UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF MISSISSIPPI

IN RE:

EMILY LASHA COOPER, **CASE NO. 11-52095-KMS**

DEBTOR. **CHAPTER 13**

MEMORANDUM OPINION AND ORDER: (1) DENYING AMENDMENT OF PLAN, (2) DENYING CONFIRMATION OF PLAN, AND (3) CONDITIONALLY APPROVING SETTLEMENT ORDER

On July 2, 2012, there came on for hearing (the "Hearing") the Motion to Amend Plan (the "Motion to Amend") (Dkt. No. 47) filed by the Debtor, Emily LaSha Cooper (the "Debtor"), in the above-styled bankruptcy case.[1] There also came on for consideration: (1) the Order Approving Joint Motion for Authority to Settle and Compromise Disputed Claims and Issues (Dkt #37) (the "Settlement Order") (Dkt. No. 39), proposed by both the Debtor and Memorial Hospital at Gulfport ("MHG"), (2) the Amended Chapter 13 Plan (the "Amended Plan") (Dkt. No. 41), filed by the Debtor, and (3) the Letter Memorandum with Authorities (the "Memorandum") (Dkt. No. 54), submitted by MHG in support of the Motion to Amend. Having reviewed the pleadings and being fully advised in the premises, the Court finds for the reasons set forth below that: (1) the Motion to Amend should be denied, with leave to modify the Amended Plan consistent with this Opinion, (2) the Settlement Order should be approved, conditioned upon the amendment of the Amended Plan conforming to this Opinion, and (3) the confirmation of the Amended Plan, as currently proposed,

[1] On January 3, 2012, the issues surrounding the amendment and confirmation of the Debtor's payment plan were transferred to the undersigned. (Dkt. No. 28). The main case remains assigned to the Honorable Katharine M. Samson, United States Bankruptcy Judge.

should be denied.[2]

Jurisdiction

This Court has jurisdiction over the parties and the subject matter of this matter pursuant to 28 U.S.C. § 1334. This is a core proceeding pursuant to 28 U.S.C. §157(b)(2)(L). Notice of the Motion to Amend was proper under the circumstances.

Facts

The Debtor filed a voluntary petition for relief (the "Petition") (Dkt. No. 1) under chapter 13 of the Bankruptcy Code on September 9, 2011, simultaneously filing her proposed payment plan (the "Plan") (Dkt. No. 2) and bankruptcy schedules (Dkt. No. 4). In Schedule F, the Debtor listed $74,736.00 in total unsecured claims, including a debt to MHG in the amount of $3,516.00, and a total student loan debt of $11,422.00. The largest debt listed in Schedule F is a loan deficiency in the amount of $55,804.00, which the Debtor incurred following the foreclosure sale of her home.[3] In Schedule I, the Debtor listed average monthly income of $2,058.38, with payroll deductions of $523.72. Similarly, in the Chapter 13 Statement of Current Monthly Income and Calculation of Commitment Period and Disposable Income[4] ("Form B22C"), the Debtor listed current monthly

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[2] The following constitutes the findings of fact and conclusions of law of the Court pursuant to Federal Rules of Bankruptcy Procedure 7052.

[3] A proof of claim filed in this case indicates a "mortgage deficiency" of only $22,117.40. (Cl. 4-1).

[4] This calculation is known as the "Means Test," a two-step inquiry which determines whether a debtor has enough disposable income to fund a payment plan under chapter 13. 11 U.S.C. § 707(b)(2) as a matter of law. If so, the debtor's decision to file a chapter 7 petition is presumed to be an abuse of process, and the case may be dismissed or, with the debtor's consent, converted to a filing under chapter 13. *See* Bolen v. Adams, 403 B.R. 396 (N.D. Miss. 2009).

income of $2,222.10, and an annualized income of $26,665.20.[5] (Dkt. No. 6). In Schedule J, the Debtor listed $1,997.00 in average monthly expenses. When the expenses listed in Schedule J and the payroll deductions listed in Schedule I are added together, the sum is subtracted from the income listed in Form B22C, and then the difference is multiplied by 36, the Debtor's "disposable income," as defined in 11 U.S.C. § 1325(b)(2),[6] is negative $10,750.32.[7]

The Debtor is married and has three children. Given the size of her household, the Debtor's annualized income of $26,665.20 is well below the applicable median family income in Mississippi ($63,211.00) for purposes of § 1325(b)(3). Notably, the Debtor's below-median income rendered her eligible for chapter 7 relief under the "Means Test,"[8] except that she had previously received a discharge under chapter 7. (Case No. 04-53591-ERG, Dkt. No. 42). Because she had commenced that case "within 8 years before the date of the filing of the petition," she was not qualified for chapter 7 relief. *See* 11 U.S.C. § 727(a)(8).

