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BANKRUPTCY LAW

IN RE GOEB: DEEMPHASIZING THE GOOD FAITH REQUIREMENT OF CHAPTER 13

A. INTRODUCTION

In *In re Goeb*,¹ the Ninth Circuit held that a Chapter 13 repayment plan need not provide for substantial repayment to unsecured creditors to have been proposed in good faith.² *Goeb* addresses the question of the role that the good faith requirement plays in a Chapter 13 repayment plan.³

Straight bankruptcy proceedings are governed by Chapter 7 of the Bankruptcy Reform Act of 1978 (1978 Act).⁴ Once bank-

1. 675 F.2d 1386 (9th Cir. 1982) (per Choy, J.; the other panel members were Schroeder, J. and Hatter, D.J., sitting by designation).

2. *Id.* at 1389. The debtors in *Goeb* proposed a five year plan which would have paid their secured and priority creditors in full but unsecured creditors only one cent on the dollar. The bankruptcy court refused to confirm the plan because they did not intend to substantially repay their unsecured creditors. The bankruptcy court found that the plan violated the good faith requirement of Chapter 13. *Id.*

3. As of this writing, only four other circuits have addressed this same issue. The District of Columbia Circuit held that Chapter 13 plans which provided full repayment for secured and cosigned debts, but only provided nominal repayment to other creditors do not violate the good faith requirement because "section 1325(a)(3) does not require any particular level of minimum repayment as a prerequisite to Chapter 13 plan confirmation." *Barnes v. Whelan*, 689 F.2d 193 (D.C. Cir. 1982). The Seventh Circuit stated that determination of good faith must be ascertained on a case by case basis, with substantiality of repayment as one factor. *In re Rimgale*, 669 F.2d 426, 431 n.14 (7th Cir. 1982). The Eighth Circuit held that a Chapter 13 plan which proposed to pay nothing to any creditor was not proposed in good faith because it "amounts to an abuse of Section 1328 (granting a more generous discharge than in Chapter 7) and of the spirit of the chapter, that the debtor 'make payments' under a plan." *In re Terry*, 630 F.2d 634, 635 (8th Cir. 1980). In *Deans v. O'Donnell*, 692 F.2d 968, 970 (4th Cir. 1982), the court found it could not manipulate the good faith requirement of Chapter 13 so as to impose a rigid substantial repayment requirement. The proper course was to apply the statute as written and let Congress impose additional requirements if it so chooses.

4. 11 U.S.C. §§ 101-151326 (1979 & Supp. 1982). Although this note is confined to the current Bankruptcy Act, a brief history of the Act is appropriate. There are basically four major bankruptcy acts which Congress has promulgated. The first, the Bankruptcy Act of 1841, repealed by the Act of March 3, 1843, 52 Stat. 614 (1843), introduced many of the features which are still part of current bankruptcy laws such as voluntary proceedings, and certain duties and rights of the trustee in collecting the assets of the debtor.

ruptcy is declared, either through voluntary or involuntary petition, the debtor is discharged from virtually all preexisting debts.⁵ Chapter 13, however, is an alternative to straight bankruptcy and provides the debtor an option to submit to a court supervised repayment plan to repay his debts over a three year period.⁶ Proceeding by way of Chapter 13 is strictly voluntary.

As an inducement to debtors to utilize the Chapter 13 repayment plan rather than straight bankruptcy, Chapter 13 offers several advantages over Chapter 7.⁷ Chief among these is the liberal discharge provision which allows a debtor to discharge almost all of her unsecured debts.⁸ Chapter 7, on the other hand,

Section 12 of the Bankruptcy Act of 1898 introduced the wage earner repayment plan. 30 Stat. 544, 549-66 (1898), amended by the Act of June 25, 1910, Pub. L. No. 294, 36 Stat. 838 (1910), and by the Act of May 27, 1926, Pub. L. No. 301, 44 Stat. 662, 662-68 (1926). Section 12 was repealed by the Chandler Act of 1938, Pub. L. No. 74-696, 52 Stat. 840, 840-940 (1938). The Chandler Act attempted to expand bankruptcy legislation after the ravages of the Great Depression. For a general history and analysis of this important act, see J. WEINSTEIN, *THE BANKRUPTCY LAW OF 1938—THE CHANDLER ACT (1938)*. The most current bankruptcy legislation is the Bankruptcy Reform Act of 1978, 11 U.S.C. §§ 101-151326 (1979 & Supp. 1982). For an in-depth discussion of the history of bankruptcy in the United States, see generally C. WARREN, *BANKRUPTCY IN UNITED STATES HISTORY (1935)*.

5. This rather sweeping statement is heavily qualified in the bankruptcy code. 11 U.S.C. § 524 (1979) states what effect a discharge has on the wide range of debts which are not dischargeable in a Chapter 7 proceeding. See *infra* note 8 and accompanying text.

6. 11 U.S.C. §§ 1301-1330 (1979) governs repayment plans. See *infra* notes 32-45 and accompanying text.

7. Chapter 7 has three key limitations. First, it prohibits discharge of debts obtained by fraud, 11 U.S.C. §§ 523, 727 (1979 & Supp. 1982), see note 9 *infra*, thereby punishing the dishonest debtor. Second, Chapter 7 has a six year bar on future Chapter 7 proceedings, 11 U.S.C. § 727(a)(8), thereby prohibiting the repeat debtor. Finally, Chapter 7 does not allow a debtor to discharge certain types of liability such as student loans. See *infra* note 9. These limitations are not present in a Chapter 13 proceeding. See *infra* note 8. Also, in a Chapter 13 proceeding, the debtor is allowed to retain control of his property, which is not true in a Chapter 7 proceeding, in which the trustee gets ownership in all of debtor's nonexempt property. See 11 U.S.C. §§ 701-766 (1979).

