.D. Mo. 2007) (holding that the debtors failed to show that remaining in their current residence was necessary where the debtors feared that moving would worsen their daughter's depression and stating that the debtors' concerns were insufficient without "qualified medical evidence offered in support of [their] belief"); *In re Oliver*, 350 B.R. 294 at 303 (Bankr. W.D. Tex 2006) (holding that the debtor failed to show medical expenses for his diagnosed depression, anxiety and bipolar disorder were necessary without "provid[ing] any corroborating evidence of how these conditions were affecting his income or expenses); *see also In re Stanley,* 438 B.R. 860, 865 (Bankr. D.S.C. 2010*)*. Holding that the debtors failed to show special circumstances because, although they proved the wife had severe depression, they could not prove the debt maintenance they sought to pay was "reasonable and necessary" where they incurred it as a result of the wife's excessive purchasing to cope with her depression.

Is it a Marital Adjustment or Special Circumstances?

Usually, if something does not fit into the marital adjustment or the standard deductions of the Form 122C, the common tactic by debtors is to try to take the expense deduction as a special circumstance. The focus of the marital adjustment deduction is whether the expense is purely personal to the NFS. The focus of the special circumstances is the §707(b)(2)(B)(i) language. Notably the marital adjustment in Chapter 13 is in the Form 122C-1 calculation of the commitment period. If a debtor has a deduction that might qualify for either the marital adjustment or a special circumstance, it generally will help the debtor to claim this deduction as a marital adjustment deduction in the Form 122C-1 in an effort to qualify for the 36-month commitment period. If used as a special circumstance, that indicates the case has already been deemed a 60-month commitment period case. The debtor basically gets more bang for the deduction if successful in using it as a marital adjustment.

Line 46 – Change in Income or Expenses (Lanning Line)

Hamilton v. Lanning, 560 U.S. 505 (2010), hereafter "Lanning," did not eliminate Form 122C-2. 11 U.S.C. §1325(b)(3) still exists and was not repealed. Section 1325(b)(3) incorporates the deductions under §707(b)(2)(A) and (B) which is the second part of the Means Test. Line 46 was added to Form 122C-2 after the decision of Lanning. *See also, In re Scott,* 2013 WL 5567319 (Bankr. N.D. Ohio 2013) ("[t]he court's discretion to take such changes into account does not, however, allow it to alter the Bankruptcy Codes' formula for calculating an above-median income debtor's disposable income [under Form 122C-2].")

If asserting a post-petition reduction in income, then also provide for the related reduction in taxes on income, reduction in retirement contributions, and show your calculations so we understand how you obtained the numbers. Provide evidence. Debtors always say they will no longer get the overtime, and when we ask for the post-petition pay advices, all of the overtime is usually still there. Save yourself time and get your client's documents that prove the request. Good examples of Lanning income reduction: debtor no longer has a second job, the spouse no longer works, or there is a new job at a lower salary.

The Lanning line works both ways, if the income increases or expenses are reduced, it can be used to increase the disposable income.

The Lanning Line is a great way to adjust for bonuses. For purposes of making the plan affordable, Line 2.4 of the Plan should provide that Debtor will pay the Trustee the net bonus each year.

Common problems:

- Figures used are not supported by the pay advices.
- Use the gross amount of pension payments on Form 122C-1.
- Allowable expenses that we see on Schedule J are omitted from 122C-2.
- NFS marital adjustment items are put in the body of Form 122C-2, instead of 122C-1. A marital adjustment item is the actual amount pro-rated over 60 months, and Form 122C-2 uses standards.

- Priority taxes overstated.

- Not using the maximum administrative expense of 10%.

- If debtor receives child support, review whether the debtor is eligible to take deductions for child support used to support the child. If the child is still a dependent this deduction is likely always applicable. (Line 40)

- Provide NFS pay advices, tax returns and credit card statements – always.

- Provide balance due on NFS' vehicle and date the vehicle loan will be paid in full. Provide balance due on NFS' 401(k) loan and date the loan will be paid in full.

- Most cases where debtor is self-employed or operates a business the debtor must have liability insurance. Be sure they have it and send us proof. Send us personal and business bank statements for the 6 month period.

- Properly calculate the §1325(a)(4) liquidation calculation. Bankruptcy Code Section 726 provides for the order of distribution in Chapter 7. Priority claims under Section 507 are paid before unsecured creditors. Thus, priority claims can be deducted from the liquidation value of a non-exempt asset in arriving at the required amount to be distributed to unsecured creditors.

- Amended plans, budgets, and Form 122C should be filed with the Court, not emailed or sent to our portal.