Disposable Income Requirements under Chapter 13 of the Bankruptcy Code

Robert G. Drummond
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I. INTRODUCTION

Chapter 13 of the Bankruptcy Code offers unique benefits to debtors seeking to reorganize their financial affairs and to creditors seeking repayment of all or a portion of their debts. Under Chapter 13, debtors may retain non-exempt assets in return for committing a portion of their future income to repay their creditors. This portion of the debtor’s future income which must be committed to repay creditors is known as disposable income. The disposable income requirement was added to Chapter 13 by the Bankruptcy Amendments and Federal Judgeship Act (BAFJA) of 1984.1 Disposable income requirements are important as a means for creditors and Trustees to ensure that they will receive maximum repayment when consumer debtors seek to reorganize their financial affairs under Chapter 13 of the Bankruptcy Code.2

Creditors are becoming increasingly active in the confirmation process by looking to the disposable income requirement as a way to oppose confirmation. Creditors and Trustees may object to confirmation of Chapter 13 plans which appear to allow the debtor to reorganize without committing as much income as

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possible to funding the plan. Creditors and Trustees are searching for means of applying new-found disposable income to payments under the plan in order to increase the amount paid on allowed claims. Trustees and creditors recognize that increasing the scope of the disposable income requirement will result in increased distributions to creditors.

In reorganizing under Chapter 13, debtors have employed a variety of methods in attempting to minimize the disposable income requirement. Debtors often seek to expand the scope of reasonable expenses which they believe are necessary to maintain their households. Also, debtors may claim that income is protected from the disposable income requirement because the income is from exempt sources, or that the income is reasonably necessary for maintenance of the debtor and his dependents.

Furthermore, debtors operating under the terms of a confirmed Chapter 13 plan may face future unanticipated changes in their disposable income which creditors and Trustees may seek to have committed to the creditors under the terms of a modified plan. Debtors are seeking means to prevent being forced to commit such unanticipated disposable income to Chapter 13 plans. In this regard, debtors may argue that the income was not part of their "projected" disposable income and, thus, is beyond the reach of creditors and the Trustee. In sum, the disposable income requirement under Chapter 13 is an important factor for creditors and debtors to examine carefully, both at the time a decision is made to file a consumer bankruptcy and throughout the term of the consumer reorganization plan.

However, the disposable income requirement is a flexible concept which has challenged the interpretive power of the courts. Consequently, courts have struggled to balance the interests of creditors and debtors both in defining the disposable income requirement and weighing exactly what expenses are reasonable and necessary for maintenance of the debtor's household. In striking a balance between the interests of creditors and debtors with respect to the disposable income requirement, courts have sought to refrain from interfering with the debtor's lifestyle while determining which expenses the debtor should be allowed to incur.

This article examines the disposable income requirement, its evolution, and its future in Chapter 13. Part II discusses the evolution of the disposable income requirement through its codification under BAFJA in 1984. Part III discusses the funding of a Chapter 13 plan and the implications of such funding for the
disposable income requirement. Part IV examines problems in determining the composition of disposable income. Finally, Part V discusses a major area of controversy with respect to the disposable income requirement—determining the allowable expenses of the debtor.

II. THE DISPOSABLE INCOME REQUIREMENT

A. Income Requirements Pre-1984

Under the old Chapter XIII of the Bankruptcy Act, debtors were not required to commit a specific portion of their income to payments under a Chapter 13 plan. However, the courts retained a general power of supervision over the future earnings of the debtor during the period of the plan. The same was the case under the Bankruptcy Reform Act of 1978 (1978 Act). The 1978 Act contained no explicit disposable income requirement. The 1978 Act merely transferred the general power of supervision over the future income of the debtor from the court to the Trustee. Consumer reorganization cases under the 1978 Act did not require a debtor to pay general unsecured creditors any more than they would have received under a liquidation in Chapter 7.

Furthermore, payments to unsecured creditors under the 1978 Act bore no relationship to the debtor's income or the amount of individual unsecured debts. Neither the debtor's projected nor actual income was considered as a criterion in the confirmation process. No requirement existed as to the portion of a debtor's income which had to be committed to payments under the plan. Payments to the unsecured class of creditors were

4. The pre-1978 Bankruptcy Act provided that a plan "shall provide provisions for the submission of future earnings or wages of the debtor to the supervision of the court for the purposes of enforcing the plan." 11 U.S.C. § 1046(4) (1976).
6. The Code states that a Chapter 13 plan shall "provide for the submission of all or such portion of future earnings or other future income of the debtor to the supervision and control of the trustee as is necessary for the execution of the plan." 11 U.S.C. § 1322(a)(1) (1994).
7. The requirement that Chapter 13 debtors pay creditors at least as much as they would have received if the debtors had filed under Chapter 7 is commonly known as the "best interests of the creditors" test, which appears at 11 U.S.C. § 1325(a)(4) (1994).
either dictated in terms of a minimum percentage to be paid to the class of unsecured creditors or by specific payment schemes which provided for exact payments to some creditors. The debtor often scheduled payments to the class of unsecured creditors without examining the claims filed by unsecured creditors or being aware of the total amount of claims filed.

As can be seen from the foregoing discussion, the interests of unsecured creditors were often neglected under the 1978 Act. Creditors had no way of accessing additional income which the debtor received over and above his regular monthly expenses. That was true for the periods before and after confirmation. Under this system, the debtor's motivation to pay any more than necessary to meet the best-interests-of-creditors test was purely voluntary.

**B. Court Ordered Income Requirements Pre-1984**

Prior to the addition of the 1984 amendments, courts had begun to shift from an approach based on minimum percentage payment requirements to one making confirmation contingent upon a debtor's ability to make payments based on household income and expenses. Courts began to reason that the "good faith" confirmation requirement obliged debtors to make at least some payment to their unsecured creditors under a Chapter 13 plan. Those courts attempted to impose some kind of a minimum payments rule on Chapter 13 debtors.

However, courts split with respect to whether Chapter 13 plans which did not commit payments to the unsecured class met the good faith requirements. Many courts required varying

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12. Tenny v. Terry (In re Terry), 630 F.2d 634, 635 (8th Cir. 1980); Ravenport v. Rimale (In re Rimale), 669 F.2d 426, 431 (7th Cir. 1982); Lawrence Tractor Co. v. Gregory (In re Gregory), 705 F.2d 1118, 1121-23 (9th Cir. 1983) (confirming a plan providing for nominal payment). This was further complicated by variations in application of the good faith test. Compare In re Beaver, 2 B.R. 337, 341 (Bankr. S.D. Cal. 1980 (using an objective test and finding that the "best effort" of the debtor was not enough to fulfill the good faith requirement where repayment to the creditors was only one percent) with Ravenot v. Rungale, 669 F.2d 426, 432 (Bankr. 7th Cir. 1982) (remanding for application of a subjective test in which bankruptcy court must evaluate whether "proposed payments indicate 'a fundamental fairness in dealing with one's creditors'").
percentages to be paid to the unsecured class, even though such payment may not have been necessary for the debtor to meet the best interests of creditors test.\textsuperscript{13} Some debtors, seeking to circumvent these distribution requirements, would propose plans to pay one percent of the claims in the unsecured class.

