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UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF WASHINGTON

In Re:)	
)	No. 97-06242-W11
STEPHENS, JACKIE E.,)	
)	MEMORANDUM DECISION RE:
Debtor.)	CREDITOR MARIAH WOLFF'S
)	MOTION TO DISMISS FOR BAD
)	FAITH

THIS MATTER came on for hearing before the Honorable Patricia C. Williams on August 26, 1999 upon creditor Mariah Wolff's Motion to Dismiss for Bad Faith and Motion for Appointment of Examiner. The debtor was represented by Dan O'Rourke; creditor Mariah Wolff was represented by Victoria Vreeland; and Robert D. Miller, the Assistant United States Trustee, was present. The court reviewed the files and records herein, heard argument of counsel and was fully advised in the premises. The court now enters its Memorandum Decision.

Creditor Wolff filed a motion under 11 U.S.C. § 1307(c) to dismiss the case for cause and in the alternative to appoint an examiner under 11 U.S.C. § 1104(c). Creditor Wolff in her Motion to Dismiss for cause cites to 11 U.S.C. § 1307(c) which applies to petitions filed under Chapter 13. Although this petition was originally filed as a Chapter 13, the case was converted to a Chapter 11 on September 8, 1998. The applicable Code section for

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TS. MCGREGOR, CLERK
U.S. BANKRUPTCY COURT
EASTERN DISTRICT OF WASHINGTON

MEMORANDUM DECISION RE: . . . - 1

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1 dismissal for cause in Chapter 11's is 11 U.S.C. § 1112(b). The
2 court will address creditor Wolff's motion pursuant to the
3 applicable statute.

4 Section 1112(b) of the Bankruptcy Code provides that "on
5 request of a party in interest . . . and after notice and a
6 hearing, the court may . . . dismiss a case under this chapter . .
7 . for cause. . . ." Although bad faith is not expressly mentioned,
8 it has been incorporated into the section by judicial
9 interpretation. See *In re Thirtieth Place, Inc.*, 30 B.R. 503, 505
10 (9th Cir. BAP (Ariz.) 1983); *Matter of Little Creek Dev. Co.*, 779
11 F.2d 1068, 1071 (5th Cir. (Tex.) 1986); *In re HBA East, Inc.*, 87
12 B.R. 248, 258 (Bankr. E.D.N.Y. 1988). The requesting party is not
13 required to show malice in a challenge for bad faith. *In re*
14 *Southern Cal. Sound Sys., Inc.*, 69 B.R. 893, 901 n. 2 (Bankr. S.D.
15 Cal. 1987). The party is merely required to show that the case was
16 filed "for a purpose other than that sanctioned by the Bankruptcy
17 Code." *Id.*

18 "The existence of good faith depends on an amalgam of factors
19 and not upon a specific fact. The test is whether a debtor is
20 attempting to deter and harass creditors or attempting a speedy,
21 efficient reorganization on a feasible basis." *In re Marsch*, 36
22 F.3d 825, 828 (9th Cir. 1994). Once a movant establishes the
23 existence of a genuine issue concerning the debtor's lack of good
24 faith, the debtor then bears the burden of proving good faith by a
25 preponderance of the evidence. See *In re Setzer*, 47 B.R. 340, 345
26 (Bankr. E.D.N.Y. 1985); *In re Yukon Enterprises, Inc.*, 39 B.R. 919,
27 921-22 (Bankr. C.D. Cal. 1984); *In re Spenard Ventures, Inc.*, 18
28 B.R. 164, 166 (Bankr. D. Alaska 1982).

1 The courts have considered lists of factors typically present
2 in bad faith filings. The most influential list is found in the
3 *Matter of Little Creek Development Co., supra.*

4 Several, but not all, of the following conditions usually
5 exist. The debtor has one asset, such as a tract of
6 undeveloped or developed real property. The secured
7 creditors' liens encumber this tract. There are
8 generally no employees except for the principals, little
9 or no cash flow, and no available sources of income to
10 sustain a plan of reorganization or to make adequate
11 protection payments pursuant to 11 U.S.C. §§ 361,
12 362(d)(1), 363(e), or 364(d)(1). Typically, there are
13 only a few, if any, unsecured creditors whose claims are
14 relatively small. The property has usually been posted
15 for foreclosure because of arrearages on the debt and the
16 debtor has been unsuccessful in defending actions against
17 the foreclosure in state court. Alternatively, the
18 debtor and one creditor may have proceeded to a stand-
19 still in state court litigation, and the debtor has lost
20 or has been required to post a bond which it cannot
21 afford. Bankruptcy offers the only possibility of
22 forestalling loss of the property. There are sometimes
23 allegations of wrongdoing by the debtor or its
24 principals. The 'new debtor syndrome,' in which a one-
25 asset entity has been created or revitalized on the eve
26 of foreclosure to isolate the insolvent property and its
27 creditors, exemplifies, although it does not uniquely
28 categorize, bad faith cases.

