# CAN A CHAPTER 13 PLAN PROVIDE FOR A DEBTOR'S "SAVINGS"?

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Judge Isgur observed, at a 2015 meeting of the Bankruptcy Rules Committee addressed to the topic of the adoption of a national uniform model chapter 13 plan, that the principal reason that chapter 13 plans fail is because debtors encounter, over the life the plan, unanticipated financial crises. Many chapter 13 debtors, after all, find themselves in bankruptcy in the first place on account of the failure to plan adequately for changes in their financial circumstances. It therefore is not surprising, Judge Isgur explained, that in the absence of a mechanism for handling a financial hiccup in while in chapter 13, many chapter 13 debtors will find themselves unable to complete the terms of a (typically) five-year chapter 13 plan. The problem with the national uniform chapter 13 plan, Judge Isgur explained, is that it deprived individual bankruptcy courts the flexibility to innovate by adding plan provisions designed to address problems like this one.

The Southern District of Texas does, indeed, have a novel provision in its current Uniform Chapter 13 Plan. Paragraph 14 of that form plan reads as follows:

> **14. Emergency Savings Fund.** Line 21 of Schedule J (the Debtor(s)' expense budget) includes a provision for an emergency savings fund by the Debtor(s). Deposits into the emergency savings fund will be made to the Trustee. Withdrawals from the emergency savings fund may be made by application to the Court, utilizing the form application from the Court's website. Withdrawals should be requested only in an emergency. The form application need only be served electronically, and only to persons subscribing to the Court's CM/ECF electronic noticing system. An application will be deemed granted on the 15th day after filing unless (i) an objection has been filed; or (ii) the Court has set a hearing on the motion. The Debtor(s) may request emergency consideration of any application filed under this paragraph. The balance in the emergency savings fund will be paid to the Debtor(s) following (i) the granting of the discharge in this case; (ii) the dismissal of this case; or (iii) the conversion of this case to a case under chapter 7, except on those circumstances set forth in 11 U.S.C. § 348(f)(2).

The deposits into the emergency savings fund will be:

| Month of First Deposit of this Amount | Month of Last Deposit of this Amount | Amount | Total |
|---|---|---|---|
| Pre-modification savings deposits | | | |
| | | | |
| | | | |
| | | | |
| | | TOTAL | |

Schedule J, as the form plan notes, is where the debtor lists his or her monthly expenses. Line 21 is for expenses not otherwise identified, labeled "Other: Specify__________________."

In substance, this provision permits a debtor to *add* to his or her budgeted expenses an amount that will be dedicated to "savings." That "savings account," maintained (without charge) by the chapter 13 trustee, is available to the debtor if he or she runs into a financial emergency over the life of the plan. But if the debtor does not tap into this savings account over the life of the plan, and otherwise either completes the plan successfully or has the case dismissed or converted, this amount is returned to the debtor.

Interesting idea, to be sure. And perhaps a sound policy judgment. But does it comport with the Bankruptcy Code? Section 1325 of the Code requires a chapter 13 debtor, in order to obtain confirmation of a plan, either to pay creditors in full, or to commit, to the plan, "all of the debtor's projected disposable income to be received" during the duration of the plan. 11 U.S.C. § 1325(b)(1).

"Disposable income," in turn, is defined by the Code as "current monthly income received by the debtor . . . less amounts reasonably necessary to be expended" for "maintenance or support of the debtor or a dependent of the debtor," for certain "charitable contributions" not to exceed 15 percent of the debtor's gross income, and, if the debtor is engaged in business, for the payment of business expenses."

For debtors with below median income, the "amounts reasonably necessary to be expended" includes the "full amount needed for 'maintenance or support,'" *Hamilton v. Lanning*, 560 U.S. 505, 510 (2010), which amounts are typically determined by reference to the budget the debtor sets forth on Schedule J.

For debtors with *above* the median income in their state, however, an entirely different (more formulaic) scheme applies. Specifically, the debtor's expenses "shall be determined in accordance with subparagraphs (A) and (B) of section 707(b)(2)," 11 U.S.C. § 1325(b)(3), which

are the provisions of the Code that set forth the "means test" under which debtors with substantial disposable income are deemed ineligible to file for chapter 7, and must instead proceed under chapter 13 (where they would be required to devote that disposable income to a plan).

