

FOR PUBLICATION



UNITED STATES BANKRUPTCY COURT CENTRAL DISTRICT OF CALIFORNIA

In re:

CHRISTOPHER PAASCH,

Debtor,

Case No. LA 02-43601--SB

CHAPTER 7

**ORDER DENYING
CHAPTER 13 PLAN
CONFIRMATION**

DATE: August 22, 2005
TIME: 2:00 pm
CRTRM.: 1575 (Roybal)

1 **I. INTRODUCTION**

2 Debtor Christopher S. Paasch, a
3 racehorse trainer, has proposed an amended
4 Chapter 13¹ plan in this case, pursuant to which
5 most of his plan payments would come from
6 money that he intends to borrow from one of his
7 clients. The Court finds that such a plan is not
8 confirmable and denies confirmation.

9 **II. RELEVANT FACTS**

10 Christopher Paasch ("Paasch") requests
11 the court to confirm his chapter 13 plan, proposed
12 principally to deal with support and property
13 division payments owing to his ex-wife Arlene
14 Kovnick. Pursuant to the plan, Paasch proposes
15 to pay \$2,399 per month for the benefit of his
16 creditors during the remaining 26 months of his 36-
17 month plan. Under the plan, the administrative
18 claims and the unsecured claims of Kovnick and
19 the IRS claim will be paid in full. The remaining
20 unsecured creditors will receive payment of 4.93%
21 of their claims.

22 However, based on his disposable
23 income, Paasch admits that he can only afford
24 plan payments of \$508 per month after the
25 payment of reasonable and necessary living
26 expenses. Paasch proposes to cover the shortfall
27 of \$1,891 per month by borrowing \$50,000 from a
28 client, and to repay the loan after the completion of
his chapter 13 plan.

Nancy Curry, the chapter 13 trustee,
objects to confirmation of the plan, in part on the
grounds that Paasch does not have sufficient
disposable income to fund the proposed plan
under § 1325(b)(2). Thus, she argues, the plan is
merely an effort to forestall creditors from
exercising their rights against him. Paasch claims
that by borrowing \$50,000 and adding that amount
to his actual surplus of \$508 per month, he is
making the required "best efforts" to pay his
creditors and that the plan is proposed in good
faith.

III. ANALYSIS

¹Unless otherwise indicated, all chapter,
section and rule references are to the
Bankruptcy Code, 11 U.S.C. §§ 101-1330 (West
1999) and to the Federal Rules of Bankruptcy
Procedure, Rules 1001-9036.

Section 1325² requires the confirmation of
a chapter 13 plan if it meets six requirements: (1)
the plan complies with other provisions of
bankruptcy law; (2) all preconfirmation fees and
charges have been paid; (3) the plan has been
proposed in good faith and not by any means
forbidden by law; (4) creditors will receive present
value equal to what they would receive in a
chapter 7 liquidation; (5) for secured claims, the
claimant accepts the plan, the debtor surrenders
the collateral, or the plan meets the "fair and

²Section 1325(a) provides:
The court shall confirm a plan if—
(1) the plan complies with the provisions
of this chapter and with other applicable
provisions of this title;
(2) any fee, charge, or amount required
under chapter 123 of title 28, or by the
plan, to be paid before confirmation, has
been paid;
(3) the plan has been proposed in good
faith and not by any means forbidden by
law;
(4) the value, as of the effective date of
the plan, of property to be distributed
under the plan on account of each
allowed unsecured claim is not less than
the amount that would be paid on such
claim if the estate of the debtor were
liquidated under chapter 7 of this title on
such date;
(5) with respect to each allowed secured
claim provided for by the plan—
(A) the holder of such claim has
accepted the plan;
(B)(i) the plan provides that the
holder of such claim retain the
lien securing such claim; and
(ii) the value, as of the
effective date of the plan, of
property to be distributed under
the plan on account of such
claim is not less than the
allowed amount of such claim;
or
(C) the debtor surrenders the
property securing such claim to
such holder; and
(6) the debtor will be able to make all
payments under the plan and to comply
with the plan.