17 Resort to the protection of the bankruptcy laws is not
18 proper under these circumstances because there is no
19 going concern to preserve, there are no employees to
20 protect, and there is no hope of rehabilitation, except
21 according to the debtor's 'terminal euphoria.'

20 *Matter of Little Creek Development Co., supra*, at 1073 (5th Cir.
21 1986).

22 Many types of factual situations have lead to allegations of
23 bad faith. *In re Karum Group, Inc.*, 66 B.R. 436 (Bankr. W.D. Wa.
24 1986), determined that commencement of a reorganization proceeding
25 solely to avoid the state law requirement of filing a supercedes
26 bond constituted bad faith. *Southern Cal Sound Systems, supra*,
27 determined that commencement of a reorganization proceeding solely
28 for the purpose of rejecting an executory contract constituted bad

1 faith.

2 The Ninth Circuit held that if the purpose of the filing was
3 not consistent with the purpose and spirit of the Bankruptcy Code,
4 then cause exists to dismiss the Chapter 11.

5 The term 'good faith' is somewhat misleading. Though it
6 suggests that the debtor's subjective intent is
7 determinative, this is not the case. Instead, the 'good
8 faith' filing requirement encompasses several, distinct
9 equitable limitations that courts have placed on Chapter
10 11 filings. [Cite deleted] Courts have implied such
11 limitations to deter filings that seek to achieve
12 objectives outside the legitimate scope of the bankruptcy
13 laws. . . . Pursuant to 11 U.S.C. § 1112(b), courts have
14 dismissed cases filed for a variety of tactical reasons
15 unrelated to reorganization. While the case law refers
16 to these dismissals as dismissals for 'bad faith' filing,
17 it is probably more accurate in light of the precise
18 language of section 1112(b) to call them dismissal 'for
19 cause.'

20 *Marsch, supra*, at 827 (9th Cir. 1994).

21 This proceeding was commenced on November 14, 1997 as a
22 Chapter 13. After a hearing on creditor's Motion to Dismiss on the
23 basis of eligibility, on August 7, 1998 the court determined that
24 the debtor was ineligible for Chapter 13 relief and on September 8,
25 1998 the debtor converted to a Chapter 11 proceeding. By agreement
26 of the parties, testimony for this hearing was submitted in
27 deposition form. The following factual conclusions result from the
28 review of the deposition testimony cited by the parties. The court
has accepted all the debtor's deposition testimony as true.

29 Creditor Wolff, pursuant to her state court lawsuit, entered
30 into a settlement agreement with the debtor in July 28, 1995 by
31 which the debtor was to pay creditor Wolff \$300,000 by February 15,
32 1996. [Exhibit 2]. Most of the payments were to occur upon the
33 sale of real estate listed by the debtor in his contemporaneous
34 affidavit. [Exhibit 3]. In that affidavit, the debtor also

1 represented that the list of real estate comprised all of his
2 holdings and that he had no expectation of financial gain from any
3 partnership, financial arrangement or contract except those listed.
4 Debtor was to execute contemporaneous Deeds of Trust in favor of
5 creditor Wolff on certain listed real estate. Eventually the
6 settlement agreement was reduced to judgment.

7 Debtor did not provide the Deeds of Trust until August 26,
8 1995. Meanwhile, he had sold his principal residence to his
9 girlfriend Ms. Paulus on August 25, 1995 (in which they both still
10 reside) and received \$34,935 cash proceeds. On July 17, 1995, he
11 sold the 14th Avenue rental property to Ms. Paulus and received
12 \$14,612 cash proceeds. Statement of Affairs. Pursuant to an
13 option agreement dated June 30, 1995, he sold the Montana property
14 on May 20, 1996 which property was not listed in the affidavit
15 (Exhibit 3). [Stephens Depo. of 2/27/98, p. 136. All references
16 are to this deposition unless otherwise noted.] The bankruptcy
17 schedules list an unimproved parcel in Ohio owned by the debtor for
18 several years having a value of \$10,000. This parcel was not
19 listed in the affidavit.