8. 11 U.S.C. § 1328 (1979) allows a debtor to discharge all debts still owed upon completion of the repayment plan. The only two exceptions are support payments and any debts whose last payment is due after the plan is completed. 11 U.S.C. §§ 513(a)(5), 1322(b)(5) (1979). This last exception is for long term debts such as mortgage payments. Otherwise, all other debts are dischargeable, whether obtained by fraud or any other type of nondischargeable debt under Chapter 7. 11 U.S.C. § 1328(b) (1979) allows a debtor to be excused from completing the repayment plan if the situation so warrants. This is basically a hardship discharge. However, under 11 U.S.C. § 1328(c) (1979) the discharge granted does not include the enumerated exceptions to discharge of 11 U.S.C. § 523(a) (1979 & Supp. 1982). Thus, if a chapter 13 debtor fails to complete the repayment plan, his discharge will be limited to that of a chapter 7 liquidation.

has a long list of nondischargeable debts.⁹

The existing potential for abuse—from the position of the unsecured creditor—arises when a debtor proposes a Chapter 13 repayment plan for the sole purpose of taking advantage of the liberal discharge provisions. Chapter 13 requires only that the debtor's unsecured creditors receive as much repayment under Chapter 13 as would have been received under Chapter 7.¹⁰ Therefore, all a debtor need do is propose a repayment plan offering to pay her unsecured creditors as much as they would be entitled to under Chapter 7 and the plan could be confirmed.¹¹ As a result, the debtor would be paying off her debts as if it were straight bankruptcy, but would be receiving all the benefits of a Chapter 13 repayment plan. The requirement that the plan be proposed in good faith has been imposed by Congress to insure that such abuses do not occur.¹²

B. BACKGROUND

1. *Development of and Distinction Between Chapter 13 and Chapter 7*

To be declared bankrupt under Chapter 7 a debtor files a petition with the court.¹³ Upon filing, an automatic stay becomes effective which prevents any creditor from attempting to collect money owed him.¹⁴ A trustee is appointed to collect the non-exempt assets of the debtor at the time she declared bank-

9. 11 U.S.C. §§ 523, 727 (1979 & Supp. 1982) list the debts which a Chapter 7 debtor cannot discharge. They include taxes owed to the government as priority creditors, or if incurred as a result of making a fraudulent return; debts arising from fraud or illegality; any debt not listed on the Chapter 7 petition; any support obligation; any debt arising from the debtor's willful injury to another entity or entity's property; or any student loans. This list is not exhaustive and is meant only to highlight the relevant areas.

10. 11 U.S.C. § 1325(a) (1979) lists the requirements for confirmation of a repayment plan. Subsection (a)(4) states that "the value . . . 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 . . ." 11 U.S.C. § 1325(a)(4) (1979).

11. This is so as long as the plan complies with the other applicable provisions of Chapter 13. See *infra* notes 38-46 and accompanying text.

12. See *infra* note 47 and accompanying text.

13. The petition can be either voluntary or involuntary. 11 U.S.C. §§ 301, 303 (1979).

14. Once a debtor files a petition, all collection proceedings against the debtor are stopped. 11 U.S.C. § 362 (1979).

ruptcy¹⁵ and distribute these assets to the debtor's unsecured creditors *pro rata*, depending on their position within Chapter 7's priority scheme.¹⁶

Although this definition is somewhat misleading in its simplicity, it is important to note that none of the debtor's post-petition assets are involved in the repayment to her creditors. The only assets which go toward repaying her debts are those non-exempt assets she owned at the time she filed under Chapter 7.¹⁷

Straight bankruptcy proceedings created an anomalous situation for the unsecured creditor by precluding the application of any of the debtor's post-bankruptcy earnings to satisfy the creditor's claim.¹⁸ These assets were often those upon which the creditor relied, as in consumer lending transactions, in extending the credit.

Consumer credit is usually extended in reliance on the wage earner's ability to pay off the debt out of his future earnings.¹⁹ It is generally not extended based on the present worth of the wage earner's assets because creditors wanting to levy on assets in case of default would be frustrated by the applicable state exemption laws.²⁰ Even if the assets were not exempt, they often would be encumbered up to or exceeding their liquidation value.²¹ The repayment alternative to straight bankruptcy was a response to this situation.

15. The creditors who have undisputed allowed unsecured claims come together to elect a trustee. 11 U.S.C. § 702 (1979). See 11 U.S.C. § 704 (1979) for a detailed description of the trustee's duties.

16. There exist several classes of claims and creditors which must be satisfied *pro rata* within each class prior to moving onto the next class. 11 U.S.C. § 507 (1979).

17. 11 U.S.C. § 541(a)(6) (1979) states that "earnings from services performed by an individual debtor after the commencement of the case" are not to be included as part of the debtor's estate.

18. *Id.*

19. 5 COLLIER ON BANKRUPTCY § 1300.01 (1982).

20. See, e.g., CAL. CIV. PROC. CODE § 690-690.60 (West 1980) listing what property a debtor may claim as exempt in a California collection proceeding.

21. This situation is especially true today since the adoption of the Uniform Commercial Code in most jurisdictions. The U.C.C. protects purchase money lenders by creating an automatic perfected security interest in the goods the consumer bought. U.C.C. § 9-302(1)(d) (1977). For example, if a consumer buys a hot tub under an installment contract, the seller has a perfected security interest in that hot tub. No other creditor can levy on the tub to satisfy his claim.