Prior to filing the Petition, the Debtor's health insurer, Blue Cross/Blue Shield of Mississippi ("Blue Cross/Blue Shield"), issued two checks made payable to the Debtor in the combined amount of $24,760.18, representing payment for medical services provided the Debtor while she was a patient at MHG. Blue Cross/Blue Shield paid these benefits to the Debtor, rather than to MHG directly, because MHG was not a participant in the Debtor's health insurance plan.

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[5] $2,222.10 per month ×12 months $26,665.20 per year.

[6] Unless specifically noted otherwise, code sections hereinafter will refer to the United States Bankruptcy Code, located at Title 11 of the United States Code.

[7] $2,222.10 - ($1,997.00 + $523.72)   −$298.62. −$298.62 × 36   −$10,750.32.

[8] 11 U.S.C. § 707(b)(2)(A); *see supra* n.4.

When she was admitted as a patient at MHG on June 8, 2010, the Debtor signed an agreement acknowledging that she was supposed to send MHG any payment she received from Blue Cross/Blue Shield. (Dkt. No. 27). The agreement states, in pertinent part that "[t]o insure that your account balance(s) is properly credited, please send the payment and the explanation of benefits from your healthcare plan within 10 days of receipt to [MHG]." (Dkt. No. 27). In a letter dated March 15, 2011, MHG reminded the Debtor of her agreement to send the proceeds from the insurance benefit checks to MHG. (Dkt. No. 27). Instead, the Debtor endorsed the checks and did not forward the funds to MHG.

Initially, the Debtor proposed to pay into the Plan, *via* the chapter 13 trustee (the "Trustee"), $30.00 dollars twice each month (or $60.00 each month) for 36 months, the term of the Plan, for a total payment of $2,160.00. (Dkt. No. 2). The Plan proposed to pay the Debtor's attorney $1,914.00, the amount that remained due after the Debtor had already paid him $886.00, for a total attorney's fee of $2,800.00. The Plan would not pay anything to the general unsecured creditors, including MHG, whose debts would be discharged upon completion of the Plan, unless they were excepted by statute. 11 U.S.C. §1328. Thus, the Plan did not distinguish among any class of creditors. (Dkt. No. 2).

MHG filed the Objection to Confirmation of Chapter 13 Plan (the "Objection") (Dkt. No. 27) on December 30, 2011, alleging that the Debtor did not propose the Plan in good faith, as required under § 1325(a)(3). MHG accused the Debtor of filing her Petition in bad faith because MHG's debt "would be nondischargeable in a chapter 7 case under § 523(a)(2)(A) and/or

§ 523(a)(6)."[9] (Dkt. No. 27).

The Debtor did not file a written response to the Objection. Rather, the Debtor and MHG resolved their dispute and together on February 29, 2012, filed a Joint Motion for Authority to Settle and Compromise Disputed Claims and Issues (the "Settlement Motion") (Dkt. No. 37). No objection was filed to the Settlement Motion. The parties then submitted for the Court's review and approval the Settlement Order. In the Settlement Order, the Debtor agreed to amend her Plan to include the following provisions, as set forth below in pertinent part:

> 1. The Debtor will agree to the entry of a judgment confirming that MHG's claim in the amount of $24,760.18[10] constitutes a nondischargeable debt.
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> 2. The Debtor will amend the Plan so that it will pay MHG $120.00 per month for 36 months.
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> 3. Within 30 days after completion of the amended plan, or upon dismissal of the case, whichever comes first, the Debtor will begin paying $120.00 per month directly to MHG until the amount of $24,760.18 has been paid in full.
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> 4. Once the case is dismissed or closed, or once the amended plan is completed, MHG may enroll a judgment in the amount of the remaining balance in the judgment rolls of any county in which the Debtor does, or may later own land. Thereafter, if the Debtor defaults on her payments, MHG may pursue its normal collection remedies as provided by Mississippi law for the remaining balance due.

(Dkt. No. 39)

Consistent with the proposed Settlement Order, the Debtor filed the Amended Plan on April 11, 2012. The Amended Plan classifies and treats MHG's claim differently from all other unsecured

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[9] Section 523 renders certain debts nondischargeable, including any debt obtained by "false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition" under § 523(a)(2)(A), and any debt for "willful and malicious injury by the debtor" under § 523(a)(6).