20 Debtor argues that even assuming these actions violated the
21 agreement between him and the creditor, those actions took place
22 more than two years before the commencement of this proceeding and
23 are not relevant to the question of whether the debtor commenced
24 this bankruptcy proceeding in bad faith. Such historical course of
25 conduct by the debtor is relevant. The question of whether the
26 debtor commenced this proceeding in order to effect a meaningful
27 reorganization must necessarily place great emphasis on events and
28 conditions immediately before and during the proceeding. A debtor

1 may have a history of engaging in improper conduct and yet change
2 that course of conduct and commence a bankruptcy proceeding and
3 successfully reorganize his financial affairs. However, that past
4 improper conduct is relevant in considering the debtor's purpose in
5 commencing the proceeding and the likelihood of a successful
6 reorganization.

7 By the time of the bankruptcy filing, several of the
8 properties referenced in the settlement agreement had been sold
9 with some of the proceeds paid to creditor Wolff. The Statement of
10 Affairs indicates that from the sale of property, the debtor
11 received \$49,728 in 1995; \$49,728 in 1996 and \$58,440 in 1997.
12 Schedule "A" indicates that the debtor still retained a four plex,
13 a duplex and a rental home all of which were encumbered by creditor
14 Wolff's Deed of Trust.¹ According to the Statement of Affairs, the
15 debtor received rental income, net of expenses, of approximately
16 \$12,000 in 1996 and approximately \$10,000 in 1997. The debtor's
17 Schedule "I" and the operating statements do not indicate if any
18 rental income was received during the pendency of the proceeding.

19 This proceeding is clearly a continuation of the battle
20 between the debtor and creditor Wolff (since July, 1995 there have
21 been state court supplemental proceedings, writs of garnishment and
22 threats of fraudulent transfer actions). There are six unsecured
23 creditors in addition to creditor Wolff on the debtor's schedules
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26 ¹One property has been listed for sale since October, 1995
27 with the same realtor who purchased the Montana property. As no
28 motion to approve sale has even been filed, it appears this
property still has not yet been sold although the debtor stated he
"has no complaints" concerning the realtor. [Stephens Depo., p.
124.]

1 and the total owed those six creditors is \$14,089. This consists
2 of two credit cards, the debtor's lawyer and accountant, a utility
3 and Mrs./Mr. Gatten, the owner of the corporation which
4 occasionally employs the debtor. Mr. Gatten is also the individual
5 to whom the debtor transferred a boat in January, 1997 in partial
6 payment of a debt. Statement of Affairs. The debtor testified
7 that he will be paying the accountant as soon as he is able
8 [Stephens Depo., p. 154] and will be paying an obligation to
9 another corporation owned by Mr./Mrs. Gatten. That obligation
10 relates to the fact that this unrelated corporation for some
11 unexplained reason has been providing insurance benefits for the
12 debtor through North American Insurance and the debtor believes he
13 must repay and intends to repay those premiums. [Stephens Depo., p.
14 155]. Neither the unrelated corporation or North American
15 Insurance were listed on the schedules.

16 In order to determine whether the true purpose of this
17 bankruptcy proceeding was to reorganize a financially distressed
18 business, the pre-petition and post-petition operation of that
19 business must be examined. The debtor's business activities
20 generally fall into three categories: 1) the rental of and
21 investment in real property; 2) performing geological consulting
22 work; and 3) acting as an officer and employer of a corporation.
23 In addition to the rental of real property describe above, the
24 debtor is the president of the corporation Blue Ridge which is
25 owned by Mr./Mrs. Gatten. [Williams 9/25/97 Depo., p. 6]. In the
26 past 4 to 5 years, he has received compensation of at least \$30,000
27 a year and the debtor sets his own salary. [Stephens Depo. of
28 1/3/97, p. 15]. In early 1997 when creditor Wolff issued a writ of

1 garnishment to Blue Ridge, the debtor elected to do no more work
2 for that corporation but started again once he filed bankruptcy.
3 [Stephens Depo., p. 107]. During 1997 he received total
4 compensation from Blue Ridge of \$4,500. Ms. Paulus is the office
5 manager for Blue Ridge which has two additional employees. The
6 only evidence in the record other than the monthly operating
7 statements (which will be addressed later) of post-petition
8 compensation received from Blue Ridge is debtor's testimony that
9 during the first two months of 1998 he received \$6,500. [Stephens
10 Depo., pp. 81-82].