Chapter XIII of the Chandler Act of 1938²² (Chandler Act) was the first major piece of legislation to deal with this alternative. As a result of the Great Depression, individual bankruptcies increased dramatically.²³ Chapter XIII's goal was to reduce the occurrence of bankruptcy by allowing debtors to restructure their debt schedules.²⁴ Although well intended,²⁵ several flaws in its system impeded its goal. First, the definition of wage earner under Chapter XIII included only persons whose principle income came from wages, salary, or commissions,²⁶ thereby excluding persons on social welfare programs, small business owners and other self-employed individuals relying primarily on trade credit to produce income. Second, if a married couple wanted to use Chapter XIII to repay debts for which they were jointly liable, both spouses had to qualify as wage earners to qualify for a joint petition.²⁷ Third, the debtor had to procure the unanimous consent of her unsecured creditors before the plan could be approved,²⁸ virtually eliminating any plan which paid less than the full amount of all unsecured debts. Last, there was a six year bar on subsequent discharges under this chapter.²⁹

22. Pub. L. No. 74-696, 52 Stat. 840, 840-940 (1938).

23. 5 COLLIER ON BANKRUPTCY § 13.03 (1982). No major piece of bankruptcy legislation has been enacted without being preceded by a recessionary economy. As the economy expanded, so did the intensity of recessions. Thus, more and more wage earning consumers were falling into debt and being subjected to state collection practices. The 1978 Act was a direct result of the recession of 1974-75. See DIRECTOR AD. OFF. U.S. CTS. ANN. REP., Table F, at A-78 (1975).

24. Chapter XIII required the wage earning debtor to subject his future earnings to the supervision of the court. This alleviated the problem of creditor harassment and benefitted everyone by insuring that the assets of the debtor would be equitably distributed to all creditors by the trustee. The plan would continue for a minimum of three years during which time the debtor would make regular payments to the court until the plan had been completed. There was a special discharge provision if the debtor, through no fault of his own, was unable to complete the plan. This was not available for the first three years of repayment, and was generally only granted if the debtor became disabled or lost his job. See J. WEINSTEIN, *THE BANKRUPTCY LAW OF 1938—THE CHANDLER ACT* (1938).

25. In sponsoring this act, Congressman Chandler hoped that this new bankruptcy act would "usher in an era of lasting prosperity and good feeling." J. WEINSTEIN, *supra* note 24, at iii.

26. Chandler Act of 1938 § 606(8) (repealed 1978) (current version at 11 U.S.C. § 109(e)(1979)).

27. Chandler Act of 1938 § 606(3), (6), (8) (repealed 1978) (current version at 11 U.S.C. § 302(a) (1979)).

28. Chandler Act of 1938 §§ 651, 652 (repealed 1978) (current version at 11 U.S.C. § 1325(a)(4) (1979)).

29. Chandler Act of 1938 § 14(c)(5) (current version at 11 U.S.C. § 727(a)(8), (9) (1979)). For an in depth study of the flaws of chapter XIII, See *Bankruptcy Act Revi-*

Chapter XIII was not drafted to cope with a vast expansion in consumer credit or with a huge increase in wage earner defaults.³⁰ Moreover, Chapter XIII could not deal with the rapid growth of consumer credit following World War II, as well as the effect the adoption of the Uniform Commercial Code had on the consumer lending industry in the 1960's.³¹ In response to these problems, Chapter XIII was repealed and replaced by Chapter 13 of the 1978 Act.³²

The amended Chapter 13 changed the former repayment provisions in five ways. First, it gave debtors more flexibility in formulating a repayment plan.³³ Second, it more particularly defined the rights of secured and unsecured creditors.³⁴ Third, it broadened the class of debtors.³⁵ Fourth, it placed a limit on the length of a plan.³⁶ And finally, it reduced indirect pressure from the debtor's family and friends by protecting consumer co-debtors.³⁷

2. Chapter 13 Repayment Plans

Chapter 13 enables an individual with a regular income³⁸ to repay his debts out of his future income over an extended period of time.³⁹ The debtor must propose a repayment plan to the

sion, Hearings on H.R. 31 and 32 before the Subcomm. on Civil and Const. Rights of the Comm. on the Judiciary of the House of Representatives, 94th Cong., 2d Sess. 1315-1324 (1976). For a detailed study of the conflicting role of the chapter XIII trustee, see Comment, The Chapter XIII Trustee: "Trustee" or Dispensing Agent?, 21 ME. L. REV. 53 (1969).

30. H.R. REP. NO. 595, 95th Cong., 1st Sess. 3-5 (1977), reprinted in 1977 U.S. CODE CONG. & AD. NEWS 5965-66.

31. *Id.*

32. 11 U.S.C. §§ 1300-1330 (1979).

33. 11 U.S.C. § 1322 (1979). This section outlines what the plan may provide for each class of creditor. This gives the debtor many more options when structuring the repayment plan than was previously available under Chapter XIII.

34. 11 U.S.C. §§ 501-510 (1979). These sections outline the rights of creditors and those persons who have claims against the debtor.

35. An individual with regular income is defined by the code as one "whose income is sufficiently stable and regular to enable such individual to make payments under a plan under chapter 13 . . ." 11 U.S.C. § 101(24) (1979).

36. 11 U.S.C. § 1329(c) (1979) does not allow a court to approve a plan which will exceed three years, unless for cause shown, and then only up to five years.

