

**UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
WESTERN DIVISION**

**In re: Ballard Dwight Brannan and
Carol Lynn Brannan
Debtors.**

**Bankruptcy Case No. 02 B 71411
Chapter 13**

**MEMORANDUM OPINION AND ORDER DENYING THE CHAPTER 13
TRUSTEE'S OBJECTION TO CONFIRMATION AND MOTION TO DISMISS**

This matter comes before the Court on the Objection to Confirmation of the Chapter 13 Plan and Motion to Dismiss filed by Lydia S. Meyer, the Standing Chapter 13 Trustee, (the "Trustee"). The Trustee objects on the basis that funds received pre-petition from a workers' compensation settlement should be available for distribution to creditors as disposable income. Ballard and Carol Brannan, the debtors (the "Debtors"), voluntarily disclosed the existence of \$14,000 in a deposit account from the settlement on Schedule B and have claimed the settlement proceeds as exempt on Schedule C. For the reasons stated below, this Court finds that the settlement proceeds are not subject to the disposable income test under Section 1325(b).

JURISDICTION

This Court has jurisdiction pursuant to 28 U.S.C. § 1334. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(B) and (L).

STIPULATED FACTS

The relevant facts in this case have been agreed to by stipulation of the parties and are as follows:

1. The Court has jurisdiction over the parties hereto and the subject matter herein.

2. The Debtors filed for relief under Chapter 13 of the United States Bankruptcy Code on March 26, 2002.
3. Prior to the filing of the Debtors' petition for relief, the Debtors settled a workers' compensation claim.
4. The Debtors clearly and voluntarily disclosed the existence of \$14,000 from the settlement on Schedule B of their schedules.
5. The Debtors claimed the \$14,000 settlement proceeds as exempt on Schedule C pursuant to Illinois exemptions. Illinois has opted out of the federal exemptions, and the proceeds are properly claimed as exempt under Illinois law.
6. Debtors proposed a plan which calls for payments of \$405 per month for 36 months plus one installment of \$4,000, for a total of \$18,580.
7. After the payment of filing fees to the Clerk of the Bankruptcy Court, attorney's fees in the amount of \$1,200 and trustee fees, there will be approximately \$15,459.90 available for distribution to unsecured creditors.
8. Based upon the claims filed, unsecured creditors will receive an approximate distribution of 34.9% of their claims.

DISCUSSION

The issues presented by the Trustee's objection to confirmation are: (1) whether the Debtors' workers' compensation settlement is a pre-petition asset and as such should not be considered income received during the plan period; and (2) even if classified as a pre-petition asset, whether the settlement proceeds can be considered

for purposes of the disposable income test under 11 U.S.C. § 1325(b)(1)(B) .

It is the Debtors' contention that the workers' compensation settlement constitutes a pre-petition asset. They assert that to require a debtor to surrender a pre-petition asset would be inconsistent with §1306(b), which provides that the debtor shall remain in possession of all property of the estate, and §1303, which gives the debtor, exclusive of the trustee, the rights and powers of a trustee under § 363. They further contend that § 1303 gives a debtor exclusive authority to determine the extent to which pre-petition assets will be used in furtherance of a Chapter 13 plan. Finally, the Debtors assert that to define a pre-petition asset as disposable income for confirmation purposes would, in essence, convert Chapter 13 cases to both repayment plans and Chapter 7 liquidation proceedings. The Trustee's position appears to be that, notwithstanding its status as a pre-petition asset, the settlement proceeds must be considered for purposes of the disposable income determination.

"When a bankruptcy petition is filed, virtually all property of the debtor at that time becomes property of the estate." *In the Matter of Yonikus*, 996 F.2d 866, 869 (7th Cir. 1993). The definition of property of the estate includes "all of the debtor's interests, legal and equitable." *Id.* It is clear that in the context of a Chapter 13 case the definition of property of the estate is somewhat broader by virtue of §1306, which supplements the provisions of §541. "A debtor's interest in property may be either *excluded* from the estate under 11 U.S.C. § 541 or *exempted* under § 522." *Id.* The Yonikus Court stated that "[n]o section of the Bankruptcy Code excludes a debtor's interest in workers' compensation benefits." *Id.* at 870. Section 522(c) provides that "property exempted under this section is not liable during or after the case for any debt of the debtor that

arose ... before the commencement of the case....”

The debtors rely on *In re Burgie* for the proposition that “[p]ostpetition disposable income does not include prepetition property or its proceeds.” 239 B.R. 406, 410 (9th Cir. BAP 1999). Such a position seems consistent with the plain meaning of § 1325(b)(1)(B), which states the debtor’s “projected disposable income *to be received* . . . will be applied to make payments under the plan.” (Emphasis added.) The creditor’s rights are balanced by the liquidation analysis required under § 1325(a)(4) as well as the good faith requirement of § 1325(a)(3). There would be no need for the subjunctive phrase “if the estate of the debtor were liquidated under chapter 7” if the liquidation of pre-petition assets were not merely theoretical. Thus, this Court concludes that a debtor’s pre-petition assets are not to be considered for purposes of the disposable income test.