The 1978 Act introduced the "feasibility test"\textsuperscript{14} and the "best interests of creditors test"\textsuperscript{15} under the same section as the good faith confirmation requirement.\textsuperscript{16} Some courts relied only on those two tests when examining payments committed under the Chapter 13 plan.\textsuperscript{17} Those courts would confirm a plan if the debtor demonstrated that the payments could be made and that the unsecured creditors would receive at least as much as they would have received if the debtor had filed a Chapter 7 petition.\textsuperscript{18} Thus, such courts took no account of the debtor's income and measured only whether the debtor could afford to pay, or whether the creditors would receive at least as much as they would have received under a Chapter 7 liquidation. Where the debtors planned to pay their creditors at least as much as they would have received under Chapter 7, the plans were often confirmed without further scrutiny.\textsuperscript{19}

\textsuperscript{13} See infra note 15 and accompanying text.
\textsuperscript{14} The feasibility test states: "Except as provided in subsection (b), the court shall confirm a plan if the debtor will be able to make all payments under the plan and to comply with the plan." Public L. No. 95-598, 92 Stat. 2549, 2649 (1978) (codified at 11 U.S.C. § 1325(a)(6)).
\textsuperscript{15} The best interests of the creditors test states:
Except as provided in subsection (b), the court shall confirm a plan if the value, as of the effective date of the plan, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under chapter 7 of this title on such date.

\textsuperscript{16} Under the old chapter XIII, creditors were entitled to vote on a plan under 11 U.S.C § 1056(a)(4). Fearing that this would vest so much power in the creditors that debtors would avoid chapter XIII, Congress enacted the feasibility test to replace it. H.R. Rep. No. 595, 95th Cong., 1st Sess. 123-24 (1977).
\textsuperscript{18} In re Wolf, 22 B.R. 510, 513 (Bankr. 9th Cir. 1982); In re Garcia, 6 B.R. 35, 37 (Bankr. D. Kan. 1980).
\textsuperscript{19} 11 U.S.C. § 1325(a)(4) (1994); In re Wolf, 22 B.R. 510, 513 (Bankr. 9th Cir. 1982).
C. Legislative Responses Pre-1984

Prior to the 1984 Amendments, Congress too had begun to look at ways in which a Chapter 13 debtor could be compelled to commit income for the benefit of creditors. In 1980, Congress passed legislation which would have amended Chapter 13 to add a "good faith effort" confirmation requirement. Two years later, Congress considered legislation which prohibited a debtor from filing a Chapter 7 Bankruptcy if he could pay a reasonable portion of his debts.

In 1980, the Senate passed a bill which would have added a confirmation requirement that the plan represent "the debtor's bona fide effort." Two years later, the Senate considered a bill which eliminated a debtor from Chapter 7 eligibility if he could pay a portion of his pre-petition debts out of projected future income. Such a proposal would have enabled the courts to apply a mechanical test at the time of confirmation. The Senate report indicated that repayment of 75% of the nonmortgage debt would be a reasonable portion and 25% would be considered unreasonable. The Bankruptcy Court could determine what amount was reasonable for a debtor to repay between 25% and 75%. Senate Bill 2000 failed to pass and was reintroduced in the 98th Congress. Later, the projected future income test was replaced with the substantial abuse test under Chapter 7.

D. Changes Under BAFJA

The 1984 amendments to the code added the disposable income requirement as a condition for confirmation of a debtor's proposed Chapter 13 plan. The disposable income requirement was added at Section 1325(b) of the Code, which provides:

If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the Court may not approve the plan unless, as of the effective date of the plan —
(A) the value of the property to be distributed under the plan

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23. Id.
26. Id.
on account of such claim is not less than the amount of such claim; or (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. 27

The disposable income requirement arises in cases in which unsecured creditors may be discharged without receiving payment of 100% of their allowed claim. 28 The disposable income requirement provides that, in the face of an objection by an unsecured creditor or the Trustee, the debtor must propose a plan which commits 100% of his projected disposable income to payments under the plan. 29 Disposable income is defined in the Code as:

[Income which is received by the debtor and which is not reasonably necessary to be expended (A) for the maintenance or support of the debtor or a dependent of the debtor; and (B) if the debtor is engaged in business, for the payment of expenditures necessary for the continuation, preservation, and operation of such business. 30

Thus, in the event that creditors were not being paid in full, Congress authorized the courts to measure a debtor's ability to pay when confirming a Chapter 13 plan. 31 Under the provision, the court may not confirm the plan in the face of an objection from the Trustee or a creditor. Presumably no objection would be raised by the Trustee or a creditor when a plan paid 100% of all unsecured claims. 32

It was noted that the disposable income test, if invoked by unsecured creditors or the Trustee, should serve as the standard for determining whether the debtor is reasonably capable of paying more than originally proposed. 33 Complimenting the dis-

28. The applicable statute for allowance of claims provides that “[a] claim or interest, proof of which is filed under section 501 of this title, is deemed allowed, unless a party in interest, including a creditor of a general partner in a partnership that is a debtor in a case under chapter 7 of this title, objects.” 11 U.S.C. § 502(a) (1994).
32. The courts have made clear that 11 U.S.C. § 1325(b)(1)(B) (1994) requires denial of confirmation of a 100% plan that omits to pay interest on unsecured claims where the plan does not provide that all of the debtor's disposable income be applied to making payments under the plan for three years.
33. Oversight Hearings before the Subcomm. of Monopolies and Commercial law
posable income requirement was the "substantial abuse" provision under Chapter 7. That provision allows the court to dismiss a case when it appears that a consumer debtor has committed substantial abuse. It is substantial abuse of the bankruptcy process when a consumer debtor is able to fund a Chapter 13 plan and has some ability to repay his creditors, but instead seeks the benefit of a discharge under Chapter 7.