11 The debtor also provides consulting services as a geologist
12 through his wholly owned corporation Jackie Stevens & Associates,
13 Inc. On February 27, 1998, he testified he was working 20 hours a
14 week for "himself" and working for Maya Gold. He did not remember
15 a single entity or person to whom he personally provided consulting
16 services in 1997. [Stephens Depo., pp. 37-38]. Nor did he know if
17 he had any records which would reflect such consulting service nor
18 did he know if Jackie Stevens & Associates filed tax returns or had
19 income.² Later he stated it was "probably true" he had no
20

21 ²The debtor testified in his deposition on February 27, 1998
22 on page 39, lines 3-15 as follows:

23 Q: In 1997, for whom did you provide personal consulting
24 services?
25 A: I don't know.
26 Q: You don't know?
27 A: No.
28 Q: You don't remember one entity or person you provided
personal consulting services for in 1997?
A: No. That doesn't mean I didn't.
Q: Do you have any documents that would reflect for whom you
provided consulting servicing as Jackie E. Stephens or
Jackie E. Stephens & Associates, Inc., in 1997?
A: I don't know.

1 consulting income from 1994 through 1997. [Stephens Depo., p. 160].
2 The debtor's other business is referred to as "Maya Gold".³
3 The debtor testified that it is a Honduras corporation. [Stephens
4 Depo., p. 6]. Generally the debtor performs geologic exploration
5 work for it. He owns 10% of the corporation but did not remember
6 how much cash capital he contributed, if any, but indicated that
7 his contribution was work which he contributed from "time to time."
8 [Stephens Depo., p. 46]. He testified that Maya Gold was
9 incorporated in 1997 and that he is the president. It has no
10 employees. It has a bank account in Honduras on which the debtor
11 is the only signatory. [Stephens Depo., pp. 47-48]. The other two
12 owners of Maya Gold live in Costa Rica. Essentially, the debtor
13 contacts these other two individuals and asks them to put money
14 into the Maya Gold account. He then travels to Honduras and takes
15 the money out of the account. [Stephens Depo., p. 67]. He thinks
16 these two individuals have collectively contributed about \$75,000
17 to Maya Gold, [Stephens Depo., p. 165] but that there is no
18 understanding when they will stop contributing or what
19 circumstances would cause them to stop contributing. There is no
20 written agreement among the owners. [Stephens Depo., pp. 52-53].
21 The debtor testified that he is to be paid \$350 day for each day he
22 prospects for Maya Gold and that the purpose of the contributions
23 made by the other owners is to pay for the prospecting. He
24 determines how often and when he travels to Central America and how

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28 ³Blue Ridge, Maya Gold and Jackie Stevens & Associates all
have the same business address.

1 Honduras in an amount he determines and then returns to Spokane
2 with the cash. [Stephens Depo., pp. 55-57].

3 The Statement of Affairs reflects that in 1997 he received
4 \$44,000 from Maya Gold. His Schedule "I" indicates that he is
5 employed by Maya Gold for \$5,000 a month.

6 The debtor pre-petition had no checking account and all funds
7 received from Maya Gold or other income were kept "in my pocket."⁵
8 Monthly checks representing proceeds from a real estate contract
9 were taken to various banks and cashed. [Stephens Depo., p. 94].
10 In response to questions about the use of income or proceeds from
11 the sale of property to purchase assets, the debtor consistently
12 maintains that the funds were used for "general things" and
13 "survival" which the court interprets to mean living expenses. The
14 debtor produced no records to demonstrate the use of the 1995 or
15 1996 income of \$99,556 each year or the 1997 income of \$106,880.⁶

16 As to post-petition income, the only evidence is the debtor's
17 operating statements. On February 16, 1999, the debtor filed an
18 operating statement for September, 1998 (when the case was converted

19
20 ⁵The debtor testified in his deposition held on February 27,
20 1998 at page 67, lines 13-22, the following:

21 Q: In your trips to Honduras to get paid and you have the
22 cash and you come back to the U.S., have you - what have
23 you done with the cash that you have been paid from Maya
24 Gold in '97?

