MODIFICATION OF CHAPTER 13 PLANS

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“If you want to make enemies, try to change something.” ~Woodrow Wilson

Introduction

The Chapter 13 debtor and counsel grapple to get a firm hold on the debtor’s financial circumstances when preparing the plan. However, the debtor’s circumstances on the day of filing the Chapter 13 plan are more likely than not to change. Life is not static. The debtor’s financial circumstances may take a turn for the worse due to job loss, disability, or unforeseen medical problems. On the other hand, the debtor’s circumstances may improve due to an increase in income or a reduction in expenses. The Bankruptcy Code contemplates this under 11 U.S.C. §§ 1323, 1329(a).

I. Statutory requirements for modification and procedure.

Before a plan has been confirmed, only the debtor may seek modification pursuant to 11 U.S.C. § 1323. Court approval is unnecessary as long as the modified plan complies with § 1322 which governs necessary components of Chapter 13 plans. The Code does not limit the type of modification that may be made pre-confirmation. Once a plan has been confirmed, however, the debtor’s ability to modify is more restricted.

After confirmation the debtor, trustee or holder of an allowed unsecured claim may modify the plan before completion of plan payments under 11 U.S.C. § 1329(a). Although the Code does not expressly prohibit the bankruptcy court from modifying the plan, the Bankruptcy Appellate Panel in the First Circuit held that it is statutorily precluded from instructing a debtor to file a modified plan. In re Muessel, 292 B.R. 712, 716 (B.A.P. 1st Cir. 2003).[1] Post-confirmation plans may be modified to effectuate a change in: (1) the amount paid to creditors; (2) the time for such payments; (3) the amount of the distribution to a creditor whose claim is provided for by the plan to the extent necessary to take account of any payment of such claim other than under the plan; or in limited circumstances (4) amounts to be paid by the debtor to purchase health insurance for the debtor and dependents. 11 U.S.C. § 1329(a).

To modify a post-confirmation plan, the proponent must file a motion. Fed. R. Bankr. P. 9013.[2] It must identify the proponent of the modification and attach the proposed modification. Fed. R. Bankr. P. 3015(g). The motion must be clear as to the specific nature of the modification proposed. At least 21 days' notice must be provided to the debtor, trustee and all creditors to file objections to the proposed modification. Fed. R. Bankr. P. 3015(g). If an objection is filed, the matter becomes contested and as a result a hearing will be scheduled. Fed. R. Bankr. 9014. A notice of the hearing, together with a copy of the proposed modified plan, or a summary thereof, must be served on the same parties, as well as the U.S. Trustee. Fed. R. Bankr. P. 3015(g). At a hearing on the matter, the proponent of the modified plan bears the burden of proof as to the conditions for its confirmation.[3]

II. Under what circumstances are post-confirmation modifications permitted?

Several issues arise in the world of Chapter 13 modifications. There is currently a split in authority as to whether modification is dependent on a change in debtors' financial circumstances or whether the Code's plain language permits modification absent such a showing.

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[1] Cf. Collier v. Valley Fed. Sav. Bank (In re Collier), 198 B.R. 816 (Bankr. N.D. Ala. 1996).

[2] A "request for an order, except when an application is authorized by [the] rules, shall be by written motion, unless made during a hearing." Fed. R. Bankr. P. 9013.

[3] In re Kearney, 439 B.R. 694, 696 (Bankr. E.D. Wis. 2010) (debtor bears burden if proponent); In re Than, 215 B.R. 430, 434 (B.A.P. 9th Cir. 1997)(creditor bears burden); In re Brown, 332 B.R. 562, 564 (Bankr. N.D. Ill. 2005) (trustee bears burden if debtor objects).

Other issues are whether the disposable income test applies at modification, and whether the applicable commitment period may be modified. Finally, how will the recent U.S. Supreme Court cases of Lanning and Ransom affect modifications?

A. Are financial changes in a debtor's circumstances a prerequisite?

Several courts have required some showing of a change in financial circumstances before the court will allow modification. However, courts differ as to the degree of change that is necessary and basis of authority requiring change.

