SO ORDERED.

SIGNED this 14th day of September, 2016.

Janice Miller Karlin
United States Chief Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
DISTRICT OF KANSAS

In re:

Frederick Prins and
Rosella Marie Prins

Debtors.

Case No. 14-22063-7

Order Denying Debtors' Motion to Convert

Debtors Frederick and Rosella Prins ("Debtors") move to convert their Chapter 7 case filed two years ago, in August 2014, to a Chapter 13, relying on 11 U.S.C. § 706(a).[1] The Chapter 7 Trustee, Christopher Redmond ("Trustee" or "Chapter 7 Trustee"), objects, arguing that Debtors cannot convert their case because they are not eligible to be debtors under Chapter 13 as required by § 706(d). He argues Debtors are attempting to abuse the bankruptcy process and further delay the equitable

[1] Doc. 59. For the remainder of this decision, all references to Title 11 of the United States Code will be to section number only.

administration of their Chapter 7 estate through conversion.[2] Because a converted case would undoubtedly be subject to a dismissal for cause under § 1307(c) due both to Debtors' failure to act in good faith and their inability to consummate a plan that would allow them to retain their residence—their stated goal—the Court denies Debtors' motion.

I. Findings of Fact and Procedural History[3]

The main source of contention surrounding Debtors' bankruptcy filings concerns debts they owe for the purchase of their primary residence located in Leawood, Kansas. They purchased the home in December, 2013 for approximately $483,460. North American Savings Bank ("NASB") loaned Debtors $311,500 and the rest of the purchase money came from two sources: $162,534 from Mr. Prins's boss, Robert Balderston and $9,425 from Debtors. Debtors agreed to give Balderston a second mortgage to secure the loan, but Balderston failed to record the mortgage until almost nine months later, on September 5, 2014. Debtors had filed their Chapter 7 case eight days earlier.

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[2] Doc. 70.

[3] As this case has a long and complicated procedural history, the facts described below are taken from a variety of sources and, unless otherwise indicated, come from either testimony at the hearing on Debtors' motion to convert held August 22, 2016, documents filed in Debtors' Chapter 7 case (case no. 14-22063), documents filed in the adversary proceedings in Debtors' Chapter 7 case (case nos. 16-6044 and 16-6071), or Debtors' Chapter 13 case (case no. 15-22260). *See Job v. Calder* (*In re Calder)*, 907 F.2d 953, 954 n.2 (10th Cir. 1990) ("Under Fed. R. Evid. 201(b)(2), which is applicable in bankruptcy cases, *see* Fed. R. Bankr. P. 9017, a court may take judicial notice of facts that are not subject to reasonable dispute in that they are "capable of accurate and ready determination by resort to sources whose accuracy cannot reasonable be questioned." (internal quotation omitted)).

Mr. Prins lost his job with Mr. Balderston a few months later—in April, 2014, and Debtors were unable to make the required payments of $2,810 and $2,000, respectively, owed to NASB and Balderston.[4] Although Mr. Prins found another job within a few months,[5] which paid an even higher salary than his job with Balderston,[6] Debtors were unable to cure the delinquency then owed to NASB because it demanded Debtors cure the entire (then four month's) delinquency.

Debtors filed a Chapter 7 petition on August 28, 2014; their budget showed a negative $3,244 cash flow even though Mr. Prins was now earning gross monthly wages of $11,249. In their schedules, Debtors valued their home at $445,000 and listed NASB and Balderston as secured creditors holding claims totaling $473,397. Debtors claimed an exempt interest in the property under Missouri law— specifically RSMo §

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[4] *See* Case no. 14-22063, Doc. 1, p. 33; Ex. C. The NASB payment is an escrowed loan, meaning it includes the estimated amount needed to pay homeowner's insurance and real property taxes.

[5] Mr. Prins testified under oath he found the new job with APCO in July, 2014, but his sworn Schedule I filed August 28, 2014 indicates he had been employed by APCO for three months. That would put his new employment date more like the end of May and therefore he was only out of work a couple of months. *See* Case no. 14-22063, Doc. 1, p. 31.

[6] Debtors' Statement of Financial Affairs dated August, 2014 showed that Mr. Prins earned $131,000 in 2013. Mr. Prins testified at the August 22, 2016 hearing that his salary from his next employer—APCO—increased to $135,000 annually. He further testified he was now making $10,000 per month from Kintz Group. Exhibit U, a payroll stub for Mr. Prins from Kintz Group, LLC, showed Debtor had made $79,633 through August 14, 2016—approximately the first 32 weeks of the year. Thus, it appears Mr. Prins is now earning around $129,400 annually, with the opportunity for commissions. Exhibit U also showed that Mr. Prins is not withholding wages for payment of state or federal income taxes. Upon questioning, he admitted that although more than two quarters of 2016 have passed, he has not filed any self-employment returns or paid any estimated taxes on those earnings.

513.430.1(3)[7]—but valued that interest at $0.00.[8] Debtors also stated on Schedule B that they owned two cars—a 2011 Ford Explorer worth $28,000 and a 2007 Hummer H3 worth $15,000. Debtors listed both vehicles as exempt on Schedule C but, again, valued the exemption at $0.00.[9] No party objected to Debtors' exemptions and they were thus allowed for the amounts claimed.

Beginning in October, 2014, the Chapter 7 Trustee made several requests for copies of Debtors' 2014 state and federal tax returns and informed Debtors they were not to dispose of any refunds until the Trustee had received the returns. Those returns were, obviously, not due until mid-April, 2015, so these requests appear aimed at insuring Debtors understood their duty to produce those returns when timely filed, and at insuring Debtors understood the estate was entitled to receive almost 8/12 of any refund.