E. The 1986 Act

The 1986 Act substituted the word "and" for "or" at the end of Section 1325(b)(2)(A). With that minor amendment, Congress indicated that the disposable income requirement should not exclude the debtor who is engaged in business as a sole proprietor. The provision recognizes that a debtor engaged in business will need to pay the operating expenses of the business and that the operating expenses should be considered when calculating projected disposable income. Thus, the change allows a debtor engaged in business to incur expenses while operating that business and still meet the disposable income requirement.

III. FUNDING A CHAPTER 13 PLAN

Under BAFJA, the debtor's decision to file the case under Chapter 13 instead of under Chapter 7 remains voluntary. Yet debtors with incomes adequate enough to fund Chapter 13 plans often fail to recognize the substantial benefits and protections Chapter 13 offers over Chapter 7. For example, certain debts which are nondischargeable in Chapter 7 are dischargeable in Chapter 13. Other advantages are that the Chapter 13 debtor


34. The Code provides in pertinent part:
After notice and hearing, the Court, on its own motion or on a motion by the United States Trustee, but not at the request or suggestion of any party in interest, 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. There shall be a presumption in favor of granting the relief requested by the debtor.

36. Zolg v. Kelly (In re Kelly), 841 F.2d 908 (9th Cir. 1988).
37. 11 U.S.C. § 1325(b)(2)(A) (1994) (providing for the maintenance or support of the debtor or a dependent of the debtor).
has an absolute right to dismiss the case\textsuperscript{39} and has the ability to strip down and restructure certain secured debts,\textsuperscript{40} classify debts\textsuperscript{41} and retain non-exempt property.\textsuperscript{42}

A. Income and Property of the Estate

Property of the bankruptcy estate is defined at Section 541 of the Bankruptcy Code and includes all legal and equitable interests of the debtor at the commencement of the case.\textsuperscript{43} Congress expanded the definition of property of the estate for individuals involved in Chapter 13 cases by the enactment of Section 1306 of the Code. That section broadens the definition of property of the estate to include earnings from services performed by the Chapter 13 debtor after the commencement of the case, but

\begin{itemize}
\item \textsuperscript{39} 11 U.S.C. § 1328 (1994).
\item \textsuperscript{41} 11 U.S.C. § 1322(b)(1) (1994).
\item \textsuperscript{42} 11 U.S.C. § 1325(a)(4) (1994).
\item \textsuperscript{43} The code defines property of the estate as follows:
\begin{enumerate}
\item The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:
\begin{enumerate}
\item Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.
\item All interests of the debtor and the debtor's spouse in community property as of the commencement of the case that is—
\begin{enumerate}
\item under the sole, equal, or joint management and control of the debtor; or
\item liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable.
\end{enumerate}
\item Any interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 of this title.
\item Any interest in property preserved for the benefit of or ordered transferred to the estate under section 510(c) or 551 of this title.
\item Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date—
\begin{enumerate}
\item by bequest, devise, or inheritance;
\item as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree; or
\item as a beneficiary of a life insurance policy or of a death benefit plan.
\end{enumerate}
\item Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.
\item Any interest in property that the estate acquires after the commencement of the case.
\end{enumerate}
\end{enumerate}
\end{itemize}

\textsuperscript{11} U.S.C. § 541(a) (1994).

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before the case is closed, dismissed, or converted.\textsuperscript{44} Section 1306 represents an expansion of the class of eligible debtors from the former Chapter XIII to include debtors whose income is from exempt sources.\textsuperscript{45}

In enacting section 1306, Congress correctly recognized that consumer debtors include a class of petitioners who receive income from sources other than employment or services performed. Retirees, health and welfare benefit recipients, devisees, and others may qualify as "individuals with regular income" for purposes of qualifying for eligibility under Chapter 13.\textsuperscript{46}

Congress recognized that debtors should be entitled to fund a Chapter 13 plan with pensions and social security income and that such benefits could not be used to fund a consumer reorganization plan if they were not property of the estate.\textsuperscript{47} The Senate report for the Bankruptcy Code noted that Chapter 13 of the old Bankruptcy Act was defective because it did not permit some individuals with regular income from sources such as social security and pensions to qualify because their incomes did not come from "wages, salaries or commissions."\textsuperscript{48} Both Senate and House reports indicated that individuals with pension, social security or investment incomes should be able to work out payment plans with their creditors rather than seeking discharge under Chapter 7.\textsuperscript{49}

Courts acknowledged that the purpose of the revision was to make social welfare recipients eligible for Chapter 13 relief.\textsuperscript{50}

\textsuperscript{44.} The Code provides in pertinent part:
(a) Property of the estate includes, in addition to the property specified in section 541 of this title—
(1) all property of the kind specified in such section that the debtor acquires after the commencement of the case but before the case is closed, dismissed, or converted to a case under Chapter 7, 11, or 12 of this title, whichever occurs first; and
(2) earnings from services performed by the debtor after the commencement of the case but before the case is closed, dismissed, or converted to a case under Chapter 7, 11, or 12 of this title, whichever occurs first.
(b) Except as provided in a confirmed plan or order confirming a plan, the debtor shall remain in possession of all property of the estate.

\textsuperscript{11}U.S.C. \textsuperscript{\textregistered} 1306 (1994).

\textsuperscript{45.} United States v. Devall, 704 F.2d 1513, 1515-16 (11th Cir. 1983).

\textsuperscript{46.} 11 U.S.C. \textsuperscript{\textregistered} 101(30) (1994).


\textsuperscript{50.} \textit{See, e.g.,} Toson v. United States, 18 B.R. 371, 373 (Bankr. N.D. Ga. 1982).
However, courts acknowledged that the revision gave them no authority to order the Social Security Administration to pay over benefits to the Bankruptcy Trustee. But social security benefits can be used to fund a Chapter 13 debtor's plan if the debtor proposes such a plan. The anti-assignment provisions of the 1984 Act prohibited the involuntary assignments of social security benefits. Therefore, the Bankruptcy Court cannot order the transfer of social security benefits directly to the Trustee, but the debtor may voluntarily submit to such an order.

Property of the estate also includes post-petition income, whether from exempt sources or not, and is correctly applied to fund a Chapter 13 plan. By making post-petition income property of the bankruptcy estate, Congress ensured that certain income would not be put beyond the reach of the disposable income requirement. Congress made clear that income received by a debtor after the filing of the petition, whatever its source, may be considered as property of the estate, used to fund a Chapter 13 plan, and applied to meet the disposable income requirement. In sum, the 1984 Amendments significantly expanded the availability of Chapter 13 and offered new advantages to both creditors and debtors in Chapter 13 relief.

B. An Individual With Regular Income

The Code provides certain eligibility requirements for Chapter 13 relief. To be eligible for Chapter 13 relief, the debtor

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51. *Devall*, 704 F.2d at 1516 (holding a debtor may voluntarily fund a plan with social security income).

