In the United States Bankruptcy Court
for the
Southern District of Georgia
Brunswick Division

In the matter of:	)	
	)	Adversary Proceeding
CARL L. MICHALAK	)	
(Chapter 7 Case Number 01-42312)	)	Number 01-4151
	)	
Debtor	)	FILED at 3 O'clock & 10 min P M Date 9-24-02
	)	
CYNTHIA LEE	)	MICHAEL [illegible] CLERK United States Bankruptcy Court Savannah, Georgia
	)	
Plaintiff	)	
	)	
v.	)	
	)	
CARL L. MICHALAK	)	
	)	
Defendant	)	

MEMORANDUM AND ORDER

Debtor Carl L. Michalak ("Debtor") filed his Chapter 7 case on August 7, 2001. Debtor's former wife, Cynthia Lee ("Wife") petitioned this Court to declare that Debtor's obligations to her pursuant to their divorce decree are non-dischargeable. The Court has jurisdiction over this proceeding under 28 U.S.C. § 157(b)(2)(I). Having heard the evidence presented at trial on May 29, 2002, I make the following Findings of Fact and Conclusions of Law in accordance with the requirements of Bankruptcy Rule 7052(b).

FINDINGS OF FACT

Debtor and Wife were married in 1983. Their marriage effectively ended shortly

(25)

after their marital residence flooded and Debtor tried to start a new business. In June 2000 the parties separated and on February 2, 2001, they were divorced by order of the Chatham County Superior Court.

The Debt Obligations

The parties' divorce decree incorporates a separation agreement in five sections dated November 11, 2000 ("the Agreement"), which created certain obligations running from Debtor to Wife. The sections pertinent to the instant issues are captioned "Real Estate," "Monetary Settlement," "Accrued Debts," and "Manner of Payments."

The "Real Estate" section evidences that the parties contemplated selling their marital residence on Washington Avenue for a minimum specified sum, after which they were to divide the net proceeds, with Wife receiving an additional sum to be computed on the basis of the projected sales price.

The "Monetary Settlement" section created certain obligations of Debtor. He was to pay Wife: (1) $36,000.00 per year for ten years, adjusted annually to reflect a 5% cost-of-living increase; (2) $14,000.00 not later than two years from the date of the separation agreement; and (3) $20,000.00, representing a portion of inheritance monies left to Wife by her mother, no later than three years from the date of the divorce. He was also to provide Wife with health insurance and with a vehicle of her choosing at a monthly cost of no more than $350.00 per month. In addition, Wife was entitled to remain as beneficiary under Debtor's life insurance policy if she

chose to pay the premium for that policy.[1]

The $14,000.00 lump sum payment was to be used for the purpose of treating Wife's periodontal disease and for some cosmetic surgery. Debtor testified that the $14,000.00 was to have been paid out of any realized profit from the sale of the residence. The agreement, however, stated that the $14,000.00 was to have been paid "in addition to above provisions." The "above provisions" were the real estate provision and the $36,000.00 annual support payment.

The "Accrued Debts" section obligated Debtor to "pay any and all debts incurred on behalf of business, or of a personal nature, i.e. credit cards held mutually or separately, mortgages, personal loans, etc., accrued while legally married, and in an expedient manner." As of April 2002 the approximate balance of Debtor's credit card obligations under the Agreement was $41,000.00.

The "Manner of Payments" section provided that Debtor was to pay his obligations to Wife through his business, and Wife agreed to accept those payments as "salary and bonus monies" and to assume responsibility for taxes due on those payments. Those obligations were to continue beyond Debtor's death and without respect to the remarriage of either party.

[1] Because the Agreement did not obligate Debtor to pay the policy premiums and Wife evidently chose not to do so, the policy lapsed, and any obligation of Debtor with respect to that provision is moot.

The Parties

Debtor is fifty-five years of age. He completed two years of college and worked as a construction supervisor for various companies until he developed heart trouble. He was evaluated for a heart transplant, but when none was available in time to save his life, he opted to have heart valve replacement surgery. Currently, his condition and the drugs he must take to control it limit his physical activity and restrict the type of work that he can perform.