Debtors received their general discharge on January 13, 2015. The Trustee continued to send Debtors requests for a copy of their 2014 tax returns through

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[7] This statute exempts "property of any kind, not to exceed in value six hundred dollars in the aggregate." RSMo § 513.430.1(3). It is not clear why Debtors chose to exempt their house under this exemption, instead of the homestead exemption, RSMo § 513.475, which exempts up to $15,000. However, as the exemption was allowed, this issue is not dispositive.

[8] Pursuant to § 522(b)(3)(A), Debtors' domicile was deemed to be in Missouri, as they had moved to Kansas less than 2 years prior to filing their petition. While it appears Debtors could have claimed a Missouri homestead exemption, which can be used extra-territorially but is limited to $15,000, they did not. *See In re Woodruff*, No. 04-63288, 2005 WL 1139891, *3 (Bankr. W.D. Mo. Apr. 28, 2005) ("Nothing in the Missouri homestead statute limits its applicability to Missouri real estate.").

[9] Debtors claimed their cars exempt under RSMo § 513.430(5), which allows an exemption for "[a]ny motor vehicle, not to exceed three thousand dollars in value in the aggregate."

September, 2015; Debtors ignored those requests. Only after the Trustee was forced to file a motion to compel turnover of the returns—on September 3, 2015—did Debtors finally provide copies to the Trustee. The Trustee responded—the very same day he received the returns—that under a pro rata formula, Debtors were required to turnover $9,198.25 of the $13,989 refund.

Notwithstanding numerous reminders from the Trustee that they were not entitled to retain $9,198.25 of the refund, Debtors spent the entire $13,989. Mrs. Prins testified she opted to use the money to pay their sons' education expenses (in mid-October 2015) instead of turning over any portion to the Trustee. The Trustee continued to inquire about the status of the refunds and request the amount owed the estate, but Debtors continued to ignore his inquiries. The Trustee was forced to file yet another Motion to Compel, this time for turnover of the refund, due to Debtors' total lack of cooperation.[10]

Simultaneous to the above dispute over tax returns, both NASB and Balderston requested and received relief from the automatic stay so they could pursue their *in rem* rights against Debtors' Leawood property.[11] NASB filed a foreclosure petition in state court requesting foreclosure of its mortgage (noting Debtors still owed the principal amount of $310,962.11) and an order of sale. An unopposed judgment was entered

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[10] *See* Case no. 14-22063, Doc. 78.

[11] Because no one objected to either motion, the Court granted NASB's motion for relief from the automatic stay on October 24, 2014 and granted Balderston's on March 30, 2015. *See* case no. 14-22063, Docs. 19 and 37. Neither order indicated the Trustee had abandoned the estate's interest in that real property, and thus it remained property of the Chapter 7 estate.

ordering a foreclosure sale with the proceeds going first to NASB and then to Balderston.[12]

On the eve of the sheriff's sale—October 27, 2015—Debtors filed another bankruptcy while their Chapter 7 case remained open for administration. The second filing, a Chapter 13 petition, was assigned to the Honorable Judge Robert Berger ("the Chapter 13 case").[13]

Debtors' Chapter 13 schedules were distinctly different from those filed in their Chapter 7 case less than a year earlier. First, Debtors now valued their house on Schedule A at $456,000, instead of $445,000, and listed $544,000 of debt secured by the house, up significantly from the value listed on Schedule A in their Chapter 7 case ($473,397). Second, Debtors now attempted to exempt their house under Kansas exemption laws (although it had been found non-exempt in their Chapter 7) and claimed an exemption of $81,000. Third, on Schedule D, Debtors listed NASB as a secured creditor with a $375,000 claim and Balderston with a $169,000 claim—adding the note that Balderston did not have a "valid mortgage, recorded in violation of the automatic stay."[14] Fourth, during 2015, Debtors replaced their 2011 Ford Explorer with two used BMW vehicles—a 2007 328i valued at $7,714 and a 2010 X3 valued at

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[12] *See* Case no. 16-6044, Doc. 19, Ex. 3, p. 6.

[13] *See* Case no. 15-22260.

[14] Case no. 15-22260, Doc. 1, p. 9. As noted above, Debtors' Chapter 7 case was filed on August 28, 2014 and Balderston's mortgage was recorded September 5, 2014. While the Trustee has filed a recent complaint requesting the Court avoid Balderston's lien, no decision has been made regarding that lien.

$13,204. Finally, Debtors' Schedule I revealed Mr. Prins had a different employer than when he filed the Chapter 7 case—and that his net income from that employment was now $10,000 monthly.[15] This Schedule I also reported that Mrs. Prins was now receiving Social Security income of $2,800 a month, although she testified $900 of that actually belongs to one or more of their children.[16]

Although fourteen months earlier Debtors had sworn they had a negative cash flow of $3,244, they now filed a plan in this new Chapter 13,[17] calling for monthly plan payments of $5,813. The plan proposed to pay NASB $2,800 a month in post-petition mortgage payments while paying their pre-petition arrearage pro rata through the Chapter 13 Trustee, William Griffin. In the non-standard language section of paragraph 9(b) of their plan, Debtors stated: "There is a second mortgage on Debtor's [sic] home held by Robert Balderston. The mortgage was recorded on September 5, 2014 in violation of the automatic stay on their previous Chapter 7 filed on August 28,

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[15] Debtor disclosed that his average gross income in the six months prior to filing his Chapter 13 was actually $13,776.98/month, not $10,000 a month. *See* Case no. 15-22260, Doc. 21, p. 29. Debtors' Form 22C-1 shows the median family income for a family of five in Kansas is $84,117; thus, even without counting the family's $33,600 annual Social Security Disability income, their income was essentially double ($165,323) that for a median income family of five in Kansas. *Id.* at p. 31.

[16] Although Mrs. Prins testified she received $1,700 a month in Social Security Disability benefits and her son received $900 a month, she also testified the total was actually $2800 a month, not $2600 a month. Even more significantly, Debtors failed to include any of that income in their 2014 Schedule I on Line 8e, where it is required to be disclosed, although she was clearly receiving that income by August, 2014, the month of filing. *See* Case no. 14-22063, Doc. 1, p. 32, ¶ 8e.