The present case presents the question as to whether a workers’ compensation settlement constitutes a pre-petition asset merely because it is settled pre-petition and received in a lump sum. Whether the proceeds were received pre-petition or post-petition but pre-confirmation does not determine whether the proceeds should be considered in the disposable income test of § 1325(b). Instead, if the proceeds represent future income, then they constitute earnings and, as such, must be included in the disposable income test. Thus, in order to determine whether the proceeds received constitute a pre-petition asset or post-petition income, Courts must look into the nature of the workers’ compensation award.

Some courts have focused on the manner in which the workers’ compensation payments were received in order to determine whether they should be considered

income under §1325(b). “Arguably, a lump-sum workers’ compensation settlement award is not considered ‘income’ as the term is used in §1325(b)(2) because it is not regularly or periodically received by the debtor.” *In re Minor*, 177 B.R. 576, 582 (Bankr. E.D. Tenn. 1995). However, Judge Lundin explained in his Chapter 13 Treatise:

The term income is not defined by the Code. This undefined term does appear several other places in Chapter 13, and its lack of clear meaning creates some problems for Section 1325(b) purposes.

...
There is nothing in the code to require that income be regular or periodic for 1325 (b) purposes.”

2 KEITH M. LUNDIN, Chapter 13 Bankruptcy § 5.35, at 164-3 (2d ed. 1994).

Other cases appear to look at whether the asset in question consists of an anticipated stream of payments. To the extent the asset consisted of a stream of payments, they were considered projected disposable income and required for funding of the plan. See *In re Burgie*, 239 B.R. at 410 (citing cases).

The *Minor* court refused to treat lump-sum and stream of payments awards differently. The court explained that although the benefits were received in a lump sum, they were primarily based on weekly disability benefits that would have otherwise been paid to one of the debtors during the period of their plan. Based on that, the court felt it could not treat debtors who received their payments in a lump sum differently from those who received it in periodic payments over the life of the plan. 177 B.R. at 582-83.

This Court agrees that the treatment to be accorded workers’ compensation benefits requires that one look into the very nature of those benefits. Generally, the Illinois Workers’ Compensation Act, 820 ILCS 305/1 *et seq.* (the “Act”), seeks to provide a series of benefits, including compensation for accidental injuries or death suffered in the course of employment by Illinois workers. The Illinois Appellate Court described the

purpose of the act as follows:

The Workers' Compensation Act is a humane law of a remedial nature. The underlying purpose of the Act is to provide financial protection for workers whose earning power is interrupted or terminated as a consequence of injuries arising out of and in the course of their employment.

World Color Press v. Industrial Comm'n, 619 N.E.2d 159, 162 (Ill. App. Ct. 1993) (quoting *Hardin Sign Co. V. Industrial Comm'n*, 506 N.E.2d 1066, 1069 (Ill. 1987)).

Under the Workers' Compensation Act, there are four categories of benefits created by the legislature: temporary total disability, permanent total disability, temporary partial disability and permanent partial disability.

The Act provides a method to calculate compensation in nonfatal cases. 820 ILCS 305/8 (West Supp. 2002). Under section (b), the Act provides benefits for temporary total disability (TDD). The Illinois Supreme Court stated that an award of TDD "is calculated to replace lost wages during periods of actual disability and has no other purpose, apart from assuring medical treatment." *Freeman United Coal Mining Co. v. Industrial Comm'n*, 459 N.E.2d 1368, 1372 (Ill. 1984). "Temporary incapacity might be described as the period of the healing process." *World Color Press*, 619 N.E.2d at 162 (quoting *Briggs Manuf. Co. v. Industrial Comm'n*, 570 N.E.2d 1152 (Ill. App. Ct. 1989)). These benefits are clearly income as they are a substitute for wages the worker would have earned absent his temporary total disability.

Subsections (c), (d) and (e) go on to describe other available benefits.

Subsection (e) sets forth a schedule wherein the loss of use of various body parts is measured in terms of weeks of compensation. However, the purpose behind subsection (e) "is not merely to replace lost wages or provide financial protection for workers whose earning power is terminated, but is broad enough to accommodate the pain and

inconvenience that accompany the specific case of loss of both hands, both arms, both feet or both eyes even though the employee remains able to work.” *Freeman United Coal Mining Co. v. Industrial Comm’n*, 459 N.E.2d 1368, 1371 (Ill. 1984) (quoting *National Lock Co. v. Industrial Comm’n*, 338 N.E.2d 405 (Ill. 1975) (internal quotations omitted)). Moreover, disability pursuant to subsection (e) is “permanent and total only by legislative pronouncement; it is not inconsistent with a continuing ability to work, and in that event the pension mandated for it is not to be affected by the employee’s return to work.” *Id.* (Citations omitted).

In contrast, permanent total disability is one which renders the employee wholly and permanently incapable of work. 820 ILCS 305/8(f) (West Supp. 2002). “It can form the basis of an award only if the employee is able to show that his injuries have left him without a market for his skills, so that he is for practical purposes unemployable.” *Id.* at 1371(citations omitted). Clearly this type of award would constitute future income.