Debtor was employed by Witter and Associates when Debtor and Wife moved to Savannah. He resigned from Witter in June 1999 for the purpose of opening and developing Lee-Michaels, Inc. ("L-M"), an environmental engineering business devoted to (1) collecting certain types of waste to be used as fertilizer and (2) preparing environmental reports. L-M's customers included Intercat and Willamette Industries, a paper mill in Savannah. When the Willamette contract came for renewal, Debtor formed a new company, C. R. Michaels, Inc. ("CRM") and renewed the Willamette contract in the name of the new company.

Wife is forty-seven years of age and is in good health. During the parties' marriage, she worked for a law firm, a retirement home, and as a real estate appraiser. She was also an officer and shareholder in L-M. When the parties separated, she had no job and no separate resources available, but one year after the parties separated, she began selling funeral arrangements. She is currently paid on a "draw against commission" basis which amounts to approximately $450.00 in monthly net income. She asserts that her commissions amount to somewhat less than the federal minimum wage in a full-time job.

Wife used her knowledge of construction management, which she studied in college for two years, in overseeing the renovation and improvement of homes in which the parties lived during the course of their marriage. The renovations allowed the parties to rapidly build equity in those residences. On one house, they realized a $100,000 profit in a period of approximately four years, at least a portion of which was attributable to the renovations which she conceived and supervised as well as to the general advance in the real estate market. The parties used the profit realized in sales of previous houses to establish themselves in Savannah, where they purchased a new home.

Wife presents herself well. She is clearly capable of earning more than the federal minimum wage on a consistent basis. She shares living expenses on a fifty-fifty basis with a roommate and drives a car which her roommate bought for her to use because the vehicle she received at the time the parties separated needs approximately $1,500.00 in transmission repairs.

Financial Considerations

The parties' residence on Washington Avenue was severely damaged as a result of the flooding that occurred in 1999. They applied for a federal disaster loan and while the application was pending, they undertook repairing the house. Wife assumed that Debtor would pay the bills for the renovation from the proceeds of the insurance. When the receipts for the disaster loan were slow in coming, however, some of the construction bills were paid out of cash advances on credit cards for which Wife is liable for payment. In particular, one disbursement in the approximate amount of $11,000.00 and a second in the approximate amount of $6,500.00 were utilized for this purpose.

Debtor, who remained in the marital home on Washington Avenue after the parties separated, attempted without success to sell that property, which was encumbered by three mortgages. With the property under threat of imminent foreclosure, Debtor filed for Chapter 7 protection. The Chapter 7 Trustee, Wiley A. Wasden III, was unable to sell the property for an amount sufficient to retire the three mortgages, and this Court granted relief from stay to allow the mortgage holders to foreclose. The parties realized no profit from the subsequent sale.

The major customer for CRM, Debtor's current business, is Willamette Corporation, which at the time of the divorce had a contractual relationship with L-M, Debtor's former business in which Wife owns stock and serves as an officer. His work with Willamette had accounted for approximately 90% of L-M's business income. In 2001, L-M had a gross profit of approximately $80,000.00, a little more than $36,000.00 of which went to Wife in accordance with the requirements of the divorce agreements. After forming CRM, Debtor continued to use the "Lee-Michaels, Inc." checking account.

Debtor concedes that he has a greater future earning capacity than does Wife. His company grossed $480,000.00 last year and has a pre-tax gross profit of approximately twenty percent. His capacity for future earning, however, is tempered by his serious medical condition. In addition, without regard to his health complications, the fact that he is eight years older than Wife indicates that he is likely to have a career path of shorter duration than that of Wife.

Neither of the parties' budgets for personal expenses reveals any significant excess income. *See* Exs. P-3, D-1. Wife's budget reflects that she is sharing expenses with her

current companion on a fifty-fifty basis. Debtor, on the other hand, is not in an expense-sharing arrangement with his current companion; in fact, he provides monetary support for her and her child. A little more than one-half of Debtor's business's 2001 gross profit went to Wife for her $36,000.00 per year, plus tax withholding and payment of her car "allowance." Debtor's business may improve in the future, but there is certainly no guarantee that it will do so.