[17] *See* Case no. 15-22260, Doc. 16, filed November 10, 2015.

2014. This lien will be avoided."[18] Debtors also proposed to repay at $400/month the $9,198.25 refund they had improperly withheld from the Chapter 7 Trustee, $957 to three car creditors, and 100% to their unsecured creditors.

Both the Chapter 7 Trustee and Mr. Balderston objected to Debtors' plan. The Chapter 7 Trustee objected on the grounds that Debtors claimed their house as an exempt asset of the Chapter 13 estate when it remained a non-exempt asset of the still open Chapter 7 estate. He noted that because Debtors have no right, title, or interest in it, they could not propose to retain it. Balderston objected to Debtors' plan because it did not provide for the repayment of his lien. Additionally, the Chapter 13 Trustee filed a motion to dismiss because Debtors failed to make the required $5,813 monthly plan payments.[19] By the time of the March 22, 2016 hearing on the objections to confirmation and motion to dismiss, Debtors were already over $23,000 delinquent in their plan payments, and another $5,813 plan payment was due in nine days.[20]

Debtors' counsel advised the Court at the hearing that Debtors preferred to deal with the issue surrounding Balderston's mortgage and potential equity in the house

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[18] Case no. 15-22260, Doc. 60, ¶ 9(b).

[19] The original plan called for payments of $5,525, the first amended plan called for payments of $5,679, and the second amended plan called for payments of $5,813. The increase is likely due to notices that NASB had filed with the Court regarding payment changes.

[20] The motion to dismiss calculated Debtors' delinquency at $11,204 through December, 2015. *See* Case no. 15-22260, Doc. 47. Thus, by the end of March, Debtors owed another three months' worth of plan payments, or approximately $17,439, though they had made a partial payment of $2,762.50 in January. *See* Ex. A. In fact, although § 1326(a)(1) requires the first plan payment be made within 30 days of filing, Debtors never made even one full plan payment during the entire pendency of the Chapter 13 proceeding.

in their still-pending Chapter 7 case. As a result, Debtors agreed their Chapter 13 case could be dismissed.[21]

Within a few months of the dismissal, however, Debtors apparently had a change of heart and filed three motions in their Chapter 7 case. Again, that case remained open because the Trustee had assets to administer—specifically, the estate's portion of Debtors' 2014 refund and potentially Debtors' non-exempt residence if the Trustee determined the estate would benefit from its sale. Debtors' three motions requested orders from the Court: (1) vacating their discharge;[22] (2) vacating the order granting relief from stay to Balderston;[23] and (3) converting their case to one under Chapter 13 (although their counsel had expressly admitted the Chapter 7 proceeding was the better forum for adjudicating issues surrounding the Leawood real estate).[24] This Court has recently denied both motions to vacate on procedural grounds.[25] As to the third motion, however, the Court required evidence before deciding whether to grant Debtors' motion to convert.

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[21] *See* Ex. B, p. 5, lines 3–9 and case no. 15-22260, Doc. 79.

[22] Case no. 14-22063, Doc. 55.

[23] *Id*. at Doc. 57.

[24] *Id.* at Doc. 59.

[25] The Court declined to vacate Debtors' discharge order (Doc. 55) because that motion had been filed more than a year after the prior order had been entered, and thus outside the one year period required by Fed. R. Civ. P. 60(c)(1) (applied in bankruptcy courts under Fed. R. Bankr. P. 9024). *See* Case no. 14-22063, Doc. 106. The Court declined to vacate the stay relief order to Balderston because vacating a stay can only be granted in an adversary proceeding. *See* Fed. R. Bankr. P. 7001(7). *See id.* at Doc. 89.

At the trial, Stephanie Wright (an assistant vice president and default manager at NASB), William Griffin (the Trustee in Debtors' Chapter 13 case), and each of the Debtors testified. Debtors, who the Court found articulate and seemingly well-educated, testified primarily on the circumstances surrounding their two bankruptcy cases and their motivation for filing for bankruptcy relief—supposedly to save their home. Both admitted that they had spent the entirety of their 2014 tax refund (which totaled $13,989) on personal expenses when they knew a substantial percentage of it ($9,198.25) was an asset of their Chapter 7 estate and not theirs to spend. Debtors testified they hope to make a second Chapter 13 plan work, though they recognize that their plan payment would have to substantially increase to "between $6,200 to $7,000" from the $5,813 they were unable to pay under their last Chapter 13 case.[26] In fact, although their prior Chapter 13 case was pending for five months, meaning they should have made payments for at least four of those months (approximately $23,252), the total Debtors paid during that entire plan was $2,762.50. And the Chapter 13 Trustee was required to return all but $158.84 of that to Debtors when their case was dismissed.

Debtors therefore retained over $23,000 during the pendency of their case and

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[26] There are at least two reasons their payment would now have to be so much higher—assuming Debtors even have the legal right to retain the real estate in light of it being non-exempt property. The first reason is because of the provisions of §1322(d): a Chapter 13 plan cannot "provide for payments over a period that is longer than 5 years." Since the Chapter 7 proceeding from which they seek conversion was filed in August, 2014, they would now have approximately 48 months to cure the arrearage to NASB (assuming a not as-of-yet filed plan could be confirmed, after notice and hearing, in the next month). In addition, that arrearage has grown considerably because Debtors have failed to make a single payment to NASB since April, 2014.

simply spent it. They saved nothing between the dismissal of their Chapter 13 case and the hearing on their motion to convert, admitting at trial that, at most, they might have $1,000 total savings.

Debtors did not produce at trial an updated budget (which most debtors provide in the form of amended Schedules I and J) to support their optimism that they can now pay $6,200–$7,000 monthly if allowed to convert. Nor did they submit to the Court a proposed Chapter 13 plan so the Court, the Trustees, or Mr. Balderston could analyze its feasibility.

