

Notes

The Effect of the Indiana Divorce Law upon the Application of Section 17a(7) of the Bankruptcy Act

I. PHILOSOPHICAL HISTORY

Generally, two theories have provided the theme for the evolution of American bankruptcy law in the twentieth century. The first concept was that there should be an equal distribution of the assets of the insolvent debtor among his general creditors.¹ Historically, this consideration gave strong impetus to the enactment of bankruptcy legislation. Commerce needed to be protected from the dishonest debtor who was about to secrete or was secreting his assets for the purpose of hindering, defrauding, or delaying his creditors.²

In response to the need for legal control over the person who had removed, or was about to remove, himself or his property from the reach of the law, early bankruptcy legislation was initially directed toward criminal conduct.³ Born in continental Europe and England during the middle ages, bankruptcy law grew as a weapon against the commercial trader who fled from the commercial center or who concealed his property to prevent his creditors from exercising legal remedies.⁴ Relief was strictly creditor-oriented. Proceedings were involuntary in that they could only be instituted by an aggrieved creditor.⁵ A remedy did not exist that could be exercised by the debtor in his own behalf. In addition, the then existing involuntary creditor proceedings provided only for the liquidation of assets and distribution of the proceeds; there was no provision for

¹See *In re Harwald Co.*, 497 F.2d 443 (7th Cir. 1974). See generally Loiseaux, *Domestic Obligations in Bankruptcy*, 41 N.C. L. REV. 27 (1962).

²See *In re Time Sales Fin. Corp.*, 474 F.2d 1197 (3d Cir. 1971). In discussing the purposes of the Bankruptcy Act the court said: "One of the chief purposes of the bankruptcy laws is 'to secure a prompt and effectual administration and settlement of estates of all bankrupts . . .'" *Id.* at 1201 (quoting *Katchen v. Landy*, 382 U.S. 323, 328 (1966) (quoting *Ex Parte Christy*, 44 U.S. (3 How.) 292, 312 (1845))).

³COMMISSION ON BANKRUPTCY LAWS OF THE UNITED STATES, REPORT OF THE COMMISSION ON BANKRUPTCY LAWS 77 (CCH 1973). [hereinafter cited as COMMISSION ON BANKRUPTCY LAWS]. The commission was created by Congress in 1970 to study, analyze, evaluate, and recommend changes to the Bankruptcy Act to meet adequately the needs of present day technical, financial, and commercial activities. Pub. L. No. 91-354, 84 Stat. 468 (1970).

⁴Trieman, *Escaping the Creditor in the Middle Ages*, 43 LAW Q. REV. 230 (1927).

⁵COMMISSION ON BANKRUPTCY LAWS, *supra* note 3, at 77.

the discharge of the obligations left unsatisfied after distribution of the debtor's assets.⁶

As time passed, however, a second concept developed an increasing importance: an honest debtor should be given a fresh start in the community.⁷ Relief should be afforded to the debtor as well as to his creditors. The cooperative action roots of modern bankruptcy law date back to the English common law which provided for contracts of composition⁸ and assignments for the benefit of creditors. Those insolvency laws were premised on the need of an unfortunate debtor to meet his obligations by equitably apportioning his assets among his creditors. Unlike the earlier creditor-protection statutes, these laws provided for voluntary filing by the debtor.⁹ In addition, relief included a discharge among the available remedies as well as liquidation of assets and distribution of the proceeds to creditors.¹⁰

This concept of rehabilitation did not evolve solely for the benefit of the debtor, but also for the benefit of the economic community as a whole. An individual who is required to live under an impossible debt load becomes a burden on society, tends to be less productive, and is removed from the marketplace as a viable purchaser of goods and services. Rehabilitation of the debtor makes sound economic and social sense.¹¹

It is also important to note the change in the nature of the debtor applying for bankruptcy relief. Prior to World War II, bankruptcy was primarily a businessman's remedy; however, the evolution, growth, and maturation of the consumer credit economy has turned bankruptcy from the almost exclusive province of the entrepreneur into the haven of the wage earner.¹² Indeed, the number of bankruptcies in the United States has increased dramatically since 1950.¹³ The growth has been mainly in the number of consumer bankruptcies which grew from 8,566 in 1946 to a peak of 191,729 in 1967 as

⁶*Id.*

⁷See *In re Nickerson & Nickerson, Inc.*, 530 F.2d 811 (8th Cir. 1976); *Fallick v. Kehr*, 369 F.2d 899 (2d Cir. 1966).

⁸A contract of composition is defined as:

An agreement, made upon a sufficient consideration, between an insolvent or embarrassed debtor and his creditors, whereby the latter, for the sake of immediate or sooner payment, agree to accept a dividend less than the whole amount of their claims, to be distributed *pro rata*, in discharge and satisfaction of the whole.

BLACK'S LAW DICTIONARY 357-58 (rev. 4th ed. 1968).

⁹COMMISSION ON BANKRUPTCY LAWS, *supra* note 3, at 77.

¹⁰*Id.*

¹¹*Bostwick v. United States*, 521 F.2d 741 (8th Cir. 1975).

¹²COMMISSION ON BANKRUPTCY LAWS, *supra* note 3, at 45.