1 equitable” test; and (6) the plan is feasible (i.e., the
2 debtor will be able to comply with the plan and
make the payments thereunder).

3 If the trustee objects to the confirmation of
4 the plan, § 1325(b) imposes a seventh
5 requirement, that the court may not confirm the
6 plan unless either (a) all allowed unsecured claims
are paid in full, or (b) the debtor applies all of his
projected disposable income for three years to
make the plan payments (the “best efforts” test).³

7 ³Section 1325(b) provides in relevant
8 part:

9 (1) If the trustee or the holder of an
10 allowed unsecured claim objects to the
confirmation of the plan, then the court
11 may not approve the plan unless, as of
the effective date of the plan—

12 (A) the value of the
property to be distributed under
13 the plan on account of such
claim is not less than the
amount of such claim; or

14 (B) the plan provides
that all of the debtor’s projected
15 disposable income to be
received in the three-year period
16 beginning on the date that the
first payment is due under the
17 plan will be applied to make
payments under the plan.

18 (2) For purposes of this
subsection, “disposable income”
19 means income which is received
by the debtor and which is not
20 reasonably necessary to be
expended—

21 (A) for the maintenance
or support of the debtor or a
22 dependent of the debtor,
including charitable
23 contributions (that meet the
definition of “charitable
24 contribution” under section
548(d)(3)) to a qualified religious
25 or charitable entity or
organization (as that term is
26 defined in section 548(d)(4)) in
an amount not to exceed 15
27 percent of the gross income of
the debtor for the year in which
28 the contributions are made

For debtors not engaged in business, “disposable
income” is defined in § 1325(b)(2)(A) as income
not reasonably necessary for the maintenance or
support of the debtor or the debtor’s dependents.

A. Good Faith

Section 1325(a)(3) requires that a chapter
13 plan be “proposed in good faith and not by any
means forbidden by law.” Although “good faith” is
not defined by the statute or its legislative history,
the Ninth Circuit has held that a “good faith test . .
. . should examine the intentions of the debtor and
the legal effect of the confirmation of a Chapter 13
plan in light of the spirit and purposes of Chapter
13.” *In re Chinichian*, 784 F.2d 1440, 1444 (9th
Cir. 1986); *see also In re Goeb*, 675 F.2d 1386,
1389-90 (9th Cir. 1982); H.R. REP. NO. 96-1195, at
24-25 (1980); S. REP. NO. 95-989, at 126, 142
(1978); H.R. REP. NO. 95-595, at 412, 430 (1977).
The trustee contends that Paasch’s chapter 13
plan fails the good faith test because he proposes
to borrow \$50,000 from a client to make his plan
payments.

The general purpose of a plan under
chapter 13 is to provide a fresh start to the debtor,
while, at the same time, providing for payment of
debts owing to creditors. Under chapter 7, a
debtor gives up all of his or her nonexempt assets
for sale by the trustee and distribution (after paying
administrative expenses) to creditors pro rata, after
the payment of priority creditors. *See* §§ 541, 725,
726(b).

Chapter 13, however, is based on quite a
different deal between the debtor and the
creditors: under chapter 13, the debtor is entitled
to keep all of his or her assets at the time of filing,
in exchange for making payments to the creditors
over a period of three to five years. *See* §§
1306(a)-(b), 1322(d); *see also* H.R. REP. NO. 95-
595, at 118 (1977) (describing benefit of chapter
13 repayment plan over chapter 7 liquidation as
allowing debtor to protect and retain his assets).
Creditors are protected under this arrangement by
a requirement that the payments to creditors must
be at least as much as they would receive under a
chapter 7 liquidation. *See* § 1325(a)(4).

