

UNITED STATES BANKRUPTCY COURT

Eastern District of California

Honorable Ronald H. Sargis
Bankruptcy Judge
Sacramento, California

March 25, 2014 at 3:00 p.m.

71. [13-32494-E-13](#) THEODORE/MOLLY MCQUEEN MOTION TO CONFIRM PLAN
CAH-2 C. Anthony Hughes 1-20-14 [58]

Local Rule 9014-1(f)(1) Motion - Opposition Filed.

Correct Notice Provided. The Proof of Service states that the Motion and supporting pleadings were served on Chapter 13 Trustee, all creditors, parties requesting special notice, and Office of the United States Trustee on January 20, 2014. By the court's calculation, 64 days' notice was provided. 42 days' notice is required. That requirement was met.

Tentative Ruling: The Motion to Confirm the Plan has been set for hearing on the notice required by Local Bankruptcy Rule 3015-1(d)(1), 9014-1(f)(1), and Federal Rule of Bankruptcy Procedure 2002(b). The Trustee and the Creditor having filed an opposition, the court will address the merits of the motion at the hearing. If it appears at the hearing that disputed material factual issues remain to be resolved, a later evidentiary hearing will be set. Local Bankr. R. 9014-1(g).

The court's tentative decision is to deny the Motion to Confirm the Amended Plan. Oral argument may be presented by the parties at the scheduled hearing, where the parties shall address the issues identified in this tentative ruling and such other issues as are necessary and appropriate to the court's resolution of the matter. If the court's tentative ruling becomes its final ruling, the court will make the following findings of fact and conclusions of law:

11 U.S.C. §1323 permits a debtor to amend a plan any time before confirmation. Here, the Chapter 13 Trustee ("Trustee") and G and K Heaven's Best, Inc. ("Creditor"), a creditor with a secured claim against Debtors, have filed objections to the Motion to Confirm the Amended Chapter 13 Plan for several grounds, set forth below.

CHAPTER 7 LIQUIDATION

Trustee's Objection

The Trustee argues that the Plan may not pay unsecured creditors at least what they would receive in the event of a Chapter 7 case, pursuant to 11 U.S.C. § 1325(a)(4). Dckt. 78. The Trustee states offers the following facts in support of his argument:

A. **JEWELRY:** Debtors had valued their jewelry once at \$5,100.00 (Dckt.

No. 9, Schedule B, Page 5, Item 7), but now at \$1,050.00. Dckt. No. 64, Page 3, Item 7 and Dckt. No. 76. Debtors changed their claim of exemption under California Code of Civil Procedure § 703.140(b)(5), reducing it from \$3,575.00 for the jewelry to claim. Dckt. No. 9, Pages 17-18, to claim an exemption of \$5,996.67 in accounts receivable and \$7,625.00 in business equipment. Dckt. No. 64. Pages 12-14. Debtors now describe the jewelry as \$50 in costume jewelry and wedding rings purchased at \$5,550.00. Dckt. NO. 64, Page 3. Debtors do not describe any gemstones the rings may have. The Debtors' opinion of the value of this jewelry may not be convincing to the court based on these circumstances.

- B. **ACCOUNTS:** Debtors originally claimed two Chase accounts were closed post-petition on September 26, 2013, with balances of \$2,045.78, two business accounts with Chase were closed post-petition September 26, 2013, with balances of \$1,669.55, and two accounts were opened with SAFE Credit Union--at an undisclosed date--with value of \$6,895.87, and claimed as not property of the bankruptcy estate. Dckt. No. 9, Pages 1 and 5. Where the Debtor now admits they are operating as a sole proprietorship, Dckt. No. 76, Page 6, Item 13, it is not clear how the value of these accounts is \$0.00 and not property of the estate.
- C. **OTHER PERSONAL PROPERTY:** Debtors now claim a \$1.00 interest in a cross-complaint against G&K Heaven's Best, Inc., Dckt. No. 75, and an adversary has been filed (Adversary No. 14-02027), where the complaint alleges that Debtors scheduled the Defendant at \$235,00.00 for a secured claim, and seeks to avoid their consensual lien as unperfected. Based on this complaint, the value of the asset may be \$235,000.00 for the estate if the lien is avoided, as 11 U.S.C. § 551 automatically preserves it for the estate.
- D. **BUSINESS, EQUIPMENT, AND ACCOUNTS RECEIVABLES:** Because Debtors maintain that they own a corporation called Eliminator Enterprises, Inc., which did business as "Heaven's Best of Sacramento" and ceased doing operations as of September 1, 2013, and Debtors are still operating the sole proprietorship of "Heaven's Best of Sacramento," but does not disclose when the business started, Trustee cannot determine the value of Debtor's business, inventory, and accounts receivable. Dckt. No. 76, Page 6.

