

FILED

SEP 04 2003

UNITED STATES
BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

UNITED STATES BANKRUPTCY COURT
DISTRICT OF ARIZONA

In Re) Chapter 11
PALM VALLEY NURSING FACILITY, L.P.,) No. 01-15615-ECF-GBN
Debtor.)
JOANN P. WEBB,) No. 02-486-ECF-GBN
Debtor.) (Jointly Administered)
WILLIAM NYE,) Adversary No. 02-590
Plaintiff,)
vs.) FINDINGS OF FACT,
JOANN P. WEBB,) CONCLUSIONS OF LAW
Defendant.) AND ORDER

The complaint of creditor William Nye ("Plaintiff") to determine the dischargeability of a debt was tried to the Court as a bench trial on February 27 and April 24, 2003. Closing argument was presented on July 29, 2003.

The Court has considered the stipulated pretrial order of December 20, 2002, sworn witness testimony, admitted exhibits and the facts and circumstances of this case. An interim order was entered on August 29, 2003, announcing the Court's decision. The following

1 findings and conclusions are now entered:

2 **FINDINGS OF FACT**

3 1. Defendant Jo Ann P. Webb filed a voluntary chapter 11 reorganization case
4 within the District of Arizona on January 10, 2002. Plaintiff filed an adversary complaint against
5 Ms. Webb (“debtor”) on April 17, 2002, seeking a declaration that his claim would not be
6 discharged in her bankruptcy. The personal chapter 11 is being jointly administered with the
7 reorganization case filed for debtor’s business, the Palm Valley Nursing Facility.

8 Plaintiff and defendant were married on June 23, 1990 and lived in a suburb of
9 Des Moines, Iowa. Shortly before the marriage, the parties negotiated and signed a prenuptial
10 contract on June 15, 1990. Exhibit (“Ex.”) 1. Both parties were represented by legal counsel.
11 Testimony (“test”) of William P. Nye of February 27, 2003.

12 2. There was a marked disparity in the parties’ premarital income and assets.
13 Ms. Webb had a net worth of \$9,240,165, while Mr. Nye reported \$757,444. *See* exhibits A and
14 B attached to Ex. 1. The prenuptial agreement expressly provided an alimony award of \$5,000
15 monthly to the husband in the event of a subsequent divorce. Such payments were to be made
16 by debtor until plaintiff remarried, cohabited with another or either party died. No alimony was
17 to be paid debtor in the event of divorce. Ex. 1 at p. 3.

18 3. The agreement was originally proposed and drafted by debtor’s attorney to
19 protect her extensive financial and business interests. Debtor objected to the concept of paying
20 alimony to an able-bodied man, but was told by her attorney that if the agreement did not provide
21 for alimony in a specific amount, a judge would “write one in” in the event of divorce. Debtor
22 was aware of the difficulties when such matters are litigated. Her prior divorce resulted in a
23 dramatic, very public 48-day trial and an appeal to the Iowa Supreme Court. Debtor’s attorney
24 originally proposed alimony of \$2,000 per month. When plaintiff’s attorney returned his draft
25 version of the agreement, a \$5,000 alimony award was inserted. Ms. Webb was perplexed by
26 this, but agreed to sign, as the document had to be executed prior to the marriage ceremony. She
27

1 is a business person experienced in dealing with lawyers and legal documents. The parties signed
2 the document on June 15, 1990 and were married on June 23, 1990. Test. of Jo Ann P. Webb;
3 Ex. 1 at pgs. 4-5.

4 4. The alimony provisions of the premarital agreement were originally not a
5 major consideration for plaintiff, who viewed the agreement as principally preserving their
6 individual property and financial interests. Plaintiff was 50 or 51 years old at the time of the
7 marriage, was in reasonably good health, worked as a deputy U.S. Marshal and a private
8 investigator and had investment income from farming. His annual income at the time was
9 \$45,000 to \$50,000.

10 During the four to four and one-half year marriage, plaintiff found it increasingly
11 difficult to pursue his career, as he contends he had to spend time on debtor's business and
12 personal matters, including litigation. Debtor did not ask him to give up his occupation in order
13 to assist her, however. The parties lived well and traveled. As demands on his time increased
14 during the marriage and his personal income declined, his potential alimony right became more
15 important. Test. of Mr. Nye. Debtor recalls specifically requesting plaintiff's assistance regarding
16 the construction of a building. In her opinion he did not do well. Accordingly, her normal
17 procedure was to hire a contractor for a project and have the plaintiff watch. Test. of Ms. Webb.