¹³See Pub. L. 91-354, 84 Stat. 468 (1970).

the amount of personal debt outstanding climbed from 31 billion dollars to 338 billion dollars in the same span of years.¹⁴

A number of studies of personal bankruptcies have been conducted over the past twenty years.¹⁵ In terms of marital status, the studies uniformly indicate that consumer bankrupts are more likely than the general population to be separated, divorced, or experiencing domestic difficulty. In fact, it appears that a substantial portion of all non-business bankrupts fall within that category. As noted by the Commission on the Bankruptcy Laws of the United States in its report of July 30, 1973, upon reviewing study information:

Brunner reported that 18.2% of the bankrupts in his sample were divorced, separated, or had divorces pending, as distinguished from corresponding 5% figure of the general population. Siporin states that 15 of 30 families reported serious marital conflicts. Herrmann indicated that 1/3 in his group were involved in divorce proceedings within a period 1 year prior to or one year after the date of the petition. Mathews similarly reported that 33% were experiencing or had experienced marital difficulty. The Brooks statistics showed that 24.7 percent of the debtors had been divorced or were divorced at the time of filing. The Brookings Report represented six percent of its sample as separated and nine percent as divorced. Stabler reported that 36 percent of the bankrupts, as distinguished from 19.3 percent of his control group, had been previously married.¹⁶

To this second basic concept, rehabilitation of the debtor, the law has appended numerous exceptions resulting from competing ideas and interests which have been allowed to override the idea of a fresh start. The evolution of bankruptcy law has established a pattern whereby discharge is increasingly available to the honest debt-

¹⁴D. STANLEY & M. GIRTH, *BANKRUPTCY: PROBLEM, PROCESS, REFORM* 25 (1971).

¹⁵G. Brooks, *Report of Bankruptcy Statistics in Southern District of Indiana, 1973* (unpublished); G. Brunner, *Personal Bankruptcies: Trends and Characteristics*, (Bur. of Bus. Res. Monograph No. 124, Ohio State Univ., 1965); R. Herrman, *Casual Factors in Bankruptcy: A Case Study*, (Inst. of Gov't Affairs Occasional Paper No. 6, Univ. of Calif., Davis, 1965); H. Mathews, *Causes of Personal Bankruptcies*, (Bur. of Bus. Res. Monograph No. 133, Ohio State Univ., 1969); D. STANLEY & M. GIRTH, *BANKRUPTCY: PROBLEM, PROCESS, REFORM*, ch. 4 (1971); M. Siporin, *Family Problem Solving and Wage Earner Families*, (unpublished study, 1963), *synopsized in A Study of Bankruptcy Court Debtors*, 20 PERS. FIN. L.Q. REV. 92, (1966); G. Stabler, *The Experience of Bankruptcy*, (Credit Ass'n of Rockford, Ill., 1966), *as reported in J. Lee, Senate Comm. on the Judiciary, 92d Cong., 1st Sess., Bankruptcy Study Plan 14-16* (Comm. Print 1971).

These studies are referred to in COMMISSION ON BANKRUPTCY LAWS, *supra* note 3, at 70.

¹⁶COMMISSION ON BANKRUPTCY LAWS, *supra* note 3, at 53 (footnotes omitted).

or, with a parallel development that the number of obligations not affected by bankruptcy discharge is gradually increasing.¹⁷ The honest debtor will receive a discharge almost as a matter of right, but that discharge may not relieve him of many of the troublesome burdens which plague society in today's complex and competitive world.¹⁸ Thus, bankruptcy courts increasingly must address the multiple problems of daily and family life affected by discharge.¹⁹

Social attitudes about the family have also undergone dramatic change in the past few decades. The pattern of divorce laws has grown from relatively restrictive legislation to the present no-fault divorce statutes.²⁰ Since 1970 more than thirty states have adopted a system of no-fault divorce or have added no-fault grounds to their existing divorce statutes.²¹ Indiana joined this revolution in 1973.²²

For a number of reasons, the female in mid-twentieth century society is not entirely dependent on the male. Today, when a woman marries, she does not lose her independence and identity, as she once did. The number of double-income families has continually increased in recent decades.²³ Women no longer necessarily lose their earning power as a result of marriage and, therefore, may not be rendered destitute by the loss of a husband through divorce. One might also read into modern divorce and remarriage statutes the suspicion that the concept of the "used woman" has changed or is changing. To the ancient Anglo-Saxon notion that for each woman there is but one man, one may now add "one at a time."²⁴ While in many states the idea of a continuing obligation by a husband to a divorced wife is changing, federal bankruptcy law has not changed relative to family obligations.

As early as 1904, the United States Supreme Court in *Wetmore v. Markoe*²⁵ asserted:

The bankruptcy law should receive such an interpretation as will effectuate its beneficent purposes and not name it an instrument to deprive dependent wife and children of the support and maintenance due them from the husband and father, which it has ever been the purpose of the law to enforce. Systems of bankruptcy are designed to relieve the honest debtor from the weight of indebtedness which has

¹⁷Loiseaux, *supra* note 1, at 27.

¹⁸*Id.*

¹⁹*See id.* at 28.

²⁰*See id.* at 27.

²¹Note, *Alimony in Indiana Under No-Fault Divorce*, 50 IND. L.J. 541 (1975).

²²IND. CODE §§ 31-1-11.5-1 to 24 (1976).

²³Loiseaux, *supra* note 1, at 28.