While Debtor lists 29 items of equipment as worth \$27,810.00, Dckt. No. 76, and previously itemized 44 accounts receivable with some including work done as old as 2012, and as recently as late as September 2013 with a value of \$20,769.50, Dckt. No. 9, Debtor now claims that the accounts are only 70% collectible and the equipment is worth only \$6,925.50. Dckt. No. 76, Pages 6-7. Trustee argues that based on the foregoing, the plan may not pay unsecured creditors at least what they would receive in the event of a Chapter 7.

Creditor's Objection

Additionally, Creditor argues that the Chapter 13 Plan does not meet the Chapter 7 Liquidation Test and "is disputed." Dckt. 71. Creditor

asserts that the Plan does not meet the Chapter 7 Liquidation Test, on the grounds that there is more non exempt equity in the residence than the amount Debtors have listed on their Schedule A. Creditor disputes the valuation of the property located at 5300 Kenneth Avenue, Carmichael, California. Creditor argues that Debtors have not met their burden of proof in valuing the property, and requests further briefings to be provided the opportunity to have a licensed real estate appraisal be conducted on Debtors' residence.

Creditor also disputes the values listed for two vehicles, Debtors' 2003 Ford E250, and 2005 Chevrolet Astro Cargo Van; Creditor provides copies of the Kelley Blue Book valuations of both cars, and argues that Debtors' valuation of the vehicles are too low. Creditor also states that Debtors fail to include alleged Safe Credit Union accounts which held \$6,400.87 in funds pre-petition, and that Debtors assert a "nominal value" to the client lists being disputed by the creditor.

Debtor's Response

Debtors' Counsel filed a response, stating the Debtors mistakenly believed the three rings listed on their Schedules were only worth \$5,100.00, when they discovered they could only pawn them for \$165. Dckt. 83. Debtors now value their jewelry at \$1,050.00 with the description as \$50 in costume jewelry and wedding rings purchased at \$5,550.00. Dckt. No. 64, Page 3, Item 7 and Dckt. No. 76. Debtors do not describe any gemstones the rings may have. The additional description provided in Counsel's reply is no evidence for the court to consider.

Debtor's Counsel also states the Debtors closed the Chase bank accounts 9/26/2013, the day after the bankruptcy was filed, and opened accounts with SAFE Credit Union. The source of the funds with SAFE Credit Union were accounts receivables, and/or ongoing business operation proceeds, and/or proceeds from JPMorgan Chase Bank accounts closed on 9/26/2013 listed on Items 2 and 13 of Schedule B. The bank balance with JPMorgan Chase was property of the estate, but the bank accounts with SAFE Credit Union was not property of the estate.

Debtor's Counsel does not explain how the value of these accounts are \$0.00 and not property of the estate, as they are operating the business as a sole proprietorship. The court does not find Counsel's argument convincing. Further, the argument of Debtor's Counsel does not constitute evidence.

Debtor's Counsel also offers argument regarding the "Other Personal Property" and the Business Equipment and Accounts Receivables listed on their Schedules. Debtor currently lists 29 items of equipment as worth \$27,810.00, Dckt. No. 76, and previously itemized 44 accounts receivable with some including work done as old as 2012, and as recently as late as September 2013 with a value of \$20,769.50, Dckt. No. 9, Debtor now claims that the accounts are only 70% collectible and the equipment is worth only \$6,925.50. The court is not certain what to believe.

BEST EFFORTS

Trustee's Objection

The Trustee argues that Debtors' Plan does not represent Debtors' best efforts under 11 U.S.C. § 1325(b). Dckt. 78. Debtor is under the median income, and proposes plan payments of \$875.00 for 4 months, \$480.00 for 20 months, then \$1,480.00 for 12 months (36 months total), with a 5% dividend to unsecured, which totals \$15,210.01. The prior plan called for payments of \$875.00 for 60 months, with a 1% dividend to unsecured creditors, which totaled \$2,768.00.

Trustee states that Debtors owned a corporation dba Heaven's Best of Sacramento prior to filing. Beginning September 1, 2013, Debtor began operating the business as a sole proprietor. Debtor lists gross income from the Business on Schedule I at \$11,000.00 per month; however, Form B22C reflects the six month average income of only \$1,900.00. Trustee states that the Statement of Financial Affairs, Question 1, reflects the year to date income of \$10,433.00 from the business, which does not appear to be listed on Form B22C.