52. The debtor is the only party that may propose a plan at the commencement of a case. 11 U.S.C. § 1321 (1994).


55. *In re Hagel*, 13 Mont. B.R. 377 (1994), aff'd, 184 B.R. 793, 797 (Bankr. 9th Cir. 1995).

56. *Devall*, 704 F.2d at 1513.

57. The Code provides in pertinent part:

Only an individual with regular income that owes, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts of less than $250,000 and noncontingent, liquidated, secured debts of less than $750,000, or an individual with regular income and such individual's spouse, except a stockbroker or a commodity broker, that owe, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts that aggregate less
must demonstrate that he is an individual with regular income. As one court recognized:

Obviously, the thrust of the Chapter 13 revision was to make its provision available to a range of persons wider than the prior law. Expansion of the class to whom Chapter 13 is available comports with the basic legislative goal: to encourage financially overextended individual debtors to make greater use of voluntary repayment plans and thereby improve debtor relief, by allowing ratable distribution of future income without necessarily liquidating their non-exempt assets, and creditor recovery, by guaranteeing repayment of most, if not all, of the claims over an extended period.

Without a source of regular income from employment or some other source, the debtor will be unable to fund a Chapter 13 reorganization plan. It follows that the regular income requirement was imposed for eligibility purposes.

C. Disposable Income Is Based on Income from All Sources

I. Income from Exempt Sources

All of the debtor's income is to be included in the calculations of projected disposable income. Nontaxable income, such as personal injury damages, government benefits, and inheritances have been determined to justify modification to reflect increased disposable income. The court In re Schnabel recognized:

As Judge Lundin noted, §1325(b) does not qualify income by reference to its exempt status. Where there is no express limitation in the text, the Debtor bears an “exceptionally heavy” burden of persuading the Court that Congress intended one. In

than $250,000 and noncontingent, liquidated, secured debts of less than $750,000 may be a debtor under chapter 13 of this title.


58. 11 U.S.C. § 101(30) (1994) (defining an individual with regular income as an “individual whose income is sufficiently stable and regular to enable such individual to make payments under a plan under chapter 13 of this title, other than a stockbroker or a commodity broker”).


63. See also Agribank, FCB v. Honey (In re Honey), 167 B.R. 540 (Bankr. W.D. Mo. 1994).
Patterson, the Supreme Court considered whether "applicable nonbankruptcy law" in §541(c)(2) referred only to state law. The Court found that "[t]he text contains no limitation on 'applicable nonbankruptcy law' relating to the source of the law" and refused to impose one. Similarly, without an express or even implicit limitation in §1325(b)(2) on "income" relating to its exempt status, this Court will not impose one. The Debtor's social security and pension payments are "income[ ] received by the debtor," and, to the extent not reasonably necessary for support, must be devoted to the repayment of unsecured creditors.64

The Schnabel Court correctly ruled that exempt income contributes to disposable income to be paid under the Chapter 13 plan.65 Debtors should be required to commit exempt income to payment of reasonable living expenses prior to committing income from nonexempt sources to the payment of such expenses. The disposable income requirement does not exclude income from exempt sources.66

Where a portion of the household income was derived from exempt sources (social security income), the debtors would be required to spend the exempt income on the expenses which were reasonably necessary for the maintenance of their household prior to any other expenses.67 Thus, the debtors would be left with the nonexempt income for full funding of the plan and meeting the disposable income requirement. One court recognized that to allow debtors to retain exempt income without committing it to payments under the Chapter 13 plan thwarts the legislative intent of Chapter 13.68 Recognizing that Chapter 13 offers the benefits of a broader discharge than one under Chapter 7,69 the court found that consumer lenders should be able to

66. Hagel, 184 B.R. at 796.
67. Id. at 796.
68. In re Minor, 177 B.R. at 580 (quoting In re Schnabel, 153 B.R. 809, 818 (Bankr. N.D. Ill. 1993)).
look to the debtor’s exempt income for the repayment of consumer loans as a quid pro quo for the broader discharge provisions of Chapter 13.70

Issues have arisen at the time of confirmation regarding whether income from exempt sources is property of the estate. The definition of “property of the estate” is different from the definition of “disposable income.” An estate in bankruptcy consists of all the interests in property, legal and equitable, possessed by the debtor at the time of filing and the income the debtor receives before the case is closed.71 “An exemption is an interest withdrawn from the estate (and hence from the creditors) for the benefit of the debtor.”72 The property which may be exempted must first become property of the estate.73 Property of the estate includes virtually all of the debtor’s property, while disposable income includes only that income not necessary for the maintenance of the debtor or dependents of the debtor.74 Thus, the debtor may support himself with exempt income, which is property of the estate, thereby leaving non-exempt income available to fund a Chapter 13 plan.

2. Disposable Income Is Distinct from Taxable Income

Disposable income is unrelated to income from a taxable income approach. Courts have held that the definition of “income” for the purpose of computing disposable income “is not necessarily calculated or premised on a strict Tax Code approach . . . .”75 The calculation of disposable income differs from the Tax Code approach because it relates to both the debtor’s income and expenses.76 Also, the debtor’s spouse’s income contributes to the maintenance of the household and therefore must be included in the disposable income calculation.77 An increase in the debtor’s income prior to confirmation could effect dispos-


73. Id.
able income, but only if there is no change in the debtor's related expenses.\(^7\)

IV. DETERMINING COMPOSITION OF DISPOSABLE INCOME

A. Actual Versus Projected Disposable Income

Although the statute clearly refers to "projected" disposable income, courts are split as to whether the projected disposable income requirement under Chapter 13 should be based on "actual" disposable income or "projected" disposable income. Commentators have recognized that the calculation of projected disposable income may be difficult, if not impossible. For example, Collier states:

To some extent this task is, of course, impossible. The court has no way of knowing whether debtors will continue to work at their current incomes, or whether they will be laid off or become disabled or suffer other diminutions of income. The court does not know whether the debtor will live for three years.\(^7\)

The disposable income issue becomes complicated when determining whether the court must project disposable income or rely on actual income figures. In Rowley v. Yarnall,\(^6\) the Eighth Circuit determined that a Chapter 12 debtor must commit all actual disposable income in order to meet the disposable income test.\(^8\) The Rowley court reasoned that in a Chapter 12 case "projected disposable income" means the net disposable income actually received by the debtors during the plan period. The court stated:

We hold that section 1225(b)(1)(B) imposes a duty on debtors to include a provision in their reorganization plan that promises payment of net disposable income received during the plan period to unsecured creditors in the event that the Trustee or holder of an allowed unsecured claim objects to confirmation of

