

1 F O R P U B L I C A T I O N

2 UNITED STATES BANKRUPTCY COURT

3 EASTERN DISTRICT OF CALIFORNIA

4 SACRAMENTO DIVISION

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6) Case No. 97-26738-B-7
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11) Adv. No. 97-2634
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In re
WILLIAM R. SMITH,

Debtor.

CAROL SUE SMITH,

Plaintiff,
vs.
WILLIAM R. SMITH,

Defendant.

18 Dennis K. Cowan, Esq., Redding, California, appearing for
19 plaintiff.
20 Byron Lee Lynch, Esq., Redding, California, appearing for
21 defendant.

22 MEMORANDUM DECISION

23 A trial of this adversary matter was held on August 28,
24 1998. Plaintiff Carol S. Smith appeared with Dennis K. Cowan,
25 Esq., and debtor and defendant William Roy Smith appeared with
26 Byron Lee Lynch, Esq. Having considered the evidence and written
27 and oral arguments, as well as the proposed findings of fact and
28 conclusions of law lodged on November 25, 1998, the court
concludes the obligations of the debtor to the plaintiff are
nondischargeable in bankruptcy.

1 I. Facts

2 The parties are separated spouses. Prior to the filing
3 of the debtor's chapter 7 petition, the superior court entered a
4 judgment of legal separation on January 6, 1997. That judgment
5 also preliminarily divided the community property of the parties.
6 The debtor received most of the community property, including the
7 former marital home located at 12124 East Stillwater, Redding,
8 California (the "residence"), and was ordered to pay to the
9 plaintiff an equalizing payment of \$58,058.19.

10 The award of the residence to the debtor, however, was
11 expressly contingent upon the equalizing payment being paid to
12 the plaintiff. Until paid, record title remained in the name of
13 both parties. If not paid, the superior court retained
14 jurisdiction to compel a sale of the residence.

15 The superior court found that the residence was worth
16 \$190,000.00, and that it was subject to secured debt of
17 \$106,147.24. There is no evidence that these amounts have
18 changed significantly.

19 To date, the residence remains in the name of both
20 parties, the debtor lives in the residence, and the equalizing
21 payment is unpaid. The superior court has taken no further
22 action because of the imposition of the automatic stay occasioned
23 by the filing the chapter 7 petition on May 2, 1997.

24 The debtor claimed a homestead exemption in the
25 residence in the amount of \$69,588.56 under California Code of
26 Civil Procedure § 704.710 *et seq.* No objection to the exemption
27 was filed by the plaintiff or any other party in interest. The
28

1 time to file objections has expired.

2 The plaintiff filed a timely dischargeability complaint
3 under 11 U.S.C. § 523(a)(5) and (a)(15). The debtor does not
4 dispute that an obligation to pay \$1,500.00 on account of the
5 plaintiff's attorney's fees incurred in the separation proceeding
6 is nondischargeable under 11 U.S.C. § 523(a)(5).

7 II. Discussion

8 The controversy in this proceeding is whether the
9 \$58,058.19 equalizing payment is nondischargeable under 11 U.S.C.
10 § 523(a)(15). Section 523(a)(15) provides:

11 (a) A discharge under section 727 . . . of this title
12 does not discharge an individual debtor from any debt—

13 (15) not of the kind described in paragraph (5)
14 that is incurred by the debtor in the course
15 of a divorce or separation or in connection
16 with a separation agreement, divorce decree
or other order of a court of record, a
determination made in accordance with State
or territorial law by a governmental unit
unless—

17 (A) the debtor does not have the ability to
18 pay such debt from income or property of
the debtor not reasonably necessary to
19 be expended for the maintenance or
support of the debtor or a dependent of
the debtor and, if the debtor is engaged
20 in a business, for the payment of
expenditures necessary for the
21 continuation, preservation, and
operation of such business; or

22 (B) discharging such debt would result in a
23 benefit to the debtor that outweighs the
detrimental consequences to a spouse,
former spouse, or child of the debtor.

24 A.

25 The plaintiff has met her burden of proof under section
26 523(a)(15). She has established that the \$58,058.19 is a non-
27 support obligation incurred in connection with a legal separation

1 from her spouse. Samayoa v. Jodoin (In re Jodoin), 196 B.R. 845,
2 852-54 (Bankr. E.D. Cal. 1986), *affirmed*, 209 B.R. 132 (B.A.P.
3 9th Cir. 1997).

4 B.

5 Absent proof by the debtor that he either cannot afford
6 to pay the \$58,058.19 or, if he can afford to pay it, that the
7 benefit of a bankruptcy discharge to him outweighs its
8 detrimental consequences to the plaintiff, the equalizing payment
9 is nondischargeable. Id. The debtor has not met this burden.

10 1.