Where Debtor apparently took possession of the accounts receivable, and equipment of their corporation prior to filing, and those accounts receivable totaled enough to put the Debtor over the applicable state median income, the Trustee believes that the Debtor is above the median income and the plan should be a 60 month plan.

Creditor's Objection

Creditor also argues that Debtors' Plan does not meet the Current Monthly Income Test and Debtors are both over the median income. Dckt. 71. Creditor states that the debtors' Currently Monthly Income and Calculation of Commitment Period and Disposable Income reflects that the debtors are both under the median income, and as a result has no Monthly Disposable Income pursuant to 11 U.S.C. 1325(b)(2). Creditor argues that the debtors disclose no income from the business to which they transferred prior to bankruptcy, to themselves, which the debtors propose earns \$11,000.00 per month, and no payments have been made to this secured creditor since prior to April 2013, and then the form must be corrected.

Debtor's Response

Counsel for Debtor responds, stating the Schedule I income of \$11,000 per month is the gross proceeds debtors expect from the sole proprietorship which started Sep. 2013. Dckt. 83. Debtors state the 6-month (March 2013 to August 2013) Means Test income is the income debtors received from Eliminator Enterprises, Inc. as owner's draw. The Statement of Financial Affairs Item 1 YTD income of \$10,433 is the gross proceeds from the sole proprietorship for the month of Sep. 2013, which should not be counted in the means test. Trustee also believes that the accounts receivable that they took over from the corporation are high enough to put debtors over median income, but Debtors state they took the accounts receivable in Sep. 2013. The debtors filed for bankruptcy in Sep. 2013, and means test should only count the income debtors received from March 2013 to Aug. 2013.

However, the argument from Counsel is not evidence that the court can

consider. Debtor began operating the business as a sole proprietor before the filing of the bankruptcy petition (which was filed September 25, 2014). The court does not understand how Form B22C reflects the six month average income of only \$1,900, where Debtor lists gross income from the business at \$11,000 per month on Schedule I.

ATTORNEY'S FEES

Trustee argues that the Plan provides for only \$3,500.00 in attorney fees under the local "no look" fee, pursuant to LBR 2016-1(c). Dckt. 78. No estimate or disclosure is given as to what attorney fees are projected for the adversary in which Debtors' Counsel is also representing Debtors. NO Amended 2016(b) Attorney Disclosure Statement has been filed, and the Plan may not be feasible unless these actions are done.

Counsel for Debtors states that 11 U.S.C. 329 and Bankruptcy Rule 2006 only require debtors' attorney to disclose attorney fees paid or agreed to be paid within one year prior to the bankruptcy filing. Dckt. 83. Debtors' bankruptcy was filed 9/25/2013. This is incorrect and a misreading of the clear language of 11 U.S.C. § 329, which states (Emphasis Added),

§ 329. Debtor's transactions with attorneys

(a) Any attorney representing a debtor in a case under this title, or in connection with such a case, whether or not such attorney applies for compensation under this title, shall file with the court a statement of the compensation paid or agreed to be paid, **if such payment or agreement was made after one year before the date of the filing of the petition**, for services rendered or to be rendered in contemplation of or in connection with the case by such attorney, and the source of such compensation.

The statute requires disclosure for any payments made after one-year before the filing – which period includes the period after the filing. The statute does not say, "if such payment or agreement was made *during the period* after one year before the date of the filing of the petition *and the filing of the petition*."

For the one-year period from 9/25/2012 to 9/25/2013 debtors' attorney did not get paid or get agreement from client to pay for the adversary proceedings. In fact, Debtors' attorney states he disclosed on the Disclosure of Compensation of Attorney for Debtors, Page 44 of Docket 9, that the \$6,000 attorney fee does not include "Representation of the debtors in any dischargeability actions, ... or any adversary proceeding." To neutralize trustee's objection, debtors' attorney states he will file an amended Disclosure of Attorney Fee to overdisclose the monthly \$1,000 attorney fee for representation in the adversary proceedings. This is not an "overdisclosure," but the minimum disclosure required by 11 U.S.C. § 329.