CONCLUSIONS OF LAW

Generally, all individual debts are dischargeable in a Chapter 7 bankruptcy, but 11 U.S.C. § 523(a) provides exceptions to dischargeability. Wife asserts two such exceptions as bases for her nondischargeability claim. Those exceptions involve certain debts to a debtor's former spouse subject to the requirements in §§ 523(a)(5) and (a)(15). At issue as to dischargeability in this case are the following obligations of Debtor to Wife: (1) the $36,000.00 yearly payment; (2) the $14,000.00 lump sum payment; (3) the $350.00 monthly payments; (4) the $20,000.00 lump sum payment; and (5) the $41,000.00 debt payment. Pursuant to the findings, conclusions, and reasons stated below, I conclude that the $20,000.000 payment is dischargeable and that each of the other listed obligations is nondischargeable.

1. The $36,000.00, $14,000.00, and $350.00 payment obligations are nondischargeable under application of § 523(a)(5).

Section 523(a)(5) provides that a Chapter 7 discharge

> does not discharge an individual debtor from any debt–

> . . .
> (5) to a . . . former spouse . . . of the debtor, for alimony to, maintenance for, or support of such spouse . . . in connection with a separation agreement, divorce decree or other order of a court of record . . . or property settlement agreement, but not to the extent that–
> . . .
>
> > (B) such debt includes a liability designated as alimony, maintenance, or support, unless such liability is actually in the nature of alimony, maintenance, or support; . . . .

In Smith v. Smith (In re Gene Kyle Smith), Adv. Nos. 96-2054 & 96-2085, Ch. 7 Case No. 95-20524 (Bankr. S.D. Ga. Dec. 30, 1997), this Court articulated the following legal framework for an (a)(5) determination:

> The burden of proof in establishing the § 523(a)(5) exception is on the non-debtor spouse. However, although exceptions from discharge are normally construed strictly against the objecting creditor in order to provide the debtor with a "fresh start," policy considerations require a bankruptcy court to construe domestic relations exceptions more liberally.
>
> Under [§] 523(a)(5), the non-debtor spouse must show that the obligation in issue is actually in the nature of support. If this burden is met, the burden of going forward shifts to the debtor to rebut the evidence that the provision is actually in the nature of support under [§] 523(a)(5). The ultimate burden remains with the creditor seeking to except the debt from discharge. . . .
>
> . . . . [T]he bankruptcy court must independently assess the character of an obligation arising out of a divorce and determine whether it is in the nature of alimony. Section 523(a)(5) requires that the bankruptcy court determine nothing more than whether the payment obligation is in the nature of "alimony, maintenance, or support." No precise inquiry into the parties' present

> financial circumstances is required; only a simple inquiry into the nature of the obligation, liquidating known amounts and leaving any issue of future modifications to the applicable state court.
>
> In determining whether a debtor's obligations is in the nature of support, the intent of the parties [or the trier of fact] at the time of the settlement agreement or trial is dispositive. While a label placed upon spousal obligation is not dispositive in determination of dischargeability, it is indicative of the parties' intent.

Id. slip op. at 10-12 (internal citations omitted).

The relevant time for making the § (a)(5) analysis is the time of the decree. Id. at 11. Factors critical to a determination of the parties' intent with respect to the provisions of a divorce settlement include any comparative disparities in their earning capacities, their potential business or employment opportunities, their physical conditions, their educational backgrounds, their probable future financial needs, and the benefits they would have received had their marriage not ended. Id. at 12 (citing Dennis v. Dennis (In re Dennis), 25 F.3d 274 (5th Cir. 1994)).

In this case, several provisions in the divorce decree are properly handled under § 523(a)(5). Two of these provisions were undisputedly in the nature of support – the provision for the $36,000.00 yearly payment to Wife, which was coupled with provisions for cost-of-living increases over a ten-year period, and the provision for health insurance. Indeed, Debtor did not dispute at trial the parties' intentions as to those provisions. The debts incurred pursuant to those provisions are therefore held non-dischargeable and Debtor remains

obligated to pay those sums to Wife as required by the divorce decree.

A third provision appearing to be in the nature of support is the $14,000.00 lump sum payment to Wife. Although Debtor testified that the $14,000.00 was to have been paid out of any profit realized from the sale of the residence, the agreement expressly stated that the $14,000.00 was to have been made "in addition to" both the real estate provision and the $36,000.00 annual support payment. Because the sum was derived in contemplation of Wife's future medical treatment or surgery and reflects a good-faith negotiation between the parties wherein they attempted to determine the out-of-pocket expenses for elective or non-covered dental and cosmetic surgical services, I find that the payment is closely related to Debtor's obligation to maintain health insurance, and as such, I hold that sum to be non-dischargeable.