²⁴*Id.*

²⁵196 U.S. 68 (1904).

become oppressive and to permit him to have a fresh start in business or commercial life, freed from the obligation and responsibilities which may have resulted from business misfortunes. Unless positively required by direct enactment the courts should not pressure a design on the part of Congress in relieving the unfortunate debtor to make the law a means of avoiding enforcement of the obligation, moral and legal, devolved upon the husband to support his wife and to maintain and educate his children.²⁶

There has been a continuing conflict between the concept of giving the debtor a fresh start, as espoused by the bankruptcy law, and the debtor's continuing obligations and duties to his family as reflected in federal and state court decisions. This conflict is evident in the courts' attempted application of section 17a(7) of the Bankruptcy Act to family law situations.

II. THE BANKRUPTCY ACT AND INDIANA CASE LAW

Section 17a(7) of the Bankruptcy Act provides: "A discharge in bankruptcy shall release a bankrupt from all of his provable debts, whether allowable in full or in part, except such as . . . are for alimony due or to become due, or for maintenance or support of wife or child" ²⁷

When it is apparent that a divorce is inevitable, it is common for a husband, wife, and their representatives to negotiate a settlement agreement, which is then attached or incorporated into the decree. Such agreements take a variety of forms in an attempt to deal with the future rights and property of the spouses. The agreement may include nothing more than a division of the presently-owned prop-

²⁶*Id.* at 77.

²⁷Bankruptcy Act § 17a(7), 11 U.S.C. § 35a(7) (1976). On November 6, 1978, Congress enacted a new codification of bankruptcy law, the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (effective Oct. 1, 1979) (to be codified at 11 U.S.C. §§ 101-151326). Section 17a(7) of the present Act will be replaced by § 523(a)(5) of the new code:

(a) A discharge under section 727, 1141, or 1328(b) of this title does not discharge an individual debtor from any debt

. . . .

(5) to a spouse, former spouse, or child of the debtor, for alimony to, maintenance for, or support of such spouse or child, in connection with a separation agreement, divorce decree, or property settlement agreement, but not to the extent that—

(A) such debt is assigned to another entity, voluntarily, by operation of law, or otherwise; or

(B) such debt includes a liability designated as alimony, maintenance, or support, unless such liability is actually in the nature of alimony, maintenance, or support;

This language does not specifically alter the thrust of § 17a(7).

erties of the parties, or it may make provision for future payments to the wife and child.²⁸ If the parties have not been able to agree prior to the final divorce hearing, the court will enter a decree or order establishing the rights of the parties to the property accumulated and providing for the future obligations of the husband in a manner consistent with state law.²⁹

In the event of the husband's bankruptcy, the exact nature of the settlement agreement or decree is often at issue in applying section 17a(7) of the Bankruptcy Act. The problem is to place the obligations in the appropriate legal pigeonhole.³⁰

"Alimony," as used in section 17a(7), is generally agreed to be an allowance from a divorced husband's estate made to the divorced wife for her maintenance and support.³¹ If a debt is determined to be one arising as an element of a property settlement, normally it is dischargeable in bankruptcy.³² The difficulty, however, arises in determining whether the language used in property settlement agreements refers to the type of obligation contemplated by the term "alimony" used in the Bankruptcy Act.

The recent case of *Nichols v. Hensler*,³³ which supposedly is dispositive of the issue in Indiana,³⁴ is demonstrative of the problem. In that controversy, the former wife of the bankrupt had initiated supplemental proceedings to collect a judgment for arrearages in alimony. The United States District Court for the Southern District of Indiana held that the obligation to make payments to a former wife pursuant to the property settlement agreement was not discharged in bankruptcy. The husband appealed.³⁵

Before the entry of the divorce decree, the parties had entered into a written "Property Settlement Agreement."³⁶ The agreement had allocated specifically described property, including real estate,

²⁸See, e.g., IND. CODE § 31-1-11.5-10 (1976).

²⁹See, e.g., *id.* § 31-1-11.5-9.

³⁰The difficulty in interpretation and application stems from the variety of meanings given the terms "alimony" and "property settlement" in the legislation and case law of the various states and in the intentional or unintentional misuse of those terms as labels in divorce settlement agreements.

³¹See *Norris v. Norris*, 324 F.2d 826 (9th Cir. 1963); *In re Baldwin*, 250 F. Supp. 533 (D. Neb. 1966); 1A COLLIER ON BANKRUPTCY ¶ 17.18, at 1669-70 (14th ed. 1977 rev.); 3A COLLIER ON BANKRUPTCY ¶ 63.13, at 1839 (14th ed. 1977 rev.).

³²*Caldwell v. Armstrong*, 342 F.2d 485 (10th Cir. 1965); *Goggans v. Osborn*, 237 F.2d 186 (9th Cir. 1956).

³³528 F.2d 304 (7th Cir. 1976).

³⁴*Accord, In re Woods*, 561 F.2d 27 (7th Cir. 1977); *In re Boswell*, No. 76-2118 (7th Cir. Apr. 20, 1977).

³⁵528 F.2d at 304.

