

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF INDIANA
HAMMOND DIVISION

IN RE:)
)
JUDITH K. ROGAN,) CASE NO. 08-23221 JPK
) Chapter 13
Debtor.)

MEMORANDUM OF DECISION REGARDING MOTIONS FOR
RELIEF FROM THE AUTOMATIC STAY FILED BY DEXIA CREDIT
LOCAL AND THE UNITED STATES OF AMERICA

On November 21, 2008, Dexia Credit Local (“Dexia”) filed its Motion to Modify Automatic Stay. On December 12, 2008, the United States of America (“United States”) filed its Motion to Join Dexia’s Motion to Modify Stay. Each of these motions initiated a separate contested matter. However, because proceedings with respect to both motions have been conducted concurrently – and due to the symmetry of the issues raised by each motion – this order addresses both motions and yet constitutes the final determination pursuant to Fed.R.Bankr.P. 9014(c)/Fed.R.Bankr.P. 7052/Fed.R.Civ.P. 52(a) separately with respect to each motion.

In their respective motions, Dexia and the United States seek relief from the automatic stay of 11 U.S.C. § 362(a) so that they can pursue actions against the Chapter 13 debtor Judith K. Rogan (“Judith”) which were pending against her in the United States District Court for the Northern District of Illinois at the time that she filed her petition initiating this Chapter 13 case on September 27, 2008. Judith of course opposes both motions.

After several preliminary hearings, and other conferences with the parties, a final hearing was held on February 20, 2009.¹ The court has jurisdiction of these contested matters pursuant to 28 U.S.C. § 1334(a) and (b), 28 U.S.C. § 157(b)(1), and N.D.Ind.L.R. 200.1(a)(1) and (2) of the Rules of the United States District Court for the Northern District of Indiana. The contested matters are core proceedings pursuant to 28 U.S.C. § 157(b)(2)(G).

¹ By consent of the parties, the 30-day period provided for by 11 U.S.C. § 362(e)(1) and the 60-day period specified by 11 U.S.C. § 362(e)(2) have both been extended.

The course of proceedings that led the parties to this junction has been nicely laid out by Dexia in its Motion to Modify Automatic Stay, and the court can do no better than Dexia's synopsis to set the stage for its discussion of the creditors' motions:

Since early 2002, Dexia, the United States ("U.S."), and Edgewater Medical Center ("EMC") have pursued a series of fraud cases in the Northern District of Illinois ("NDIL") against Debtor's husband, Peter G. Rogan ("Peter Rogan"), and his wholly-owned or controlled companies. See *Rogan v. United States*, 2008 WL 282351, at *1 (N.D. Ind. 2008). The cases of Dexia and the U.S. are in the United States District Court before Judges Matthew Kennelly and John Darrah, respectively, while EMC's cases are in the U.S. Bankruptcy Court before Judge Bruce Black. These cases have resulted in judgments for tens of millions of dollars against Peter Rogan and his companies. . . . (Motion to Modify Automatic Stay, ¶ 1 of "factual Background")

The judgment granted to Dexia in case number 02 C 8288 in the United States District Court for the Northern District of Illinois, Eastern Division, on May 3, 2007 states:

On April 11, 2007, the Court found defendants Peter Rogan ("Rogan"), Braddock Management I.P ("Braddock"), Bainbridge Management, Inc. ("Bainbridge") and counter-claim plaintiffs Edgewater Property Company ("EPC") and PGR Properties, Inc. ("PGR") in default. Due notice having been given, the Court now grants Plaintiff Dexia Credit Local's Motion for Entry of Default Judgment against defendants Rogan, Braddock, Bainbridge, and counter-claim plaintiffs PEC and PGR. In granting plaintiff's motion for default judgment, the Court hereby:

- (i) Finds that Bainbridge and Braddock are Rogan's alter-egos, that the corporate veils of Bainbridge and Braddock are therefore pierced, and that Rogan is therefore liable for any judgment entered against Bainbridge or Braddock;
- (ii) Enters judgment in favor of plaintiff and against defendants Rogan, Braddock and Bainbridge as follows: (8) actual damages of \$53,082,978.03; (b) pre-judgment interest of \$18,103,779.99; (c) punitive damages of \$53,082.978.03; and (d) costs in the amount of \$10,976.74. The Court also awards plaintiff post-judgment interest in an amount to be determined once the judgment is satisfied; and

- (iii) Dismisses with prejudice the counterclaim of EPC and PGR.