In re Murphy holds that the doctrine of *res judicata* prevents modification of a confirmed plan pursuant to § 1329(a) absent a "substantial" and "unanticipated" post-confirmation change in the debtor's financial condition.[4] In another case, In re Savage, the court denied the debtors' motion to modify because the debtors failed to provide support that the change was "material" and "adverse" and they therefore lacked "just cause."[5] The In re Nelson court denied a debtor's motion to modify because her changes in financial circumstances were not only anticipated, but they were her own fault, e.g., she married a man with a disability who only worked sporadically which increased her expenses.[6]

Another court considered the debtor's financial changes, but only as a factor in its analysis, not as a prerequisite to modification. In the case In re Brown, the court denied the debtor's motion to modify her plan which sought to reduce payments to creditors and to surrender her vehicle, which was filed on the very day that the debtor brought her vehicle in for

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[4] Murphy v. O'Donnell (In re Murphy), 474 F.3d 143, 149 (4th Cir. Va. 2007); see also, Ledford v. Brown (In re Brown), 219 B.R. 191, 194 (B.A.P. 6th Cir. Ohio 1998); In re Butler, 174 B.R. 44, 47 (Bankr. M.D.N.C. 1994); In re Algee, 142 B.R. 576, 580 (Bankr. D.D.C. 1992); In re Arnold, 869 F.2d 240, 243 (4th Cir. Va. 1989).
[5] In re Savage, 426 B.R. 320, 324-25 (Bankr. D. Minn. 2010) (debtors sought to modify plan to decrease payments and the payment period due to a reduction in receipt of child support payments by Mrs. Savage).
[6] In re Nelson, 189 B.R. 748, 750 (Bankr. D. Minn. 1995).

repairs.[7] The court declared that a confirmed plan has no *res judicata* effect, and that the Code does not require the debtor to make a showing of "substantial and unanticipated" financial changes to qualify for modification of a confirmed plan.[8] The court has the ultimate discretion to allow the modification and it may consider the debtor's changes in financial circumstances as a factor.[9] The court denied the debtor's motion because she failed to demonstrate that she could not maintain the plan payments due to changes in her financial circumstances.[10] Essentially, the debtor's proposed plan was not made in good faith; she simply decided the car repairs would be too expensive.[11]

B. First Circuit—Modification is not limited by *res judicata* or "unanticipated, substantial changes."

Numerous courts have held that a confirmed plan is governed by the doctrine of *res judicata* and therefore it may not be modified absent unanticipated, substantial changes.[12] The First Circuit Court of Appeals in the case of Barbosa v. Soloman disagrees.[13] In Barbosa, Chapter 13 debtors sold property of the estate, free and clear under § 1327, after confirmation but before the case was closed.[14] The debtors' unsecured creditors and trustee moved to modify the debtors' plan to utilize the proceeds to pay 100% of the unsecured creditors' claims rather than the 10% which was to be distributed under the confirmed plan.[15] The debtors argued that they anticipated the sale of the assets at the time of confirmation, as evidenced by a stipulation with a

[7] In re Brown, 2011 Bankr. LEXIS 2652 at *2 (Bankr. S.D. Ind. July 8, 2011).
[8] Id. at *4.
[9] Id.
[10] Id. at *14.
[11] Id.
[12] Ledford v. Brown (In re Brown), 219 B.R. 191, 194 (B.A.P. 6th Cir. Ohio 1998); In re Butler, 174 B.R. 44, 47 (Bankr. M.D.N.C. 1994); In re Algee, 142 B.R. 576, 580 (Bankr. D.D.C. 1992); In re Arnold, 869 F.2d 240, 243 (4th Cir. Va. 1989).
[13] Barbosa v. Soloman, 235 F.3d 31, 40 (1st Cir. Mass. 2000).
[14] Id. at 32.
[15] Id.

secured creditor.[16] The trustee and unsecured creditors failed to prove that the debtors experienced substantial and unanticipated circumstances; thus the debtors argued that modification of the confirmed plan was barred by the doctrine of *res judicata*.[17]

