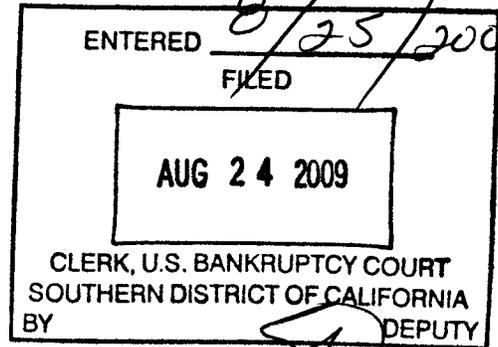


1 WRITTEN DECISION - FOR PUBLICATION



8 UNITED STATES BANKRUPTCY COURT
9 SOUTHERN DISTRICT OF CALIFORNIA

10
11 In re) Case No. 06-03013-LT13
12 TICH HUA, fdba DTD PRECISION) ORDER AFTER EVIDENTIARY
13 AUTO REPAIR,) HEARING ON UNITED STATES
14 Debtor.) TRUSTEE'S OBJECTIONS TO
15) CONFIRMATION OF CHAPTER 13
16) PLAN

17 This case has a lengthy history. It was originally filed
18 as a Chapter 7 petition on October 6, 2006. The real estate
19 lender quickly filed a motion for relief from stay, which was not
20 opposed, and relief was granted. Subsequently, the debtor
21 stipulated to extending the time within which the United States
22 Trustee could file a complaint objecting to discharge.

23 On April 12, 2007 the United States Trustee filed a
24 complaint seeking denial of a discharge pursuant to 11 U.S.C.
25 § 727(a)(3), (a)(4) and/or (a)(5). At the center of the complaint
26 are the facts that debtor refinanced his real property in
December, 2005 netting almost \$67,000; and that debtor purchased

1 fourteen or more items of jewelry at a cost of over \$23,000 in
2 the first four months of 2006, which he promptly resold. The
3 United States Trustee's complaint alleges that debtor is unable
4 to produce books and records to explain what happened to either
5 the proceeds or the jewelry except for generally unsupported
6 claims that the proceeds were dissipated through his and his
7 wife's gambling. A collateral allegation was that debtor made
8 a false oath when signing his Schedules because he omitted any
9 mention of the purchase or sale of the jewelry. Although not
10 tied to any of the § 727 causes of action, the United States
11 Trustee also alleged that debtor provided false income
12 information to credit card companies and to the real estate
13 lender as part of the debtor's applications.

14 Debtor filed his answer to the complaint, and the case
15 proceeded. Approximately six months after the complaint was
16 filed, the debtor converted the Chapter 7 case to one under
17 Chapter 13. Both the Chapter 13 Trustee and the United States
18 Trustee objected to confirmation of the debtor's Chapter 13 plan.
19 The United States Trustee's objection recited:

20 The Debtor converted this case to
21 chapter 13 after the UST filed a complaint
22 objecting to his discharge. The allegations
23 in the complaint show evidence of the
24 Debtor's bad faith in filing his bankruptcy
25 case including, but not limited to,
26 overstatements of income in credit
applications, misstatements regarding the
debtor's employment, the misuse of credit
cards and the consultation of a bankruptcy
attorney within six months of running up
credit cards. Based on the Debtor's bad
faith in filing the case, the plan should not

1 be confirmed pursuant to 11 U.S.C.
2 § 1325(a)(3) and (a)(7).

3 The United States Trustee also challenged the plan's feasibility.

4 The United States Trustee's objection to confirmation came
5 on for evidentiary hearing and, after taking evidence, post-
6 hearing briefs were submitted and the matter was thereafter taken
7 under submission. The Court has subject matter jurisdiction over
8 the proceeding pursuant to 28 U.S.C. § 1334 and General Order
9 No. 312-D of the United States District Court for the Southern
10 District of California. This is a core proceeding under
11 28 U.S.C. § 157(b)(2)(L).

12 In support of her objection to confirmation the United
13 States Trustee repeats the oft-quoted statement to the effect
14 that: "the principal purpose of the Bankruptcy Code is to grant
15 a 'fresh start' to the honest but unfortunate debtor.'" Marrama
16 v. Citizens Bank of Massachusetts, 549 U.S. 365, 367 (2007).

17 Marrama goes further and says:

18 An issue that has arisen with disturbing
19 frequency is whether a debtor who acts in bad
20 faith prior to, or in the course of, filing a
21 Chapter 13 petition by, for example,
 fraudulently concealing significant assets,
 thereby forfeits his right to obtain Chapter
 13 relief.