³⁶*Id.* at 305. The parties specifically titled their accord "Property Settlement Agreement."

securities, automobiles, and insurance policies, between the husband and wife. In addition, after providing for adjusting payments of cash from one party to the other, the agreement had provided:

The Husband shall pay to the Wife a sum certain of One Hundred Twenty-One Thousand Dollars (\$121,000.00) in equal monthly installments of One Thousand Dollars (\$1,000.00) each, the first installment of which shall be due and payable on or before the first day each calendar month thereafter, until One Hundred Twenty-One (121) of such installments have been paid; and it shall be agreed between Husband and Wife that the sum of Two Hundred Fifty Dollars (\$250.00) of each said monthly installments shall be considered as payment to Wife for the support and maintenance of such minor children as shall be in her care and custody; the balance of such monthly installments shall be considered as payment by Husband to Wife for and as payment of alimony.³⁷

The divorce decree recited that, in the agreement, the parties had agreed "to divide all of the marital property,"³⁸ subject to the court's approval and the entry of the divorce decree. In addition, the decree found the agreement to be "a fair and equitable division of the marital property"³⁹ and incorporated the agreement by reference.⁴⁰

Despite the express description of the obligation created by paragraph eleven of the agreement as "alimony," the husband maintained: "Section 17a(7) does not except the obligation from discharge, because, under the terms of the divorce decree and in the view of alimony taken by Indiana law, the obligation was incurred as an element of a property settlement rather than as support for the former wife."⁴¹

The Seventh Circuit Court of Appeals described the controlling issue as being "whether the term 'alimony' as used in the agreement . . . refers to the type of obligation contemplated by the term 'alimony' used in the Bankruptcy Act"⁴² (*i.e.*, income and support for a former wife). To resolve that question, the court found that, because Indiana was the situs of the divorce, its law was determinative.⁴³

³⁷*Id.*

³⁸*Id.* at 306.

³⁹*Id.*

⁴⁰*Id.*

⁴¹*Id.* at 307.

⁴²*Id.*

⁴³*Id.* at 308.

The court pointed out that the applicable Indiana decisions were not entirely clear.

There are cases which adopt the conventional definition of alimony as "an allowance out of the divorced husband's estate made the divorced wife for her support and maintenance." A second line of cases derives its authority from the decision of the Indiana Supreme Court in *Shula v. Shula*, "Alimony is awarded in Indiana for the purpose of making a present and complete settlement of the property rights of the parties." It does not include future support of wife, nor is it intended as a medium for providing financial compensation for injured sensitivities during marriage. The primary factor in fixing alimony is the existing property of parties⁴⁴

Following a somewhat detailed review of all of the pertinent Indiana case law,⁴⁵ the court concluded: "It thus appears that one proper consideration, among others, for an award of alimony in Indiana has been the relative income of the wife. An allocation to the wife on that basis is tantamount to an allowance for support."⁴⁶ In applying its conclusion to the subject settlement agreement, the court found that the labels used in the agreement were not dispositive, but the basis for the creation of the obligation determined whether the parties intended an equalization of property rights or they intended the agreement to be one for support and maintenance.⁴⁷ The court then remanded the case to the district court for further hearing relative to whether the alimony awarded under the agreement represented a further division of marital property or was based upon the income of the parties.⁴⁸

The decision established two precedents for the Seventh Circuit. First, in following the lead of other circuits,⁴⁹ the court decided that

⁴⁴*Id.* at 308-09 (citations omitted).

⁴⁵*Id.* at 307-08 (citing *McDaniel v. McDaniel*, 245 Ind. 551, 201 N.E.2d 215 (1964); *Shula v. Shula*, 235 Ind. 210, 132 N.E.2d 612 (1956); *Wellington v. Wellington*, 158 Ind. App. 649, 304 N.E.2d 347 (1974); *Doner v. Doner*, 158 Ind. App. 306, 302 N.E.2d 511 (1973); *Sidebottom v. Sidebottom*, 140 Ind. App. 657, 225 N.E.2d 772 (1967), *rev'd on other grounds*, 249 Ind. 572, 233 N.E.2d 667 (1968); *Smith v. Smith*, 131 Ind. App. 38, 169 N.E.2d 130 (1960); *Wallace v. Wallace*, 123 Ind. App. 454, 110 N.E.2d 514 (1953); *Ceiga v. Ceiga*, 114 Ind. App. 205, 51 N.E.2d 493 (1943); *Rariden v. Rariden*, 33 Ind. App. 284, 70 N.E. 398 (1904)).

⁴⁶528 F.2d at 308.

⁴⁷*Id.* at 309.

⁴⁸*Id.*

⁴⁹*In re Nunnally*, 506 F.2d 1024 (5th Cir. 1975); *In re Waller*, 494 F.2d 447 (6th Cir. 1974); *Martin v. Henley*, 452 F.2d 295 (9th Cir. 1971); *Caldwell v. Armstrong*, 342 F.2d 485 (10th Cir. 1965); *Norris v. Norris*, 324 F.2d 826 (9th Cir. 1963); *Poolman v. Poolman*,

in determining the nature of the husband's obligation, the court must refer to the divorce law of the state in which the divorce was granted to find the relevant considerations in determining the settlement.⁵⁰ Second, the court concluded that an Indiana property settlement may have elements of Bankruptcy Act "alimony" which would render such an obligation nondischargeable.⁵¹

Two subsequent decisions have cited *Nichols v. Hensler* as controlling in Indiana. In *In re Boswell*,⁵² the ex-wife had been granted an alimony judgment of \$13,100, due in \$25 weekly payments, the district court found the payments to be for the "maintenance and support"⁵³ of the ex-wife "rather than a property settlement and thus nondischargeable under Section 17a(7) of the Bankruptcy Act."⁵⁴ The court refused to certify the question of whether alimony can be construed as future support to the Indiana Supreme Court because it said that the issue was decided in *Nichols v. Hensler* and no "Indiana cases decided since *Nichols* have called into question the *Nichols* holding."⁵⁵ The decision, stamped "unpublished order not to be cited," is interesting because it provides the insight that the Seventh Circuit Court of Appeals, even after the *Nichols* decision, was not certain of the role of Indiana law in the section 17a(7) decision-making process. The court noted in its written opinion that, under some circumstances, it might be appropriate to refer the question to the state court for its interpretation.⁵⁶