25 A: Survival. Just survival.

26 Q: Where do you put it?

27 A: In my pocket.

28 Q: So you keep all your cash in your physical possession?

A: Yes.

26
27 ⁶The original Schedule "J" shows rent at \$700 month but both
28 debtor and Ms. Paulus consistently testified that he pays her \$300
a month to live in the house. It shows monthly expenses of
\$2,373.83.

1 to a Chapter 11) through January of 1999. That operating statement
2 simply indicates that the debtor, during the pendency of the Chapter
3 11 proceeding, did not utilize the debtor-in-possession checking
4 account but remained on a cash basis. It does not indicate income
5 received post-petition, but merely refers to "Maya Gold \$5,000."
6 Attached was a sample average monthly expense Schedule "J" showing
7 expenses of \$3,339.⁷

8 After that date, the debtor utilized the debtor-in-possession
9 account. The monthly operating statements which are merely copies
10 of the bank statements from that account show total deposits from
11 February of 1999 through July 21, 1999 of \$13,945. There is no
12 indication of the source of the income. It is unknown if the
13 debtor continues to receive proceeds from the real estate contract.
14 There is no evidence as to the amount of rents from the income
15 property or the expenses associated with those rental properties.
16 Nor is there any indication of the debtor's 1998 or 1999 prospecting
17 or consulting activities and income. The debtor's proposed Plan and
18 Disclosure Statement filed April 1, 1999 contains no projections,
19 budgets or other meaningful financial information. It merely
20 indicates that the debtor will continue to conduct his business,
21 including employment with Maya Gold, and use income to make the
22 proposed plan payments.

23 **CONCLUSION**

24 A review of the totality of the facts establish that this
25 petition was filed in bad faith. Substantially all the debtor's
26 assets are encumbered by the judgment creditor's liens. The debtor
27

28 ⁷Rent is still shown at \$700 a month.

1 has no employees and the ongoing business activity of Maya Gold
2 defies any common sense or reasonable business practices. The
3 debtor has sole and exclusive control over his own cash flow and can
4 provide no credible source of income to sustain a plan of
5 reorganization. There are few unsecured creditors other than
6 insiders and the debtor's own professionals. The record is replete
7 with examples of wrongdoing by this debtor which are too numerous
8 to recount. The most obvious examples have been cited above. It
9 is clear that the timing of the debtor's filing evidences an intent
10 to delay and frustrate the legitimate efforts of the secured
11 creditor to enforce her rights.

12 Although the debtor has filed a proposed Disclosure Statement
13 and Plan, filed all reports and paid required fees, there is no
14 evidence or meaningful information regarding the amount or source
15 of post-petition income of the debtor nor the post-petition
16 operation of any of the business activities. This case involves
17 essentially a two-party dispute. The debtor can show no realistic
18 possibility of reorganizing and the bankruptcy offers the only
19 possibility of forestalling loss of the debtor's property.
20 Notwithstanding the debtor's reverence for form, the sole purpose
21 of the bankruptcy was to delay the debtor's day of reckoning. The
22 purpose of this filing was not to effectuate a reorganization but
23 was a litigation tactic. Nor does the minimal evidence concerning
24 post-petition activity indicate any meaningful efforts to reorganize
25 the debtor's business in accordance with accepted business
26 practices. Therefore, I find the petition was filed in bad faith
27 and an order will be entered dismissing this case.

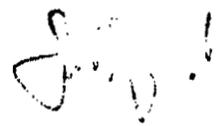
28 The Clerk of the Court is directed to file this Memorandum

1 Decision and provide copies to counsel and the Assistant U.S.
2 Trustee.

3 DATED this 24th day of September, 1999.

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PATRICIA C. WILLIAMS, Bankruptcy Judge



SEP 51

CERTIFICATE OF MAILING

The undersigned Clerk of the U.S. Bankruptcy Court for the Eastern District of Washington hereby certifies that a copy of the attachment on which this stamp appears was mailed this date to the following parties as required by the Bankruptcy Code and Rules of bankruptcy.

 Vreeland

 USA

 T.S. McGREGOR

By: J. J. Lane
Deputy Clerk

 SEP 27 1999
Date