[10] This amount is less than the amount shown in the proof of claim filed by MHG (Cl. 7-1) but is considerably more than the amount shown in Schedule F by the Debtor. (Dkt. No. 4).

claims, including the student loan claim. Notably, the MHG claim and the student loan claim[11] are the only apparently nondischargeable claims. (Dkt. No. 41). In the Amended Plan, the Debtor proposes to pay the Trustee $96.21 twice per month (or $192.42 each month), resulting in total plan payments of $6,927.12. Included in this amount is the monthly payment of $120.00, which she negotiated with MHG.

Shortly after filing the Amended Plan, the Debtor filed the Motion to Amend in which she seeks approval from the Court to amend her Plan to implement the settlement she reached with MHG. (Dkt. No. 47). All creditors and parties of interest were provided proper notice of the Amended Plan, Settlement Order, and Motion to Amend. (Dkt. No. 43). No objection was filed. At the Hearing, the Trustee expressed his approval of the favorable treatment of MHG in the Amended Plan, absent an objection from any creditor.

At the end of a hearing on the Settlement Order on April 30, 2012, the Court instructed MHG to submit a brief addressing the issue of whether the Amended Plan discriminated unfairly among the class of unsecured creditors. MHG submitted the Memorandum on May 29, 2012. No other brief was filed. The Hearing took place on July 2, 2012.

Discussion

MHG contends that the classification and treatment of its claim differently from the claims of other unsecured creditors is not unfair discrimination under § 1322(b)(1), and therefore, the Motion to Amend should be granted. (Dkt. No. 54). MHG further argues that the Debtor could not

[11] Congress amended the Code in 1990 so that debts incurred as a result of student loans are presumptively excepted from discharge in a chapter 13 case unless the debtor demonstrates that the failure to discharge that debt would impose an "undue hardship" on the debtor and the debtor's dependents. 11 U.S.C. § 1328(a)(2).

propose a payment plan that did not separately classify and treat its claim without violating the good faith provision in § 1325(a)(3). (Dkt. No. 54). In support of this latter argument, MHG asserts that its claim is nondischargeable because the Debtor's purported conversion of the insurance benefits constituted a criminal offense[12] and so "providing different treatment on this claim has an extremely rational basis." (Dkt. No. 54).

Section 1322 lists the permissible and necessary contents of a confirmable chapter 13 plan. 11 U.S.C. § 1322. Section 1322(b)(1) states that a plan may "designate a class or classes of unsecured claims, as provided in section 1122." 11 U.S.C. § 1322(b)(1). Section 1122(a), in turn, states that claims that are "substantially similar" may be grouped together in the same class. 11 U.S.C. § 1122(a). With respect to any such designated class of unsecured claims, however, § 1322(b) prohibits unfair discrimination. Because the Amended Plan provides for differing payments to separate classes of unsecured claims, the Debtor has the burden of demonstrating by a preponderance of the evidence that the proposed classification in the Amended Plan does not discriminate unfairly in violation of § 1322(b).

Before turning to the unfair discrimination analysis, the Court pauses here to address the procedural posture of the Motion to Amend and Settlement Motion. Neither the Trustee nor any creditor objected to the proposed amendment of the Plan. Notwithstanding the absence of an objection, the Court has the authority, and even the obligation, to deny confirmation of any proposed plan that does not conform to the requirements of the Code. United Student Aid Funds, Inc. v.

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[12] Section 1328 of the Code mandates that a "court shall grant the debtor a discharge of all debts provided for by the plan . . . except any debt . . . (2) of the kind specified in . . . paragraph (1)(B), (1)(C), (2), (3), (4), (5), (8), or (9) of section 523(a)." 11 U.S.C. § 1328(a)(2). MHG maintains that the Debtor's conduct in this case falls under § 523(a)(2)(A) and/or § 523(a)(6).

Espinosa,130 S. Ct. 1367, 1380-81 (2010).