In the most recent Seventh Circuit Court decision, *In re Woods*,⁵⁷ dealing with the dischargeability of alimony under section 17a(7), the court said: "The law of Indiana, determines whether Woods' assumption of the parties' debts is to be construed as dividing the marital property or as providing support"⁵⁸ Apparently, however, the court considered only Indiana law in determining the intent of the parties, rather than using the law to determine substantively whether the debt owed to the ex-wife was dischargeable in bankruptcy. In this case, the disparity between the wife's income and the husband's income at the time of the divorce was only thirty-eight dollars per week. Such a disparity was not so

289 F.2d 332 (8th Cir. 1961); *Golden v. Golden*, 411 F. Supp. 1076 (S.D.N.Y. 1976); *In re Baldwin*, 250 F. Supp. 533 (D. Neb. 1966).

⁵⁰528 F.2d at 308-09.

⁵¹*Id.*

⁵²No. 76-2118 (7th Cir. Apr. 20, 1977).

⁵³*Id.*, slip op., at 1.

⁵⁴*Id.*

⁵⁵*Id.* at 3.

⁵⁶*Id.* at 2.

⁵⁷561 F.2d 27 (7th Cir. 1977).

⁵⁸*Id.* at 29-30.

gross as to be "tantamount to an allowance for support."⁵⁹ Again the court cited *Nichols* as controlling.⁶⁰

III. INDIANA DISSOLUTION OF MARRIAGE ACT

A cursory reading of *Nichols* seems to indicate that in applying section 17a(7) the bankruptcy court is bound to apply the state's definition of the term "alimony."⁶¹ This impression was also left by a number of circuits.⁶² The *Nichols* decision and those following it have raised serious questions within the practicing bar⁶³ as to the effect of section 17a(7) when viewed against the background of Indiana's present Dissolution of Marriage Act.⁶⁴ The Act had been enacted at the time of the court's decision in *Nichols v. Hensler*, but was not applicable.⁶⁵

The statute provides:

In an action pursuant to section 3(a) [subsection (a) of section 31-1-11.5-3], the court shall divide the property of the parties, whether owned by either spouse prior to the marriage, acquired by either spouse in his or her own right after the marriage and prior to final separation of the parties, or acquired by their joint efforts, in a just and reasonable manner, either by division of the property in kind, or by setting the same or parts thereof over to one [1] of the spouses and requiring either to pay such sum as may be just and proper, or by ordering the sale of the same under conditions as the court may prescribe and dividing the proceeds of such sale.

In determining what is just and reasonable the court shall consider the following factors:

⁵⁹*Id.* at 30.

⁶⁰*Id.*

⁶¹See 528 F.2d at 307. The court spends considerable time reviewing the definition of alimony and property settlement as derived from Indiana case law. In reaching its conclusion, however, the court does not appear to have applied Indiana law.

⁶²*In re Nunnally*, 506 F.2d 1024 (5th Cir. 1975); *In re Waller*, 494 F.2d 447 (6th Cir. 1974); *Martin v. Henley*, 452 F.2d 295 (9th Cir. 1971); *Caldwell v. Armstrong*, 342 F.2d 485 (10th Cir. 1965); *Norris v. Norris*, 324 F.2d 826 (9th Cir. 1963); *Poolman v. Poolman*, 289 F.2d 332 (8th Cir. 1961); *Golden v. Golden*, 411 F. Supp. 1076 (S.D.N.Y. 1976); *In re Baldwin*, 250 F. Supp. 533 (D. Neb. 1966).

⁶³During the most recent bankruptcy law seminars (1976-77) conducted by the Indiana Continuing Legal Education Forum in the Indiana cities of Bloomington, Indianapolis, Marion, Gary, Fort Wayne, New Albany and Evansville, the issue was repeatedly raised. Interviews with Edward Hopper, partner in the law firm of Hopper & Opperman; David Kleiman, partner in the law firm of Dann Pecar Newman Talesnick & Kleiman; and Steven Ancel, partner in the law firm of Ancel Friedlander Miroff & Ancel, in Indianapolis (June 15, 1977).

⁶⁴IND. CODE §§ 31-1-11.5-1 to 24 (1976).

⁶⁵See 528 F.2d at 307.

(a) the contribution of each spouse to the acquisition of the property, including the contribution of a spouse as homemaker;

(b) the extent to which the property was acquired by each spouse prior to the marriage or through inheritance or gift;

(c) the economic circumstances of the spouse at the time the disposition of the property is to become effective, including the desirability of awarding the family residence or the right to dwell therein for such periods as the court may deem just to the spouse having custody of any children;

(d) the conduct of the parties during the marriage as related to the disposition or dissipation of their property;

(e) *the earnings or earning ability of the parties as related to a final division of property and final determination of the property rights of the parties.*⁶⁶

In addition the Act states:

*The court may make no provision for maintenance except that when the court finds a spouse to be physically or mentally incapacitated to the extent that the ability of such incapacitated spouse to support himself or herself is materially affected, the court may make provision for the maintenance of said spouse during any such incapacity, subject to further order of the court.*⁶⁷

In the next section, however, the statute provides:

To promote the amicable settlement of disputes that have arisen or may arise between the parties to a marriage attendant upon dissolution of their marriage, *the parties may agree in writing to the provisions for the maintenance of either of them, the disposition of any property owned by either or both of them and the custody and support of their children.*⁶⁸

The concern advanced is that, given the express prohibition by the legislature with respect to an award of maintenance unless there is a written agreement or incapacitation and the subsequent narrow interpretation given the law by the only appellate court decision under the Indiana Dissolution of Marriage Act, it is possible that an Indiana divorced spouse may never again find protection from a bankruptcy discharge under section 17a(7) of the Bankruptcy Act

⁶⁶IND. CODE § 31-1-11.5-11 (1976) (emphasis added).