The court noted that § 1329 does not establish criterion for modification of post-confirmation plans.[18] However, the Code does provide that modified plans must be proposed in good faith under 11 U.S.C. § 1325(a)(3) and comply with the "best interests of the creditors" test and the "ability to pay" standard pursuant to 11 U.S.C. § 1325(a)(4), (5), (6).[19] Rejecting the debtors' argument, the court reasoned that the Code is entirely silent with respect to the doctrine of *res judicata*.[20]

Furthermore, the court expressly refused to adopt the "unanticipated, substantial changes" test espoused by numerous courts, as the Code is also silent in this respect.[21] In 1984, Section 1329(a) was amended to grant trustees and unsecured creditors standing to seek modification of confirmed plans to adjust payments in order to carry out the "ability to pay" standard if debtors experience a change in financial circumstances.[22] The legislative history indicates Congress had anticipated that modification would be necessary in some instances due to changes in debtors' financial circumstances when it amended the statute, but the history does not reference any requirement that the changes be "substantial" or "unanticipated."[23]

Turning to the particular facts of Barbosa, the court explained that allowing the debtors to keep the proceeds of the sale for themselves after stripping down their mortgage would be

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[16] Id. at 38.
[17] Id.
[18] Id.
[19] Id.
[20] Id.
[21] Id. at 41.
[22] Id. at 40 (citing the Oversight Hearings on Personal Bankruptcy Before the Subcommittee on Monopolies and Commercial Law of the Committee on the Judiciary, House of Representatives, 97th Cong., 1st and 2nd Sess. 22-23 (1981-1982)).
[23] Id. at 41.

antithetical to the bankruptcy system and also Congress's intention to allow the trustee and unsecured creditors to apply the "ability to pay" standard throughout the duration of the plan when the debtors had the ability to pay 100% to unsecured creditors.[24] The court was satisfied with the safeguards expressly provided in the Code and affirmed the district court's order upholding the bankruptcy court's judgment permitting modification.[25]

C. Lanning and Ransom address changes in financial circumstances.

(i) Lanning—known or virtually certain changes

In Hamilton v. Lanning, the debtor's Form 22C indicated artificially high income, as it included a one-time payment that resulted from a buy-out deal from her employer.[26] The debtor proposed a plan that was based on her more realistic expectation of income looking forward.[27] The trustee touted the "mechanical approach" when opposing the plan on the basis that the statute requires the plan payment to be based on projected disposable income, which is calculated by multiplying disposable income, as found on Form 22C, over the number of months in the commitment period.[28] The bankruptcy court overruled the trustee's objection and confirmed the debtor's plan which proposed payments more in line with reality as reflected on her Schedule I.[29]

The trustee appealed to the Tenth Circuit Bankruptcy Appellate Panel, which affirmed the bankruptcy court and held that if the disposable income calculation of Form 22C does not accurately reflect a debtor's ability to fund a plan the amount may be modified.[30] The trustee then appealed to the U.S. Court of Appeals for the Tenth Circuit which also affirmed and held

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24 Id.
25 Id.
26 Hamilton v. Lanning, 130 S. Ct. 2464, 2470 (2010).
27 Id.
28 Id.
29 Id. at 2470-71.
30 In re Lanning, 380 B.R. 17, 24-25 (B.A.P. 10th Cir. 2007).

that the current monthly income is a starting point for projecting disposable income, but is subject to the debtor showing a substantial change of circumstances, to be determined by the bankruptcy court on a case-by-case basis.[31] The Appeals Court observed that a debtor may be denied bankruptcy protection if Form 22C shows disposable income, but the debtor cannot propose a feasible plan due to the actual reality of the debtor's current and anticipated future income.[32] Further, the Appeals Court found that the legislative intent was to require a debtor to pay the maximum that the debtor could afford; thus, adjusting monthly disposable income to reflect reality under the "forward looking approach" serves Congress's purpose. [33]

The trustee appealed to the United States Supreme Court, which also affirmed. The Court embraced the "forward looking approach" and held that the bankruptcy court may account for changes in the debtor's income or expenses that are "known or virtually certain at the time of confirmation" when examining the debtor's projected disposable income.[34]