A. Unfair Discrimination

The separate classification of claims is permissible under § 1322(b)(1) in some circumstances. Mickelson v. Leser (In re Leser), 939 F.2d 669, 671 (8th Cir. 1991). However, there is no controlling precedent that addresses the facts presented here. Although discrimination that is based solely on the nondischargeability of a claim is generally considered to be unfair, there is no provision in the Code that defines the parameters of fairness in the context of nondischargeable debts. This Court has noted in a previous decision that the Fifth Circuit Court of Appeals has "provide[d] guidance regarding unfair discrimination in general." In re Taylor, 2011 WL 4962946, No. 11-02007-NPO, at *2 (Bankr. S.D. Miss. Oct. 19, 2011). Of particular interest are two Fifth Circuit cases which have applied the unfair discrimination test to the preferential treatment of cosigned consumer debt. Also of particular interest are three recent bankruptcy cases that have applied the unfair discrimination test to the favored treatment of student loan debt. Although none of these cases is directly applicable, they are helpful to the Court's analysis.

1. Cosigned Consumer Debt

The Fifth Circuit in Chacon v. Bracher (In re Chacon), 202 F.3d 725 (5th Cir. 1999), considered whether § 1322(b)(1) exempted cosigned consumer debt from the unfair discrimination test. Section 1322(b)(1) was amended in 1984 specifically to permit a debtor to treat consumer claims differently when an individual is jointly liable with the debtor on that debt. After finding no ambiguity in the language of § 1322(b)(1), the Fifth Circuit noted that "[i]f a cosigned debt could be prioritized only if it does not discriminate, then the 'however' clause serves no purpose whatsoever." Chacon, 202 F.3d at 726. The Fifth Circuit concluded that "[d]ifferences in treatment are not discriminatory if they rationally further a legitimate interest of the debtor and do not disproportionately benefit the cosigner, *e.g.* by reimbursing interest where none is due or reimbursing more than the actual amount of the cosigned debt." Id.

The debtor in Chacon proposed to pay the cosigned debt in full, with 12% interest, before any distributions were made to the general unsecured creditor class. The Fifth Circuit denied the confirmation of the plan because the debtor presented no evidence or justification for the "high and preferential interest rate." Id. at 726-27.

The Fifth Circuit revisited the issue in In re Ramirez, 204 F.3d 595 (5th Cir. 2000). There, the debtor proposed a plan to repay a cosigned loan in the amount of $844.00 plus 12% interest. Once the debt was paid in full, after 33 months, the trustee would begin distributing plan payments to the debtor's general unsecured creditors, whose overall payment was approximately 20%. If the money designated for paying the cosigned consumer debt and interest were distributed equally among all the unsecured creditors, the distribution would increase by 5%. Id. at 596. The Fifth Circuit recognized that the facts of Ramirez were analogous to those in Chacon both cases involved plans in which the debtors proposed to pay cosigned consumer debts in full with 12% interest. As a result, the Fifth Circuit denied the confirmation of the plan because "In re Chacon is controlling." Id.

2. Student Loan Debt

More recently, other bankruptcy courts in the Fifth Circuit have considered whether a chapter 13 debtor may treat student loan debt preferentially. In particular, there is articulate and thoughtful discussion of this issue in three recent bankruptcy cases. First, in In re Simmons, 288 B.R. 737 (Bankr. N.D. Tex. 2003), the bankruptcy court reviewed four plans for confirmation, each of which treated student loan debt more favorably than all other general unsecured debt. The chart below summarizes the distributions proposed in three of the four plans, and the expected distributions to all creditors if the proposed plan did not distinguish between the student loan creditors and general unsecured creditors.

Plans	**General Unsecured**	**Student Loan**	**All Unsecured**
Shockey Plan	0.00%	100.00%	36.00%
Bruchey/Crnkovic Plan	6.35%	65.50%	11.70%
Goodwin Plan	0.00%	100.00%	16.30%

Id. at 741-42. On the issue of plan confirmation, the Simmons court concluded that: (1) the Shockey Plan constituted unfair discrimination because $8,440.14 in disposable income remained for distribution to unsecured creditors but was paid only to student loan creditors; (2) the Bruchey/Crnkovic Plan constituted unfair discrimination because $9,451.20 in disposable income remained for distribution to unsecured creditors, but of that total, $7,577.84 was allocated to student loan debt; and (3) the Goodwin Plan did not constitute unfair discrimination because the debtor proposed to pay the student loan creditor from income above and beyond her disposable income. Id. at 754-57.

The main issue addressed by the court in Simmons was whether the Code prohibited "chapter 13 debtors from separately classifying and preferentially treating nondischargable student loan obligations." Id. To determine the definition of "unfair discrimination," the bankruptcy court examined the legislative history, then applied principles of statutory construction, concluding: "Had Congress intended to allow preferential treatment of nondischargeable claims of any sort surely [the sections] would have said so." Id. at 748. Thus, the court found that "the Code offers no exception that would permit a chapter 13 debtor to discriminate . . . in favor of a nondischargeable student loan to the detriment of other unsecured creditors." Id. at 749.