22 Id. Marrama has to be understood in its factual context, which
23 involved concealment of an asset in the pending Chapter 7 case.
24 When the trustee discovered and pursued the asset, the debtor
25 sought to convert the case to Chapter 13. So while the debtor's
26 bad faith conduct was committed prior to conversion, it was

1 committed in conjunction with the filing of his chapter 7
2 petition and thereafter.

3 The point is simply illustrated. If the Congress had
4 intended to make debtors ineligible for any bankruptcy protection
5 or relief if they committed wrongful conduct before filing any
6 bankruptcy petition, they could easily have said so in 11 U.S.C.
7 § 109. But Congress did not. To the contrary, Congress provided
8 that debts that arose prepetition because of wrongful conduct
9 might be individually nondischargeable pursuant to 11 U.S.C.
10 § 523(a), but the facts involved in how those debts arose are
11 relevant to their individual dischargeability, but not to a
12 debtor's eligibility to be a debtor under Title 11 of the
13 United States Code.

14 To accentuate the point, 11 U.S.C. § 523(a) provides in
15 part:

16 (a) A discharge under section 727, 1141,
17 1228(a), 1228(b), or 1328(b) of this title
18 does not discharge an individual debtor from
19 any debt -

20 (4) for fraud or defalcation while
21 acting in a fiduciary capacity,
22 embezzlement, or larceny; . . .

22 If Congress intended to preclude from bankruptcy eligibility
23 persons who committed dishonest acts such as embezzlement
24 or larceny, as examples, they could have said so easily.
25 Instead, they structured a system that provided for the
26 nondischargeability of those sorts of debts while discharging

1 the rest. That enhanced the possibility that nondischargeable
2 debts would receive some payment eventually because there were
3 fewer debts competing for the debtor's post-discharge resources.
4 To turn the process around and judicially create an exception
5 denying debtors access to bankruptcy protection generally for
6 committing the sorts of dishonest acts Congress has provided for
7 in § 523(a) as individual nondischargeable debts turns Congress'
8 carefully structured design on its head.

9 To be sure, the phrase "honest but unfortunate debtor" has
10 a long and ill-defined history. In Williams v. United States
11 Fidelity & Guaranty Co., 236 U.S. 549, 554-55 (1915), the Supreme
12 Court wrote:

13 It is the purpose of the bankrupt act to
14 convert the assets of the bankrupt into cash
15 for distribution among creditors, and then to
16 relieve the honest debtor from the weight of
17 oppressive indebtedness, and permit him to
18 start afresh free from the obligations and
19 responsibilities consequent upon business
20 misfortunes.

21 In Local Loan Co. V. Hunt, 292 U.S. 234, 244 (1935), the court
22 repeated:

23 One of the primary purposes of the
24 Bankruptcy Act is to 'relieve the honest
25 debtor from the weight of oppressive
26 indebtedness, and permit him to start afresh
free from the obligations and
responsibilities consequent upon business
misfortunes.'

The Court then added:

This purpose of the act has been again and
again emphasized by the courts as being of
public as well as private interest, in that

1 it gives to the honest but unfortunate debtor
2 who surrenders for distribution the property
3 which he owns at the time of bankruptcy, a
4 new opportunity in life and a clear field for
5 future effort, unhampered by the pressure and
6 discouragement of pre-existing debt.

7 Id.

8 It is important to recognize that the shape, scope and
9 objectives of America's bankruptcy law have changed over the
10 intervening years, as the Supreme Court recognized in Grogan v.
11 Garner, 498 U.S. 279, 286-87 (1991). There, the court observed
12 in addressing the burden of proof for nondischargeability
13 proceedings:

14 This Court has certainly acknowledged that a
15 central purpose of the Code is to provide a
16 procedure by which certain insolvent debtors
17 can reorder their affairs, make peace with
18 their creditors, and enjoy "a new opportunity
19 in life with a clear field for future effort,
20 unhampered by the pressure and discouragement
21 of preexisting debt. "[Citation omitted.] but
22 in the same breath that we have invoked this
23 "fresh start" policy, we have been careful to
24 explain that the Act limits the opportunity
25 for a completely unencumbered new beginning
26 to the "honest but unfortunate debtor." Ibid.