37. 11 U.S.C. § 1301(a)(1) (1979). This section specifically prohibits creditors from acting against the co-debtor if the debt was created to secure a consumer good.

38. *See supra* note 35.

39. 11 U.S.C. § 1322 (1979) states that the plan shall provide for the repayment of the debts listed as property of the estate. 11 U.S.C. § 1322(c) (1979) limits the plan to

bankruptcy court which provides for the submission of that portion of the debtor's future income to the supervision and control of the Chapter 13 trustee as would be necessary to complete the plan.⁴⁰

For the plan to be confirmed, the bankruptcy court must find that it conforms to all applicable provisions of the bankruptcy code.⁴¹ This includes having all administrative fees paid prior to the commencement of the plan,⁴² obtaining the approval of all the debtor's secured creditors,⁴³ and insuring that the plan provides that the unsecured creditors of the debtor will receive what they would have under a straight bankruptcy proceeding.⁴⁴ Finally, the court must find that the debtor will be able to complete the repayment plan on time,⁴⁵ and that the debtor is proposing this plan in good faith.⁴⁶

The good faith requirement of section 1325(a)(3) has been utilized by many courts to insure that the debtor's unsecured creditors are substantially repaid.⁴⁷ Thus, while a Chapter 13 repayment plan does not explicitly require substantial repayment to unsecured creditors, courts are reluctant to approve a repayment plan *unless* it provides for the substantial repayment of unsecured creditors.⁴⁸

three years unless the court grants an extension, but only up to five years.

40. 11 U.S.C. § 1322 (1979).

41. 11 U.S.C. § 1325(a)(1) (1979).

42. 11 U.S.C. § 1325(a)(2) (1979).

43. 11 U.S.C. § 1325(a)(5) (1979).

44. 11 U.S.C. § 1325(a)(4) (1979).

45. 11 U.S.C. § 1325(a)(6) (1979).

46. 11 U.S.C. § 1325(a)(3) (1979).

47. See, e.g., *In re Bellgraph*, 6 BANK. CT. DEC. (CRR) 480 (W.D.N.Y. 1980); *In re Chaffin*, 2 COLLIER BANKR. CAS. 2d (MB) 229, 6 BANKR. CT. DEC. (CRR) 426 (D. Kan. 1980); *In re Cloutier*, 1 COLLIER BANKR. CAS. 2d (MB) 909, 6 BANK. CT. DEC. (CRR) 196 (D. Colo. 1980); *In re Cook*, 1 COLLIER BANKR. CAS. 2d (MB) 780, 6 BANKR. CAS. DEC. (CRR) 219 (S.D.W. Va. 1980); *In re Hall*, 2 COLLIER BANKR. CAS. 2d (MB) 310, 6 BANKR. CT. DEC. (CRR) 476 (E.D. Va. 1980); *In re Harland*, 1 COLLIER BANKR. CAS. 2d (MB) 973, 6 BANKR. CT. DEC. (CRR) 235 (D. Neb. 1980); *In re Madden*, 1 COLLIER BANKR. CAS. 2d (MB) 1093 (S.D. OHIO 1980); *In re Marlow*, 1 COLLIER BANKR. CAS. 2d (MB) 705, 6 BANKR. CT. DEC. (CRR) 77 (N.D. Ill. 1980); *In re Montano*, 2 COLLIER BANKR. CAS. 2d (MB) 431, 6 BANKR. CT. DEC. (CRR) 487 (D.D.C. 1980); *In re Rayburn*, 6 BANKR. CT. DEC. (CRR) 453 (N.D. Ga. 1980).

48. The good faith requirement in Chapter 13 repayment plans has sparked a great deal of scholarly comment. See generally Note, *Good Faith, Zero Plans, and the Purpose of the Bankruptcy Code Chapter 13: A Legislative Solution to the Controversy*, 61 B.U.L. REV. 773 (1981); Note, *Chapter 13 De Minimus Plans: Toward a Consensus on*

3. Interpretation of the Good Faith Requirement Prior to Goeb

Bankruptcy courts within the Ninth Circuit have, with few exceptions,⁴⁹ uniformly viewed the good faith requirement of Chapter 13 as compensating for its liberal discharge provisions.⁵⁰ These courts have used the good faith requirement to insure that a debtor's repayment plan will provide for substantial repayment to her unsecured creditors.⁵¹ The following cases from the various districts within the Ninth Circuit are illustrative of how the good faith requirement has been utilized.

In *In re Bloom*,⁵² the bankruptcy court found that a one percent repayment plan to debtor's unsecured creditors violated the good faith provision of Chapter 13.⁵³ *Bloom* reasoned that a one percent repayment plan was more like a Chapter 7 proceeding because both avoided paying most of the debt.⁵⁴ This, the court found, frustrated Chapter 13's goal of debt repayment.⁵⁵

"Good Faith", 9 HOFSTRA L. REV. 593 (1981); Note, *Bankruptcy: Good Faith and the Zero Payment Plan in Chapter 13*, 69 KY. L.J. 327 (1981); Note, *Filing for Personal Bankruptcy: Adoption of a "Bona Fide Effort" Test under Chapter 13*, 14 MICH. J. L. REFORM 321 (1981); Note, "Good Faith" and Confirmation of Chapter 13 Composition Plans: Analysis and a Proposal, 65 MINN. L. REV. 659 (1981).