The Trustee called NASB's representative, Ms. Wright, to testify about its records. She testified that between the time the loan closed in December, 2013 and the trial approximately 32 months later, Debtors made a total of two mortgage payments (on March 31, 2014 for the months of February and March, 2014). One other payment, made June 30, 2014, was returned due to insufficient funds. Thus, the March 31, 2014 payment was the last time NASB received any money on its loan. As of the hearing, the delinquency on NASB's loan had grown to roughly $80,000.[27]

Finally, Mr. Griffin—the Chapter 13 Trustee on the first Chapter 13 case and the person who would be the Trustee were conversion allowed—testified to the events that occurred in Debtors' previous Chapter 13 case. He also testified, after hearing Debtors testify to their albeit vague potential Chapter 13 plan and after hearing the

[27] Because Debtors have wholly failed to perform on their NASB loan, NASB also needed to advance two years of real property taxes and homeowners' insurance costs to protect the collateral securing its loan. The negative escrow balance is now $21,738. *See* Ex. C.

testimony from the NASB representative, about the feasibility of a possible plan.

According to Mr. Griffin, and after a review of Debtors' prior Chapter 13 plan, Debtors would need to propose payment of the following over the remaining approximate 48 months to have a confirmable plan:

1. $80,000 delinquency to NASB;
2. the ongoing $2,810 mortgage payment to NASB (x 48 months = $134,800);
3. at least the value of the non-exempt real property over and above NASB's debt (if Balderston's lien can be avoided), estimated at approximately $70,000;[28]
4. $9,198.25 owed to the Chapter 7 Trustee;
5. payments on the three automobiles that Debtors' prior plan proposed at $957 per month; and
6. at least $2,500 in their own attorney fees.[29]

This sum would be on top of Debtors' monthly household expenses, which they reflected in their 2015 Chapter 13 Plan totaled $5,250 per month (excluding their house payment). Mr. Griffin testified that, based on his twenty six years experience as a Chapter 13 trustee, and Debtors' demonstrated poor performance in their recent Chapter 13, his opinion was that Debtors could not feasibly sustain a budget and plan payment that met that criteria.

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[28] The actual value of the real estate, and therefore the amount Debtors might be required to pay if Balderston's lien is avoided, has not been determined. Debtors estimated its fair market value at $456,000 in Schedule A of their recent Chapter 13 case. If Balderston's lien is not avoided by the Chapter 7 Trustee, they would need to pay his entire $2,000 per month mortgage payment.

[29] This Court also ordered Debtors to pay $500 in attorney fees to the Chapter 7 Trustee due to their total lack of cooperation regarding the 2014 tax refunds. *See* Case no. 14-22063, Doc. 50, Order Granting Motion to Compel (finding that "[d]ue to the Debtors' disregard for their responsibility and obligation to comply with the Trustee's requests, the Trustee has had to expend a great deal of time and expense in this matter" and awarding $500 to counsel for Trustee). No evidence was received whether Debtors have paid this fee.

II. Conclusions of Law

Debtors request the Court allow them to convert their two-year old Chapter 7 case to one under Chapter 13 so they may continue to occupy their home, attempt to avoid Balderston's mortgage and pay the value of his avoided lien to unsecured creditors, and cure the ever-increasing delinquency they owe NASB. A hearing to determine whether a debtor's estate should be administered under Chapter 7 or Chapter 13 is a core proceeding under 28 U.S.C. § 157(b)(2)(A), over which this Court may exercise subject matter jurisdiction.[30]

A. Standard of Review under § 706(a)

Section 706(a) states that a "debtor may convert a case under this chapter to a case under chapter 11, 12, or 13 of this title at any time, if the case has not been converted" previously. Subsection (d) continues: "Notwithstanding any other provision of this section, a case may not be converted to a case under another chapter of this title unless the debtor may be a debtor under such chapter." The Supreme Court interpreted these two subsections in *Marrama v. Citizens Bank of Massachusetts*[31] to include an implicit reference to § 1307(c) and held that "a chapter 7 debtor may forfeit his right to proceed under Chapter 13 if the converted case would be subject to immediate dismissal or conversion for cause under § 1307(c)."[32] Thus, the Court evaluates a motion to convert under § 706(a) based on what constitutes cause for dismissal or

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[30] 28 U.S.C. §§ 157(b)(1), 1334(b).

[31] 549 U.S. 365 (2007).

[32] *In re Ortega*, 434 B.R. 889, 892 (Bankr. D. Kan. 2010) (interpreting *Marrama*).

conversion under § 1307(c).[33]

Subsection (c) of § 1307 contains a non-exclusive list of eleven causes for dismissing or converting a Chapter 13 case.[34] In *Gier v. Farmers State Bank of Lucas, Kansas (In re Gier)*,[35] the Tenth Circuit recognized bad faith (or a lack of good faith) as an additional "cause" under § 1307(c) to convert or dismiss a Chapter 13 case.[36] According to *Gier*, in order to dismiss or convert a case under § 1307(c) for bad faith, courts should analyze the facts under a "totality of the circumstances" test.[37] The *Gier* court adopted the Seventh Circuit's analysis in *In re Love*,[38] which "provided the following nonexhaustive list of factors relevant to a § 1307(c) bad faith inquiry:

> [T]he nature of the debt, including the question of whether the debt would be nondischargeable in a Chapter 7 proceeding; the timing of the petition; how the debt arose; the debtor's motive in filing the petition; how the debtor's actions affected creditors; the debtor's treatment of creditors both before and after the petition was filed; and whether the debtor has been forthcoming with the

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[33] *See In re Werts*, 410 B.R. 677, 689 (Bankr. D. Kan. 2009) ("Thus, it is appropriate for bankruptcy courts to evaluate a motion based on § 1307(c) when a Chapter 7 debtor seeks to convert a case to Chapter 13.").