The statutory provisions governing
nondischargeability reflected a congressional
decision to exclude from the general policy
of discharge certain categories of debts -
such as child support, alimony, and certain
unpaid educational loans and taxes, as well
as liabilities for fraud. Congress evidently
concluded that the creditors' interest in
recovering full payment of debts in these
categories outweighed the debtors' interest
in a complete fresh start.

Exemplifying the point is the decision of the Third Circuit
Court of Appeals in In re Lilley, 91 F.3d 491 (1996). There, the

1 debtor had been convicted of willful failure to file federal tax
2 returns, and had run up a large tax debt. He filed a Chapter 7
3 petition, during which the bankruptcy Court determined the tax
4 debt was nondischargeable. Then Congress increased the debt
5 ceiling for chapter 13 and debtor filed under that chapter. The
6 IRS filed a motion to dismiss based on the debtor's prepetition
7 conduct which, on appeal, the district court granted. The Third
8 Circuit reversed, noting that while the debt was nondischargeable
9 in Chapter 7, it was dischargeable in Chapter 13. The court
10 concluded:

11 It is therefore wholly implausible that
12 Congress would hold that the type of conduct
13 in which Mr. Lilley admittedly engaged is so
14 egregious as to warrant dismissal of his
15 petition, but benign enough that the debt
16 incurred as a result of this conduct would be
17 dischargeable if no effort to dismiss his
18 petition were made.

19 91 F.3d at 496. The Third Circuit remanded for a good faith
20 totality of the circumstances analysis.

21 The case of Handeen v. Le Maire, 898 F.2d 1346 (8th Cir.
22 1990), although decided before Lilley, takes the analysis one
23 step further. LeMaire was convicted of aggravated assault
24 involving a shooting. A civil judgment followed, then the debtor
25 filed under Chapter 13. The court rejected Handeen's argument
26 that debtor's prepetition criminal conduct made the subsequent
civil judgment nondischargeable in Chapter 13, just as it would
be in Chapter 7. The court instead focused on the issue of
debtor's good faith and set out a multi-factor list of items

1 which it had applied in earlier cases. The court recognized,
2 however, that many of those factors had been subsumed in
3 11 U.S.C. § 1325(b), and said that what remained of the factors
4 was:

5 "[w]hether the debtor has stated his debts
6 and expenses accurately; whether he has made
7 any fraudulent misrepresentation to mislead
8 the bankruptcy court; or whether he has
9 unfairly manipulated the Bankruptcy Code."

8 898 F.2d at 1349. The court continued:

9 Thus, in considering whether LeMaire proposed
10 his plan in good faith, factors such as the
11 type of debt sought to be discharged and
12 whether the debt is nondischargeable in
13 Chapter 7, and the debtor's motivation and
14 sincerity in seeking chapter 13 relief are
15 particularly relevant.

13 Id. Interestingly, a majority of the appellate court judges was
14 appalled at the thought that a debtor might discharge such a debt
15 through Chapter 13, even though it recognized that Congress had
16 provided what some call a "superdischarge" as added incentive to
17 use Chapter 13 over Chapter 7.

18 The Fifth Circuit took a different view in In re Chaffin,
19 836 F.2d 215, 216 (1988). There, the court stated:

20 We adhere to our holding that the fact that
21 Chaffin is invoking chapter 13 to obtain
22 discharge of a debt previously held non-
23 dischargeable in Chapter 7 because it was
24 incurred through fraud cannot, as a matter of
25 law, suffice to show bad faith.

24 To the extent courts were previously correct in concluding,
25 as some did, that resort to Chapter 13 to discharge a debt that
26 was or would be nondischargeable in Chapter 7 was somehow an

1 unfair manipulation of the Bankruptcy Code, notwithstanding
2 Congress' intent in designing the carrot of the super-discharge,
3 Congress largely eliminated the super-discharge in 2005, revising
4 11 U.S.C. § 1328 to provide that any debt "of the kind specified
5 . . . in paragraph (1)(B), (1)(C), (2), (3), (4), (5), (8), or
6 (9) of section 523(a)" would not be discharged in Chapter 13.
7 Nor would a debt "(4) for restitution, or damages, awarded in a
8 civil action against the debtor as a result of willful or
9 malicious injury by the debtor that caused personal injury to an
10 individual or the death of an individual."

11 To the extent the United States Trustee's objection to
12 confirmation is predicated on this debtor's prepetition behavior
13 that gave rise to the specific debts that he now seeks to address
14 by way of his Chapter 13 plan, the Court finds and concludes that
15 such an argument is not supportable, and is hereby rejected.