⁶⁷*Id.* § 31-1-11.5-9(c) (emphasis added).

⁶⁸*Id.* § 31-1-11.5-10(a) (emphasis added).

because alimony may not be granted to a divorced spouse in Indiana. Certainly it would be unfair to impose such a penalty upon Indiana residents while citizens of the other forty-nine states labor under no such disability.

IV. THE EFFECT OF INDIANA CASE LAW UNDER THE DISSOLUTION OF MARRIAGE ACT IN INTERPRETING SECTION 17a(7)

One of the few cases decided under the Dissolution of Marriage Act is *Wilcox v. Wilcox*.⁶⁹ In that case, the parties were married in 1949 during their final year as college students. While both parties had graduated, only the husband had continued his education, receiving his Doctor of Philosophy degree in 1952. The wife had worked to support the husband during that time so that he could continue his education. The wife had not been employed outside the home after the husband had received his doctorate. During that period, she had raised their three children. All the offspring had been emancipated at the time of the divorce. Dr. Wilcox was a tenured professor at Purdue University where he had been continuously employed since receiving his advanced degree.

The parties were unable to agree to a property settlement before trial and, after a hearing, the court awarded the entire marital assets of \$42,000 to the wife. The wife appealed the decision alleging that the court abused its discretion in not taking into consideration the husband's discounted future income as a marital asset to be divided as part of the property settlement. The husband cross-appealed alleging error in the distribution of the total marital assets to the wife.

In affirming the lower court's decision, the Indiana Court of Appeals, stated:

When determining what is to be divided there is nothing in the statute which lends itself to the interpretation that future income is "property" and therefore divisible. It appears that a vested present interest must exist for the item to come within the ambit of "marital assets." We cannot say that Gerald has a vested present interest in his future earnings and the legislature cannot be said to have considered it as such.⁷⁰

The opinion further stated:

To allow the discounting of a future stream of income to be called "property" runs contra to the statutory provisions

⁶⁹365 N.E.2d 792 (Ind. Ct. App. 1977).

⁷⁰*Id.* at 795.

forbidding maintenance without a showing of incapacitation. *Regardless of the label attached to an award above the value of the marital assets, its true nature would shine through as maintenance. Therefore, absent a showing of incapacitation by Gloria, she may not receive maintenance, regardless of the label she attempts to attach to the requested award.*⁷¹

V. FEDERAL QUESTION

It appears, however, that the concern of the practicing bar over the direction of Indiana law as related to section 17a(7) is unfounded. The specific circumstances which will be controlling in determining the applicability of section 17a(7) is a federal question to be established substantively by the federal courts. Federal bankruptcy legislation was enacted because of the growing dissatisfaction with the hodgepodge of insolvency laws emerging in the states and the resulting desire for national uniformity in bankruptcy relief and administration.⁷² At the Senate debate on the adoption of the 1938 revision of the Bankruptcy Act, Senator Joseph O'Mahoney stated:

[I]t is interesting to recall the striking fact that when the Constitution of the United States was adopted one of the powers granted the Central Federal Government was the power to pass a uniform national bankruptcy act. I suppose nothing is more local or individual than a person's debts; yet the framers of the Constitution, in presenting that instrument to the people of the United States, decreed that the Central Government should have complete control of bankruptcy.⁷³

The controlling principle that any state legislation which frustrates the full effectiveness of a federal law is rendered invalid by the supremacy clause of the Constitution⁷⁴ is well established.⁷⁵ The doctrine of *Erie R.R. v. Tompkins*⁷⁶ requires the application of state substantive law only in cases where federal court jurisdiction is based upon diversity of citizenship.⁷⁷ Federal law alone is applied

⁷¹*Id.* (citations omitted) (emphasis added).

⁷²Shimm, *Impact of State Law on Bankruptcy*, 1971 DUKE L.J. 879.

⁷³83 CONG. REC. 8679 (1938).

⁷⁴U.S. CONST. art. VI, cl. 2.

⁷⁵*Perez v. Campbell*, 402 U.S. 637 (1971).

⁷⁶304 U.S. 64 (1938).

⁷⁷In matters coming before the federal court under the concepts of ancillary or pendent jurisdiction, the court also applies substantive state law. See *Hurn v. Oursler*, 289 U.S. 238 (1933); *Moore v. New York Cotton Exch.*, 270 U.S. 593 (1926).

to any issue arising in areas where federal power is "exclusive." Bankruptcy is recognized as such an area.⁷⁸ In these areas there is federal common law.⁷⁹ Clearly, with respect to the Bankruptcy Act, the courts do not have to look to state law to determine a state definition of alimony, any more than the courts have been obligated to adopt the state definition of insolvency.⁸⁰ As was noted by the Second Circuit Court of Appeals in *Fore Improvement Corp. v. Selig*,⁸¹ "Congress is not required to direct the federal courts to look to state law for the definition of state-created rights asserted in bankruptcy, as it is when federal jurisdiction rests solely on diversity of citizenship."⁸²

That the federal courts are free to establish the standards for the application of section 17a(7) without reference to state law is also reinforced by the fact that Congress has not expressly directed the application of state law in this section as it specifically has done with respect to issues of exemptions,⁸³ claims for taxes,⁸⁴ and claims for rents⁸⁵ under the Bankruptcy Act.