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79. 5 *Collier on Bankruptcy*, § 1325.08, at 1325-67 (Lawrence P. King, ed., 15th ed. 1995).
80. 22 F.3d 190 (8th Cir. 1994).
81. Chapter 12 includes a disposable income requirement identical to that appearing under Chapter 13:

[T]he plan provides that all of the debtor's projected disposable income to be received in the three-year period, or such longer period as the court may approve under section 1222(c), beginning on the date that the first payment is due under the plan will be applied to make payments under the plan.

the plan.\textsuperscript{82}

In \textit{In re Anderson},\textsuperscript{83} however, the Ninth Circuit Court of Appeals correctly determined that projected disposable income is the income that the debtor projects he will receive at the time of confirmation of the plan.\textsuperscript{84} The \textit{Anderson} court held that actual disposable income can only be paid after a Trustee or party in interest requests and obtains an order for modification of a Chapter 13 debtor's plan.\textsuperscript{85} Only after a court-approved modification of the plan would any increased disposable income of the debtor have to be paid over to the Trustee.\textsuperscript{86}

In \textit{Anderson}, the Trustee requested that the debtors sign a "best effort certification" which would constitute an agreement by the debtors to pay all actual disposable income to the Trustee.\textsuperscript{87} The Trustee would review the actual income on a periodic basis and adjust their payments without further order of the court, according to his determination of their annual income.\textsuperscript{88} The Andersons refused to sign the certification, and the bankruptcy court denied confirmation of their Chapter 13 plan.\textsuperscript{89} The district court affirmed the bankruptcy court's order denying confirmation.\textsuperscript{90} The Ninth Circuit Court of Appeals determined that Section 1325(b)(1)(B) requires "payment of all projected disposable income" as calculated at the time of confirmation and rejected the Trustee's attempt to impose a more burdensome requirement.\textsuperscript{91} The court suggested that, in the event the debtor's disposable income increases, the Trustee may request modification of a plan.\textsuperscript{92} Thereupon, the Trustee has the burden of showing a substantial change in the debtor's ability to pay since the confirmation hearing.\textsuperscript{93} The Trustee must also show that the prospect of the change had not been taken into account at the time of confirmation.\textsuperscript{94} The court recognized that, by providing the Section 1329 mechanism to modify a confirmed plan,

\begin{footnotesize}
\textsuperscript{82} Rowley, 22 F.3d at 193.
\textsuperscript{83} 21 F.3d 355 (9th Cir. 1994).
\textsuperscript{84} \textit{Id.} at 358.
\textsuperscript{85} \textit{Id.}
\textsuperscript{86} \textit{Id.}
\textsuperscript{87} \textit{Anderson}, 21 F.3d at 356-57.
\textsuperscript{88} \textit{Id.}
\textsuperscript{89} \textit{Anderson}, 21 F.3d at 357.
\textsuperscript{90} \textit{Id.}
\textsuperscript{91} \textit{Id.} at 357.
\textsuperscript{92} \textit{Id.} at 358.
\textsuperscript{93} \textit{Anderson}, 21 F.3d at 358.
\textsuperscript{94} \textit{Id.} at 357.
\end{footnotesize}
Congress plainly did not vest Trustees with unfettered authority to adjust payments under the terms of the confirmed Chapter 13 plan. 95

In view of Anderson, it appears that the Trustee must monitor debtors’ actual income in order to make a determination about whether to seek a modification under Section 1329. Implementing such a requirement would be extremely burdensome on the Trustee. The Trustee would be required to monitor actual income figures for thousands of debtors, a task which would render the Trustee’s duties impractical and uneconomical.

Other courts have taken a middle course and attempted to impose a fixed percentage of changes in income to be paid under the terms of the plan. 96 Such treatment may be questionable when the projected disposable income cannot be calculated. Yet, such a requirement appears to anticipate future changes in the debtor’s income. In view of the fact that Congress provided for changes in disposable income by providing a mechanism for modification of a confirmed plan, such treatment may lack fairness and practicality. Changes in projected disposable income generally cannot accurately be calculated for a period of years into the future. Debtors may anticipate such changes, but generally cannot be certain that they will occur. Debtors should not be expected to guarantee such changes. And, as noted, the Trustee may propose a modification if changes occur in the debtor’s disposable income.

B. Calculating Projected Disposable Income

The disposable income requirement is correctly limited to “projected” disposable income. As the Ninth Circuit Court of Appeals recognized:

The language of the statute is clear. If the holder of an allowed unsecured claim or trustee objects to the confirmation of a Chapter 13 plan and the plan proposes less than full payment of a creditor’s claim, the plan may be approved only if “as of the effective date of the plan”, it provides for payment of “all of the debtor’s projected disposable income to be received in a three year period beginning on the date that the first payment is due under the plan . . . .” The Fifth Circuit, in Matter of Killough, described the two-part process for arriving at . . . [the] “project-
ed disposable income” figure. “For practical purposes, this task is usually accomplished by multiplying the debtor’s monthly income by 36. Next, the Bankruptcy Court must assess the amount of the debtor’s income that is ‘disposable’. Projected disposable income is usually calculated by multiplying the debtor’s monthly income by the number of months in the plan. From this amount, the debtor’s expenses are subtracted. As seen above, unanticipated increases in disposable income may constitute a change in circumstances warranting modification of the plan. The Trustee may then seek to modify the plan in order to increase plan payments based on the debtor’s increased disposable income. The debtor has a duty to report interests acquired in property after the petition. Furthermore, the debtor has a duty to cooperate with the Trustee and must transfer books and records to the Trustee. Thus, the Trustee has a means to monitor and propose modified plans according to changes in the debtor’s disposable income. However, the Trustee lacks the authority to alter the amount of a debtor’s payments unilaterally.