The Simmons court reviewed the various standards for unfair discrimination, including the standard set out in Chacon. Id. at 751. The bankruptcy court reasoned that Chacon and Ramirez established the following two-prong test for fair discrimination in treatment between classes: (1) the discrimination must serve a rational, legitimate purpose of the debtor; and (2) the discrimination may not over-favor the advantaged class. In order to translate the second element to unfair discrimination in general, the Simmons court reversed it so that "for discrimination to be fair, the amount to be received by the class discriminated against must not be less than the class would have been entitled to receive had there been no discrimination among classes." Id. Subsequently, the court concluded that a chapter 13 plan does not discriminate unfairly if: (1) the discrimination has a rational basis; and (2) the class discriminated against receives under the plan a return at least equal to what the class would have received if (a) there were no discrimination and (b) 36 months of the debtor's disposable income were applied to make payments under the plan.[13] Id. at 753.

The bankruptcy court's review of the Shockey Plan illustrates how the new two-prong test is applied. The Shockey Plan proposed to provide "pro rata payments to their student loan creditors beginning in the nineteenth month" of the plan, and not to pay any amount of their disposable income to their general unsecured creditors. Id. at 755. The Simmons court concluded that the Shockey Plan violated the prohibition against unfair discrimination in § 1322(b)(1) because it improperly proposed

[13] Conversely, class discrimination is unfair when the class discriminated against "receives less under a plan than it would have received, absent discrimination, if the plan dedicated to payments three years of the debtor's disposable income. A plan which does not discriminate [may be] confirmable . . . even if less than three years of disposable income is dedicated to plan payments." Simmons, 288 B.R. at 753.

to distribute to the student loan creditors more than their fair share of the available disposable income.

The second recent case that the Court finds helpful is In re Boscaccy, 442 B.R. 501, 503 (Bankr. N.D. Miss. 2010). There, the issue addressed by the bankruptcy court was whether to confirm a chapter 13 plan when a "plan proponent separately classifies an unsecured student loan debt and treats that debt more favorably than the claims of other general unsecured creditors." Boscaccy, 442 B.R. at 504. Three debtors in consolidated bankruptcy cases proposed to bring their student loan obligations current, which would also "necessitate greater payments to the student loan creditors than the payments proposed to the general unsecured creditor classes." Id. The debtors proposed to treat the student loans as long-term debt, which they argued they were explicitly allowed to do under § 1322(b)(5).[14] They also argued that § 1322(b)(5) rendered the unfair discrimination limitation in § 1322(b)(1) inapplicable.

Although the Boscaccy court believed that the classification of student loans as "nondischargable" indicated a congressional intent that such debts be paid, the court nevertheless concluded that the long-term debt provision in § 1322(b)(5) did not supersede the unfair discrimination provision in § 1322(b)(1). The court found that § 1322(b)(1) and § 1322(b)(5) must be read together and that a determination must be made in each case as to whether the proposed long-term treatment of student loan debt was unfair. Boscaccy, 442 B.R. at 509-11.

To determine whether the discrimination at issue was "unfair" under § 1322(b)(1), the Boscaccy court considered an array of various tests adopted by other courts. Id. at 508. The court

[14] Section 1322(b)(5) allows a debtor to cure a default and remain current on a debt when the last payment "is due after the date on which the final payment under the plan is due." 11 U.S.C. § 1322(b)(5).

twice mentioned the four-prong test set forth by the Eighth Circuit Court of Appeals in Leser, 939 F.2d at 672, which involved the preferential treatment of child support payments. The fairness of proposed discrimination in Leser was determined by whether: (1) the discrimination has a reasonable basis; (2) the debtor can carry out a plan without the discrimination; (3) the discrimination is proposed in good faith; and (4) the degree of discrimination is directly related to the basis or rationale for the discrimination. The bankruptcy court in Boscaccy also discussed a modified version of the four-prong test developed later in In re Gregg, 179 B.R. 828 (Bankr. E.D. Tex. 1995). In Gregg, the four prongs, as modified, were whether: (1) the discrimination has a reasonable basis; (2) such classification is necessary for the debtor's rehabilitation in a chapter 13 case; (3) the discrimination was proposed in good faith; and (4) the degree of differential treatment is directly related to the basis for the discrimination. Gregg, 179 B.R. at 830.