Furthermore, I find that the provision for payment for transportation purposes is in the nature of support. Each party had a vehicle at the time of their divorce. Fully aware of that fact, Debtor agreed to provide for Wife to lease or purchase a vehicle for a monthly payment not to exceed $350.00 per month for a period of four years. Transportation is a fundamental need, and the existence of reliable transportation is in many cases a pre-condition to obtaining and keeping gainful employment. Therefore, I hold that the $350.00 payments are non-dischargeable.

The provisions for the $20,000.00 lump sum payment and the $41,000.00 debt payment, however, do not appear to have been in the nature of support. With respect to

the $20,000.00 lump sum payment, I find that the parties contemplated that amount to be partial compensation to Wife, rather than support of Wife. The terms of the separation agreement explained that the $20,000.00 sum was reimbursement to Wife for personal inheritance funds, and the parties arrived at that figure during their good-faith, pre-divorce negotiations. I find, therefore, that the preponderance of the evidence shows that the $20,000.00 provision was not in the nature of support, but, rather, was a division of property.

The provision for paying the $41,000.00 accrued credit card debt also appears not appear to have been in the nature of support. While any sum paid by one spouse to another as part of a domestic relations order inevitably contributes to – or if not paid, is detrimental to – the standard of living of the recipient spouse and therefore in a generic sense could be deemed to have been in the nature of support, Wife's basic needs were specifically contemplated and addressed in other provisions of the divorce decree, whereas the debt repayment was addressed in its own discretely captioned provision.

I conclude, therefore, that § 523(a)(5) applies to except the $36,000.00, $14,000.00, and monthly $350.00 obligations from discharge but does not apply to the $20,000.00 and $41,000.00 obligations.

2. The $20,000.00 debt obligation has been extinguished.

A true pre-petition division of property is not subject to challenge as a

voidable preference or fraudulent conveyance and is thus unaffected by bankruptcy.[2] As an example, title to property awarded through the course of domestic relations proceedings will ordinarily be unaffected. *See* Bush v. Taylor, 912 F.2d 989, 990 & 992-93 (8th Cir. 1990) (affirming bankruptcy court's determination that portion of debtor's government pension awarded to debtor's ex-spouse in divorce was constructive trust, thus not dischargeable "debt"); Hall v. Hall (In re Hall), 51 B.R. 1002, 1004 (S.D. Ga. 1985) (characterizing pension proceeds due non-debtor spouse as vested property interest which, upon equitable distribution, becomes sole and separate property of that spouse).

In this case, I find that the source of the $20,000.00 payment was to have been the profit realized in the sale of the marital residence. The parties' testimony conflicts as to the intended source of the payment: Debtor asserts that the anticipated profit from the sale of the residence, which never materialized, was to have been the source of that payment, and Wife disagrees. Because, however, the agreement expressly explains that the $20,000.00 sum "represent[ed] a portion of the inheritance monies left to [Wife]," and because the inheritance monies had been invested in the parties' residence, I find that a preponderance of the evidence supports Debtor's testimony that the source of the payment was to have been the profit realized upon sale of the residence. When the agreement was adopted by the domestic relations court, it was coupled with and became an encumbrance upon a true pre-petition division of property. Because the parties were unable to sell the home and to realize any

[2] Because it was not "the intent of the . . . Bankruptcy Code to convert the bankruptcy courts into family or domestic relations courts – courts that would in turn willy-nilly, modify divorce decrees of state courts insofar as these courts had previously fixed the amount of alimony and child support of debtors," Carver v. Carver, 954 F.2d 1573, 1579 (11th Cir. 1992) (citations omitted), this Court affords deference to Georgia court decisions in cases involving divorce.

equity, the mutually anticipated source for payment of these sums was insufficient. I find, therefore, that Debtor's $20,000.00 payment obligation was extinguished upon foreclosure and sale of the property.