97. Anderson, 21 F.3d at 357 (internal citations ommitted).
98. Id.; see also 11 U.S.C. § 1329(c) (1994).
99. Anderson, 21 F.3d at 358.
100. Id. The Code provides in pertinent part:
(a) 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, to—
(1) increase or reduce the amount of payments on claims of a particular class provided for by the plan;
(2) extend or reduce the time for such payments; or
(3) alter the amount of the distribution to a creditor whose claim is provided for by the plan to the extent necessary to take account of any payment of such claim other than under the plan.
(b)(1) Sections 1322(a), 1322(b), and 1323(c) of this title and the requirements of section 1325(a) of this title apply to any modification under subsection (a) of this section.
(b)(2) The plan as modified becomes the plan unless, after notice and a hearing, such modification is disapproved.
(c) A plan modified under this section may not provide for payments over a period that expires after three years after the time that the first payment under the original confirmed plan was due, unless the court, for cause, approves a longer period, but the court may not approve a period that expires after five years after such time.
102. FED. RULE BANKR. PROC. 1007(h) (1996).
104. The Code provides that the confirmed plan is binding on the debtor and each creditor:
In calculating disposable income, courts have mistakenly distinguished between income from exempt sources and income from the proceeds of an exempt asset. In this regard, the Bankruptcy Appellate Panel for the Ninth Circuit recently confirmed that the disposable income requirement does not distinguish between types of income. The court correctly held that social security income, although exempt, should be included in disposable income and used to fund a plan. Nonetheless, the Panel erroneously noted a distinction between funding a plan with an exempt stream of income—such as social security income—and funding a plan with the sale or liquidation of an exempt asset—such as a personal injury claim. Such reasoning fails to recognize that liquidation of exempt assets can also generate additional disposable income for the purposes of funding a plan. Also, the debtors' ability to claim an exemption is independent from their ability to repay debts. In sum, the source of income is irrelevant to the calculation of disposable income and courts should include income from the proceeds of exempt assets in that calculation.

V. DETERMINING THE REASONABLENESS OF THE DEBTOR'S EXPENSES

(a) The provisions of a confirmed plan bind the debtor and each creditor, whether or not the claim of such creditor is provided for by the plan, and whether or not such creditor has objected to, has accepted, or has rejected the plan.

(b) Except as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor.

(c) Except as otherwise provided in the plan or in the order confirming the plan, the property vesting in the debtor under subsection (b) of this section is free and clear of any claim or interest of any creditor provided for by the plan.


106. In re Hagel, 184 B.R. 793 (Bankr. 9th Cir. 1995).

107. Id. at 799.

108. Id. at 797 n.3.

109. The applicable statute does not distinguish between income from exempt sources and income from the liquidation of exempt assets. See 11 U.S.C. § 1325 (b)(1)(B).

A. Expenses Necessary for Maintenance of the Household

When determining disposable income, problems arise in projecting a debtor's expenses similar to those that arise in projecting income. The court is likewise called upon to speculate about the debtor's living and business expenses over the term of the plan. Collier notes that "[s]uch a projection would require the Court to guess whether the debtor would have additional children, unexpected marital separations, medical bills, home repairs, or a wide variety of other future medical expenses. Obviously, this is impossible." Nonetheless, courts are called upon to determine which expenses are necessary, and generally do so based upon the debtor's best estimates. The courts have applied two tests to determine which income and expenses are reasonably necessary for maintenance in support of the household—the "good-faith" test and the "reasonably necessary" test.

1. The Good Faith Test

Some courts have applied a "good faith" test to measure what is reasonably necessary for maintenance in support of the debtor. The good faith inquiry is applicable to the good faith requirement necessary for continuation under section 1325(a)(6) of the Code. However, courts have confused the good faith requirement with the disposable income requirement. Such confusion probably arises from case law written before the disposable income requirement was enacted. In fact, the good faith inquiry is much broader than the disposable income requirement.

In making a good faith inquiry, the court may look to numerous factors. For example, the court in In re Humphrey held "that as long as the debtors are using all of their disposal income to fund the plan section 1325(b)(1)(B) is satisfied . . . ." That court reasoned that the propriety of the debt or expenses incurred by the debtor is to "be analyzed within the confines of the good faith standard of section 1325(a)(3)." The Humphrey court implied, therefore, that so long as the debtor is spending all of his income and not committing a portion of

111. 5 COLLIER ON BANKRUPTCY ¶ 1325.08, at 1325-68 to -69 (Lawrence P. King ed., 15th ed. 1995).
115. Id. (implying some interaction between the disposable income requirements and the good faith test).
his income to savings, he is using all of his disposable income and meets the disposable income test. Thus, the good faith test may fail to measure whether a particular category of expense is reasonably necessary for maintenance of the debtor or dependents of the debtor. In effect, the good faith approach assumes that all of the debtor’s expenses are reasonable.  

2. The Reasonably Necessary Test

Other courts have correctly recognized that any decision as to whether a particular expense is reasonable depends upon the specific circumstances of the debtor and is best left to the sound discretion of the judge. Some courts have determined that various expenses are not acceptable and that the disposable income test is not met where debtors are committing a portion of their income to expenses which they deem to be unreasonable or unnecessary. These courts correctly recognize that the good faith requirement for confirmation is a separate inquiry from the disposable income requirement. Each debtor’s circumstances are unique and the court should be allowed to make a case by case determination that certain expenses are reasonable. The disposable income test is not contingent on the good faith test. The confusion between the two standards results from those pre-1984 cases in which courts had no other standard to rely on than the good faith standard.

The “reasonably necessary” test at section 1325(b) of the Code only applies to recurring expenses for food, clothing and shelter that are paid directly by the debtor. The reasonably necessary test does not apply to obligations that a debtor is attempting to repay through the plan. Automobile payments made by the Trustee as part of payments under the debtor’s plan are not considered disposable income. On the other hand,

116. This fails to recognize that the Court should inquire into the reasonableness of the expense.
120. This reasoning fails to recognize those instances where a debtor is not paying unsecured claims in full, yet, seeks to pay for luxury items or unnecessary expenses through the plan.
121. But see In re Lindsey, 122 B.R. 157, 158 (Bankr. M.D. Fla. 1991) (holding that making payments for the financial benefit of the debtor through the Chapter 13 Trustee rather than directly by the debtor is not a reason to exclude payments from
payments for "recreation home maintenance, clothing and personal grooming" may detract from disposable income.\textsuperscript{122} In short, any inclusion in the plan of generous sums for unnecessary expenses shows an unwillingness on the debtor's part to modify his lifestyle in order to satisfy his obligations.\textsuperscript{123}

B. A Spending Cushion

Miscellaneous expenses are left to the discretion of the court.\textsuperscript{124} The Bankruptcy Court should not "inject itself" in the debtor's "personal choices" of expenditures of household expenses.\textsuperscript{125} Nor should the debtor's standard of living be altered by the court. On the other hand, the disposable income requirement may call for sacrifice on the debtor's part if it was the debtor's lifestyle that caused him to seek bankruptcy relief.\textsuperscript{126}

However, courts are reluctant to dictate the lifestyle of the debtor. The court should not interfere with such matters as entertainment, movies, cable television, music lessons, sports leagues, health clubs, and education support for children, so long as the court can determine that the expenses are reasonably necessary for the maintenance of the household.\textsuperscript{127} To the extent that the debtor is spending his income on items that are frivolous, or that are not necessary for the maintenance of the household, the court should not hesitate to deny confirmation based on the disposable income requirement.\textsuperscript{128}

However, the courts may allow a general cushion in expenses.\textsuperscript{129} Many debtors wish to propose spending for "miscellaneous" expenses which are not included in any other category of the reasonable necessity test of 11 U.S.C. § 1325(b)(2) (1994)).