11 The debtor is employed as a logging truck driver. He
12 normally works approximately six months per year and draws
13 unemployment benefits for the rest of the year. His average net
14 income, including unemployment benefits, is approximately
15 \$1,875.00 per month. His living expenses average approximately
16 \$1,972.00 per month. Were the debtor a chapter 13 debtor, the
17 court would conclude that he had no disposable income within the
18 meaning of 11 U.S.C. § 1325(b). Cf. Armstrong v. Armstrong (In
19 re Armstrong), 205 B.R. 386, 392 (Bankr. W.D. Tenn. 1996);

20 While the debtor's employment income and his
21 unemployment benefits are insufficient to permit him to repay the
22 \$58,058.19 in the foreseeable future, the residence, if sold,
23 would permit him to pay the plaintiff. Prior to filing
24 bankruptcy, the debtor was not adverse to selling the residence.
25 He sought the permission of the state court to sell the residence
26 but his proposed terms were rejected.

27 ///

1 Unsurprisingly, now that the debtor has filed
2 bankruptcy and his former spouse wants him to sell the residence,
3 he refuses to do so. He further maintains that the bankruptcy
4 court cannot consider his equity in the residence when
5 determining whether he can afford to make the equalizing payment
6 because he claimed that equity exempt. Because it is exempt, it
7 cannot be levied upon either during or after the completion of
8 the chapter 7 case. 11 U.S.C. § 522(c).¹

9 Section 523(a)(15)(A), however, asks whether a debtor
10 has the ability to pay, either from income or property, a non-
11 support marital obligation. Exemptions have no impact on what a
12 debtor can afford to pay. Exemptions are only relevant when a
13 creditor seeks to compel a recalcitrant debtor to pay a debt.

14 For example, if a debtor has \$1,000,000.00 in an exempt
15 pension plan, a judgment creditor may not levy on the plan. But
16 this does not mean that debtor is unable to pay the debt. It
17 means he is unwilling to pay it.

18
19 ¹ 11 U.S.C. § 522(c) provides: "Unless the case is dismissed,
20 property exempted under this section is not liable during or after the case
21 for any debt of the debtor that arose, or that is determined under section 502
of this title as if such debt had arisen, before the commencement of the case,
except –

22 (1) a debt of the kind specified in section 523(a)(1) or 523(a)(5) of
this title; or

23 (2) a debt secured by a lien that is –

24 (A) (i) not avoided under subsection (f) or (g) of this section
or under section 544, 545, 547, 548, 549, or 724(a) of this title;
and

25 (ii) not void under section 506(d) of this title; or

26 (B) a tax lien, notice of which is properly filed; or

27 (3) a debt of a kind specified in section 523(a)(4) or 523(a)(6) of this
28 title owed by an institution-affiliated party of an insured depository
institution to a Federal depository institutions regulatory agency
acting in its capacity as conservator, receiver, or liquidating agent
for such institution.

1 More importantly, the reference to property in section
2 523(a)(15)(A) must necessarily include exempt property. Non-
3 exempt property is property of the bankruptcy estate and subject
4 to sale by the trustee for the benefit of all creditors. A
5 chapter 7 debtor will have only exempt property at his or her
6 disposal. As noted by the bankruptcy court in Woodworth v.
7 Woodworth (In re Woodworth), 187 B.R. 174, 177, n. 1 (Bankr. N.D.
8 Ohio 1995):

9 Section 523(a)(15)(A) uses the term "income or property
10 of the debtor." This necessarily means exempt property
11 and postpetition income as non-exempt property and
prepetition income are property of the estate and
cannot be used for debtor's maintenance and support.
12 Also see In re Smither, 194 B.R. 102, 111 (Bankr. W.D. Ky. 1996)
13 (exempt property is considered under section 523(a)(15)(B) when
14 balancing the benefit/hardship of a discharge). If the court did
15 not consider exempt property, then, the phrase "or property of
16 the debtor" would be effectively written out of section
17 523(a)(15)(A).

18 In many cases, including exempt property in the
19 analysis will benefit the plaintiff little. If a bankruptcy
20 court finds an obligation is nondischargeable based on the
21 existence of exempt property but the plaintiff is prohibited by
22 the section 522(c) from levying upon that exempt property, the
23 court may have handed the plaintiff nothing more than a pyrrhic
24 victory.

25 In this case, the foresight of the superior court
26 prevents this result. Its award of the residence to the debtor
27 was interlocutory. If the debtor fails to pay the \$58,058.19,
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1 the superior court retained jurisdiction to make a different
2 division of the parties' community property. This may take the
3 form of ordering the sale of the residence and dividing the sale
4 proceeds between the parties.

5 2.

6 The debtor made no serious attempt to argue that the
7 benefit of a bankruptcy discharge outweighed its detrimental
8 consequences to the plaintiff.