49. See, e.g., *In re Webb*, 1 COLLIER BANKR. CAS. 2d (MB) 465 (N.D. Cal. 1980). In *Webb*, the court confirmed a plan which was to pay unsecured creditors only 1% of their debts because they would have received nothing had the debtor gone through Chapter 7. As such, the plan satisfied § 1325(a)(4) which requires that in order for a Chapter 13 plan to be confirmed, unsecured creditors must receive at least as much as they would under Chapter 7. The court concluded that the 1% amount was sufficient.

50. *In re Howard*, 1 COLLIER BANKR. CAS. 2d (MB) 634 (S.D. Cal. 1980) stated that "[t]he draft[ers] intended debtors to deal fairly and justly with their creditors. As a reward for such dealing, [Chapter 13] debtors were given the 'super' discharge provided for in Section 1328(a)" *Id.*

51. *In re Beaver*, 1 COLLIER BANKR. CAS. 2d (MB) 609 (S.D. Cal. 1980), stated that a "one percent plan . . . cannot be held to constitute a meaningful attempt to repay . . ." *Id.* at 615. The court also found that Congress intended the good faith requirement to insure that meaningful repayment would occur. *Id.*

52. 1 COLLIER BANKR. CAS. 2d (MB) 1098 (C.D. Cal. 1980).

53. *Id.* at 1104. The debtors in *Bloom* owed unsecured debts totaling \$273,614.00. The plan they submitted would have paid \$2,736.14, or 1%, back to their unsecured creditors.

54. *Id.* at 1102. The court found that a Chapter 7 debtor has no motive to repay his creditors since he is seeking a discharge from debts. The court analogized this non-repayment motive to a *de minimus* Chapter 13 repayment plan and found that "[a] debtor who files the nominal . . . Chapter 13 plan is really no different. If he proposes to pay his creditors . . . one percent of the creditors [sic] claims it cannot be honestly argued that this debtor wants to pay his bills . . ." *Id.*

55. *Id.*

The court also noted that the requirement a debtor be able to meet all payments under the plan evidenced Congress' intent that the Chapter 13 debtor make meaningful payments, a requirement which a one percent plan does not meet.⁵⁶ Second, the court contrasted Chapter 7 and 13, reasoning that the good faith requirement was imposed in order to compensate for the restrictions which apply to Chapter 7 proceedings but are absent from Chapter 13.⁵⁷

In *In re Beaver*,⁵⁸ the court refused to confirm a plan which would have paid debtor's unsecured creditors only one percent of the outstanding debt.⁵⁹ Turning to the legislative history, the court concluded that Congress intended for Chapter 13 to allow creditors to significantly reduce their losses as opposed to the losses they would suffer under straight bankruptcy via Chapter 7.⁶⁰ The court found that Congress wanted to discourage marginal repayment plans and included the good faith requirement to facilitate that goal.⁶¹ The court concluded that the good faith requirement meant more than honesty; good faith "requires a fundamental fairness in dealing with one's creditors."⁶²

56. *Id.* at 1103. This requirement is found in 11 U.S.C. § 1325(a)(6) (1979). The court also pointed out that the term "individual with a regular income" evidenced Congress' intent that the payments made by the debtor be substantial in light of all the circumstances; otherwise the requirement of section 101(24), *see note 35, supra*, becomes useless. 1 COLLIER BANKR. CAS. 2d (MB) 1098, 1103.

57. 1 COLLIER BANKR. CAS. 2d (MB) at 1104. *See supra* notes 7-9 and accompanying text. The court asked if it can "be seriously argued that Congress could have intended to adopt at the same time [it was imposing the restrictions on discharge in Chapter 7], a scheme under Chapter 13 which would render totally illusory the creditor protections and the debtor limitations set forth in the three principles of the dishonest debtor, the repeater . . . , and the various exceptions to discharge? Such a congressional purpose seems inconceivable to me." *Id.* at 1103.

58. 1 COLLIER BANK. CAS. 2d (MB) 609 (S.D. Cal. 1980).

59. *Id.* at 615. The debtor was unemployed and supporting herself and her two children on \$580 per month unemployment compensation. She listed her assets as \$955 in personal property all of which she declared exempt. She had \$3,206 in debts to unsecured creditors.

60. *Id.* at 613. The court found that while the Chapter 13 debtor has several benefits such as the retention of her property, thereby avoiding the stigma of bankruptcy liquidation, the rights of unsecured creditors were not left unconsidered by Congress. "Losses to creditors otherwise accruing in a liquidation were seen as being *significantly* reduced in a Chapter 13 setting." *Id.* (emphasis in original).

61. *Id.* at 614. The court found that "Congress has now placed on the courts the responsibility to insure that fair dealing is accomplished in Chapter 13 proceedings. They achieved this . . . in the requirement of a specific finding of good faith before a plan can be confirmed." *Id.*

62. *Id.*

The court in *In re Anderson*⁶³ found that because a debtor could have made a more substantial repayment to his unsecured creditors than the one percent repayment plan he proposed, the good faith requirement provision of Chapter 13 had been violated.⁶⁴ The court held that if unsecured creditors' claims are to be abrogated despite the debtor's ability to pay, straight bankruptcy through Chapter 7 is more appropriate.⁶⁵ "If such a debtor is to avoid bankruptcy and gain the benefits of Chapter 13, the *quid pro quo* is that he should pay according to his ability and circumstances, thereby providing fairly and responsibly for his creditors within the spirit of Chapter 13. That is what the 'good faith' requirement demands."⁶⁶

In *In re Burrell*,⁶⁷ the district court, reversing a bankruptcy court which had ruled that a Chapter 13 repayment plan must provide for a 70 percent repayment to unsecured creditors,⁶⁸ held that while substantial repayment to unsecured creditors is required in a Chapter 13 plan,⁶⁹ the analysis of the bankruptcy court in reaching a 70 percent repayment requirement was reversible error.⁷⁰ The court focused on the judicial construction of

63. 2 COLLIER BANKR. CAS. 2d (MB) 594 (S.D. Cal. 1980).

