

**UNITED STATES BANKRUPTCY COURT
FOR THE WESTERN DISTRICT OF PENNSYLVANIA**

IN RE:

DAVID J. CEGAN,	:	Bankruptcy No. 01-30278 BM
	:	
Debtor	:	Chapter 7

LINDA CEGAN,	:	
	:	
Plaintiff	:	
v.	:	Adversary No. 02-2601 BM
	:	
DAVID J. CEGAN,	:	
	:	
Defendant	:	

Appearances: Donald E. Calaiaro, Esq., for Plaintiff
Frank E. Yourick, Jr., Esq., for Defendant

MEMORANDUM OPINION

Plaintiff Linda Cegan seeks a determination that a debt in the amount of \$190,155 owed to her by debtor David Cegan, her estranged spouse, is in the nature of alimony, maintenance, or support and therefore is excepted from discharge by § 523(a)(5) of the bankruptcy Code.

Debtor maintains that the debt is not excepted from discharge by § 523(a)(5). The debt, he asserts, is not in the nature of alimony, maintenance or support of plaintiff but instead qualifies as equitable distribution of marital property.

Judgment will be entered in favor of plaintiff and against debtor. The debt is in the nature of alimony, maintenance, or support of plaintiff and is excluded from discharge by § 523(a)(5).

- FACTS -

Plaintiff and debtor were married in June of 1976 and separated in October of 1997. They have three adult children as a result of their marriage. Plaintiff was 49 years old and debtor was 52 years old in December of 1999.

Plaintiff initiated a divorce action against debtor in 1997 after their separation. In addition to a divorce, plaintiff requested alimony and equitable distribution of marital property in the complaint. The record does not indicate whether her request for a divorce is still pending.

Plaintiff graduated from high school in 1969. She worked as a full-time homemaker for the first seven years of their marriage. In 1983 plaintiff began working on a full-time basis without pay for a business owned by her husband. Plaintiff quit this job in 1991 to attend college and graduated with a degree in nursing in 1996. She took the exam to obtain her license but failed to pass on it four different occasions prior to December of 1999. She passed the exam some time thereafter but has never been employed as a nurse.

Plaintiff's only source of income in December of 1999 was alimony *pendente lite* in the amount of \$3,400 per month. Debtor also was required to provide plaintiff with a car, to pay her car and medical insurance, and to pay fifty percent of her unreimbursed medical costs.

Debtor has a college degree in business administration and owns two businesses. He started Financial Search Group, Ltd., an employment consulting firm, in 1978 and National Car Detailing, Inc., which is in the business of detailing automobiles, in 1982. Both businesses were operating in 1999.

Plaintiff's request for alimony and equitable distribution of marital property was tried before a special master in December of 1999. The master's report and recommendations were issued on January 3, 2000.

After stating that there was no precise way to determine wife's earning capacity due to her lack of recent employment, the master determined that plaintiff had a monthly net earning capacity of \$1,100 in 1998 and also in 1999. Master's Report and Recommendation, p. 5.

The master further determined that debtor's monthly net income from the businesses was \$7,410 in 1998 and was \$4,775 in 1999. The entirety of his income during these years came from Financial Search Group. Monthly loan repayments in the amount of \$367 were all that debtor received from National Car Detailing during this period. Master's Report and Recommendation, pp. 6-7.

Due to the substantial reduction in debtor's income from 1998 to 1999, the master recommended that alimony *pendente lite* debtor was required to pay to plaintiff be reduced from \$3,400 per month to \$1,470 per month and that arrearages be reduced accordingly. Master's Report and Recommendation, pp. 6-7.

After identifying and assigning values to the various marital assets, the master determined that the total value of the marital estate was \$388,995. Master's Report and Recommendation, pp. 8-13.

The master then made specific recommendations concerning what was characterized as "equitable distribution of marital property". After noting that plaintiff's earning capacity was "vastly inferior" to debtor's even if plaintiff were fully utilizing her earning capacity, the master concluded that plaintiff's prospects for acquisition of capital

assets and income in the future were “considerably less” than debtor’s. A 55%-45% distribution of marital assets in plaintiff’s favor was recommended. Plaintiff should receive marital assets totaling \$200,547 in value while debtor should receive marital assets totaling \$188,448 in value. Master’s Report and Recommendation, p.14.

The master specifically recommended that plaintiff be awarded the marital property component and contents of a condominium in Myrtle Beach, South Carolina, in addition to certain other personalty already in her possession, all of which were valued at \$ 27,195. In addition, the master recommended that plaintiff receive \$173,352 in cash from debtor. The remainder of the marital assets should be distributed to debtor. Master’s Report and Recommendation, pp. 14-15.