9 The plaintiff is 51 years old and is totally disabled
10 as a result of a stroke in 1990. She is unable work. Her income
11 consists of \$697.00 per month from a private disability insurance
12 policy and \$1,035.00 per month from Social Security. The private
13 disability insurance benefit will terminate when she turns 65, at
14 which time she can expect to receive \$368.00 per month in pension
15 benefits from her former employer, Pacific Telesis. The
16 plaintiff's living expenses are approximately equal to her
17 income.

18 Comparatively speaking, the debtor is much more
19 financially secure. As discussed above, he is employable, he has
20 discharged all of his pre-petition debts to other creditors, and
21 he has been conditionally awarded property with an equity
22 exceeding \$80,000.00. Consequently, the detriment of the
23 discharge to the plaintiff outweighs its benefit to the debtor.

24 C.

25 Having concluded that the debtor's obligation to the
26 plaintiff is nondischargeable, the court is compelled to qualify
27 this conclusion and its judgment. The qualification is necessary

1 because the superior court retained jurisdiction over the
2 community property and could alter its division between the
3 parties.

4 The superior court's judgment converted the plaintiff's
5 interest in the residence and the other community property into a
6 \$58,058.19 claim against the debtor. A discharge in bankruptcy
7 discharges claims against a debtor unless excepted from
8 discharge. 11 U.S.C. §§ 101(5) & (12), 523(a), 524(a)(1). In
9 this case, the claim will be excepted from the debtor's discharge
10 pursuant to section 523(a)(15).

11 That claim, however, may disappear if the superior
12 court exercises its reserved jurisdiction and alters its
13 judgment. For example, rather than award the residence to the
14 debtor and compel him to pay \$58,058.19 to the plaintiff, it may
15 instead order the sale of the residence then divide the sale
16 proceeds between the former spouses.² Such a judgment would not
17 create a claim against the debtor. The proceeds from the sale of
18 the residence would represent the plaintiff's interest in
19 property.

20 A bankruptcy discharge does not extinguish an interest
21

22 ² In fulfilling its obligation to divide community property equally
23 between the former spouses, the superior court may award an asset to one party
24 on "such conditions as it deems proper". Cal. Family Code § 2601. Such
25 conditions may include an award to the other party of a greater share of other
26 community property or of a cash payment in lieu of his or her community
27 property interest in the asset. Alternatively, the court may divide the asset
28 in kind, or order the asset sold and the net equity divided between the
parties. In re Marriage of Brigden, 80 Cal. App.3d 380, 390 (1978); In re
Marriage of Davis, 68 Cal. App.3d 294, 306 (1977); Cal. Family Code § 2553.
The superior court may retain jurisdiction to divide an asset at a later date.
Cal. Family Code § 2550.

1 in property. 11 U.S.C. § 727(b). See Gendreau v. Gendreau (In
2 re Gendreau), 122 F.3d 815, 818-819 (9th Cir. 1997). Such a
3 situation would be analogous to Chandler v. Chandler (In re
4 Chandler), 805 F.2d 555, 557-558 (5th Cir. 1986). In Chandler,
5 the court held that an obligation to turnover proceeds of
6 retirement pay representing ex-wife's former community property
7 interest was an obligation to turnover her sole property and was
8 not a dischargeable debt. Also see Aldrich v. Imbrogno (In re
9 Aldrich), 34 B.R. 776, 780 (B.A.P. 9th Cir. 1983).

10 Therefore, if the superior court alters its present
11 division of community property and eliminates any requirement
12 that the debtor pay money to the plaintiff, there will be no debt
13 to be discharged. The plaintiff's right to receive community
14 property or her share of the net proceeds from a court ordered
15 sale is an interest in property that is not capable of discharge.

16 III. Conclusion

17 For the foregoing reasons, the court will enter a
18 judgment in favor of the plaintiff and against the debtor
19 providing that his obligation to pay \$1,500.00 to the plaintiff
20 is nondischargeable pursuant to 11 U.S.C. § 523(a)(5). The
21 judgment will also provide that the debtor's obligation to pay
22 \$58,058.19 to the plaintiff is nondischargeable pursuant to 11
23 U.S.C. § 523(a)(15). However, if the superior court alters its
24 division of community property so as to eliminate any requirement
25 that the debtor pay this amount, then there is no debt to
26 discharge. This may occur if the superior court orders the sale
27 of the residence and then divides the net sale proceeds between
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1 the parties. An award to the plaintiff of a portion of the net
2 proceeds represents her interest in property. Her interest in
3 property is unaffected by the debtor's discharge.

4 A separate judgment will be entered.

5 Dated:

6 By the Court

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Michael S. McManus
9 United States Bankruptcy Judge
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