16 Moreover, the court notes in passing that although afforded
17 a full window of opportunity while the case was pending in
18 Chapter 7, no creditor filed an adversary claiming the debt owed
19 to it was nondischargeable. The result is that the debts the
20 United States Trustee asserts arose from debtor's prepetition
21 conduct were all dischargeable in the Chapter 7 proceeding long
22 before debtor's conversion of the case to Chapter 13. Indeed,
23 in Chapter 13 debtor proposes to pay a dividend to creditors that
24 would have received nothing in Chapter 7.

25 All of the foregoing said, it still remains for the Court to
26 assess debtor's claims of good faith both in filing the present

1 petition under Chapter 13, as required by 11 U.S.C. § 1325(a)(7),
2 and in proposing his Chapter 13 plan, as required by 11 U.S.C.
3 § 1325(a)(3). In the Objection to Confirmation filed by the
4 United States Trustee, that office argued debtor's bad faith
5 in terms of pre-BAPCPA Chapter 7 cases. However, the office
6 provided no persuasive authority for the notion that
7 § 1325(a)(7)'s good faith requirement should be measured by
8 Chapter 7 analysis, much less that Congress intended such an
9 approach. And even then, the conduct attributed to debtor as
10 evidencing his bad faith was his conduct prior to filing his
11 initial petition under Chapter 7. That is in distinct contrast
12 with Marrama v. Citizens Bank of Massachusetts, 549 U.S. 365
13 (2007), where the debtor's conduct was post-filing in concealing
14 a significant asset and then trying to convert to Chapter 13
15 to keep the asset after the trustee started to pursue it for
16 creditors.

17 In looking at good faith filing under § 1325(a)(7), In re
18 Hieter, 2009 WL 692301 (Bankr. D. ID 2009), is helpful. There,
19 the court recognized:

20 Because BAPCPA effectively codified the
21 good faith filing requirement previously
22 employed in the case law, that case law is
applicable to any analysis of § 1325(a)(7).

23 Subsection (a)(7) was added to § 1325 by BAPCPA in 2005. After
24 reviewing prior authorities, the court advised:

25 In making a determination of good faith,
26 this Court should consider:

1 1) whether the debtor has misrepresented
2 facts in his or her petition or plan,
3 unfairly manipulated the Bankruptcy
4 Code, or otherwise filed the Chapter 13
5 petition or plan in our inequitable
6 manner.

7 2) the debtor's history of filings and
8 dismissals;

9 3) whether the debtor's only purpose in
10 filing for Chapter 13 protection is to
11 defeat state court litigation; and

12 4) whether egregious behavior is
13 present.

14 Ho v. Dowell (In re Ho), 274 B.R. 867, 876
15 (9th Cir. BAP 2002). The Ninth Circuit has
16 stated that a good faith test "should examine
17 the intentions of the debtor and the legal
18 effect of the confirmation of a Chapter 13
19 plan in light of the spirit and purposes of
20 Chapter 13." [Citations omitted.]

21 In this case, almost all the United States Trustee's objections
22 concern debtor's conduct prior to filing the original Chapter 7
23 petition, and those objections have largely been addressed.
24 Debtor is not attempting to avoid or defeat state court
25 litigation, nor is he trying to evade nondischargeability
26 litigation in the Chapter 7. Moreover, if allowed to proceed and
ultimately receive a discharge, that discharge will not reach any
wider than a discharge in Chapter 7 would have - there would be
no super-discharge, and the debtor will have had to fully perform
his proposed plan over five years to receive the discharge,
paying monies he would not have had to pay in Chapter 7.

The United States Trustee argues that if allowed to proceed
in Chapter 13 debtor will avoid the consequences of a possible

1 adverse ruling in their objection to discharge adversary in the
2 Chapter 7. And it is certainly possible that the United States
3 Trustee might have prevailed in that proceeding had it gone
4 forward. The issue thus boils down to whether seeking to avoid
5 § 727 litigation by converting to Chapter 13 and proposing to pay
6 all disposable income for five years--assuming that was debtor's
7 intent--is somehow bad faith on debtor's part. Even when a
8 debtor was seeking to discharge a debt previously held
9 nondischargeable, courts have concluded that is not enough to
10 definitively establish bad faith. In re Chaffin, 836 F.2d 215,
11 216 (5th Cir. 1988). There, the court remanded and instructed
12 the lower court to assess whether debtor had proposed to commit
13 all projected disposable income for three years to funding the
14 plan. In addition, the court noted that while the creditor had
15 obtained the nondischargeability judgment in Chapter 7, the
16 creditor had not objected to the Chapter 13 plan. The appellate
17 court stated: "The liberal policy of Chapter 13, affording a
18 clean start even to a debtor with a tainted past, likewise
19 requires a clear justification for denying confirmation of a plan
20 to which no creditor has objected." 836 F.2d at 216-17.