18 5. The parties separated in the summer of 1994. A Polk County, Iowa divorce
19 action was subsequently filed by debtor. Each party was represented by counsel. At plaintiff's
20 request, the Iowa court required debtor to pay temporary support, establishing the amount as
21 \$4,500 monthly by order of October 11, 1994. Exs. 29-30. Plaintiff's attorney argued for the
22 temporary support award based on the provision for alimony in the prenuptial agreement and the
23 disparity in the parties' income. Debtor acknowledged making the support payments. Test. of
24 James C. Carney; Ex. 31.

25 6. Rather than litigate the validity of the prenuptial agreement, the parties
26 through counsel agreed to installment payments by debtor to plaintiff of \$350,000. Ex. 3. The
27

1 initial payment of \$150,000 was described as a property settlement transaction that was not
2 taxable to plaintiff. Plaintiff understood this payment to be a property settlement and not a support
3 award. Nye direct test. An additional \$200,000 was payable to plaintiff over the next four years.
4 Attorney Shindler's letter of December 16, 1994, Ex. 3 at p. 1. Debtor's attorney stated the
5 \$200,000 in annual "...payments will be described as a property settlement for purposes of
6 dissolution but will be contingent on William Nye surviving Jo Ann Webb-Nye and as a result
7 will be structured as deductible for federal income tax purposes for Jo Ann Webb-Nye and
8 taxable to William Nye." *Id.* Less than a week later, another of debtor's attorneys referred to the
9 annual payments to be made to plaintiff as "support payments." Attorney Smith's letter of
10 December 22, 1994, Ex. 4.

11 7. A formal agreement was signed by the parties, debtor's two divorce attorneys
12 and plaintiff's attorney on January 23, 1995. The Iowa court approved the document on
13 January 26, 1995. Exhibit 6 at p. 9. The annual payment amounts were revised, but remained
14 deductible by debtor and taxable to plaintiff. All payments are clearly identified as property
15 settlement payments, even though the future annual payments terminate if plaintiff dies. *Id.* at
16 p. 5. The parties clearly waived their respective rights to alimony in the agreement. *Id.* at p. 6.

17 8. Debtor and her divorce attorney did not want the decree to provide for
18 alimony. Plaintiff had health issues, debtor believed, was in his fifties in age and she did not want
19 to open the door to an alimony award which could later be increased by a court. Tax
20 consequences were also an important consideration. Attorney Smith was brought into the case
21 just to handle tax implications for debtor. Test. of Steven H. Shindler. Plaintiff's divorce
22 attorney believes the annual payments actually were support, but were characterized otherwise
23 by debtor for tax planning purposes. Test. of Carney.

24 9. Although the payments were labeled as a property settlement in the divorce
25 agreement, debtor and her professionals identified them as alimony payments subsequently. For
26 example, debtor made the required \$61,000 annual payment for 1997 by a personal check, clearly
27

1 marked as an alimony payment. Ex. 14; test. of Ms. Webb. Debtor's attempt to blame the
2 alimony notation on her accountant for the check she personally signed is not credible to this fact
3 finder.

4 Her 1995 federal income tax return, which covered the initial \$150,000 lump
5 sum property settlement payment, not conditioned on plaintiff surviving debtor, does not reflect
6 alimony deductions. Test. *id.*; Ex. 19. Plaintiff reported his 1995 receipt of \$4,500 temporary
7 monthly support on his personal return as alimony received. Nye test.; Exs. 9-11.

8 Debtor's tax return for 1996 deducts her annual settlement payment to plaintiff
9 of \$68,000 as "alimony paid." Test. of Ms. Webb; Ex. 20 at form 1040, p. 1. The attached letter
10 of September 25, 1997 from her CPA reminds her that she is responsible for the accuracy of the
11 information she provided and she is to contact his office if she has questions. *Id.* at
12 September 25, 1997 letter, p. 2. Plaintiff reported receipt of the funds as "alimony received." Ex.
13 12.