123. Whitelock, 122 B.R. at 593.
127. See, e.g., In re Riegodedios, 146 B.R. 691 (Bankr. E.D. Va. 1992) ("All disposable income does not mean debtor's prison . . . .").
128. In re Farmer, 186 B.R. 781, 783 (Bankr. D. R.I. 1995) (relying upon the good faith requirement to deny confirmation where a debtor planned to pay nothing to the unsecured creditors and failed to explain a spending cushion of $150.00 per month).
expenses in the debtor's schedules. The cushion depends upon the amount of the debtor's other household expenses. The debtor's cushion may include his spending in categories of discretionary expenses such as recreation, clothing and entertainment.

The Montana Bankruptcy Court has reasoned that an excessive cushion may be the basis for denial of confirmation. The Trustee and creditors must recognize that the debtor cannot project his expenses accurately for the entire length of the plan. However, the debtor should not be allowed to build in a large cushion based upon unknown future expenses.

C. Luxury Items

Some courts have denied confirmation of proposed Chapter 13 plans because the debtor wishes to retain some type of luxury item. This leaves the court in a quandary about how to define a luxury item. Specifically, courts have encountered difficulty in using a subjective versus an objective approach. What may appear to be a luxury item for one debtor may be a necessity for another. Courts would find an objective approach impossible to administer because debtors' circumstances vary enormously. For example, the size of a debtor's home and the resulting mortgage payments, the type of vehicle owned by the debtor, and the size of expense items for food, utilities, insurance, and clothing all vary tremendously from case to case.

Yet the definition of a luxury item is closely aligned with the definition of "disposable income." Courts have recognized the danger that a debtor may be living a luxurious lifestyle at the expense of the creditors whose claims are being discharged. For example, courts have found that a boat is not necessary for the maintenance of the debtor, and that retention of a second home or additional mortgage payments are not reasonably neces-

133. The Code provides little direction. See 11 U.S.C. § 523(a)(2)(C) (1994) (providing "luxury goods and services do not include goods or services reasonably acquired for the support or maintenance of the debtor").
134. In re Hedges, 68 B.R. 18 (Bankr. E.D. Va. 1986); see also In re Cordes, 147 B.R. 498 (Bankr. D. Minn. 1992) (holding that the good faith test prohibited the debtors from making direct payments for a boat while paying unsecured creditors only 46% of their claims).
These findings preclude confirmation because such unnecessary expenses violate both the disposable income test and the prohibition on unreasonable discrimination among creditors in a class.\textsuperscript{136}

Other courts have employed a more subjective approach to the reasonably necessary test by looking at each individual debtor’s circumstances to determine what is “reasonably necessary” for the maintenance of the debtor’s household. Such courts have generally avoided requiring debtors to make drastic changes in their lifestyles.\textsuperscript{137} A more subjective approach takes into consideration the wide variation in debtors’ needs and circumstances. It means that a court is more likely to show restraint in changing or dictating a debtor’s lifestyle when evaluating the reasonableness of certain expenses.

The debtor, however, may seek to retain a particular luxury item while living a generally frugal lifestyle. Essential activities and expenses go beyond some bare minimum that the debtor requires to live on.\textsuperscript{138} For example, one debtor was allowed to retain three vehicles,\textsuperscript{139} while another was not allowed to retain and pay for a Corvette sports car when payments on a less expensive automobile would be much lower.\textsuperscript{140} These cases reflect that circumstances differ from case to case: one debtor may need several automobiles to provide transportation for several members of his household, whereas another may not need a luxury car to meet transportation needs.

In sum, a debtor who uses post-petition income to pay for a luxury vehicle or any other luxury item, whether directly or through the Trustee, does not apply all of his disposable income to payments to debts under the plan and does not meet the disposable income requirements.\textsuperscript{141} However, the courts are in disagreement as to whether the debtor’s payment of both pre-petition debts and post-petition expenses deduct from the

\textsuperscript{135} In re Cardillo, 170 B.R. 490, 491 (Bankr. D.N.H. 1994).

\textsuperscript{136} In re Kasun, 186 B.R. 62, 64 (Bankr. E.D. Va. 1995).

\textsuperscript{137} In re Tinneberg, 59 B.R. 634, 635 (Bankr. E.D.N.Y. 1986).

\textsuperscript{138} See In re Gonzales, 157 B.R. 604 (Bankr. E.D. Mich. 1993). There ought to be some allocation for recreation, clubs, entertainment, newspapers, magazines, etc.

\textsuperscript{139} In re Marshall, 181 B.R. 599 (Bankr. N.D. Ala. 1995).

\textsuperscript{140} In re Rogers, 65 B.R. 1018 (Bankr. E.D. Mich. 1986); see also In re Reyes, 106 B.R. 155, 158 (Bankr. N.D. Ill. 1989) (denying confirmation where debtor sought to retain “extravagant 4-wheel drive vehicle”); In re Jones, 119 B.R. 996 (Bankr. N.D. Ind. 1990) (denying confirmation where debtor sought to retain luxury car).

\textsuperscript{141} In re Gibson, 142 B.R. 879 (Bankr. E.D. Mo. 1992) (denying confirmation when debtor retained luxury cars by paying for the cars through plan).
debtor's disposable income. But any expenditure for a luxury item effectively detracts from the debtor's disposable income. Thus, the same standard should apply to pre- and post-petition debts.

D. Maintenance and Support of Dependents of the Debtor

A dependent of the debtor may be any person who is reasonably dependent on the debtor for support. This definition is not necessarily related to the definition of dependent for federal tax purposes. Parents, children and relatives of the debtor may be dependents. The age of the relative may be critical in determining if the expense should be allowed. Also, a court may distinguish between a moral and a legal duty to support a particular relative. Persons not related to the debtor may face a more critical test of whether they are allowable dependents. Expenses related to allowable dependents may detract from a debtor's disposable income. On the other hand, it is uncertain whether the income they contribute adds to disposable income of the household. Finally, it is unlikely that a court

142. In re Rybicki, 138 B.R. 225 (Bankr. S.D. Ill. 1992); see also In re Lindsey, 122 B.R. 157 (Bankr. M.D. Fla. 1991). Disposable income is affected by a debtor's payment of a post-petition expense because the expense is included in the debtor's list of budgeted expenses and subtracted from the debtor's gross income. 11 U.S.C. § 1325(b) (1994) does not explicitly distinguish between pre-petition debts and post-petition expenses.