64. The debtors had listed unsecured debts of \$10,022.00 and secured debts of \$2,805.00. The debtors' real purpose in proposing a Chapter 13 plan was to enable a restructuring of the contracts they had with a car company and a department store. This was a good faith plan under Chapter 13. *Id.* at 595.

65. *Id.* at 596. "Where a debtor can afford to pay reasonable amounts for a reasonable length of time but elects to make only token payments on his unsecured debts, the plan is unfair and should not be confirmed." *Id.*

66. *Id.* at 597.

67. 2 COLLIER BANKR. CAS. 2d (MB) 1019, 6 BANKR. CT. DEC. (CRR) 900 (N.D. Cal. 1980), *rev'g* 1 COLLIER BANKR. CAS. 2d (MB) 474, 5 BANKR. CT. DEC. (CRR) 1321 (N.D. Cal. 1980).

68. The debtor had submitted a plan which would have provided a 15 percent repayment to each of his unsecured creditors. The bankruptcy judge interpolated the 70% repayment requirement from § 727(a)(9) which sets forth the six-year bar rule for a Chapter 7 discharge. The six-year rule precludes the discharge of a debtor under Chapter 7 if that debtor had previously obtained a Chapter 13 discharge within six years unless that plan had repaid 100% of the allowed unsecured claims or both payment of 70% of the claims and a finding that the plan was proposed in good faith. 2 COLLIER BANKR. CAS. 2d (MB) at 1024.

69. *Id.* The district court stated that it "concur[s] with the bankruptcy court that a Chapter 13 plan must provide for substantial payments to unsecured creditors." *Id.* at 1024-25.

70. *Id.* at 1026. The court found that "[t]he legislative history provides no support for the argument that Congress intended to incorporate into the confirmation standards of § 1325 the requirements of the exception to the six-year bar rule found in § 727(a)(9). In fact, the presence of those tests in § 727(a)(9) suggests that their absence in § 1325(a)

Chapter XIII which stated that "Congress clearly intended to encourage wage earners to repay their debts in full, rather than go into straight bankruptcy or composition . . ." ⁷¹ and concluded that, due to Congress' silence on this point in subsequent amendments, no change from this construction was intended. ⁷²

In sum, the various bankruptcy courts within the Ninth Circuit have construed the good faith requirement as a shield to protect the rights of unsecured creditors when the debtor utilizes Chapter 13, instead of Chapter 7 with its attendant restrictive discharge provisions. ⁷³ Before confirming a plan, the bankruptcy courts have made sure that the repayment plan in fact provides for substantial repayment to the unsecured creditors. ⁷⁴ Anything less than substantial repayment violates the good faith provision of Chapter 13, and this interpretation accords with the intent of Congress. ⁷⁵

4. *Legislative History*

Congress intended to encourage debtors to restructure their debts and avoid straight bankruptcy by going into Chapter 13 rather than Chapter 7. ⁷⁶ However, Congress did not intend that Chapter 13 be used solely for its expansive discharge provision because "[i]t is also necessary to prevent Chapter 13 plans from turning into mere offers of composition plans under which payments would equal only the nonexempt assets of the debtor." ⁷⁷

was intentional rather than accidental." *Id.* at 1025.

71. *Perry v. Commerce Loan Co.*, 383 U.S. 392, 395 (1966).

72. 2 COLLIER BANK. CAS. 2d (MB) at 1024. The court stated that "[i]f Congress had intended to abolish the substantiality requirement [as construed in *Perry*], it could have done so unambiguously. Because it did not, this court must conclude that no change was intended." *Id.*

73. See *supra* note 7 and accompanying text.

74. *In re Campbell*, 1 COLLIER BANKR. CAS. 2d (MB) 653 (S.D. Cal. 1980) stated that "payments under a Chapter 13 plan are to be substantial . . ." *Id.* at 656.

75. See *supra* note 50.

76. "The new chapter 13 will permit almost any individual with regular income to propose and have approved a reasonable plan for debt repayment based on that individual's exact circumstances. As in current law, 100 percent payment plans will be encouraged . . ." S. REP. NO. 989, 95th Cong., 2d Sess. 12 (1978), reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5787, 5799. See also text accompanying note 71, *supra*.

77. S. REP. NO. 989, 95th Cong., 2d Sess. 12-13 (1978), reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5787, 5799. The reason for this recent legislation is that the Supreme Court in *Northern Pipeline Construction Co. v. Marathon Pipeline Co.*, 102 S. Ct. 2858 (1982) found that Congress had violated the Constitution in the 1978 Act by granting broad judicial powers to the bankruptcy judges without conferring on them the same

This approach finds support in the current legislation in Congress.⁷⁸ Recent proposals attempt to tighten up the discharge provisions of Chapter 13 by not allowing the debtor to discharge those debts which Chapter 7 would not allow.⁷⁹ In sum, these bills would equalize the discharge provisions between Chapters 7 and 13,⁸⁰ and in addition, would provide for a minimum standard in order to qualify for Chapter 7.⁸¹

The legislative history of both the 1978 Act and pending legislation are consistent in revealing Congress' desire to have debtors repay their creditors as much as they can by allowing the debtor to restructure her debts.⁸² The difference lies in the method to reach that result. Chapter 13 at present seeks to encourage repayment plans by offering an expansive discharge provision.⁸³ The legislation currently before Congress would impose a mandatory repayment plan upon the debtor if she is able to pay at least 25 percent of her debts, and equalize the discharge provision of Chapter 13.⁸⁴

C. THE *Goeb* DECISION

The Ninth Circuit, in *In re Goeb*, stated that the term good faith does not mandate that substantial repayment be made to unsecured creditors in a Chapter 13 plan.⁸⁵ The court found that

protections accorded to judges who serve on courts established under Article III of the Constitution. The Court gave Congress until December 1982 to modify the 1978 Act accordingly. This has created a huge amount of omnibus legislation aimed at re-designing the entire 1978 Act.