In the end, the Boscaccy court embraced the reasoning in In re Harding, 423 B.R. 569 (Bankr. S.D. Fla. 2010), which balanced three considerations: (1) the debtor's fresh start; (2) the clear legislative objective of debt's repayment; and (3) fair treatment of creditors as a whole. Boscaccy, 442 B.R. at 512. Of the three chapter 13 plans reviewed in Boscaccy, the court determined that two were "fair," but that the third proposed plan did "indeed constitute unfair discrimination." Id. In one plan, a debtor proposed to pay $374.00 per month to maintain a student loan debt totaling $8,500.00, but proposed to pay the general unsecured class of creditors only $112.44 per month (providing the unsecured creditor class with a 10% distribution for claims totaling $40,497.00.) Id. If the $374.00 student loan payment were used to pay all unsecured creditors equally (including student loan creditors), each unsecured creditor would receive a 36% distribution, an increase of 26%. Nevertheless, the Boscaccy court concluded that if the debtor was not allowed to maintain the payments on their sizeable student loan debt, then "the debtor would emerge from bankruptcy, insofar as this nondischargable debt is concerned, in a much worse position than the debtor was in prior to filing." Id. at 511. Therefore, after balancing the considerations set forth in Harding, the court found that the discrimination was fair.

The third recent case that the Court finds helpful is In re King, 460 B.R. 708 (Bankr. N.D. Tex. 2011), in which the bankruptcy court considered whether a plan discriminated unfairly when the debtor agreed to pay student loan creditors $32,400.00 over the term of the plan but general unsecured creditors would each receive a pro rata share of $12,449.40. The court concluded that "the test set forth in Simmons is still appropriate," although two modifications were required because of changes to § 1325(b) made by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"), Pub. L. No. 109-8, 119 Stat. 23. First, interested parties should be aware that the "determination of projected disposable income under [BAPCPA] may make it more likely for a debtor to have truly disposable income in excess of the amount [the debtor] is required to contribute to the plan." King, 460 B.R. at 712. Second, the Simmons test indicates that "a plan does not discriminate unfairly if the class discriminated against receives no less than it would have received if there were no discrimination and [sixty] months (or [thirty-six] months for below-median income debtors) of the debtor's disposable income were applied to the plan." Id.

B. MHG's Debt

As demonstrated in the above discussion, courts have applied a variety of tests in determining whether the favorable treatment of a debt in a chapter 13 plan unfairly discriminates against other creditors. L. Sepinuck, Re-thinking Unfair Discrimination in Chapter 13, 74 AM. BANKR. L.J. 341, 351-60 (2000) (identifying five different tests used by courts to determine unfair discrimination).

The view previously held by this Court with regard to unfair discrimination has been to follow the guidelines set out by the Fifth Circuit in Chacon and Ramirez.[15] The Court finds that the standard used by the bankruptcy court in King faithfully adheres to that precedent.

In King, the standard (which modifies, but otherwise adopts, the test described in Simmons) is whether: (1) the discrimination has a rational basis; and (2) the class discriminated against receives no less than it would have received if there were no discrimination and 36 months of the debtor's disposable income were applied to the plan. King, 460 B.R. at 712-13. The court in King emphasized that post-BAPCPA a debtor can still contribute excess income "by committing to pay an amount higher than his or her projected disposable income." Id. at 712. This standard embraces the recent changes to § 1325 and the emphasis placed on a debtor's projected disposable income. The Court applies the two-prong standard in King to the facts here.

1. Rational Basis

The first prong of the King standard requires that the separate classification of MHG's debt serve a rational purpose. MHG argues that the favored treatment of its debt has a rational basis, in large part, because its debt is nondischargeable. MHG's argument would have greater weight if its debt were the only nondischargeable debt. However, the student loan debt, arguably, is "substantially similar" to MHG's debt because it, too, is probably nondischargeable. They are both of the same basic type. Yet, unlike the MHG debt, the student loan debt is not classified separately from the class of general unsecured creditors who would receive nothing in the Amended Plan.