21 Based on all the circumstances of this case, the Court finds
22 and concludes that debtor has carried his burden of establishing
23 that his conversion from Chapter 7 to Chapter 13 was made in good
24 faith as required by 11 U.S.C. § 1325(a)(7).

25 As already noted, 11 U.S.C. § 1325(a)(3) requires that
26 debtor's plan have been "proposed in good faith and not by any

1 means forbidden by law." In earlier years, courts developed non-
2 exhaustive lists of factors to be considered. See, e.g., Handeen
3 v. LeMaire, 898 F.2d 1346, 1349 (8th Cir. 1990). As explained in
4 that opinion, Congress amended § 1325 to add subpart (b),
5 requiring a debtor to apply all projected disposable income for a
6 period of three years. That incorporated many of the "ability to
7 pay" factors in the earlier tests. 898 F.2d at 1349. Section
8 1325(b) was again amended as part of BAPCPA, and courts continue
9 to wrestle with its interplay with § 1325(a)(3).

10 In In re Stitt, 403 B.R. 694 (Bankr. D. ID 2008), the court
11 recognized the foregoing debate, and adopted what it called an
12 "intermediate approach":

13 Under this approach, "the sufficiency of the
14 assets devoted to the plan is not a basis for
15 a finding of lack of good faith under §
16 1325(a)(3), unless there is a showing of some
sort of manipulation, subterfuge or unfair
exploitation of the Code by the debtor.
[Citations omitted.]

17 403 B.R. at 703. The essence of those grounds for a finding of
18 bad faith have already been discussed. The Court finds and
19 concludes that the record in this case does not reveal any sort
20 of manipulation, subterfuge, or unfair exploitation of the Code.
21 Accordingly, the Court finds and concludes that debtor has met
22 his burden of demonstrating that his plan has been proposed in
23 good faith, as required by § 1325(a)(3).

24 The remaining objection of the United States Trustee is to
25 the feasibility of debtor's plan. Shortly after converting to
26 Chapter 13, on November 7, 2007 debtor filed his amended

1 schedules, including Schedules I and J. Schedule I showed that
2 debtor had been employed for one month at an auto repair shop,
3 and his non-filing spouse had been employed as a manicurist for
4 the preceding three months. Their joint net income, before
5 expenses, was \$3,220. The joint family expenses are listed on
6 Schedule J as \$2,970, leaving a net income after expenses of
7 \$250 per month for the family.

8 The United States Trustee acknowledged at the evidentiary
9 hearing that the feasibility objection was secondary to the good
10 faith arguments. However, it was pointed out that debtor's non-
11 filing spouse testified that she had monthly expenses for her
12 separate credit cards which were not included on Schedule J.
13 The net effect of that information is that the family net income
14 would be reduced below the level necessary to make the monthly
15 plan payments to the Chapter 13 trustee, and thus rendered the
16 proposed plan infeasible.

17 Feasibility is a very real concern. Countering it to some
18 degree is the United States Trustee's stipulation at the hearing
19 that debtor was current on all payments to the Chapter 13 trustee
20 over the preceding one year. The Court is also mindful that
21 while debtor is only required to propose a 36 month plan, debtor
22 has committed to making payments for 60 months. While the
23 dividend to unsecured creditors is small as a percentage, that
24 is caused in significant part by inclusion of a junior mortgage
25 obligation that became unsecured when the property was
26 foreclosed. Lastly, the Court recognizes that debtor can earn a

1 discharge of any of his scheduled debts only if he fully performs
2 his plan over 60 months. If he fails, he is back at the
3 beginning. He has an incentive to succeed.

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Conclusion

For all the foregoing reasons, the Court overrules the objections to confirmation filed by the United States Trustee. During the course of the proceedings, the Chapter 13 trustee joined in the objections of the United States Trustee, and asked to be excused from the evidentiary hearing. The Court's rulings as to the objections of the United States Trustee apply equally to the same objections of the Chapter 13 trustee.

IT IS SO ORDERED.

DATED: AUG 24 2009



PETER W. BOWIE, Chief Judge
United States Bankruptcy Court