78. "It is the intent of Congress to require the debtor to make a substantial effort to pay his bills." S. REP. No. 446, 97th Cong., 2d Sess. 46 (1982). [Hereinafter cited as SENATE REPORT].

79. *Id.* This bill would amend 11 U.S.C. § 1325(a) (1979) to require that all debts which are nondischargeable under 11 U.S.C. § 523 (1979) be incorporated into the repayment plan.

80. *Id.* This bill would conform the treatment of such debts provided for in Chapter 13 to that accorded in Chapter 7. *Id.* at 27.

81. SENATE REPORT, *supra* note 78, at 32. This bill would not allow a debtor to go into Chapter 7 unless he were unable to repay at least 25% of his outstanding debts through a Chapter 13 repayment plan. Therefore, if a debtor were able to pay off 25% of his debt, he could not go through Chapter 7 but would be forced to go through Chapter 13. This type of legislation demonstrates Congress' desire to encourage substantial repayment of debtors.

82. See *supra* notes 71, 78 and accompanying text.

83. See *supra* notes 48-51 and accompanying text.

84. See *supra* notes 80-81 and accompanying text.

85. *In re Goeb*, 675 F.2d 1386, 1389 (9th Cir. 1982).

had Congress intended to establish a substantial repayment requirement for Chapter 13 debtors, it could easily have done so.⁸⁶ The only repayment requirement Congress actually set out was that unsecured creditors cannot be paid less than the amount they would have received had the estate of the debtor been liquidated under Chapter 7.⁸⁷

The court reasoned that the presence of this explicit standard demonstrated that Congress did not intend to impose a more stringent repayment standard when it imposed a general good faith requirement.⁸⁸ The court was not persuaded by the argument that the debtor would receive a windfall at the expense of his unsecured creditors if allowed to use a *de minimus* Chapter 13 repayment plan.⁸⁹ To the contrary, the court found that pending legislation in Congress, seeking to expand the definition of good faith to include a bona fide effort on the part of the debtor, demonstrated that Congress intended to deal with the ambiguity surrounding the good faith test of Chapter 13 without resorting to a substantial repayment requirement.⁹⁰

The *Goeb* court determined that requiring substantial repayment was contrary to the statutory language and intent, and that to impose a rigid requirement under the guise of interpreting good faith would be inadvisable given Congress' awareness of the confusion.⁹¹ The court also found that it would be more ap-

86. "Had Congress wished to require all Chapter 13 debtors to substantially repay unsecured creditors, it could have spoken explicitly." 675 F.2d at 1388.

87. 11 U.S.C. § 1325(a)(4) (1979) states that:

The court shall confirm a plan if . . . 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

88. 675 F.2d at 1388.

89. *Id.*

90. *Id.* at 1389. An excerpt of the House Report reads in part:

In short, the 'good faith' effort test looks to the present and future ability of the debtor to make payments into the Chapter 13 creditor's fund during the course of the plan, while the traditional 'good faith' test examines 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.

H.R. REP. NO. 1195, 96th Cong., 2d Sess. 24-25 (1980).

91. 675 F.2d at 1389.

propriate for Congress to specify the conditions for confirmation of Chapter 13 plans.⁹²

Having determined that the good faith requirement of section 1325 did not mandate substantial repayment to a Chapter 13 debtor's unsecured creditors, the court then outlined what findings must be made before deciding whether a Chapter 13 debtor acted in good faith. The court utilized a definition of good faith which the Supreme Court had construed under Chapter IX of the Chandler Act embodying principles of equity and good conscience.⁹³ The *Goeb* court found that, as a court of equity, it should determine whether debtors acted equitably in proposing their Chapter 13 plan, and did not seek to unfairly manipulate the bankruptcy code.⁹⁴ In determining the good faith of the debtor, substantiality of repayment is only one of a number of relevant considerations which must be weighed.⁹⁵

Considering the plan before it, the court found that the debtors had proposed their plan in good faith because it provided 100 percent payment to both secured *and* priority creditors which might not have occurred had the debtors gone through Chapter 7.⁹⁶ In addition, the unsecured creditors would have received nothing in a Chapter 7 proceeding, so a *de minimus* Chapter 13 repayment plan did not violate Chapter 13's intent.⁹⁷ Finally, the proposed plan did not leave any surplus to the debtors.⁹⁸

92. *Id.*

93. *Id.* at 1390. In *American United Mutual Ins. Co. v. City of Avon Park*, 311 U.S. 138 (1940) the Court interpreted a condition on the conformation of a plan under former Chapter IX that it be offered in good faith. In attempting to define what good faith was, the Court premised the determination with the general requirement that the debtor be able to qualify for equitable relief, since bankruptcy proceedings are an equitable remedy. This is basically the clean hands doctrine. *Id.* at 145.

94. 675 F.2d at 1390.

95. *Id.*

96. *Id.* at 1391.

