IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF ALABAMA

IN RE:	)	
	)	
Evelyn Smith Davis,	)	Case No. 16-3550
	)	
Debtor.	)	

IN RE:	)	
	)	
Bennie and Sonja Connor,	)	Case No. 18-1935
	)	
Debtors.	)	

ORDER REGARDING PROCEEDS

These chapter 13 cases are before the court on a motion to approve settlement (doc. 67 in case 16-3550) and the court's order approving sale of real estate (doc. 128 in case 18-1935). The settlement in case 16-3550 relates to a personal injury case arising from a 2020 postpetition motor vehicle accident. The court approved the settlement (doc. 76) and held the nonexempt net proceeds from settlement were to be held by the trustee pending further order of the court. The sale of real estate in case 18-1935 relates to non-homestead property inherited by debtor Sonja Connor and her two sisters a year after she filed bankruptcy. The court approved the sale and ordered the trustee to hold Ms. Connor's one-third interest in the net proceeds (not claimed as exempt) pending further order of the court. The question now is what to do with the nonexempt proceeds from the settlement in *Davis* and the sale of inherited property in *Connor*.

Under Bankruptcy Code § 541, a debtor's bankruptcy estate consists of all interests in property possessed by the debtor at the time of her bankruptcy filing. Under Code § 1306, the chapter 13 estate also includes property "that the debtor acquires after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7, 11, or 12 . . . , whichever occurs first . . . ." The nonexempt proceeds in both cases are thus property of the debtors' chapter 13 estates under Code § 1306 and the confirmed chapter 13 plans in each case "consistent

with the ability-to-pay policy underlying [c]hapter 13." *See In re Waldron*, 536 F.3d 1239, 1242-43 (11th Cir. 2008).

At confirmation, a debtor's plan must satisfy several separate requirements, including the "best interest of creditors" test of Code § 1325(a)(4). Under the "best interest of creditors" test, also known as the liquidation test, unsecured creditors must receive at least as much as they would if the case were a chapter 7 liquidation. The liquidation test applies to any plan modification under Code § 1329(b)(1). The wrinkle in the hypothetical chapter 7 liquidation test is that postpetition personal injury claims and inheritances (more than 180 days postpetition) like the ones at hand would not be property of the bankruptcy estate if these cases were filed under or, absent bad faith, converted to chapter 7.

The court ordered the chapter 13 trustee to file a brief in case 16-3550, which he did, citing case law within the Eleventh Circuit that the appropriate date for applying the liquidation test to any modification, including those dealing with postpetition assets, is the time of modification – not the petition. *See, e.g.*, *In re Nachon-Torres*, 520 B.R. 306, 312-14 (Bankr. S.D. Fla. 2014); *In re Tinney*, No. 07-42020-JJR13, 2012 WL 2742457, at *3 (Bankr. N.D. Ala. July 9, 2012). The Eleventh Circuit has also stated that "'[c]ertainly Congress did not intend for debtors who experience substantially improved financial conditions after confirmation to avoid paying more to their creditors.'" *See In re Waldron*, 536 F.3d at 1246 (citation omitted). Rather, "[w]hen a debtor discloses assets acquired after confirmation to the court, his creditors may share in any unanticipated gain if the court determines that these assets are available to repay debts. . . . Under the ability-to-pay standard, creditors share both the gains and losses of the debtor." *See id.*

If it were writing on a blank slate without the benefit of Eleventh Circuit case law on this issue, the court might hold otherwise. *See* 8 *Collier on Bankruptcy* ¶1329.05[3] (Richard Levin & Henry J. Sommer eds., 16th ed.); *In re Taylor*, 631 B.R. 346 (Bankr. D. Kan. 2021). But based on the case law from the Eleventh Circuit Court of Appeals and other courts within this circuit, the court

finds that the liquidation test applies at the time of modification even for postpetition claims and inheritances that would not have been included in the bankruptcy estate if the case were a chapter 7. *See, e.g.*, *In re Nachon-Torres*, 520 B.R. at 312-14.

This ruling does not completely resolve the issue presented in these cases, though. The court must determine whether the current percentage paid to unsecured creditors in each case should be increased – in effect, modification of the confirmed plans. As the Eleventh Circuit pointed out in discussing why debtors have an ongoing duty to disclose postconfirmation assets:

> The disclosure of postconfirmation assets gives the trustee and creditors a meaningful right to request, under section 1329, a modification of the debtor's plan to pay his creditors. . . . When a debtor discloses assets acquired after confirmation, creditors may move the bankruptcy court to modify the plan to increase payments made by the debtor to satisfy a larger percentage of the creditors' claims. If postconfirmation assets were not subject to disclosure, modifications for increased payments would be rare because few debtors would voluntarily disclose new assets, and the trustee and creditors would be unlikely to obtain the information from sources other than the debtor.