[34] *See Gier v. Farmers State Bank of Lucas, Kansas (In re Gier)*, 986 F.2d 1326, 1329 (10th Cir. 1993) (holding that debtor's case was properly dismissed for cause because it was filed in bad faith).

[35] 986 F.2d 1326 (10th Cir. 1993).

[36] *Id.* at 1330.

[37] *Id.* at 1329 ("We join the Seventh Circuit and conclude that in determining whether a Chapter 13 petition has been filed in bad faith under § 1307(c), the bankruptcy court must consider the 'totality of the circumstances.'") (quoting *In re Love*, 957 F.2d 1350, 1354 (7th Cir. 1992)).

[38] 957 F.2d 1350.

bankruptcy court and the creditors.[39]

The *Gier* court stressed that the ultimate question is "whether or not under the circumstances of the case there has been an abuse of the provisions, purpose, or spirit" of Chapter 13.[40]

The Trustee has the burden of proving that Debtors lack the requisite good faith to convert their case under § 706(a).[41]

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[39] *Gier*, 986 F.2d at 1329 (quoting *Love*, 957 F.2d at 1357). The *Gier* court also referenced the factors given in *Flygare v. Boulden*, 709 F.2d 1344 (10th Cir. 1983), to assess the totality of the circumstances in a § 1325(a)(3) good faith analysis, as both good faith inquiries are similar. *Id.* Those factors are: "'(1) the amount of the proposed payments and the amount of the debtor's surplus; (2) the debtor's employment history, ability to earn and likelihood of future increases in income; (3) the probable or expected duration of the plan; (4) the accuracy of the plan's statements of the debts, expenses and percentage repayment of unsecured debt and whether any inaccuracies are an attempt to mislead the court; (5) the extent of preferential treatment between classes of creditors; (6) the extent to which secured claims are modified; (7) the type of debt sought to be discharged and whether any such debt is non-dischargeable in Chapter 7; (8) the existence of special circumstances such as inordinate medical expenses; (9) the frequency with which the debtor has sought relief under the Bankruptcy Reform Act; (10) the motivation and sincerity of the debtor in seeking Chapter 13 relief; and (11) the burden which the plan's administration would place upon the trustee.'" *Flygare*, 709 F.2d at 1347–48 (quoting *United States v. Estus (In re Estus)*, 695 F.2d 311, 317 (8th Cir. 1982)). The Court recognizes that *Flygare* has admittedly been modified by *Anderson v. Cranmer (In re Cranmer)*, 697 F.3d 1314, 1319 n. 5 (10th Cir. 2012), though notes that the Tenth Circuit's reasoning for narrowing *Flygare*'s focus was that "[s]ection 1325(b)'s 'ability to pay' criteria subsumes most' of the *Flygare* factors. As § 1325 is not at issue here, the Court reviews the facts for good faith using the eleven *Flygare* factors and considers the *Cranmer* factors as well. *See id.* ("A bankruptcy court must consider "factors such as whether the debtor has stated his debts and expenses correctly; whether he has made any fraudulent misrepresentation to mislead the bankruptcy court; or whether he has unfairly manipulated the Bankruptcy Code.") (quoting *Educ. Assistance Corp. v. Zellner*, 827 F.2d 1222, 1227 (8th Cir. 1987)).

[40] *Gier*, 986 F.2d at 1329. *See also In re Werts*, 410 B.R. at 690 (stating that the "key inquiry for courts attempting to ascertain a debtor's good faith is whether the debtor is seeking to abuse the bankruptcy process" (internal quotations omitted)).

[41] *See Condon v. Smith (In re Condon)*, 358 B.R. 317, 326 (6th Cir. BAP 2007) ("[T]he burden of proving a lack of good faith in the context of § 706(a) is on the party opposing the conversion."). This Court has previously adopted the Sixth Circuit's reasoning regarding the burden of proof under § 706(a) as the Court has been unable to locate any Tenth Circuit

B. Application of the 'Totality of the Circumstances' Test

The Trustee alleges the following facts support a finding that Debtors are attempting to convert their case to Chapter 13 in bad faith:

(1) Debtors' refusal to promptly provide him a copy of their 2014 tax returns; despite numerous requests for a copy of those returns;

(2) Debtors' failure to pay the estate's portion of their 2014 income tax to the estate when they understood their duty to do so;

(3) Debtors' failure to respond to numerous inquiries about those returns and subsequent refunds, requiring the Trustee to file motions to compel and thus wasting estate resources for the requisite costs and fees attendant to pursuing the returns and refunds;

(4) Debtors' failure to make any payment on their NASB note secured by their residence from April, 2014 through the date of the conversion trial, notwithstanding their high household income;

(5) Debtors' filing a separate Chapter 13 proceeding to stop the foreclosure sale and attempting to claim their residence as exempt when Debtors have consistently admitted it was deemed non-exempt in the Chapter 7 proceeding;

(6) Debtors' consenting to the dismissal of that Chapter 13 proceeding for the express purpose of allowing the Chapter 7 Trustee to administer the non-exempt real estate (including any attempt to avoid the Balderston mortgage), but soon thereafter seeking conversion to a Chapter 13—all the while having never made one full plan payment to the Chapter 13 Trustee during the five months that case was administered; and

(7) Debtors' failure to provide evidence to support their contention that, given their income, expenses, debt, prior dismissal of their Chapter 13 case, and remaining time to make payments (approximately 48 months), they could propose a confirmable plan if conversion were allowed.

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precedent on the issue. *See In re Werts*, 410 B.R. at 690; *see also In re Ortega*, 434 B.R. at 893 (adopting the Sixth Circuit's reasoning in *Condon* regarding the standard under which a court should deny a debtor's motion to convert).