Included among the assets awarded to debtor was the marital residence. Noting that there was “substantial equity” in the marital residence, the master concluded that debtor therefore should be able to obtain a home equity line of credit in the amount of \$80,000. The master recommended that debtor pay plaintiff \$80,000 within ninety days and an additional \$20,000 within ninety days thereafter. Debtor was to pay the remainder of the cash award to plaintiff at the rate of \$ 4,000 per month¹ with interest at the rate of 8% annually until it was paid in full. Following this recommendation, the master stated as follows:

Should he [i.e., debtor] declare bankruptcy prior to payment of this obligation in full, any outstanding unpaid equitable distribution obligation shall be deemed to be an alimony obligation and not dischargeable in bankruptcy.

1. The precise amount of these monthly installments debtor was required to make is not clear. In summarizing her recommendations, the master stated that the monthly installment was \$3,000. We need not resolve this discrepancy to decide this adversary action. Master’s Report and Recommendation, p. 19.

Master's Report and Recommendation, p. 15.

With respect to plaintiff's request for permanent alimony, the master noted that even if plaintiff were to fully exploit her limited earning capacity, plaintiff nonetheless was in need of alimony until she received a substantial portion of the above "equitable distribution" award. The master then recommended that alimony *pendente lite*, as reduced above, continue as alimony until plaintiff received the initial \$100,000 in cash set forth above. Alimony would terminate once she received this initial \$100,000. Having made this recommendation, the master then explained that it would give plaintiff "sufficient time to take the nursing boards and find gainful employment as a nurse". Master's Report and Recommendation, p. 16.

Finally, the master recommended that debtor pay plaintiff \$20,000 within sixty days for attorney's fees and costs she incurred in prosecuting her claims for alimony and equitable distribution. Master's Report and Recommendation, pp. 17-19.

The judge to whom the divorce proceeding was assigned issued an order on March 14, 2001, wherein the percentages of the marital estate plaintiff and debtor would receive were modified. Instead of 55%-45% in favor of plaintiff, distribution was modified to 60%-40% in favor of plaintiff. After making one other minor modification, the court concluded that the amount debtor was obligated to pay plaintiff would increase from \$173,352 to \$190,155. Another order declaring this order to be final issued on July 25, 2001. Neither debtor nor plaintiff appealed these orders.

Debtor made none of the above required cash payments to plaintiff. He instead filed a voluntary chapter 7 bankruptcy petition on September 27, 2001. The schedules identify assets with a total declared value of \$304,144.00 and liabilities totaling

\$906,538.70. Financial Search Group was listed as having a value of only \$5,000. National Car Detailing was listed as having a value of \$0.

It is readily apparent from the schedules that debtor seeks in this bankruptcy case to have discharged his obligation to pay plaintiff \$190,155. Plaintiff is identified as having an undisputed general unsecured claim in the amount of \$190,155 for “equitable distribution”. In addition, plaintiff’s attorney in the above proceedings was listed as having an undisputed claim in the amount of \$20,000 for “attorney’s fees for Linda Cegan”.

Plaintiff’s attorney in the above divorce proceeding brought an adversary action against debtor on January 15, 2002, seeking a determination that the above debt owed by debtor for attorney’s fees was excepted from discharge. Any question in this adversary action concerning the dischargeability of this debt was eliminated when a consent order resolving the matter was approved by this court on November 15, 2002.

Plaintiff initiated this adversary action on September 27, 2002. Count I of the complaint seeks a determination that the cash payment and alimony debtor was obligated to pay her are excepted from discharge by § 523(a)(5) of the Bankruptcy Code. Count II alternatively seeks a determination that these same obligations are excepted from discharge by § 523(a)(15) of the Bankruptcy Code.²

The adversary action now before us was tried on July 23, 2003, at which time both sides were given an opportunity to offer testimony and other evidence bearing on the remaining issue in the case.

2. Plaintiff’s motion to withdraw Count II of the complaint was granted on February 28, 2003. The question whether these obligations are excepted from discharge by § 523(a)(15) is not at issue in this adversary action.

– DISCUSSION –

The sole issue remaining for resolution in this adversary action is whether debtor's obligation to pay plaintiff the sum of \$190,155 is excepted from discharge by §523(a)(5) of the Bankruptcy Code. Debtor stipulated at trial that his obligation to pay alimony to plaintiff is excepted from discharge by this provision.