Turning again to the Motion to Modify Automatic Stay (¶¶ 2, 3, 5, 6, 7, 9, 10 and 11 of “Factual Background”):

Under Fed. R. Civ. P. 69, which states that federal judgments are to be executed under state law, Dexia, EMC, and the United States initiated postjudgment proceedings against Peter Rogan, Debtor, and several Rogan businesses in NDIL in 2007 via citations to discover assets. These supplementary proceedings against Debtor are based upon the theory that she holds assets in her name for her husband’s beneficial interest *inter alia* as his nominee, alter ego, constructive or resulting trustee, or fraudulent transferee.

U.S. Foreclosure Case. In November 2007, the United States filed suit against Mr. and Mrs. Rogan (and Dexia) to foreclose on judgment liens it asserts against two parcels of property, one in Chicago at 55 East Erie Street (“Erie Condo”) and one that was located in at 476 Wexford in Valparaiso, Indiana (“Wexford Property”).¹ (6/23/08 J. Kennelly Order, *United States v. Rogan*, 07 C 6398 (Ex. A)). The government alleges that although Mrs. Rogan holds legal title to the two parcels, she is a mere nominee of Mr. Rogan and Mr. Rogan is the equitable owner of the parcels. (*Id.*) This case as well as Dexia’s Turnover case are consolidated before Judge Kennelly. On June 23, 2008, Judge Kennelly rejected Debtor’s argument that venue was improper in NDIL and denied Mrs. Rogan’s motion to dismiss the Foreclosure Case. . . .

FN 1 The Wexford Property later was sold and the proceeds were placed in an escrow account, which now is under the jurisdiction of NDIL in the Foreclosure Case. In a settlement agreement, EMC/Dexia and the United States have agreed to share the proceeds recovered in their respective actions against Peter Rogan. Thus, although Dexia is named as a defendant in the Foreclosure Case by virtue of the fact that it also holds judgment liens referencing the disputed properties, it will share in the proceeds if the government prevails in the Foreclosure Case.

In early August 2008, Dexia filed with Judge Kennelly, on an *ex parte* basis, a 292-page motion and supporting legal memoranda, including over 500 exhibits, seeking: (a) a temporary restraining order (“TRO”) and preliminary injunction (“PI”) including the freezing of the assets of Peter Rogan, Debtor and others, including assets that Debtor holds for her husband’s benefit; and (b) turnover of the aforementioned assets to Dexia.² The assets

at issue in Dexia's motion include assets that Debtor lists in her bankruptcy schedules such as: (a) the Erie Condo (Schedule A – Real Property); (b) the escrowed proceeds from the sale of the Wexford Property (Schedule B – Personal Property – Amended, Item 20); (c) a claimed interest in the PGR Bahamas Trust (*Id.*); and (d) HSBC accounts in Vancouver, Canada that holds \$532,519.15 (U.S.) and \$9,381.81 (Canadian) . . .

FN2 Thereafter, Dexia supplemented these filings with more than 150 pages of additional briefing and more than 100 additional exhibits.

On September 4, 2008, . . . Judge Kennelly entered *ex parte* TROs against Peter Rogan, Debtor, and others. The TRO entered against Debtor included findings that Debtor, in combination with Peter Rogan and others: (i) held Peter Rogan's assets for his benefit; (ii) engaged in improper transfers of funds; (iii) concealed and transferred Rogan's assets to the detriment of Dexia; and (iv) presented a risk of immediate and irreparable damage resulting from the dissipation and concealment of Rogan's assets. . . .

On September 18 and 19, 2008, Judge Kennelly held preliminary status hearings on the TRO as it related to Judy Rogan. . . . On September 23, 2008, Judge Kennelly commenced the hearing to determine whether to convert the TROs against Debtor and others into Preliminary Injunctions ("PI").

. . .

Less than 2 hours before her testimony was to begin before Judge Kennelly, Judy Rogan filed a voluntary bankruptcy petition under Chapter 11 in the Northern District of Indiana. (Dckt. No. 1, *In re Judith Rogan*, Case No. 08-23158 (N.D. Ind.)) Appearing before Judge Kennelly at the time of Judy Rogan's scheduled testimony, Debtor's counsel informed the judge of Mrs. Rogan's bankruptcy filing and stated that she was withdrawing all proof she presented in opposition to the PI. . . . Counsel further argued that the automatic stay rendered Judge Kennelly powerless to hear Mrs. Rogan's testimony and powerless to take any action on the TRO at all, meaning that the TRO would lapse. . . . Dexia cited case law for the proposition that a freeze order alone does not violate the automatic stay so long as there is no attempt to execute upon property of the estate. . . . Voicing concern that doing nothing would subject the frozen assets to the risk of dissipation, Judge Kennelly extended the TRO for several days to give Dexia time to appear before this Court. . . .