In re Waldron, 536 F.3d at 1245 (citations omitted) (emphasis added); *see also In re Tinney*, 2012 WL 2742457, at *3.

Postpetition modification of a debtor's chapter 13 plan requires a court order, usually as the result of a motion to modify by the debtor, trustee, or an unsecured creditor:

> A [c]hapter 13 plan of confirmation has *res judicata* effect unless it is subsequently modified by a bankruptcy court order. The confirmation plan includes, *inter alia,* the claim amounts that will be paid to each creditor; therefore, the alteration of an amount to be distributed to a creditor is a modification of that plan. Section 1329 sets forth the means by which a modification may be obtained and provides that the confirmation plan may be modified upon *request* by the trustee, debtor, or holder of an unsecured claim. The "request" language of § 1329(a) presupposes that such request must be accepted or denied by order of the bankruptcy court. Absent bankruptcy court order of modification, the confirmation plan must be executed as originally approved.

In re Davis, 314 F.3d 567, 570 (11th Cir. 2002) (citations omitted) (emphasis added). The Bankruptcy Code does not provide a mechanism for modifying a plan to increase the amounts paid on unsecured claims other than a motion under § 1329. However, in this district, as in the Southern

District of Georgia, the trustee and debtors frequently agree to an order approving an increase in percentage without a motion to modify. *See In re Smith*, 637 B.R. 758, 779-80 n.23 (Bankr. S.D. Ga. 2022). It is not crystal clear whether a motion to modify is required to increase the percentage on unsecured claims. *See id.* But a motion to modify allows the debtor a chance to object if he or she contends that the percentage to unsecured creditors should not increase. As a result, going forward, if the trustee wants to increase the percentage paid to unsecured creditors because of postpetition events (such as an inheritance or liquidation of a personal injury claim) and the debtor does not agree to the increase, the trustee should file a motion to modify the plan.[1]

The realization of nonexempt postpetition assets may not always increase the amount paid on unsecured claims. Although plan modification does not require a change in circumstance, the court must still determine whether there is a legitimate reason for the proposed modification. *See In re Guillen*, 972 F.3d 1221, 1229-30 (11th Cir. 2020). For example, a modification may not be feasible because a debtor needs "part or all of the . . . proceeds for continuing medical or living expenses." *See, e.g.*, *In re Wilson*, 555 B.R. 547, 556 (Bankr. W.D. La. 2016) ("If it is shown that the debtor needs the settlement proceeds to fund medical bills or basic living expenses, then it is possible the court, in its discretion, will not approve the proposed modification on the grounds that the modification is not feasible."); *see also In re Smith*, 637 B.R. at 779-80 n.23; Keith M. Lundin, LUNDIN ON CHAPTER 13, § 127.9, LundinOnChapter13.com. Similarly, an inadequate settlement of terrible personal injuries because of low insurance limits may not constitute a "substantially improved financial condition" or "unanticipated gain" as discussed in *In re Waldron*, 536 F.3d at

[1] The local chapter 13 plan forms (and in some cases, orders modifying the plan) provide that the property of the estate does not vest in the debtor until dismissal or discharge and that unliquidated claims remain property of the estate pending further order of the court. Some versions of the plans/orders state that the liquidated claim must be paid to the trustee pending further order of the court. As a result, the court will allow the trustee to file a motion to modify after completion of plan payments where a tort claim has been pending but is not liquidated until after plan payments are completed. To do otherwise would incentivize debtors to conceal or delay settlements and unfairly penalize creditors who have relied on these provisions.

1246. In the inheritance context, a debtor may have incurred funeral expenses or other costs as a result of the death which produced the inheritance. Those issues will have to be sorted out on a case-by-case basis, and not every postpetition asset will constitute a "windfall" to the debtor that warrants plan modification. *See, e.g.*, *In re Nachon-Torres*, 520 B.R. at 312-14; *In re Wilson*, 555 B.R. at 553 ("Simply put, courts have concluded that a debtor's receipt of an increase in income, or a windfall, often provides a legitimate basis for modification of a [c]hapter 13 plan.").

These two cases remain set for status on September 14, 2022, for the court and the parties to discuss what to do with the proceeds in these cases.[2]

Dated: September 13, 2022

HENRY A. CALLAWAY
U.S. BANKRUPTCY JUDGE

[2] The court recognizes that the trustee has filed a motion to disburse in case 18-1935, which is set for hearing on October 5. And in case 16-3550, the debtor has completed plan payments and received a discharge; the court had already granted (doc. 52) the trustee's motion to modify the plan to include the claim.