The federal judiciary has availed itself of the power to establish standards and policy relative to the application of section 17a(7). The courts have established that "alimony" as used in section 17a(7) means payment in the nature of support for a former spouse.⁸⁶ They have also established as a matter of federal precedent that, if the debt is determined to be one arising under a property settlement, it is discharged in bankruptcy.⁸⁷ Moreover, the federal courts need not be bound by labels attached by the parties in their settlement

⁷⁸*Perez v. Campbell*, 402 U.S. 637 (1971).

⁷⁹Federal common law is predicated upon the United States Constitution, federal statutes, treaties, and administrative regulations. See *Unarco Indus., Inc. v. Kelley Co.*, 465 F.2d 1303 (7th Cir. 1972) cert. denied, 410 U.S. 929 (1973); *Ivy Broadcasting Co. v. American Tel. & Tel. Co.*, 391 F.2d 486 (2d Cir. 1968).

⁸⁰The Bankruptcy Act defines insolvency as liabilities in excess of assets. 11 U.S.C. § 1(19) (1976). Indiana defines insolvency as the inability of a person to pay his debts as they fall due. *Royal Academy of Beauty Culture v. Wallace*, 226 Ind. 383, 78 N.E.2d 32 (1948).

⁸¹278 F.2d 143 (2d Cir. 1960).

⁸²*Id.* at 147 (Friendly, J., concurring).

⁸³11 U.S.C. § 24 (1976).

⁸⁴*Id.* § 104.

⁸⁵*Id.*

⁸⁶See *Nichols v. Hensler*, 528 F.2d 304, 307 (7th Cir. 1976); *Norris v. Norris*, 324 F.2d 826, 828 (9th Cir. 1963); *Goggans v. Osborn*, 237 F.2d 186, 188 (9th Cir. 1956); *In re Baldwin*, 250 F. Supp. 533, 534 (D. Neb. 1966); 1A COLLIER ON BANKRUPTCY ¶ 17.23, at 1678 (14th ed. 1977 rev.); 3A COLLIER ON BANKRUPTCY ¶ 63.13, at 1839 (14th ed. 1977 rev.). See also *Wetmore v. Markoe*, 196 U.S. 68 (1904).

⁸⁷*Nichols v. Hensler*, 528 F.2d 304, 307 (7th Cir. 1976); *Caldwell v. Armstrong*, 342 F.2d 485, 488 (10th Cir. 1965); *Goggans v. Osborn*, 237 F.2d 186, 189 (9th Cir. 1956). See also *Edmondson v. Edmondson*, 242 S.W.2d 730, 736 (Mo. App. 1951).

agreements, by the state courts in their decrees or by the state legislatures in their statutes.⁸⁸ The Sixth Circuit Court of Appeals has stated: "There is no peculiar sanctity surrounding the words 'property settlement.' Bankruptcy courts sit in equity . . . and have [the] power 'to sift the circumstances surrounding any claim to see that injustice or unfairness is not done in administration of the bankrupt estate.'"⁸⁹

Although the matter is manifestly a federal question and workable federal standards have evolved against which to analyze section 17a(7) problems, the federal courts' approach to alimony has been confused and unclear. There is evidence of a reluctance to recognize the issue as a federal question and to apply federal common law. For example, the court in *In re Waller*⁹⁰ was forced to determine whether certain provisions of a divorce decree constituted dischargeable alimony. In concluding that "[t]he law of Ohio must be resorted to in order to determine what constitutes alimony, maintenance or support . . .,"⁹¹ the court relied upon *Desjardins v. Desjardins*⁹² as the controlling authority. However, *Desjardins* simply restated the proposition that, pursuant to the *Erie* doctrine, state law must be followed in diversity actions.⁹³ In fact, *Desjardins* was a diversity action wherein the court was called upon to interpret an Ohio divorce decree.

The *Waller* court, after reviewing Ohio divorce law and its uncertainty found that, in any event, a bankruptcy court is not bound by state law because it is a court of equity.⁹⁴ The court then applied the definitions established by the federal courts for alimony, support, maintenance, and property settlement under section 17a(7) to the problem before it.⁹⁵

In addition to believing that they are bound by the *Erie* doctrine, some of the federal courts' reluctance to simply treat the matter as a federal question appears to have its source in the opinion of some courts that their inquiry into the character of the alimony awarded by the state court amounts to a collateral attack on the state court judgment. The bench, in *In re Nunnally*⁹⁶ commented in a revealing footnote to its opinion:

⁸⁸*Nichols v. Hensler*, 528 F.2d 304 (7th Cir. 1976); *In re Waller*, 494 F.2d 447 (6th Cir. 1974).

⁸⁹*Avery v. Avery*, 114 F.2d 768, 770 (6th Cir. 1940) (citations omitted).

⁹⁰494 F.2d 447 (6th Cir. 1974).

⁹¹*Id.* at 448.

⁹²308 F.2d 111 (6th Cir. 1962).

⁹³*See id.* at 111, 116.

⁹⁴494 F.2d at 450.