MHG asserts that the reason behind the nondischargeability of its debt is sufficiently unique

[15] The Boscaccy court did not cite Chacon or Ramierz or any other authority from the Fifth Circuit but adopted the unfair discrimination analysis used in Harding, a decision rendered by the bankruptcy court in Florida. Boscaccy, 442 B.R. at 506-12.

so as to justify the difference in its treatment from the student loan debt. MHG points out that whereas its debt is nondischargeable based on the Debtor's unlawful conversion of the insurance benefits, the student loan debt is nondischargeable for reasons unrelated to the Debtor's conduct. As to this assertion, the Court notes that no evidence was presented at the Hearing that would support a finding of any criminal conduct by the Debtor but that the Debtor apparently concedes for purposes of settling MHG's objection to the Plan that MHG's debt is nondischargeable.

Some bankruptcy courts permit the separate classification of claims that result from criminal misconduct, based on the probability of the debtor's conviction and incarceration if the particular debt is not paid in full. *See, e.g.*, In re Etheridge, 297 B.R. 810, 816 (Bankr. M.D. Ala. 2003) (holding there was a rational basis for discrimination because "[f]ailure to [pay] would bring conviction and possible incarceration"). On the other hand, some bankruptcy courts view the separate classification of claims involving criminal misconduct as unfair because other unsecured creditors "pay the price" for the debtor's alleged wrongdoing. In re Cooper, No. 08-20973, 2009 WL 1110648 (Bankr. N.D. Tex. April 24, 2009). In that same vein, some bankruptcy courts have reasoned that fear of criminal prosecution is an insufficient basis for separate classification under a chapter 13 plan. In re Gallipo, 282 B.R. 917 (Bankr. E.D. Wash. 2002) (holding that favorable treatment of criminal shoplifting fines was unfair burden on the debtor's other creditors).

The probability of the Debtor's incarceration would have factored significantly into the unfair discrimination analysis except for MHG's acknowledgment that no criminal charges have been brought ("and none will be") against the Debtor. (Dkt. No. 54). There is just no reason to believe that if the Debtor does not pay MHG, she might lose her ability to earn income to fund the Amended Plan to the detriment of the Debtor, her dependents, and all of her creditors. The chances of that outcome is unlikely, as MHG recognizes.

The Court finds that the Debtor has not met her burden to show a rational basis for distinguishing between the Debtor's two nondischargeable debts. When the Court expressed this concern at the Hearing, counsel for the Debtor and counsel for MHG suggested as an alternative to the currently proposed Amended Plan that the Debtor be allowed to place the student loan debt and the MHG debt within the same class. If the Debtor modifies the Amended Plan in this way, then the Court would find a rational basis for the separate treatment and the new plan would satisfy the first prong of the § 1322(b) standard, as interpreted in King.

2. Disposable Income

Turning to the second prong of the King standard, the Debtor must show that the general unsecured creditors (owed $74,736.00, including MHG's debt of $3,516.00 and the student loan debt) would receive no less than they would have received if there were no discrimination in favor of MHG and 36 months of the Debtor's disposable income were applied to the Amended Plan. Under the first Plan, where there is no discrimination among the unsecured creditor class, the Debtor proposed to pay the Trustee $60.00 per month or a total of $2,160.00 over a period of 36 months. After fees are paid to the Trustee[16] and the Debtor's attorney, almost nothing would remain to be distributed pro rata to all unsecured creditors for payment of a total debt of $99,496.18 (if the debt to MHG of $24,760.18 is combined with the debt to the other unsecured debtors) or $74,736.00 (if it is not).

Under the Amended Plan, the Debtor would pay the Trustee $192.42 per month or $6,927.12

[16] A standing chapter 13 trustee may collect a percentage fee that is not more than 10% (although the actual percentage is set by the U.S. Attorney General and may be less than 10%) from all payments received under the plan. 28 U.S.C. § 586(e).

over a period of 36 months. After fees are paid to the Trustee and the Debtor's attorney and after the payments to MHG ($120.00 × 36 $4,320.00) are made, almost nothing would remain. A comparison of the treatment of the unsecured creditor class in the Plan and Amended Plan shows no substantial change. Stated simply, the general unsecured creditors are not better off in the initial Plan as they would be in the Amended Plan.

Next, application of the second prong of the King standard requires the Court to calculate the Debtor's projected disposable income. Under § 1325(b)(2), "disposable income" is calculated by deducting from the debtor's current monthly income "amounts reasonably necessary to be expended . . . for the maintenance or support of the debtor or a dependent of the debtor." 11 U.S.C. § 1325(b)(2). "Projected disposable income" is calculated based on both debtor's circumstances as of confirmation, and on "changes in the debtor's income or expenses that are known or virtually certain at the time of confirmation." Hamilton v. Lanning, 130 S. Ct. 2464, 2478 (2010).