Section 707(b)(2) explains that a debtor's expenses "shall be the debtor's applicable monthly expense amounts specified under the National Standards and Local Standards, and the debtor's actual monthly expenses for the categories specified as Other Necessary Expenses issued by the Internal Revenue Service." The statute goes on to say that, "[i]n addition," the debtor's expenses shall include an array of other specific specified categories of expenses, such as "continuation of actual expenses paid by the debtor that are reasonable and necessary for care and support" of an elderly or disabled household member, the cost of tuition to attend a private school not to exceed $1,925 per child per year, an allowance for housing and utilities in excess of the Local Standards based on actual expenses, and the cost of administering the chapter 13 case. 11 U.S.C. § 707(b)(2).

So, in short, what this long tour through the statutory language reveals is that the amount a debtor is required to pay into his or her plan is: (a) for below-median income debtors, determined by the debtor's proposed budget, but (b) for above-median income debtors, determined by application of the means test. That said, as a practical matter, because even above-median income debtors nevertheless prepare the budget required by Schedule J, it is commonly the case that such debtors propose to pay into their plan the difference between Schedule I and Schedule J, *so long as* that amount is equal to or greater than the payment that application of the means test would otherwise require.

The analytically challenging question presented by the Southern District of Texas provision, therefore, arises only for below-median income debtors, for whom adding contributions to "savings" on Schedule J would operate to reduce the debtor's contribution to a plan, and thereby reduce creditors' recoveries. Take, for example, a case in which a debtor contributed $500/month to a chapter 13 plan, and $50/month to a "savings" account designed to permit the debtor to continue those $500 monthly payments if he or she had an unexpected medical bill or a temporary reduction in income. If the debtor is able to make the 60 plan payments, he or she will have contributed $30,000 toward the payment of creditors, and will then receive back an additional $3,000 from the trustee.

As a statutory matter, is the debtor entitled to that $3,000? The argument for requiring those funds to be paid to creditors would focus on the statutory obligation to commit "all of the debtor's projected disposable income" to the plan, and the definition of disposable income to mean all of the debtor's income, less certain specific categories of amounts "reasonably necessary to be expended" for identified categories of expenses. 11 U.S.C. § 1325(b)(2).

A variety of arguments, however, can be advanced on the other side. One argument relies on the inherent imprecision of the budgeting process involved in determining "projected disposable income." No one disputes that if a debtor tightens his or her belt during the course of a chapter 13 plan and spends less than his budget predicted, the debtor is entitled to keep the resulting savings. Nor is there anything talismanic about the particular amounts that are budgeted, which are necessarily imprecise estimates of future expenditures. In a world in which none of this is that precise, anyway, what is the harm in building in a small amount of cushion? Moreover, to the extent that including such a cushion will, in the aggregate, make it more likely that debtors will be able to complete plans successfully, rather than having chapter 13 cases dismissed or converted, the inclusion of these provisions may well serve the best interests of the creditors, in any event.

One case, indeed, takes this line of argument a step further. The U.S. Bankruptcy Court for the Western District of Louisiana, for example, recently held that a chapter 13 plan can provide for debtor to contribute three percent of a debtor's income to a 401(k) retirement plan. *In re Miner*, 2017 WL 1011419 (W.D. La. March 14, 2017). The court's rationale for the decision, similar to the line of argument set out above, relies on the "play in the joints" between the formulaic forward-looking nature in which projected disposable income is calculated, and the more fluid reality of how events will transpire over a five-year period. "This Court has already found that when known or virtually certain circumstances dictate, it can deviate from the national and local standards for a debtor's expenses in above median income cases. So, for example, this Court often deviates from these standards due to large automobile insurance expenses contained in budgets. . . . Automobile insurance expenses are quite large in this division. . . . This Court sees no difference in allowing increased automobile expenses in above median income cases and also allowing a reasonable and limited retirement contribution." *Id.* at *7-8.

In fairness, this somewhat fluid form of analysis can find some support in the Supreme Court's jurisprudence. Specifically, in *Hamilton v. Lanning*, the Court held that "projected disposable income" is *not* to be determined simply by taking the debtor's prior income and

projecting it forward. Rather, it is based on a forward-looking projection of the debtor's income over the plan period. Accordingly, while past income certainly provides an important starting point, where "significant changes in a debtor's financial circumstances are known or virtually certain, a bankruptcy court has discretion to make an appropriate adjustment." 560 U.S. at 513.