14 Her return for 1997, again with a reminder from her CPA concerning her
15 responsibility for its accuracy, identifies the \$61,000 payment to plaintiff as "alimony paid."
16 Test. *id.*; Ex. 21, form 1040. Debtor's late filed 1998 return, prepared by a different CPA firm,
17 identifies the \$46,000 payment to plaintiff's listed social security number as "alimony paid."
18 Test. *id.*; Ex. 22. Ms. Webb's testimony that she had to identify the payments as alimony simply
19 because that is the only deduction option provided by the tax form is not credible to this fact
20 finder. Plaintiff reported receipt of the same amount as 1997 alimony received. Ex. 13.
21 Plaintiff reported the last payment received from debtor of \$ 46,000 as 1998 alimony received.
22 Ex. 15.

23 10. When debtor experienced business and financial difficulties, her legal
24 counsel wrote plaintiff's counsel seeking a delay in making the last payment of \$ 25,000 required
25 under the agreement. Shindler letter of January 25,1999, Ex. 17. Plaintiff responded,
26 characterizing the sum as "the last alimony payment." Letter of February 24,1999, Ex. 18.
27

1 Debtor's counsel did not object to this characterization. Nye test. Debtor has made all but the
2 last \$25,000 payment under the divorce agreement.

3 11. The court finds that at the beginning of the parties' marriage, plaintiff had
4 a significant contract right of \$5,000 monthly alimony in the event of divorce. This contract right
5 was not obtained by unfair methods. It arose through debtor's attempts, with the help of legal
6 professionals, to protect her own financial interests through a prenuptial contract. While
7 plaintiff's alimony interest, (based on contract or implied by law given the parties' income
8 disparity¹) was never verified by an Iowa court, it was sufficiently substantial to justify a judicial
9 temporary support award.

10 Debtor clearly manifested an interest in tax planning her divorce payments. As
11 the party with the most assets, it would be in her financial interest to have her obligations not
12 characterized as alimony, which could be subsequently increased by a divorce court. Following
13 the negotiated labeling of the payment stream as a property settlement and expressly not alimony,
14 debtor adopted her professionals' characterization of the payments as alimony. The testimony
15 of plaintiff and his divorce attorney that they considered the payment stream as alimony,
16 regardless of the label the agreement placed on them, is credible to this fact finder.

17 12. To the extent any of the following conclusions of law should be considered
18 as findings of fact, they are incorporated herein by reference.

Conclusions of law

20 1. To the extent any of the above findings of fact should be considered as
21 conclusions of law, they are incorporated herein by reference.

22 2. Pursuant to 28 U.S.C. § 1334 (a), jurisdiction of the jointly administered
23 bankruptcy cases is vested in the United States District Court for the District of Arizona. That
24 court has referred, under 28 U.S.C. § 157(a), all cases under title 11 of the United States Code and

26 1 The parties were required to submit personal financial information to the Iowa divorce
27 court. Nye test.

1 all adversary proceedings arising under title 11 or related to a bankruptcy case to the Arizona
2 bankruptcy court. Amended District General Order 01-15. This proceeding having been
3 appropriately referred, this court has core jurisdiction to hear and determine whether plaintiff's
4 claim is dischargeable. 11 U.S.C. §157 (b)(2)(I).

5 3. Conclusions of law are reviewed *de novo*. Factual findings are reviewed for
6 clear error. *American Law Center P.C. v Stanley (In re Jastrem)*, 253 F. 3d 438, 441 (9th Cir.
7 2001).

8 4. Section 523 (a) (5) excepts from a bankruptcy discharge any support
9 obligation resulting from a separation or divorce agreement. Whether an obligation arising from
10 a divorce actually is nondischargeable support is a question of federal law. The bankruptcy court
11 is not required to accept the description or designation of items by the parties in a settlement
12 agreement as conclusive in deciding whether the debt is nondischargeable support or a
13 dischargeable property settlement obligation. Rather, the court looks beyond the language of the
14 agreement to the substance of the obligation. The court must ascertain the intention of the parties
15 at the time they entered into the stipulated agreement. Substance prevails over form in the context
16 of § 523 (a) (5) litigation. 11 U.S.C. § 523 (a) (5); *Seixas v. Booth (In re Seixas)*, 239 B.R. 398,
17 402 (9th Cir. Bankr. 1999) (citing cases).

18 Given the conduct and circumstances of the parties, this court will not conclude
19 that the declaration in the divorce settlement that no alimony was to be paid and that all payments
20 to be received by plaintiff were a property settlement is conclusive. Given the preexistence of
21 plaintiff's contractual alimony right, preliminarily recognized by the Iowa divorce court in an
22 award of \$4,500 temporary support, the disparity in income between the parties, the clearly
23 manifested motivation of debtor to engage in tax planning as part of divorce negotiations,
24 plaintiff's and his counsel's credible belief at the time that the amounts were support and debtor's
25 after the fact labeling of the payments as alimony in her payment check and tax returns, this court
26 concludes the labeling given the payments in the settlement is not dispositive.