Section 523(a)(5) provides in part as follows:

(a) A discharge under section 727 ... of this title does not discharge an individual debtor from any debt –

(5) to a spouse ... for alimony to, maintenance for, or support of such spouse ..., in connection with ... a divorce decree or other order of court

11 U.S.C. § 523(a)(5).

To give a debtor a “better chance” at a fresh start, the various exceptions to discharge found at § 523(a) generally are strictly construed in favor of the debtor and against the objecting creditor. This policy is tempered somewhat, however, when the debt at issue arises in the course of a divorce proceeding or as a result of a separation agreement between estranged spouses. Congress decided when it enacted § 523(a)(5) to protect spouses and dependent children where their support by a debtor is involved. Matter of Crosswhite, 148 F.3d 879, 881-82 (7th Cir. 1998). The policy underlying §523(a)(5) favors enforcement of familial obligations over a fresh start for the debtor. In re Kemp, 232 F.3d 652, 653 (8th Cir. 2000).

Because plaintiff objects to the dischargeability of the above monetary obligation owed to her by debtor, she has the burden of proving that it is excepted from discharge by § 523(a)(5). Gianakas v. Gianakas (In re Gianakas), 917 F.2d 759, 761 (3d Cir.

1990). She must do so by a preponderance of the evidence. Grogan v. Garner, 498 U.S. 279, 111 S.Ct. 654, 659-61, 112 L.Ed.2d 755 (1991).

Federal law, not state law, governs whether an obligation is in the nature of alimony, maintenance or support of a spouse for purposes of § 523(a)(5). It may, for instance, so qualify under federal law while not so qualifying under state law. Gianakas, 917 F.2d at 762.

How an obligation is characterized in a court order or an agreement between spouses is not dispositive when ascertaining its “true nature” for purposes of § 523(a)(5). *Id.* We must “look beyond the label” attached to an obligation by the court or the parties when making this determination. *Id.*

Our inquiry is limited to considering the facts as they existed *at the time the obligation arose*. *Id.* Subsequent events – e.g., a later change in the respective financial situations of the parties – are not relevant in this regard.

The answer to the question whether an obligation is in the nature of alimony, maintenance or support depends on the intention extant when the obligation arose. *Id.* If, as in the present case, the relevant instrument is a court-adopted master’s report, we must strive to ascertain the intent of the court when it issued its order adopting the report. See Brown v. Brown (In re Brown), 288 B.R. 707, 712 (Bankr. W.D. Pa. 2003).

We are to consider three “factors” when undertaking to determine this intention and hence the “true nature” of an obligation.

We first should consider the language and substance of the relevant instrument or document in the context of surrounding circumstances, taking extrinsic evidence into account if necessary. However, even an obligation designated as equitable distribution

may be related to alimony, maintenance or support because state courts often will adjust the latter depending on the nature and amount of marital assets available for distribution. *Id.*

Next we should consider the respective financial situations of the parties at the time of the court order or separation agreement. Relevant considerations may include whether one spouse has custody of their minor children, was unemployed, or was in a job that paid considerably less than the other spouse was paid. *Id.*, 917 F.2d at 763.

Finally, we should consider the function the obligation served at the time it arose. An obligation that served to provide the necessities of life – e.g., food, shelter, clothing or transportation – most likely was intended as support or maintenance. *Id.*

After applying these considerations to the facts of this case, we conclude that debtor's obligation to pay the sum of \$190,155 to plaintiff was intended to be in the nature of maintenance or support of plaintiff. The obligation, in other words, lies within the scope of § 523(a)(5).

At the very least, the *initial* \$100,000 of debtor's monetary obligation to plaintiff was intended to provide maintenance or support for plaintiff. This is evident from the master's discussion of when and under what conditions plaintiff's right to receive alimony from debtor would terminate. According to the master, plaintiff was "clearly" in need of alimony until such time as she received a "substantial portion" of the so-called "equitable distribution award". The master specifically recommended that debtor continue paying alimony to plaintiff until plaintiff received the initial \$100,000 of the cash payment provided for by the above so-called "equitable distribution award". Once debtor paid this

amount to plaintiff, his obligation to pay alimony to her would terminate. Master's Report and Recommendation, p. 17.

The initial \$100,000 of debtor's monetary obligation to plaintiff was meant to serve the same purpose as alimony served in this instance. Alimony obviously was intended to provide plaintiff with a means of paying her bills and purchasing the necessities of life – e.g., food, shelter, clothing and the like. The reason why debtor's obligation to pay alimony was supposed to terminate when it did was that plaintiff presumably would be able to utilize this initial \$100,000 instead of alimony for the same purpose – i.e., to pay her bills and to purchase the above necessities of life. The initial \$100,000 of the monetary obligation, in other words, was intended to provide maintenance or support for plaintiff.