Unlike the $20,000.00 sum, the $41,000.00 debt obligation was a division of property not dependent upon receipts from its sale. The settlement Agreement provided for the $41,000.00 amount in a provision specifically captioned "Accrued Debts." That provision, which was distinct from the "Monetary Settlement" provision which identified Debtor's other obligations, reflects the parties' agreement to a division of debt payment responsibility that was unrelated to the parties' residence. I find, therefore, that the $41,000.00 obligation was not extinguished upon sale of the residence. Accordingly, the issue of dischargeability with respect to that payment is addressed by applying § 523(a)(15).

3. The $41,000.00 debt is nondischargeable under application of § 523(a)(15).

Section 523(a)(15) provides that a Chapter 7 discharge

> does not discharge an individual debtor from any debt–
> . . .
> (15) not of the kind described in paragraph (5) that is incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court of record . . . unless –
>
> (A) the debtor does not have the ability to pay such debt from income or property of the debtor not reasonably necessary to be expended for the maintenance or support of the debtor or a dependent of the debtor and, if the debtor is engaged in a business, for the payment of expenditures necessary for the continuation,

preservation, and operation of such business; or

(B) discharging such debt would result in a benefit to the debtor that outweighs the detrimental consequences to a . . . former spouse . . . of the debtor; . . . .

The language of § 523(a)(15) creates an evidentiary sequence and structure which bind this Court in this matter. Stated broadly, each party bears certain burdens of proof and production in a § 523(a)(15) determination. *See, e.g.*, Hart v. Molino (In re Molino), 225 B.R. 904, 907 (B.A.P. 6th Cir. 1998) (noting burdens of objecting creditor and debtor) ; Smith v. Smith (In re Dale Smith), Adv. No. 96-4181, Ch. 13 Case No. 96-42099, slip op. at 8-9 (Bankr. S.D. Ga. Oct. 6, 1997) (Davis, J.) (noting shifting burdens of production); Stone v. Stone (In re Stone), 199 B.R. 753, 783 (Bankr. N.D. Ala. 1996) ("[M]ultiple burdens of proof may be allocated within a case and . . . separate burdens of going forward may exist and shift back and forth for each issue for which different parties bear the burden of proof. ").

Wife has the burden of proving the objection. *See* Fed. R. Bankr. P. 4005. To meet her initial burden of production, Wife must show that the debts in issue were incurred during divorce proceedings. *See* § 523(a)(15) (excepting from discharge *any* non-support divorce debt "incurred by the debtor in the course of a divorce . . . *unless*" either of subsections (A) or (B) applies (emphases added)). If Wife makes the initial showing, she has borne her initial burden of production.

Next, Debtor may rebut Wife's showing. *See* In re Dale Smith, slip op. at 6. If he does not, a presumption arises that the debt is nondischargeable. Debtor may rebut that

presumption by showing that one of the two conditions following the "unless" is satisfied. He may show either that he does not have the means to pay those debts from income not reasonably necessary to pay expenses of himself, his dependents, or his business, or, even if he does have the means to pay, that discharging the debts would benefit him more than it would harm Wife. Id. 523(a)(15)(A), (B); *see also, e.g.,* Ashton v. Dollaga (In re Dollaga), 260 B.R. 493, 497 (B.A.P. 9th Cir. 2001) (noting disjunctive statement); Molino, 225 B.R. at 907 (noting debtor's burden to prove either of the exceptions in subsections (A) and (B)); In re Dale Smith, slip op. at 9 ("If the debtor has the ability to pay, debtor still may attempt to discharge the debt pursuant to [§] 523(a)(15)(B)."). Should Debtor fail to prove one of these elements, Wife's presumption of nondischargeability would stand and this Court must necessarily conclude that the debts are excepted from Debtor's Chapter 7 discharge.

Wife has met her initial burden for presumptive nondischargeability, in that the $41,000.00 debt obligation was included in the property settlement and divorce decree. Because Debtor has not rebutted that showing, he must show that one of the two exceptions provided in subsections (a)(15)(A) and (B) is applicable. Debtor must make these showings by a preponderance of the evidence. Molino, 225 B.R. at 907 (citing Grogan v. Garner, 498 U.S. 279, 291, 111 S. Ct. 654, 661, 112 L. Ed. 2d 755 (1991)).