97. *Id.*

98. *Id.* Contrast this result with the debtor in *Anderson*, *supra* notes 63-66 and accompanying text. That debtor had a great deal of surplus in assets after proposing his *de minimus* plan. Although not highlighted in *Goeb*, it is quite possible that those debtors not having any surplus after the provisions of the plan were implemented may have demonstrated sufficient good faith. After all, the thrust of the courts has been to follow Congress' intent in Chapter 13 plans, and Congress has stressed that each individual pay according to her ability. See *supra* note 90.

The court cautioned that *Goeb* was not a general endorsement of *de minimus* repayment plans under Chapter 13,⁹⁹ and that while this consideration is relevant to a showing of bad faith, it is not determinative.¹⁰⁰ A finding that the Chapter 13 debtor acted in bad faith cannot be made solely on the evidence of a *de minimus* repayment plan to her unsecured creditors.¹⁰¹ The *Goeb* court stressed that one must look at the totality of the circumstances of a particular debtor's situation before determining whether the debtor has proposed his Chapter 13 plan in good faith.¹⁰²

D. SIGNIFICANCE

The Ninth Circuit in *Goeb* rejected the interpretation that the good faith requirement mandates substantial repayment to a Chapter 13 debtor's unsecured creditors. The *Goeb* approach requires that the good faith inquiry be expanded beyond merely the amount of repayment, to include all relevant factors of a debtor's situation.¹⁰³ While this approach has merit, it ignores several factors.

First, although *Goeb* correctly pointed out that the term "good faith" was not defined by Congress,¹⁰⁴ the opinion did not discuss the legislative history which demonstrates Congress' intent to have Chapter 13 debtors repay a larger percentage of their debts than Chapter 7 debtors.¹⁰⁵ *Goeb* did not address the legislative history beyond the specific definition of good faith.¹⁰⁶

Second, *Goeb* found that pending legislation, which would add a "bona fide effort" condition to the section 1325(a) require-

99. 675 F.2d at 1391.

100. *Id.* The court criticized the bankruptcy court for concluding that the debtors had acted in bad faith primarily on their *de minimus* repayment plan. *Id.*

101. *Id.*

102. *Id.* "[B]ankruptcy courts cannot substitute a glance at the amount to be paid under the plan for a review of the totality of the circumstances." *Id.*

103. *Id.* at 1390. The court emphasized that the term "good faith" should be construed to include as many factors as possible. *Id.* at 1390 n.9.

104. *Id.* at 1390.

105. The House Report notes that creditor's losses under Chapter 13 "will be significantly less than if their debtors opt for straight bankruptcy." H.R. REP. NO. 595, 95th Cong., 1st Sess. 118, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5963, 6079.

106. "Congress did not specially define 'good faith', and the term by itself is sufficiently ambiguous to tolerate many interpretations . . . [W]e hesitate to infer from it an inflexible requirement like the one applied by the court below." 675 F.2d at 1388.

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ments for confirmation of a repayment plan,¹⁰⁷ evidences Congress' attempt to resolve the good faith quandary without having to resort to a substantial repayment requirement.¹⁰⁸ The term "bona fide effort" is as ambiguous as the term "good faith"; neither offers a quantifiable standard. *Goeb* found however that this addition would resolve the good faith-substantial repayment requirement controversy.¹⁰⁹ In any event, *Goeb* found it advisable to allow Congress to resolve the substantial repayment issue rather than impose a rigid interpretation of the good faith requirement.¹¹⁰

The *Goeb* opinion noted that Congress may have put the flexible good faith requirement into the code instead of a rigid repayment standard so that courts could adapt the confirmation requirements of section 1325(a) to meet the particular needs of debtors. The court concluded that good faith should be determined only after all factors have been considered in a particular debtor's situation.¹¹¹ While taking the totality of the debtor's situation into account, the court did not however, take all of Congress' intent into account, something which the bankruptcy courts did.¹¹²

The role of the good faith requirement in a Chapter 13 repayment plan has been altered by *Goeb* from a *de facto* requirement for substantial repayment to unsecured creditors into a broader, more diffuse requirement. The concern is that *Goeb* may have broadened the good faith requirement too far, thereby severely weakening it.

107. S. REP. No. 150, 97th Cong., 1st Sess. 18 (1981).

108. 675 F.2d at 1389.

109. *Id.* In support of its conclusion, the court cited to a report of the bill in which the Committee on the Judiciary noted that the good faith requirement was not meant to be construed as requiring substantial repayment, but the court then backed away from that authority by saying that that statement by a "handful of senators in a session three years after the passage of the Bankruptcy Code does not prove much." *Id.* at 1389 n.6.

110. 675 F.2d at 1389.

111. *Id.* at 1390.

112. See *supra* notes 49-75 and accompanying text. Therefore, while the various bankruptcy courts within the Ninth Circuit may have been too strict in requiring substantial repayment regardless of the debtor's situation, *Goeb* may go too far in the other direction by not considering Congress' desire to encourage repayment.

E. CONCLUSION

The Ninth Circuit in *Goeb* rejected the rigid interpretation of the good faith requirement as mandating substantial repayment to a debtor's unsecured creditors. While the bankruptcy courts within the Ninth Circuit may have been too strict in holding a Chapter 13 debtor to substantial repayment, *Goeb* has ignored the desire of Congress that Chapter 13 plans encourage a higher repayment percentage than straight bankruptcy. The result in *Goeb* may mean that Congress will have to legislate into the code a more quantifiable requirement for repayment in order to achieve its goal of substantial repayment under Chapter 13.

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