27

28

1 5. In determining whether debtor's obligation is support, the critical inquiry is
2 the shared intent of the parties at the time the obligation arose. The parties' intent is a factual
3 finding reviewed for clear error. The court should consider several factors in determining how
4 the parties truly intended to characterize the obligation. Foremost, the court should consider
5 whether the recipient spouse actually needed spousal support at the time. In determining whether
6 support was necessary, the court should examine if there was an imbalance in the relative income
7 of the parties at the time of the divorce. The court should also consider whether the obligation
8 terminates on the death or remarriage of the recipient and whether the payments are directly made
9 to the recipient in installments over a substantial time period. Finally the labels given to the
10 payments by the parties may be reviewed as evidence of intent. *Friedkin v. Sternberg*² (*In re*
11 *Sternberg*), 85 F. 3d 1400, 1405 (9th Cir. 1996) (citing cases).

12 Applying these factors, certainly plaintiff was far from indigent at the time of the
13 divorce agreement. He had farming interests, worked as a private investigator, was in reasonably
14 good health and attached a five-year-old financial statement to the agreement reflecting a net
15 worth of \$491,661. Ex.6 at attached exhibit 2; Nye cross examination test. A post-divorce
16 financial statement reflects plaintiff's net worth as of April 15, 1995 to be \$636,066. Ex. K at p.
17 2. However, it is not this court's function to award alimony, but simply to determine what the
18 parties intended in the January 1995 stipulated order. *Sternberg*, *id.* Clearly there was a
19 significant imbalance in the relative income of the parties at the time of the divorce, as the Iowa
20 court apparently recognized in awarding temporary support. Factual findings 2,5; Ex. 29.

21 Another factor favoring plaintiff is that the stream of payments terminated upon
22 plaintiff's death. Ex. 6 at p. 5, section C. The payment stream is in the form of installments
23 made directly to plaintiff over a four-year time period in substantial amounts. *Id.* Plaintiff

24 _____

25 2Subsequently the Circuit *en banc* reversed *Sternberg*'s procedural holding only to the
26 extent it presumed that mixed questions of fact and law are reviewed other than *de novo* by
27 appellate courts. *Murray v. Bammer (In re Bammer)*, 131 F. 3d 788, 792 (9th Cir. 1997) (§523
(a) (6) case).

1 credibly testified that in the years he received the payments, they exceeded his earned income.
2 Nye redirect test. Finally, while the agreement labeled the debt as a property settlement, debtor,
3 her accountants and her attorneys labeled them as alimony in business correspondence, tax returns
4 and on one of the payment checks itself. Exs. 4, 14 (at p. 3), 20-22.

5 6. The burden of proof in all nondischargeability litigation is the
6 preponderance of the evidence standard. *Grogan v. Garner*, 498 U.S. 279, 111 S.Ct. 654,
7 659-60 (1991). The court concludes that the plaintiff has met this burden in establishing that
8 the divorce settlement payments were intended at the time by the parties to constitute
9 alimony. The court is mindful that this case is far from the usual § 523 (a) (5) factual
10 circumstances of a working husband and a recipient wife and mother, caring for children.
11 However, dischargeability of § 523 (a) (5) debt is not subject to a balancing of hardships or
12 equities by the bankruptcy court. *Comer v. Comer (In re Comer)*, 27 B.R. 1018, 1020-21
13 (9th Cir. Bankr. 1983).

Order

15 The Court finds for plaintiff and against defendant. Plaintiff will promptly
16 serve and lodge a proposed judgement consistent with these findings and conclusions.
17 Defendant will have five days to object to the form of the proposed judgement.

18 Dated this 4th day of September, 2003

George B. Nielsen, Jr.
United States Bankruptcy Judge

23 Copy of the above mailed
this 9th day of September, 2003 to:

24 Jeffrey A. McKee
25 Davis, McKee & Forshey, P.L.L.C.
5333 N. Seventh Street Suite A-201
26 Phoenix, Arizona 85014

1 Craig J. Bolton
2 Jennings, Haug & Cunningham, LLP
2800 North Central Avenue Suite 1800
Phoenix, Arizona 85004-1049

3
4 *S. Diane Faure*
5 Deputy Clerk

6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28