In promulgating chapter 13, Congress
undertook a substantial revision to chapter XIII of
the former Bankruptcy Act. Congress found that,
in certain areas of the country:

[I]nadequate supervision of
debtors attempting to perform
under wage earner plans have

1 made them a way of life for
2 certain debtors. Extensions on
3 plans, new cases and *newly*
4 *incurred debts* put some debtors
5 under court supervised
6 repayment plans for 7 to 10
7 years. This has become the
8 closest thing to indentured
9 servitude: it lasts for an indefinite
10 period and *does not provide the*
11 *relief and fresh start for the debtor*
12 *that is the essence of modern*
13 *bankruptcy law.*

14 See H.R. REP. NO. 95-595, at 117 (1977)
15 (emphasis added). The Committee on the
16 Judiciary of the House of Representatives further
17 explained the legislative intent of chapter 13 as
18 follows:

19 [T]he debtor is given adequate
20 exemptions and other protections
21 to ensure that bankruptcy will
22 provide a fresh start. . . . The
23 premises of the bill with respect
24 to consumer bankruptcy are that
25 use of the bankruptcy law should
26 be a last resort; that if it is used,
27 debtors should attempt
28 repayment under chapter 13 . . .
and finally, *whether the debtor*
uses chapter 7, Liquidation, or
chapter 13, Adjustment of Debts
of an Individual, bankruptcy relief
should be effective, and should
provide the debtor with a fresh
start.

29 *Id.*

30 Paasch's proposal in this case would
31 barely make a start toward the fresh start
32 contemplated by chapter 13. Upon completion of
33 the plan, Paasch would still owe nearly \$50,000 in
34 new debt undertaken to pay off his old debt.
35 Furthermore, it is not apparent how Paasch could
36 pay this new debt. Given his present monthly
37 disposable income of \$508, it would take ten
38 additional years to pay off the new loan. This total
39 of thirteen years far exceeds the statutory limit of
40 five years for a chapter 13 plan and comes close
41 to the situation of indentured servitude that debtors
42 frequently suffered under chapter XIII. Chapter 13
43 does not contemplate such a result.

44 There is no provision in chapter 13 that
45 explicitly prohibits a debtor from borrowing money

46 for chapter 13 plan payments. However, the court
47 finds that a chapter 13 plan that proposes to fund
48 more than 70% of the payments by borrowing
49 money fails the "good faith" test, and cannot be
50 confirmed.

51 **B. Other Trustee Objections**

52 The trustee also argues that Paasch fails
53 the "good faith" requirement in two other respects.
54 First, she contends that the plan improperly divides
55 the general unsecured creditors into two
56 subclasses, one of which will be paid in full and the
57 other only 4.93%. Second, the trustee argues that
58 Paasch has not been truthful and honest with the
59 court: he has not disclosed all of his income, has
60 failed to disclose sources of income, has
61 concealed assets and has falsified his expenses.

62 Finally, the trustee argues that Paasch
63 cannot meet the "best efforts" requirement of §
64 1325(b)(1) because of his failure to disclose all
65 amounts and sources of income and his
66 concealment of assets and falsification of
67 expenses.

68 The court would likely be required to take
69 testimony on these issues before it could conclude
70 that the chapter 13 requirements for plan
71 confirmation are met. However, the court does not
72 reach these issues because its finding on
73 borrowing money to make more than 70% of the
74 plan payments is dispositive.

75 **IV. CONCLUSION**

76 The Court finds that, under the
77 circumstances of this case, the proposed plan is
78 not viable and denies Paasch of a fresh start. The
79 substitution of new debt for more than 70% of the
80 existing, old debt is simply not within the
81 contemplation of chapter 13. Moreover, without
82 the borrowed funds, Paasch lacks the disposable
83 income necessary to make his proposed plan a
84 viable one.

CERTIFICATE OF MAILING

I certify that a true copy of this ORDER DENYING CHAPTER 13 PLAN CONFIRMATION
was mailed on OCT - 6 2005 to the parties listed below:

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OCT - 6 2005

DATED: _____



Deputy Clerk