144. Id.

145. Handeen v. LaMaire (In re LaMaire), 883 F.2d 1373, 1380-81 (8th Cir. 1989) (observing that the obligation to pay rent to parents is reasonably necessary for the maintenance of the debtor).

146. In re Clements, 185 B.R. 903, 909 (Bankr. M.D. Fla. 1995) (holding that debtor's 32 year old daughter, who was recovering alcoholic, was not a dependent for the purposes of the disposable income requirement).

147. Id. at 909 (holding that debtor's adult sister who lived in a nursing home and had cerebral palsy was not a dependent of debtor where debtor paid for private nurses and other amenities not covered by medicare).

148. In re McKean, 81 B.R. 9, 11 (Bankr. W.D. Tex. 1987) (holding that co-tenant and co-tenant's daughter were not dependents of the debtor and declining to "incorporate current social theory" regarding "novel living arrangements" into "current legal theory").

149. Compare In re Edwards, 15 Mont. B.R. 182 (Bankr. D. Mont. 1996) (holding that a debtor met the disposable income requirement where his spouse's income contributed to the payment of household expenses and allowed the debtor to contribute additional income to the plan) with In re Metzger, 11 Mont. B.R. 199, 208 (Bankr. D. Mont. 1992) (holding that the proposed plan fails the disposable income requirement where debtor pays all family expenses while his spouse saves all of her income).
would allow expenses related to mere friends or roommates when calculating disposable income.  

E. Retirement Accounts

Two questions have arisen regarding retirement accounts. First is the issue of whether a debtor may voluntarily fund a retirement account and still meet the disposable income requirement. Second is the issue of whether a debtor could be compelled to withdraw funds from his retirement accounts for purposes of funding his plan.

With respect to the first issue, a debtor does not meet the disposable income requirement when he commits a portion of earnings to fund a 401-K plan which was not required as a condition of employment. Furthermore, voluntary contributions to a pension fund are not necessary for maintenance or support of the debtor, and a debtor therefore may not voluntarily commit funds to profit sharing or pension plans. These decisions indicate that a retirement account is not reasonably necessary for the maintenance and support of the debtor or a dependent of the debtor—at least for the debtor who is not using those funds for present day living expenses. Thus, the debtor who is using present day disposable income to fund future living expenses may place himself in a position which precludes confirmation of his proposed plan. In addition, the debtor’s repayment of a loan from his retirement account detracts from his disposable income.

Regarding the second issue, the Fourth Circuit recently determined that it was error for the bankruptcy court to include some hypothetical amount of income from the debtor’s individual retirement account because the account was not relevant to the disposable income requirement. Thus, a debtor cannot be re-

150. See supra note 148 and accompanying text.
156. In re Delnero, 191 B.R. 539, 542 (Bankr. N.D.N.Y. 1996) (holding that postpetition payroll deductions used to repay prepetition loans from debtor's retirement account had to be included in debtor's disposable income); In re Goewey, 185 B.R. 444, 446 (Bankr. N.D.N.Y. 1995).
157. In re Solomon, 67 F.3d 1128 (4th Cir. 1995). The court ruled that the funds
required to withdraw funds from a retirement account for the purposes of funding a Chapter 13 plan. Funds already held in the retirement account do not add to the debtor's disposable income and confirmation cannot be conditioned upon the withdrawal of pension or retirement income to fund the plan.

F. Tithing

Numerous courts have found that tithing is not reasonably necessary for the maintenance of a household and is therefore not an allowable expense. Even though a debtor may deprive himself of other expense items such as recreation, the debtor's tithing may still detract from his disposable income—precluding his proposed plan from confirmation. The debtor's other expenses are unrelated to the necessity of the charitable contribution for the maintenance of the debtor.

The Montana Bankruptcy Court adopted such reasoning in the case of *In Re Lees*. In that case, the debtors' income exceeded their expenses by over $150 per month, but their expenses included a $200 per month tithe to the Shepherd of the Valley Church. The court found that the tithe was not a reasonably necessary expense, noting that to allow such charitable donations would compel creditors "to make defacto contributions" to the benefitted charity.
Other courts have reasoned that a certain amount of discretionary spending is reasonable and that a Chapter 13 debtor may include some charitable contribution as part of his discretionary expenses. These courts seem to agree that the debtor is entitled to some reasonable amount to pay as he sees fit. This position, however, is not consistent with the definition of disposable income and fails to recognize that such contributions are made at the expense of creditors who have already extended credit to the debtor.

**G. Life Insurance**

Life insurance has been determined to detract from the debtor’s disposable income. In the case of *In re Smith*, the court determined that, absent a showing that life insurance was required by law, life insurance premiums are not reasonably necessary for the maintenance or support of the debtors, and had to be included in the disposable income for purposes of confirmation. The court likened life insurance to retirement plans and savings accounts and recognized that such accounts are means by which debtors contribute present income to future income. As such, life insurance is not a necessary expense.

**H. Income Tax Refunds**

Income tax refunds represent an over-withholding of taxes from current income and increased income upon delivery of the refund. Tax refunds are property of the bankruptcy estate. The Trustee must look at the amount of the debtor’s tax deductions and whether the debtor anticipates a tax refund. If a debtor’s budget proposes excess withholding taxes, then the debtor is not committing all projected disposable income to the plan.

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165. *Id.* at 679.


However, a distinction must be drawn between the mere possibility of receiving a tax refund and a likely projected refund. The Trustee cannot simply require submission of all future tax refunds to the plan. If tax refunds are to be included in the plan, the Trustee must demonstrate the debtor's potential for receiving tax refunds during the plan period. Thus, debtors should only be entitled to retain refunds if they have correctly calculated their disposable income by including any anticipated refund at the time of confirmation.

VI. CONCLUSION

The disposable income requirement under Chapter 13 is a major factor both in determining whether a plan meets the requirements for confirmation and in measuring the consumer debtor's reorganization efforts. The disposable income requirement will become more important as a tool for creditors seeking to maximize their distributions under Chapter 13 plans. It is not surprising that Trustees and creditors alike are examining the disposable income requirement more closely, seeking to exercise their rights to modify the proposed plan as they become aware of increased disposable income. Debtors must recognize that, in exchange for the significant benefits offered by Chapter 13, they must offer a reasonable portion of their income to their creditors. Congress and the courts have correctly recognized that debtors will find the benefits of a Chapter 13 reorganization worth the cost of complying with the disposable income requirement.