The next day, on September 25, 2008, this Court *sua sponte* closed the record of Mrs. Rogan's petition because she failed to file that appropriate documentation. (Dckt. No. 3, *In re Judith*

Rogan, Case No. 08-23158 (N.D. Ind.)) The Court's order indicated that the petition was a nullity, and should be treated as if it had never been filed. . . .

Later that same day, Dexia notified Judge Kennelly that this Court had closed Judy Rogan's bankruptcy case. Because Mrs. Rogan had withdrawn all of her proof contrary to the PI, Dexia asked Judge Kennelly to impose the preliminary injunction upon Debtor. Judge Kennelly did so.

The preliminary injunction order entered on September 25, 2008 states, in pertinent part to these contested matters, the following:

Plaintiff Dexia Cr dit Local ("Dexia"), having filed its Motion And Memorandum In Support Of Its Motion For A Temporary Restraining Order and a Preliminary Injunction Freezing Assets and an Order Turning Over the Assets of Peter G. Rogan, and the Court having considered these motions, declarations, exhibits, and memoranda of law filed in support thereof, now being advised in the premises, finds that:

1. This Court has jurisdiction over the subject matter of this case, and over the parties;
2. Venue properly lies with this Court;
3. There is good cause to believe that: (i) defendant and judgment debtor Peter G. Rogan ("Rogan") along with Judith K. Rogan, Fred Cuppy, Troy Myers, Jr. and the Peter G. Rogan Irrevocable Trust, the RPP Finance Trust, U.S. trusts in the names of Robert Cashman Rogan (EIN: XX-XXXXXXXX), Sara Caitlin Rogan (EIN: XX-XXXXXXXX), and Brian Peter Rogan (EIN: XX-XXXXXXXX) and foreign trusts in the names of Robert Cashman Rogan (EIN: XX-XXXXXXXX), Sara Caitlin Rogan (EIN: XX-XXXXXXXX), and Brian Peter Rogan (EIN: XX-XXXXXXXX) (collectively "Respondents") directly and indirectly own, control, and/or possess Assets of Rogan, but that have failed to turn over those Assets to satisfy the judgment in this case and instead have disposed of those Assets as Respondents have seen fit; (ii) Judith K. Rogan, Fred Cuppy and/or Troy Myers, Jr. have held, transferred, and/or otherwise disposed of Rogan's Assets for Rogan's direct or indirect benefit; and (iii) Respondents have
Rogan will occur from Respondents' transfer or other disposition or concealment of Rogan's Assets or records unless Respondents and their agents are preliminarily restrained and enjoined by Order of this Court. The evidence set forth in *Dexia's Motion And Memorandum In Support Of Its Motion For A Temporary Restraining Order and a Preliminary Injunction Freezing Assets and an Order Turning Over the Assets of Peter G. Rogan*, and in the accompanying pleadings, declarations and exhibits, demonstrates that Respondents have engaged in a concerted course of illegal activity by taking steps to conceal and dissipate Rogan's Assets. Respondents unjustly have retained or assisted others to retain these Assets to the detriment of Dexia. There is good cause to believe that unless they are restrained from doing so by order of this Court, Respondents will continue with these illegal actions, and they will attempt to conceal the scope of their illegal actions through the destruction of evidence and secreting of Assets;
5. Weighing the equities and considering the Dexia's likelihood of success, this Order is in the public interest;
6. No security is required because: (a) Dexia has a strong likelihood of success on the merits; and (b) the issuance of the order will not harm Respondents, as the Assets at issue will be kept in interest-bearing accounts.

. . .