1. Debtors' Prior Chapter 13 Case

While a Chapter 13 plan's feasibility is not required to be shown at the conversion stage,[42] the recent dismissal of a previous plan for failure to make plan payments can be a factor when determining whether a debtor seeks conversion in good faith.[43] Debtors explained that their first Chapter 13 case failed because they misunderstood when they needed to make their first payment (they believed they needed to start payment some time in January, 2016, not within the required 30 days from the date of filing—by November 27, 2015). They also testified to an unknown clerical error with the income withholding order, causing Mr. Prins's employer not to withhold and pay over the monthly plan payment. Once Debtors realized Mr. Prins's employer was not making their plan payments, they then made one partial direct payment to the Chapter 13 Trustee of $2,762.50—almost $3,000 short of one full payment—in January, 2016.

But this explanation wholly ignores why, after realizing their plan payments were not deducted from Mr. Prins's paycheck, they elected not to make the required

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[42] *See In re Oblinger*, 288 B.R. 781, 786–87 (Bankr. N.D. Ohio 2003) ("Given the language of § 706 and the procedural context of conversion requests under Fed. R. Bankr. P. 1017(f)(2), as motions but not contested matters, this court joins with those courts that generally hold that these types of issues (best interests of creditors, best efforts of Debtor and feasibility) should be addressed in the context of a complete record developed in a confirmation hearing on a proposed Chapter 13 plan.").

[43] *See Harris v. Boston Private Bank & Trust Co. (In re Harris)*, 497 B.R. 652, 665 (Bankr. D. Mass. 2013) (finding that the debtor could not reconvert her case from Chapter 7 to Chapter 13 because she had not shown, in good faith, that she was capable of making plan payments consistently as her previous Chapter 13 bankruptcies had failed due to her failure to make plan payments).

payments to the Chapter 13 Trustee. The employer's failure to withhold $5,813 from Mr. Prins's employment check means his check was $5,813 higher than expected in January and February and March, 2016.

After realizing the mistake, Debtors should have been able to make the payments directly. Debtors, however, made no effort to make a full direct payment to the Chapter 13 Trustee during the first three months of 2016 nor did they put the money aside so they could later use it to save their house. And they never corrected the alleged clerical error associated with the employer pay, since the Trustee never received a payment from that source, either. Instead, Debtors spent Mr. Prins's entire paycheck (plus the $2,800 Social Security benefit), including the amount they had promised to pay to the Chapter 13 trustee, for something besides their mortgage payments or insurance or property taxes.

While Debtors' misunderstanding of when they were to begin plan payments and their difficulty with the employer pay process are understandable, their inability to explain what they did with that money is not. The Debtors provided no credible testimony why they can or will do now what they chose not to do in the prior Chapter 13 case. They have had an opportunity to put their very substantial money where their mouths are. They now claim they want to make plan payments to pay off their creditors and remain in their home, but given an opportunity to spend their substantial income elsewhere, they have consistently taken that route. The Court has no faith they are sincerely motivated to make responsible decisions now.

Again, Debtors made $2,762 in plan payments during a time when almost

$28,000 was due to the Chapter 13 Trustee. Debtors admitted their $12,800 a month projected income stream was accurate and uninterrupted during that time. Debtors either tremendously understated in Schedule J their true living and other expenses, or they are hiding where they are truly spending their income. Were the Court to allow Debtors' conversion, it would likely only further delay an inevitable dismissal or reconversion while negatively affecting Debtors' creditors, whose collection rights have already been essentially stayed for two years. It would also delay the Chapter 7 Trustee's recovery of the substantial 2014 refund Debtors have now withheld for almost a year.

As the impact a debtor's actions have had on his creditors is a factor the Court must consider under the *Gier* test, and the weight of evidence supports the Trustee's argument that Debtors will not be able to propose and/or consummate a confirmable Chapter 13 plan, the Court finds that Debtors' actions in their previous Chapter 13 plan display a lack of good faith.

2. Debtors' 2014 Tax Refunds

Debtors' total disregard of the Trustee's consistent inquiries regarding their 2014 tax returns and refunds also exhibits a lack of good faith[44] and violates their duty to comply with Trustee requests under § 521(a)(3) and Federal Rule of Bankruptcy

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[44] *See Beach v. Morris (In re Beach)*, 281 B.R. 917, 921 (10th Cir. BAP 2002) ("[T]hese provisions (§ 521(a)(3) and Fed. R. Bankr. P. 4002) impress the policy that a debtor who voluntarily submits him or herself to the jurisdiction of the bankruptcy court to obtain the benefit of a discharge of debts, must fulfill certain duties to insure that estate assets are administered in accordance with applicable law.") (internal citations omitted).

Procedure 4002(a)(4).[45] The Trustee sent six requests for copies of Debtors' 2014 state and federal tax returns to both Debtors and their attorney—all of which were ignored. While Mr. Prins quibbled about whether he received each of the six Trustee email requests on which both Debtors were copied, he did not explain the following email from his own attorney dated June 15, 2015, almost three full months before the Trustee filed his Motion to Compel:

> "Dear Eric and Rosella: The trustee has sent 5 reminders that you are to provide copies of your 2014 income tax returns to him. The last reminder, sent April 15, 20015 (sic), gave you until April 29, 2015, to comply; evidently you have not done so.
>
> He has now sent a sixth reminder dated June 8, 2015. If you do not provide your returns by June 22, 2015, a motion to compel turnover will be filed and you will be ordered to pay the Trustee $500.00 in attorney's fees. This is a simple request; I don't understand why you have not complied. Again, you have until June 22, 2015, to provide the copies or the motion will be filed and you will have to pay $500.00 in attorney's fees. Please either mail the returns or deliver them personably to Christopher J. Redmond at . . . . Time is of the essence."[46]

Thus, Debtors ignored their own attorney's plea to promptly perform their statutory duties. This caused the Trustee to expend estate resources to compel performance.