The totality of circumstances and all equities are properly considered in applying § 523(a)(15). Cleveland v. Cleveland (In re Cleveland), 198 B.R. 394, 398 (Bankr. N.D. Ga. 1996). Subsection (a)(15)(A) requires that any expenses must be "reasonable" and that the debtor has the means to pay them. *See* In re Dale Smith, slip op. at 8 (noting twofold analysis: disposable

income test to determine whether expenses are reasonably necessary and consideration of debtor's ability to pay). Relevant considerations include the debtor's disposable income as measured at the time of trial, possibility of more lucrative employment opportunities, whether the debtor's debt burdens will be lessened in the future, and whether the debtor has previously made a good faith effort to satisfy the debt sought to be discharged. Id. at 8-9 (adopting factors identified in In re Walford, Adv. No. 97-01026A (Bankr. S.D. Ga. Aug. 29, 1997) (Dalis, J.)); Cleveland, 198 B.R. at 398.

Here, Debtor's business is holding its own. Debtor has not proven that CRM reasonably requires, for its "continuation, preservation, and operation," the funds that he is obligated to pay Wife under terms of the divorce Agreement. Moreover, some funds that Debtor used to operate C. R. Michaels, Inc., his new business, were taken out of the account in the name of Lee-Michaels, Inc., in which Wife was a shareholder. It appears that those funds should have been applied to his obligation to Wife.

In addition, although Debtor's health condition is a continuing question with respect to his future earning potential, evidence indicates that his health, like his business, is stable. Furthermore, because Debtor's expertise in the environmental engineering field is portable, should CRM cease to provide sufficient financial support, he has other earning potential. Looking at Debtor's situation, which reflects sufficient funds to provide for himself, his business, and support for two non-dependents, there is reason to believe that he can afford to pay his obligations to Wife. I conclude, therefore, that the funds awarded to Wife under the divorce decree are not reasonably necessary to support Debtor or his business.

In applying subsection (a)(15)(B), the circumstances to be considered include a variety of factors, such as the income and expenses of the parties, the debtor spouse's ability to pay the debt, and even intangible effects such as "some horrible non-economic detriment to health, liberty, or something else of great material value to the non-debtor party," Taylor v. Taylor (In re Taylor), 191 B.R. 760, 767 (Bankr. N.D. Ill. 1996). *E.g.*, Cleveland, 198 B.R. at 400 (Bankr. N.D. Ga. 1996). Here, the equities respecting the parties' comparative current financial situations and future financial prospects appear to weigh equally. Currently, neither Debtor nor Wife appear to have any significant excess income. *See* Findings, *supra*, at 7. Wife receives some assistance from her live-in companion, in that they share expenses. Although Debtor has no similar source of financial help, he has enough excess income to have voluntarily expended his personal funds on his companion and her child. Regarding the future, both parties are capable of improving their financial situations, but neither is assured of improvement. Debtor concedes that his earning potential is greater than Wife's, yet there is no guarantee that Debtor's business will continue to hold its own and improve. Wife currently has a low-paying job, but, in light of her education, skills and demeanor, there is no reason why she cannot find a higher-paying job; indeed, she has held several jobs with more promise than her current position.

As for other considerations that could affect the parties' respective situations in the future, they also appear – at least from this Court's prospective view – to balance out. Debtor's admittedly higher potential for earning balances out against Wife's comparative youth and good health. Neither party is financially encumbered by dependents. Both parties have apparent options for earning their livings other than their present jobs. I conclude, therefore, that Debtor has not

borne his burden to show by a preponderance of the evidence that the benefits of a discharge to him outweigh the detriment of a discharge to Wife.

Because Debtor has neither rebutted Wife's *prima facie* showing of nondischargeability nor shown that either of the exceptions in subsection (a)(15) applies, the presumption established by Wife that the $41,000.00 property-settlement payment is nondischargeable stands. Wife has successfully carried her burden of proof for nondischargeability under subsection (a)(15).

ORDER

Pursuant to the above, IT IS THE ORDER OF THIS COURT that the following obligations of Debtor to his former wife Cynthia Lee are non-dischargeable: (1) the $36,000.00 yearly support payments; (2) the $14,000.00 lump sum payment; (3) the $350.00 monthly payments; and (4) the $41,000.00 debt payment. IT IS FURTHER ORDERED that the $20,000.00 payment is discharged.

Lamar W. Davis, Jr.
United States Bankruptcy Judge

Dated at Savannah, Georgia
This 23rd day of September, 2002