More broadly, the "play in the joints" regarding the inevitable differences between the prediction that is made of a debtor's future income and expenses at the time a chapter 13 plan is confirmed, and the reality of the debtor's income and expenses over a five-year period, remains an area in which the law is underdeveloped and far from uniform across the country.

One conception is that the debtor bears both the up-side and down-side to variances in his or her income or expenses – meaning the debtor can put away savings if he or she receives a raise or reduces expenses, but would need to draw on those savings if his or her earnings were reduced – unless the change were sufficiently material to warrant a modification of the chapter 13 plan. The alternative conception is to seek to build that flexibility into the plan, such as by including provisions like the one included in the Southern District of Texas.[1]

In the absence of greater clarity from appellate courts or clarification of the Code itself, it seems likely that different jurisdictions will continue to innovate and experiment with efforts by chapter 13 debtors to "save" during the life of their plans – either to enhance the likelihood that their plans ultimately succeed and/or as part of a broader effort to save for retirement. As set forth above, whether these efforts comport with the Bankruptcy Code is uncertain. "The Bankruptcy Code," the Supreme Court has reminded us, seeks to "standardize[] an expansive (and sometimes unruly) area of law." *Radlax Gateway Hotel v. Amalgamated Bank*, 566 U.S. 639 (2012). For the foreseeable future, however, the issue of a debtor's "savings" during chapter 13 appears to be a corner of the Code in which unruly will continue to prevail over standardization.

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[1] A third approach, but one that seems difficult to explain conceptually, is to treat changes that relate to a debtor's mortgage differently from all other changes that occur after confirmation, providing that increases or decreases in a debtor's mortgage obligation (caused, for example, by changes in interest rates, taxes or insurance) do not affect the debtor, but result in increases or decreases in the distribution to unsecured creditors. Many jurisdictions, however, have model plans that are built on this conception. *See also In re Chapter 13 Plan Administration In the Brownsivlle, Corpus Christi and McAllen Divisions*, Mis. Case No. 15-701 (May 5, 2016) (addressing problems created by the fact that one chapter 13 trustee administered the S.D. Tex. model plan as if it provided that changes related to the mortgage should affect distributions to unsecured creditors, when in fact it does not).

## Debtor Savings Hypothetical

***Version 1:***

1. Debtor is an above-median income debtor.

2. Debtor's means test demonstrates that debtor has no projected disposable income, and thus no minimum distribution requirement to the holders of unsecured claims.

3. Debtor was in a prior case that failed, less than one year ago, when Debtor needed extensive car repairs. The Debtor decided at the time that having a car to get to and from work was more important than keeping the case alive. Upon the subsequent filing, the Debtor promptly filed a motion, under Section 362(c)(3)(B), to extend the stay. The Court granted the motion, finding by clear and convincing evidence that the new case was filed in good faith.

4. The evidence is undisputed that the Debtor took two steps to avoid a future dismissal. *First*, immediately after the petition date, the Debtor installed new thermostat controls in his home. These keep the temperature above 78 degrees in the Summer and below 68 in the winter. This resulted in a $150.00 per month savings on the Debtor's utility bills. *Second*, the Debtor began selling Amway products by working in the evenings. This has resulted in another $100.00 per month savings.

5. The Debtor has disclosed his $250.00 of added disposable income, and proposes to save the money in an emergency savings account.

6. The Trustee objects to confirmation, arguing that the $250.00 per month should go to the unsecured creditors. The bankruptcy court confirmed. The Trustee appeals.

***Version 2:***

1. Same facts as above, except that the Debtor is a below-median income debtor.

2. The means test does not apply. The Debtor took the new Amway job and installed the thermostat controls immediately before filing the petition. Subtracting the Debtor's Schedule J expenses from the Debtor's Schedule I income yields projected disposable income of $250/month.

3. Concerned about the risk of something unexpected occurring that might crater the plan (such as the car repairs in the earlier bankruptcy case), the Debtor proposes to pay $175/month to the trustee, and to save $75/month to deal with potential contingencies. The Debtor accomplishes this, per the S.D. Tex. Model Plan, by adding $75 to Line 21 of Schedule J. The plan provides that in the event the $75/month is not spent and the plan is completed successfully,

those funds are distributed to the debtor.  If the plan is completed successfully, the $175/month paid into the plan will permit the trustee to make a distribution of 40% to the holders of allowed unsecured claims.

4. Both the trustee and the debtor's largest unsecured creditor object to confirmation.  The bankruptcy court confirms the plan.  Both the unsecured creditor and the trustee appeal.