Debtors testified that they requested and received an extension to file their 2014 taxes and thus were unable to supply those returns to the Trustee until September 3, 2015—after the Trustee filed his motion to compel Debtors to provide copies of their

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[45] *See, generally,* § 521(a)(3) ("The debtor shall . . . if a trustee is serving in the case . . . cooperate with the trustee as necessary to enable the trustee to perform the trustee's duties under this title."); Fed. R. Bankr. 4002(a)(4) ("[T]he debtor shall . . . cooperate with the trustee in the . . . administration of the estate."); *see, e.g., Larimore v. United States (In re Russell)*, 34 B.R. 49, 51 (Bankr. M.D. Fla. 1983) (finding that the debtors had violated § 521 when they refused to turnover $8,581.71 representing the estate's interest in a tax refund).

[46] Ex. M (emphasis added).

returns. While it may certainly be true that Debtors received an extension, this does not explain why Debtors ignored (for months) their own attorney's and the Trustee's requests. This behavior not only violates Debtors' duties under the Code, but, in conjunction with Debtors' conduct during their Chapter 13 case, presents a pattern of inexcusable neglect of required obligations.

Additionally, Debtors do not dispute they are required to turnover assets of the Chapter 7 estate to the Trustee, including the estate's portion of tax refunds.[47] Failure to do so can result in a denial or revocation of discharge and possibly criminal liability.[48] While the state of Debtors' discharge is not at issue, the Court notes these consequences to highlight the importance of communicating with the Trustee and complying with requests for turnover of documents and estate property. So important are these duties that the entire purpose of filing a bankruptcy petition—to discharge debt—can hinge on their performance. Debtors have not been forthcoming with the Trustee or the Court and have created unnecessary administrative work and expense for the Trustee—both of which are factors the Court considers under the *Gier* test.

Debtors ultimately justified knowingly spending their entire refund, even that

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[47] *See In re Barowsky*, 946 F.2d 1516, 1518 (10th Cir. 1991) ("[T]he portion of an income tax refund that is based upon the pre-petition portion of a taxable year constitutes property of the bankruptcy estate.").

[48] *See* § 542(a) ("[A]n entity . . . in possession, custody, or control, during the case, of property that the trustee may use, sell or lease . . . shall deliver to the trustee, and account for, such property or the value of such property."); *In re Beach*, 281 B.R. at 921 ("A failure to turnover the Returns could result in the denial of the Debtors' discharge, or the revocation of any discharge granted. It could also make the Debtors subject to criminal liability. And also to sanctions.") (internal citations omitted).

portion owed their estate, by claiming it went to pay education expenses for their children.[49] The Court can appreciate that, in the face of immediate or unexpected expenses, turning over a tax refund may sometimes not seem a viable option. Some low income debtors opt to keep the lights on, pay prescription costs, or feed their children instead of turning over the estate's portion of their refund. The Prins, however, are not low income debtors.

Being well above-median-income debtors, the Prins failed to satisfactorily explain why they had to rely on their tax refund to pay their education costs in the first place. Debtors did not claim that the expenses were unexpected and, at the time Debtors opted to use their refund to pay the education costs, their household income was at least $12,800 per month[50]—Mr. Prins enjoyed relatively stable employment, making at least $10,000 a month, while Mrs. Prins received $2,800 a month in Social Security benefits. Additionally, Debtors elected not to make their mortgage payments, lowering their monthly expenses significantly. What, then, were Debtors doing with their substantial income, as they admittedly were not saving it for anticipated

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[49] Debtors' Schedule I in their Chapter 13 proceeding notes a $900 monthly expense for tuition. As Debtors were not making their required monthly mortgage payments for months when they elected to spend their tax refund—and therefore had plenty of income to spare—the Court does not understand why Debtors also needed the entire tax refund ($13,989), including the estate's share ($9,198.25), for educational expenses. Whether Debtors had considerably more educational expenses than they disclosed on their Schedule J or they elected to spend their income on something else, this is another example of a lack of transparency and honesty in filing required schedules and/or testifying.

[50] Although Debtors' budget shows $2,000 a month deducted for taxes on Mr. Prins's wages, he admitted at the trial that actually nothing is withheld—a fact corroborated by Exhibit U, his pay stub. Thus, Debtors received an additional $2,000 in income, which they also managed to spend without making a house payment.

expenses (such as tuition)? The answer is still a mystery.

Based on Debtors' last submitted budget,[51] which showed $5,530 excess income, the Court finds it unreasonable that Debtors did not have enough saved to pay their completely predictable education expenses. Debtors' inability—or unwillingness—to budget for this expense, and thus their resort to knowingly expending estate funds to which they were not entitled, leads the Court to conclude that, even after their general discharge, Debtors chose not to live within their means.

Not only do these circumstances reflect Debtors' disregard for the required sacrifices of the bankruptcy process, but they also suggest that Debtors' expenses are not accurately reflected in their November, 2015 budget—violating *Gier*'s emphasis on accuracy and transparency. Debtors knew they were responsible to the estate for $9,198 and made no effort to discuss their purported budgetary issues with the Trustee or set up a repayment plan. Additionally, Debtors did not own up to their actions until long after they spent the money, further delaying the resolution of the problem and administration of the asset. The Chapter 7 Trustee had to file his Motion to Compel Turnover, again using estate assets, because Debtors deliberately failed to follow the rules. The Court cannot ignore Debtors' complete lack of communication or transparency with the Trustee over the course of their Chapter 7 case.

Gier also directs the Court to consider Debtors' motivation and sincerity and analyze whether Debtors are attempting to abuse the bankruptcy process. Overall,

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[51] *See* Doc. 21, filed November 10, 2015.

Debtors' actions regarding their 2014 refunds reflect a total indifference to their obligations and a complete lack of good faith to abide by the rules of the Code. Again the Court notes that Debtors claim they wish to repay their creditors while remaining in their home, but their actions instead display an inability or unwillingness to budget effectively and a tendency to conceal the truth about their income and expenses.