(ii) Ransom's dicta anticipates modification for changed expenses

In Ransom, the Appeals Court for the Ninth Circuit affirmed both the bankruptcy court and Bankruptcy Appellate Panel which concluded that an above-median debtor cannot deduct an expense for ownership of a vehicle that is unsecured in the disposable income analysis.[35] The plain language of the Code prohibited deducting an expense that the debtor did not pay, as the debtor owned the car free and clear.[36] The United States Supreme Court affirmed.[37] Under the Code, a debtor may deduct "applicable expenses" pursuant to § 707(b)(2)(A)(ii)(I). The Code does not define "applicable" therefore the Court applied the word's ordinary meaning, i.e., an

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[31] Hamilton v. Lanning (In re Lanning), 545 F.3d 1269, 1282 (10th Cir. Kan. 2008).
[32] Id. at 1281.
[33] Id.
[34] Hamilton v. Lanning, 130 S. Ct. 2464, 2478 (2010).
[35] Ransom v. MBNA, Am. Bankr., N.A. (In re: Ransom), 577 F.3d 1026 (9th Cir. 2009).
[36] Id. at 1030.
[37] Ransom v. FIA Card Servs., N.A., 131 S. Ct. 716 (2011).

expense that is appropriate, fit, suitable, or relevant as applied to the particular debtor.[38] The Court declared that the vehicle ownership category covers expenses relating only to loan or lease payments.[39] Since the debtor in this case did not make any loan or lease payments on the vehicle, the debtor was not entitled to claim the expense.[40] The Court noted that if the debtor found himself in a position, during the course of the plan, where he required a replacement vehicle he could move to modify the plan.[41] Likewise, if a debtor pays off his car loan during the plan, a creditor can move to modify the plan to increase payments to unsecured creditors.[42]

III. Lanning and Ransom leave open questions relating to modification.

Lanning allows courts to deviate from a strict mechanical approach when analyzing the debtor's "projected disposable income" by taking into account changes in income and expenses which are known or virtually certain to occur. Ransom forbids deduction of fictitious expenses. Its dicta speaks to the parties' ability to modify the plan in the event of changes. However, Lanning and Ransom leave open questions pertaining to modification.

It remains unclear whether a change in circumstances is a prerequisite to modification based on the doctrine of *res judicata* or on some other basis. Or are the requirements of modification limited to those expressed in the Code, as held in Barbosa? The Court failed to specify any required showings for modification based on changes. Must the debtor's changed circumstance be "substantial" and "unanticipated"? If the change in circumstance is due to the debtor's own fault, is modification precluded? How does the "forward looking approach" to projected disposable income in Lanning affect modification? If an expense is virtually certain to

[38] Id. at 724.
[39] Id. at 725.
[40] Id. at 726.
[41] Id. at 730.
[42] Id. at 729.

occur based on a changed circumstance, must the debtor wait to file for modification until the expense becomes an actual one in accordance with a strict reading of Ransom?

IV. Is the "disposable income test" or "forward looking approach" applicable to modifications?

Several post-Lanning cases hold that the disposable income test of § 1325(b) does not apply to modification. Under this view, modification rests on the discretion of the judge who must apply the good faith, best interest of creditors and feasibility tests pursuant to 11 U.S.C. § 1325(a)(3), (4), (6).[43] Changed circumstances are a factor in this analysis.[44] The Code provision governing modification, § 1329, does not incorporate § 1325(b); thus the disposable income test is inapplicable to modifications.[45] The debtor's actual income and expenses at the time of modification are evaluated, not the methods provided in §§ 1325(b) and 707(b)(2).[46] The court in In re Prieto adopted this approach to modification. In its reasoning the court noted that its decision conformed to Lanning. Although Lanning dealt with confirmation of the initial plan, Lanning's intent was to determine the actual income and expenses of the debtor during the life of his plan.[47] In Prieto, the judge allowed the trustee's motion to modify to increase payments to creditors based on the debtors' increased income at that time.[48] See also, In re Crim, 445 B.R. 868, 869 (Bankr. M.D. Tenn. 2011) (court allowed debtors' motion to modify plan which proposed payment reduction from 100% to 30% for a private tuition expense that court found reasonable and necessary); In re Davis, 439 B.R. 863, 864-65 (Bankr. N.D. Ill. 2010) (court granted debtor's motion to reduce both payments to creditors and payment period after debtor lost job and separated from husband).