The Debtor in this case is a below-median income debtor who has a negative disposable income of $10,750.32 for the duration of the Amended Plan. There is no indication that this calculation requires any adjustment to account for changed circumstances. This means that the Debtor does not have a statutory minimum payment to unsecured creditors and has met the second prong of the King standard.

3. Good Faith Plan Proposal

At the Hearing and in its Memorandum, MHG focused its arguments on whether the Debtor proposed her initial Plan in good faith under § 1325(a)(3),[17] which governs the requisites for plan

[17] Section 1325(a)(3) states, in pertinent part, that the court shall confirm a plan if "the plan has been proposed in good faith and not by any means forbidden by law." 11 U.S.C. § 1325

confirmation. In Public Finance Corp. v. Freeman, 712 F.2d 219, 221 (5th Cir. 1983), the Fifth Circuit rejected the argument that the good faith analysis in § 1325(a)(3) required the debtor to pay more to unsecured creditors than the minimum payment prescribed in § 1325(a)(4). There, the Fifth Circuit adopted a "totality of the circumstances" analysis for determining when a chapter 13 plan has been filed in good faith.

MHG contends in is Memorandum that "proposing to repay nothing on this debt would constitute a lack of good faith as required by Section 1325(a)(3) and should be the basis for denial of confirmation of the plan." (Dkt. No. 54). To support its argument, MHG points out that the debt would be nondischargeable in a chapter 7 case under § 523(a)(2)(A) and/or § 523(a)(6).

There is a difference between the discharge provisions in chapter 7 and chapter 13 cases. The discharge of debts in chapter 13 cases is much broader. Thus, the discharge of an obligation under chapter 13 when the same obligation would be nondischargeable under chapter 7 has been considered a relevant factor in the § 1325(a) good faith inquiry. *See* Public Fin., 712 F.2d at 221.

The facts here, however, do not warrant an inference of bad faith because MHG's debt is also excepted from discharge under chapter 13. Although § 523(a)(6) applies only in chapter 7 cases, § 523(a)(2)(A) applies in both chapter 7 and chapter 13 cases. 11 U.S.C. § 1328. Presumably, the Debtor could not have avoided the nondischargeability of MHG's debt by filing the Petition under chapter 13. More important, she could not have deliberately chosen chapter 13 relief over chapter 7 relief because she could not have obtained relief under chapter 7 given her prior discharge.

Finally, a cursory review of the Debtor's schedules shows that her lifestyle is modest. She is married with three children. She is the sole source of income for her family. She drives a 2006 Ford Explorer XLT with a listed value of $10,980.00. Most of her unsecured debt consists of a loan deficiency following the foreclosure sale of her home. Her other unsecured debt is owed to medical providers, student loan creditors, and credit card companies. She rents her current residence for only about $650.00 per month. Given the "totality of the circumstances," the Court finds no hint of bad faith in her proposal of the Amended Plan.

Conclusion

The Court concludes that the Debtor has not satisfied the requirements of § 1322 and, therefore, that the Motion to Amend should be denied on the ground that the Debtor has not shown a rational basis for classifying the MHG debt differently from the student loan debt. This conclusion should not be interpreted as requiring all chapter 13 plans to treat nondischargeable debt the same. Under these facts, the Court finds no significant difference to justify the difference in treatment between the two nondischargeable claims.

The Court further concludes that the Debtor and MHG that the unsecured creditors are no worse off under the proposed Amended Plan than if there were no discrimination and 36 months of the Debtor's disposable income were applied to the Amended Plan. After all, the Debtor proposes to pay an amount higher than her negative projected disposable income, which the Debtor may do without violating § 1322(b)(1)'s prohibition against unfair discrimination. *See* King, 460 B.R. at 712.

Based on the facts presented in this particular case, the Court denies the Motion to Amend with leave to amend the Plan on the condition the amendment proposes the same treatment of the MHG debt and student loan debt. The Court instructs the Debtor to file another amended chapter 13 plan by August 17, 2012. Moreover, the Court approves the Settlement Order on the condition that the amendment of the Plan conforms to this Opinion. Finally, the Court denies confirmation of the Amended Plan, as currently proposed. A separate final judgment will be entered in accordance with Federal Rule of Bankruptcy Procedure 7058.

SO ORDERED.

Neil P. Olack
United States Bankruptcy Judge
Dated: August 3, 2012