Permanent partial disability is awarded when a work related injury prevents an employee from pursuing his usual and customary employment. 820 ILCS 305/8(d) (West Supp 2002). An employee must show “that the injury received by him will be reasonably certain to leave him permanently partially incapacitated from pursuing his usual and customary line of employment, and thereby be reasonably certain to permanently prevent his earning as much as he would have earned had he not been injured.” *Guest Cole Company v. Industrial Comm’n*, 155 N.E.2d 326, 328 (Ill. 1927) (citation omitted). Thus, a lump sum settlement of a permanent partial disability claim does not necessarily represent an identifiable loss of future wages, but rather seeks to compensate an injured worker for a presumed diminished earning capacity in the future.

The settlement may or may not bear any correlation to actual diminished earning capacity or actual loss of wages in the future. There is nothing in the Workers' Compensation Act that precludes a recovery based on a permanent partial disability when a worker is able to return to the same job, a comparable job or even a better paying job in the future. 820 ILCS 305/8(d)(2) (West Supp. 2002). A worker may even be compensated for certain permanent disfigurement, which, again, would generally not have any bearing on earning capacity. 820 ILCS 305/8(c) (West Supp. 2002).

An injured worker who is unable to work is compensated for actual wages lost by his temporary or total disability benefits. The permanent partial disability benefits are a useful and equitable way of compensating an injured worker but do not necessarily bear any relationship to lost future wages. The fact that the compensation is couched in terms of weeks of compensation does not alter this conclusion inasmuch as such terms reflect a convenient unit of measurement, not actual future wage loss.

Even if one were to take the position that Illinois law presumes that permanent partial disability benefits are actual compensation and correspond to real lost future wages, it is the conclusion of this Court that proper analysis under §1325 would obligate this Court to look behind the labels placed on the settlement. This analysis would not differ much from what Courts presently do under §523(a)(5), that is, look to state law for guidance, but apply the Bankruptcy Code to determine whether a particular debt is actually in the nature of alimony or maintenance. See *In re Reines*, 142 F.3d 970, 972 (7th Cir. 1998). Likewise, a Bankruptcy Court should look behind the labels of the Worker's Compensation Act to determine if the benefits are in fact a substitute for future wages.

Thus, this Court concludes that the test of whether the settlement constitutes projected income during the course of a Chapter 13 plan is accomplished by looking at the settlement itself and the debtor's post-petition employment situation. If the settlement is a bona-fide attempt to compensate the debtor for a discernable diminished earning capacity, such as in the wage differential cases¹ where physical limitations are shown to relegate a worker to a lower paying job, then the lump sum settlement can be attributed proportionately to the debtor's diminished earnings during the life of the plan. In such cases the Court must bear in mind that the lump sum settlement would represent compensation for the worker's diminished earning capacity during the balance of his/her working years. Accordingly, only a proportionate share attributable to the life of the plan should be considered for disposable income purposes. In the absence of such a showing, a pre-petition settlement of a workers' compensation claim for permanent partial disability does not constitute future earnings or future income as contemplated by §1322(a)(1).

In the present case, the Debtors will apparently continue to earn wages as their plan payments are not dependent upon the workers' compensation settlement proceeds. Based on the limited facts presented, this Court finds that the settlement proceeds do not constitute future income. The Debtors are able to work and the Trustee bases her objection on the mere fact that the proceeds are derived from a workers' compensation

¹820 ILCS 305/8(d)(1) provides in relevant part: "the employee ... shall ... receive compensation for the duration of his disability, subject to limitations as to maximum amounts fixed in paragraph (b) of this Section, equal to 66-2/3 % of the difference between the average amount which he would be able to earn in the full performance of his duties in the occupation in which he was engaged at the time of the accident and the average amount he is earning or is able to earn in some suitable employment or business after the accident."

award. That alone is not enough to sustain her objection that the proceeds constitute future income. This Court adopts the position of those courts which have clearly articulated that “[p]ostpetition disposable income does not include prepetition property or its proceeds.” *In re Burgie*, 239 B.R. at 409. The statutory language defining the income to fund the plan consistently looks forward, not to the present or past, with the phrases “projected disposable income to be received”, 11 U.S.C. § 1325(b)(1), and “the plan shall provide for the submission of all or such portion of future earnings or other future income” 11 U.S.C.A. § 1322(a). Therefore, because no portion of the settlement proceeds represents future wages, it constitutes a pre-petition asset.

Because this Court finds that the workers’ compensation settlement is a pre-petition asset which is not subject to disposable income considerations, it is not necessary to determine the effect of the Illinois exemption statute (735 ILCS 5/12-1001(g)(3)) or the special exemption created by the Act (820 ILCS 310/21).

It is hereby ordered that the Trustee’s objection to confirmation and motion to dismiss are denied.

DATE:

MANUEL BARBOSA
United States Bankruptcy Judge