The court conducted the Status Conference in this Adversary Proceeding on March 19, 2014. At the Status Conference it was disclosed that counsel Anthony Hughes, Hughes Financial Law, for Defendants/Counter Claimants, has been receiving post-petition payments of \$1,000.00 from the Debtors. The

monies are being paid from property of the estate. The payments are disclosed in the proposed Chapter 13 Plan filed in the Defendants/Counter Claimants' bankruptcy case. Bankr. E.D. Cal. 13-32494. No order authorizing the employment of special counsel to represent the Debtors in this Adversary Proceeding, as Defendants/Counter Claimants asserting claims of the estate, has been entered by the court. No order approving the payment of a post-petition retainer to counsel has been entered by this court.

It was further disclosed at the Status Conference that Anthony Hughes represented the Defendants/Counter Claimants' corporation, from which the assets were transferred on September 1, 2013. Schedule B, 13-32494, Dckt. 9. The Statement of Financial Affairs, Question 9, discloses that Hughes Financial Law was paid \$3,500.00 for the Debtors in connection with their debts or bankruptcy. At the hearing it was disclosed that Hughes Financial Law was paid \$2,000.00 for legal services in the year prior to bankruptcy provided to the Debtors' corporation.

The court issued a Order to Appear set for the same date as this Motion to Confirm and will address the attorney fees issues at that time.

BAD FAITH

Creditor objects that the plan was filed in bad faith. Dckt. 71. Creditor argues that the debtors in this case have attempted financial extortion to defraud the sellers of this viable business entity into accepting less than \$30,000 for the viable business entity sold less than 18 months ago for \$288,000. Creditor states that the petition, even as amended, is strikingly absent of any evidence, or documentation to serve, or support this bankruptcy. Creditor argues that the petition purposely undervalues the assets to force the creditors to seek counsel, incur the costs of defending unsupported accusations of value, and which counsel either failed to verify, and/or prepared in bad faith. Creditor states the Debtors have not disclosed assets, undervalued assets, not disclosed transfers, not disclosed payments, not disclosed attorney fees, and not supported their motions with evidence.

Counsel for Debtors respond by stating that the Debtor's Motion to Confirm First Amended Chapter 13 Plan was filed in good faith. Dckt. 82. Counsel continues to testify for the Debtors, stating that they have disclosed all of their assets and did not undervalue any of the assets and the transfers and payments. The court cannot consider this response as evidence in support of the plan.

Creditor has raised several issues that the court would consider bad faith, including failing to disclose assets, transfers, payments, attorney fees, and filing "liar" declarations to the court. Debtors have not met their burden of proof that they have filed the plan in good faith. See *Amfac Distribution Corp. v. Wolff (In re Wolff)*, 22 B.R. 510, 512 (9th Cir. B.A.P. 1982) (holding that the proponent of a Chapter 13 plan has the burden of proof as to confirmation).

MOTION TO VALUE

Creditor argues that the Debtors' Motion to Value the Secured Claim of G and K Heaven's Best, Inc. has not been granted nor have Debtors successfully prosecuted the Motion. Dckt. 71. Creditor states that confirmation of the plan is premature and that it opposes any confirmation that does not provide for the treatment of this creditor as a secured claimant pursuant to the Purchase Money Security Interest in the business.

Counsel for Debtors responds, stating that Debtors previously filed a Motion to Value the Secured Claim, Dckt. No. 18, and withdrew the motion, Dckt. No. 42, because debtors intended to file an adversary proceeding to avoid the UCC lien recorded 27 days before debtors' bankruptcy filing and to treat creditor as a general unsecured creditor. Dckt. 82. The Motion to Value was dismissed without prejudice, Dckt. No. 48. Debtors filed such adversary proceeding on 1/21/2014, case No. 14-02027. The status conference of the adversary proceeding is scheduled for 3/19/2014. For purposes of saving judicial cost, debtors believe time is not ripe for motion to value to be filed. Debtors intend to file motion to value after the adversary proceeding has been resolved.

The court cannot confirm a plan that calls for a valuation of real property pursuant to 11 U.S.C. § 506(a) without first hearing the Motion to Value Secured Claim. There appears to be an adversary proceeding regarding the same. Confirmation at this time may be premature.

DISPOSABLE INCOME TEST/EXPENSES

Additionally, Creditor argues that the Plan does not meet the disposable income test. Dckt. 71. Creditor states that the debtor has attached a list of "Projected Monthly Business Expenses" in docket 9 which is not correct. Creditor states that originally, the debtor listed a series of expenses which the creditor asserts are excessive and improper; (1) automotive expenses, (2) bank service charges, (3) equipment maintenance, (4) franchise agreement, (5) insurance expenses, (6) payroll expenses, and (7) professional fees. Creditor states that each of these expenses are not supported in fact, nor by any reasonably prudent businessperson attempting to anything but hide gross profit.