3. Debtors' Residence

The Court recognizes that converting from Chapter 7 to Chapter 13 to retain potential equity in a residence can be a legitimate use of the Bankruptcy Code.[52] However, the Court must consider all the circumstances surrounding a motion to convert to determine whether debtors are able, in good faith, to retain equity in their house and pay what is required to their creditors or whether they, in bad faith, wish to continue living in their house while further delaying the administration of their estate.

The most significant evidence weighing against a finding that Debtors seek to convert in good faith is Debtors' inability, almost from the moment they purchased their home, to pay their mortgage creditors as promised. Debtors have made only two mortgage payments to NASB since they bought the house in December, 2013—nearly three years ago. There is no evidence what payments Debtors made to Balderston, even

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[52] *See In re Kuhn*, 322 B.R. 377, 398–99 (Bankr. N.D. Ind. 2005) (finding that the debtor's attempt to keep her house from being administered as an asset under Chapter 7 did not, by itself, connote bad faith); *In re Dews*, 243 B.R. 337, 340 (Bankr. S.D. Ohio 1999) (finding that the debtors' conversion to Chapter 13 to save their house from being administered by the Chapter 7 trustee did not show bad faith).

before they realized he had not properly perfected his mortgage. While Mr. Prins has had essentially stable income since July, 2014, and Mrs. Prins has received $2,800 every month in Social Security disability since then, they have been wholly unable or unwilling to use their considerable income to make house payments. Even when their Chapter 13 plan required them to commence payments that would, in part, have gone to NASB as payment on their first mortgage, they failed to make even a single full payment to the Trustee.

It is important to note, also, that were Debtors allowed to convert, they would have to pay the same claims they proposed, but were ultimately unable to pay, in their prior Chapter 13 case dismissed only a few months earlier. The only difference, in fact, is a higher arrearage owed to NASB, as Debtors have continued to withhold any payment on their first mortgage. They instead elected to spend $12,800 a month on other expenses while NASB was required to advance $21,738 in taxes and insurance—thus living rent free. NASB should not be required to wait any longer.

Debtors also predicate their conversion on the assumption that Balderston's mortgage will be avoided. Debtors testified that they are willing and able to pay whatever is necessary into the Chapter 13 estate to retain the value of their admittedly non-exempt home. Mr. Griffin testified that if the Court allowed Debtors to convert their 2014 Chapter 7 to a Chapter 13, and Debtors were successful in avoiding Mr. Balderson's lien on their residence, they would need to pay roughly $70,000 over the course of their Chapter 13 plan in order to remain in their home. Conversely, if Debtors are not successful in avoiding Balderston's lien, Debtors will be responsible for paying

off any pre-petition arrears on that mortgage over the length of the plan.

The Court simply did not believe the Debtors when they testified they are sincerely motivated to save their house. Instead, the Court believes Debtors are motivated to delay as long as possible the day they are evicted for paying nothing to live in their home. As a result, this Court finds Debtors have, in bad faith, used their back-to-back bankruptcies, well timed to stop a foreclosure sale, and now coupled with this motion to convert, to manipulate their financial affairs to their sole benefit.

III. Conclusion

Courts have repeatedly noted that the "central purpose of the Bankruptcy Code is to give debtors a fresh start by discharging their preexisting debt."[53] Also true, however, is that the Code "does not dole out this substantial benefit indiscriminately," and "the opportunity for a completely unencumbered new beginning is reserved only for the honest but unfortunate debtor."[54] The Prins are not "honest but unfortunate" debtors.

Debtors have very high income, but opted not to discipline their spending to live within their substantial means. Debtors have been sending at least one child to private school, retained and purchased high prestige cars (two BMWs and one Hummer), and stayed in their high value home while not paying the mortgages. They sincerely want that high lifestyle, but they do not have a sincere motivation to pay for it. By ignoring

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[53] *Standiferd v. U.S. Trustee*, 641 F.3d 1209, 1212 (10th Cir. 2011) (holding that pre-conversion conduct can create cause for dismissal).

[54] *Id* (internal quotations omitted).

requests by the Chapter 7 Trustee and failing to maintain their previous plan payments, Debtors have cost their estate and their creditors valuable time and money. Even now, Debtors are likely not complying with the Internal Revenue Code by opting not to withhold income taxes from Mr. Prins's wages while also failing to file or pay estimated taxes.

Debtors have spent all but $1,000 of their substantial income since their last failed attempt at paying their creditors through Chapter 13. They nevertheless ask the Court to allow them to try again at a payment plan. Debtors may genuinely wish to continue to live in their house for a few more months while they file a new plan—a plan doomed to failure based on their demonstrated spending habits coupled with the amount of debt they would have to pay—but that motivation is not accompanied by any demonstrated willingness to play by the rules and make required plan payments. Debtors had a very recent chance to prove they could cash flow a plan, and demonstrated they cannot.

The Court also notes that because Debtors earn above-median income, any plan would have to last 60 months. That means that a future Chapter 13 Trustee will need to annually review Debtors' tax returns for four more years to insure there is no increase in income justifying a plan amendment, to insure there is no decrease in income that could impair future feasibility, to insure Debtors are not incurring postpetition tax debt, and to insure Debtors are, in fact, timely complying with tax filing requirements. Debtors' demonstrated non-cooperation with the Chapter 7 Trustee regarding only one year's tax returns would suggest that the administrative

burdens on a future Chapter 13 Trustee could be enormous.

As a result, under the totality of the circumstances, the Court finds that allowing these Debtors to convert their two year old Chapter 7 case to Chapter 13 would be an abuse of the provisions, purpose, and spirit of the Bankruptcy Code. It would simply further delay the administration of their Chapter 7 estate while rewarding Debtors' irresponsible financial decisions and lack of transparency. Debtors' motion to convert[55] is therefore denied.

It is so ordered.

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[55] Doc. 59.