The matter does not end there. Statements made elsewhere in the master's report compellingly indicate that the *entire* \$190,155, and not merely the initial \$100,000 of debtor's obligation, was intended to provide maintenance or support for plaintiff.

After recommending that debtor pay plaintiff a specific sum of money, the master recommended that debtor pay plaintiff \$80,000 of this amount within ninety days and pay her an additional \$20,000 within ninety days thereafter. As for the remaining balance, debtor was to make monthly installment payments with interest to debtor until the obligation was paid in full. Master's Report and Recommendation., p.15.

The following sentence leads us to conclude that the *entire* monetary obligation was intended to be in the nature of alimony, maintenance or support:

Should he [i.e., debtor] declare bankruptcy prior to payment of this obligation in full, any outstanding unpaid equitable distribution obligation

shall be deemed to be an alimony obligation and not dischargeable in bankruptcy.

Master's Report and Recommendation, p. 15.

While it obviously is for this court, and not the state court, to determine whether this obligation is or is not dischargeable pursuant to § 523(a)(5), this passage provides insight into what the state court intended with respect to the *entirety* of debtor's monetary obligation to plaintiff.

We understand this sentence as asserting, albeit perhaps inartfully, that in the event debtor filed for bankruptcy and a question as to the "true nature" of the obligation arose therein, his *entire* monetary obligation to plaintiff, not just the initial \$100,000 of it, was intended to provide maintenance or support for plaintiff as these concepts apply to § 523(a)(5) of the Bankruptcy Code. The above-stated reasons why the initial \$100,000 of debtor's obligation constituted maintenance or support for plaintiff apply with equal force to the remainder of the obligation.

Use of the phrase "equitable distribution" in the above-quoted sentence (and elsewhere) in the master's report and recommendations to characterize debtor's monetary obligation in our estimation does not undermine this conclusion. As we noted previously, we must "look beyond the label" attached to an obligation when attempting to ascertain its "true nature" for purposes of § 523(a)(5). Gianakas, 917 F.2d at 762. Characterizing an obligation as "equitable distribution" does not necessarily mean that the obligation is not in the nature of alimony, maintenance or support for plaintiff.

If the term "equitable distribution" in the above-quoted sentence is taken literally, what originally was in the nature of equitable distribution somehow would mysteriously

be transformed into an altogether different type of obligation – i.e., for alimony, maintenance or support – merely because debtor filed a bankruptcy before paying the obligation in full. We are at a loss to comprehend such a change in an obligation’s nature that is triggered by bankruptcy. Declining to construe the term “equitable distribution” as it appears in the above sentence literally and instead viewing it as part of an inartfully drafted sentence avoids this conundrum.

Consideration of the second and third “factors” identified in Gianakas, 917_F.2d at 762-73, reinforces the conclusion that debtor’s obligation to pay \$190,155 to plaintiff was intended to provide maintenance or support for plaintiff within the meaning of §523(a)(5).

There was a considerable disparity in their respective financial situations in December of 1999. Debtor’s net monthly income at the time was \$4,775. Having no basis for precisely determining plaintiff’s earning capacity because she had not been employed for several years, the master found that plaintiff had a net earning capacity of \$1,100 at the time. Master’s Report and Recommendations, pp. 5-7. The disparity in their respective monthly incomes, in other words, was \$3,675.

Unless plaintiff lived in poverty, \$1,100 per month would not have been enough for plaintiff to maintain and support herself for long. To “level the playing field” somewhat, the master recommended that debtor pay alimony to plaintiff in the amount of \$1,470 per month until debtor paid \$100,000 of the monetary obligation he owed to plaintiff.

We have determined that *all* of the \$190,155 debtor was obligated to pay to plaintiff was intended by the state court judge to provide maintenance or support for

plaintiff, the inaccurate characterization of which as “equitable distribution” notwithstanding. The function served by this obligation was to make it possible for plaintiff to pay for life’s necessities such as food, shelter and clothing which she otherwise could not have afforded upon the disintegration of their marriage.

We conclude in light of the foregoing that debtor’s obligation to pay the sum of \$190,155 to plaintiff was intended to provide maintenance or support for plaintiff for purposes of § 523(a)(5) and consequently is excepted from discharge.

An appropriate order shall issue.

/s/

BERNARD MARKOVITZ
U.S. Bankruptcy Judge

Dated: **September 25, 2004**