Counsel for Debtors responded to each item referenced by the creditor. However, the responses are not evidence, as they are provided as argument of Counsel rather than signed testimony under penalty of perjury. The court cannot consider these explanations as evidence. It appears that several of the business expenses listed by the Debtor need further explanation in the form of admissible testimony.

SCHEDULES AND DISCLOSURES

Creditor states the Debtors' schedules and disclosures need corrections. Creditor states that the Assets, Franchise Agreement, Type of Business Entity, Attorney Fees and disclosures have not been properly disclosed and require corrections before confirmation can be proctored.

Counsel for Debtor responds, stating Debtors fully disclosed their assets including real property, personal property and business assets in their Schedules A and B. Debtors disclosed in the Statement of Financial

Affairs that debtors owned a corporation from 11/2011 to 9/2013 operating the carpet cleaning business, and that debtors are now operating the carpet cleaning business as a sole proprietorship from 9/2013 to present Debtors disclosed and exempted in Schedules B and C the Chase Bank balance, which was previously owned by the corporation and then assumed by debtors after bankruptcy petition. The Franchise Agreement is part of the goodwill listed on Item 35 of the Amended Schedule B, if the franchise agreement had any material value. Attorney fees paid or agreed to be paid after bankruptcy for representation of debtors in adversary proceedings are not required to be disclosed, and attorney fees paid by a third party corporation for debt negotiation for the corporation are not required to be disclosed. Debtors' attorney hereby files an amended disclosure of attorney fee to make overdisclosure in order to neutralize creditor's objection.

Debtors explain that their business expenses have changed, and include the following chart in the Motion to Confirm Plan:

Item	Original Business Expenses	First Amended Business Expenses	Reason for change
Franchise fee	\$480.00	\$560.00	The Franchise fee is \$80 per territory. At the time of bankruptcy filing debtors mistakenly calculated the number of the territories at 6. It is 7 territories. $\$80 \times 7 = \560
Insurance Expenses	\$670.00	\$751.63	At the time of bankruptcy filing debtors believed their insurance expenses were roughly \$670.00. Now with accurate calculation debtors realize the monthly insurance expenses are \$290 business auto insurance + \$147.63 business insurance + \$314 workers' compensation insurance = \$751.63
Employee wages	\$1,220.00	\$1,488.17	At the time of bankruptcy filing debtors believed they paid their employee about \$1,220 per month. Now with review of his W-2 debtors realize that his total wages were \$17,858 for 2013, equivalent to \$1,488.17 per month
Payroll Taxes	\$490.00	\$138.85	At the time of bankruptcy filing debtors overcalculated their payroll taxes. The monthly payroll taxes are \$113.85 employer's share of employee's social security and medicare taxes + \$25 unemployment taxes = \$138.85
Professional Fees	\$555.00	\$224.00	At the time of bankruptcy filing debtors believed their professional fees were \$555.00 per month because they included the \$3,500 to Hughes Financial Law for bankruptcy attorney

Attorney fee to Hughes Financial Law	Included in professional fees	\$1,000	Debtors have intended file an adversary proceeding for 547 preference against Creditor G & K Heaven's Best, Inc. Creditor G & K Heaven's Best, Inc. filed an adversary proceeding against us for dischargeability. Debtors expect to incur about \$1,000 per month for 20 months for attorney fees from Hughes Financial Law to representing them in the two adversary proceedings.
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The Trustee and Creditor have raised several issues that greatly concern the court, which revolve around the corporation and the disclosure of those assets in the Debtor's bankruptcy. The most fatal being the Debtor has failed to produce additional evidence in support of the proposed plan. The court is also concerned with the disclosure of attorney's fees in the related adversary proceeding. It appears the Debtors still have a best effort issues, as the Form B22C reflects the six month average income of only \$1,900, where Debtor lists gross income from the business at \$11,000 per month on Schedule I. Further, there may be liquidation issues because of the different schedules filed by the Debtors. As the plan stands, it does not appear to be confirmable at this time.

The amended Plan does not comply with 11 U.S.C. §§ 1322 and 1325(a) and is not confirmed.

The court shall issue a minute order substantially in the following form holding that:

Findings of Fact and Conclusions of Law are stated in the Civil Minutes for the hearing.

The Motion to Confirm the Chapter 13 Plan filed by the Debtor having been presented to the court, and upon review of the pleadings, evidence, arguments of counsel, and good cause appearing,

IT IS ORDERED that Motion to Confirm the Plan is denied and the proposed Chapter 13 Plan is not confirmed.