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[43] In re Prieto, 2010 Bankr. LEXIS 3379, at *5, 7 (Bankr. M.D. Fla. Sept. 22, 2010).
[44] Id. at *7.
[45] Id. at *5.
[46] Id.
[47] Id. at *8.
[48] Id. at *13-14.

Prior to Lanning, the Bankruptcy Appellate Panel for the First Circuit in the case of Kibbe v. Sumski espoused a reality-based calculation of projected disposable income when it held that where the calculation on Form B22C "comports with the debtor's actual income at the time of confirmation and as reasonably anticipated for the plan commitment period, no further determination is necessary … [but if the debtor's income] is materially different from the debtor's disposable income as defined by § 1325(b)(2), the court must depart from the Form B22C calculation." [49] (Citations omitted.) While the Court did not express its views on modification, Kibbe read together with Barbosa suggests that the First Circuit may apply a reality-based evaluation of the debtor's income and expenses and factor in the debtor's changed circumstances, at least as it pertains to reduction in payment amounts.

V. How does Lanning affect reduction in the commitment period?

In the case of In re Filion, the above-median debtors fully paid the monetary amount of their plan payments and moved for discharge two months prior to the expiration of the applicable commitment period.[50] The trustee objected due to the fact that the debtors could not technically complete their plan until the expiration of their commitment period under § 1325(b).[51] The debtors argued that the trustee was improperly attempting to modify their plan after completion of all payments.[52] The central issue of the case, therefore, is whether "completion of payments under the plan" as set forth in § 1329(a) becomes effective as of the last dollar payment or at the end of the commitment period. The court noted a split in authority on this issue.[53] Siding with the Sixth, Eighth and Eleventh Circuits and the B.A.P. for the Ninth Circuit, the court held that

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[49] Kibbe v. Sumski (In re Kibbe), 361 B.R. 302, 314-15 (B.A.P. 1st Cir. 2007).
[50] In re Filion, 2011 Bankr. LEXIS 1641 at *1 (Bankr. D. Mass. May 3, 2011).
[51] Id. at *3.
[52] Id.
[53] Id. at *7-8.

the phrase imposes a durational requirement under the "temporal view."[54] The court cited Lanning in support of the temporal view and Ransom for the notion that BAPCPA was enacted to ensure maximum possible payment to creditors.[55]

The court noted that if the debtors' argument was correct, debtors could pay the plan payments the day after confirmation and receive a discharge, which would deprive creditors of the opportunity to receive maximum payment and would render 11 U.S.C. § 1325(b)(4)(A) and (B) meaningless. The Code provides creditors with the opportunity to propose modifications to plans pursuant to 11 U.S.C. § 1329(a) if a debtor experiences an increase in projected disposable income during the life of the plan.[56] "[D]ebtors must, for the prescribed life of the plan, run the gauntlet of exposure to trustee or creditor requests to increase payments."[57] The court viewed the debtors' request for a discharge as an informal attempt to modify their plan, which absent a formal motion to modify, was denied.[58]

Conclusion

Although Lanning and Ransom provided some relief from the rigid "mechanical" approach, the Court has yet to provide guidance on various modification issues. Courts in the First Circuit, however, will apparently allow a plan to be modified by reducing or increasing plan payment amounts if the plan is made in good faith, is feasible and is in the best interest of the creditors. This determination is made at the discretion of the judge and changed circumstances may be considered as a factor in this analysis. First Circuit courts favor a "forward looking approach." When evaluating modification, the courts will likely review actual income and expenses at the time of modification and will not apply the rigid mechanical approach in the

[54] Id. at *8, 11.
[55] Id. at *11, 14.
[56] Id. at *14, 15.
[57] Id. at * 15 (citing Fridley v. Forsythe (In re Fridley), 380 B.R. 538, 544 (B.A.P. 9th Cir. 2007)).
[58] In re Filion, 2011 Bankr. LEXIS 1641 at * 15, 16 (Bankr. D. Mass. May 3, 2011).

disposable income test. However, to enable the trustee and unsecured creditors to move for modification if the debtor's income does increase during the plan period, courts are less likely to allow a reduction in the applicable commitment period.