⁹⁵*Id.* at 451.

⁹⁶506 F.2d 1024 (5th Cir. 1975).

Bankrupt contends that we cannot find the \$41,779.41 an award for support since it would then be void under Texas law as permanent alimony. . . . Although it is doubtful that this is a proper forum for bankrupt to attack the divorce decree collaterally, bankrupt's argument founders on Texas case law. . . . However, Texas courts are not quick to find that permanent alimony has been ordered, and we are Erie-bound to follow in their tracks.⁹⁷

In *Waller*, the court in dicta asserted that the bankruptcy judge "did not rule on the question of whether the bankrupt's obligation to the former wife was discharged because she was not listed as a creditor"⁹⁸ and had no knowledge of the proceeding. The court then commented that had the "[c]ourt ruled on this issue, *which is peculiarly a federal question*, there may have been no necessity for it to decide what constitutes alimony, maintenance and support under Ohio law, which is a question more properly to be decided by Ohio Courts."⁹⁹

Even the Seventh Circuit, in its unpublished opinion in *Boswell*¹⁰⁰ noted that there might be circumstances in a section 17a(7) determination where it would be proper to certify the question of interpretation of alimony questions to the Indiana Supreme Court for its determination.¹⁰¹

VI. THE 1970 DISCHARGEABILITY ACT

In large measure, the lack of clarity and consistency in the federal courts' application of section 17a(7) may be a result of the procedure for contesting the dischargeability of an indebtedness which was obligatory prior to the 1970 amendments to the Bankruptcy Act.¹⁰² Prior to the amendments, the general view was that the bankruptcy court only determined the right to a discharge, but did not determine the effect.¹⁰³ The question of dischargeability was properly adjudicated in a non-bankruptcy forum when the creditor sued to enforce his claim and the bankrupt plead his

⁹⁷*Id.* at 1027 n.6.

⁹⁸494 F.2d at 451.

⁹⁹*Id.* (emphasis added); See Lee, *Case Comment*, 50 AM. BANKR. L.J. 175, 176 (1976) wherein the commentator noted that the court should have decided the alimony issue as a federal question in *In re Waller*.

¹⁰⁰No. 76-2118 (7th Cir. Apr. 20, 1977).

¹⁰¹*Id.*, slip op., at 3.

¹⁰²Pub. L. No. 91-467, 84 Stat. 990, amending §§ 2a(12), 14, 15, 17, 38 & 58 of the Bankruptcy Act.

¹⁰³1A COLLIER ON BANKRUPTCY ¶ 17.28, at 1726 (14th ed. 1977 rev.).

discharge as an affirmative defense.¹⁰⁴ As a result, the issues raised by section 17a(7) were most often determined in state courts.¹⁰⁵ While the state courts were bound to follow the decisions of the United States Supreme Court because the question was a federal one,¹⁰⁶ those courts tended to emphasize the effect of the law of the situs rather than the controlling federal viewpoint. Where the issues had been raised in the federal courts, the judiciary tended to follow the lead of their local brethren. However, in 1970, Congress amended the Bankruptcy Act and gave the federal courts general jurisdiction to determine the dischargeability of each section 17a(7) debt as well as to determine the right to a general discharge.¹⁰⁷ As a result, the courts should no longer feel constrained by the state court approach.

VII. CONCLUSION

Given that the matter involves a federal question and that there is a sufficient body of federal court precedent to be relied upon, the new Indiana Dissolution of Marriage Act and subsequent court decisions thereunder should have no direct effect upon the future application of the *Nichols v. Hensler* precedent that, if the wife's income is considered in arriving at a settlement figure, it is tantamount to support and will not be dischargeable. It is clear that the facts of each particular case will control, not the then-current status of state law, either legislative or judicially-created. State law is referred to in *Nichols* solely for the purpose of understanding the actions and agreements of the parties and the decisions of the divorce court in determining whether elements of maintenance and support could be deduced from the agreement or the decree in controversy. Whether the state courts interpret Indiana divorce law liberally or strictly, the approach taken by the Seventh Circuit allows the bankruptcy court to balance the fresh start concept of the Bankruptcy Act with the need to protect family obligations consistent with the national goals established by Congress so that general uniformity in the application of section 17a(7) can prevail throughout the country.

SORELLE J. ANCEL

¹⁰⁴Watts v. Ellithorpe, 135 F.2d 1 (1st Cir. 1943); Otto v. Cooks, Inc., 113 F. Supp. 861 (D. Minn. 1953); *In re Scandiffio*, 63 F. Supp. 264 (E.D.N.Y. 1945); Pass v. Webster, 85 Ohio App. 403, 83 N.E.2d 116 (1948); 1A COLLIER ON BANKRUPTCY ¶ 17.28, at 1727 (14th ed. 1977 rev.).

¹⁰⁵Watts v. Ellithorpe, 135 F.2d 1 (1st Cir. 1943); Otto v. Cooks, Inc., 113 F. Supp. 861 (D. Minn. 1953); *In re Scandiffio*, 63 F. Supp. 264 (E.D.N.Y. 1945); Pass v. Webster, 85 Ohio App. 403, 83 N.E.2d 116 (1948); 1A COLLIER ON BANKRUPTCY ¶ 17.28, at 1727 (14th ed. 1977 rev.).

¹⁰⁶*In re Lowe*, 36 F. Supp. 772 (W.D. Ky. 1941).

¹⁰⁷11 U.S.C. § 35(c) (1976).