I. ASSET PRESERVATION

IT IS THEREFORE ORDERED that the Respondent Judith K. Rogan, and the Rogan Entities and their officers, agents servants, employees, and attorneys, and those persons in active concert or participation with them who receive actual notice of this Order by personal service or otherwise, are hereby preliminarily restrained and enjoined until further order from this Court from:

A. Transferring, converting, encumbering, selling, concealing, dissipating, disbursing, assigning, spending, withdrawing, perfecting a security interest in, or otherwise disposing of any Assets wherever located, inside or outside the United States of America, that are owned, controlled or held by, or for the benefit of, in whole or in part, any of the Rogan Entities, or in the actual or constructive possession of any of the Rogan Entities, including without limitation:

- (1) the Peter G. Rogan Irrevocable Trust (EIN: XX-XXXXXXX);
- (2) any Assets in the control of or emanating in any way from the Peter G. Rogan Irrevocable Trust;
- (3) any Assets in the control of or emanating in any way from any business entity directly or indirectly owned by the Peter G. Rogan Irrevocable Trust including, without limitation, CFMT, Ltd. (EIN: XX-XXXXXXX or EIN: XX-XXXXXXX), CFMT of Fla, LLC (EIN: XX-XXXXXXX), Epyon Holdings, Ltd.;
- (4) the RPP Finance Trust;
- (5) any Assets in the control of or emanating in any way from the RPP Trust;
- (6) any Assets in the control of or emanating in any way from any business entity directly or indirectly owned by the RPP Trust including, without limitation, RPP Finance, Ltd. (EIN: XX-XXXXXXX);
- (7) any trust in the name of any of the Rogan children, including without limitation U.S. trusts in the names of Robert Cashman Rogan (EIN: XX-XXXXXXX), Sara Caitlin Rogan (EIN: XX-XXXXXXX), and Brian Peter Rogan (EIN: XX-XXXXXXX), and foreign trusts in the names of Robert Cashman Rogan (EIN: XX-XXXXXXX), Sara Caitlin Rogan (EIN: XX-XXXXXXX), and Brian Peter Rogan (EIN: XX-XXXXXXX) (collectively, "the Children's Trusts");
- (8) any Assets in the control of or emanating in any way from the Rogan Children's Trusts;
- (9) any Assets in the control of or emanating in any way from any business entity directly or indirectly owned by the Rogan Children's Trusts, including without limitation Boulevard Investors Ltd. (EIN: XX-XXXXXXX) and Boulevard Investors LLC (EIN: XX-XXXXXXX);
- (10) any Assets in the control of or emanating in any way from any business entity directly or indirectly owned by Rogan;
- (11) any funds in or emanating in any way from any account at any banking or financial institution directly or indirectly owned by Rogan;
- (12) Peter and Judith Rogan's interest in any real property, including without limitation the Wexford Property and the 55 E. Erie property;
- (13) any property belonging to Rogan or to which Rogan may be entitled or which may hereafter be acquired by or become due to Rogan, directly or indirectly;
- (14) any funds in or emanating in any way from in any Judith Rogan or Judith K. Rogan Revocable Trust account at any financial institution, including DWS Scudder, 1st Valpo, Oceanic Bank (The Bahamas), or HSBC;
- (15) any funds in the account(s) of Judith Rogan or the Judith K. Rogan Revocable Trust (EIN: XX-XXXXXXX) at Ameritrade; and,
- (16) any Assets held in any account in the name or for the benefit of the Rogan Entities at any bank or savings and loan institution, or any credit card processing agent, customer service agent, commercial mail receiving agency, or mail holding or forwarding company, or any credit union, online payment service, IRA custodian, money market or

mutual fund, storage company, trustee, or with any broker-dealer, escrow agent, title company, commodity trading company, precious metal dealer, or other financial institution or depository of any kind;

B. Opening or causing to be opened any safe deposit boxes, commercial mail boxes, or storage facilities titled in the name or for the benefit of any of the Rogan Entities, or subject to access by any of the Rogan Entities or under any the control of any of the Rogan Entities, without providing the Dexia and this Court prior notice and an opportunity to inspect the contents in order to determine that they contain no Assets covered by this Section; and

C. Incurring liens or encumbrances on real property, personal property or other Assets in the name, singly or jointly, of any of the Rogan Entities.

D. Transferring any funds or other Assets subject to this Order for attorney's fees or living expenses; **provided however that**, notwithstanding the above, any Respondent may petition the Court for access to funds subject to this Order to pay reasonable, usual, ordinary, and necessary living expenses and attorney's fees. No such expenses, however, shall be paid from funds subject to this Order except from cash on the person of Peter or Judy Rogan, or from an account designated by written notice to counsel for Dexia and this Court; **provided further that**, Peter and Judy Rogan may pay reasonable, usual, ordinary, and necessary living expenses, and reasonable attorney's fees, but only after written prior approval by the Dexia or as otherwise authorized by the Court.

II. REPATRIATION OF FOREIGN ASSETS AND DOCUMENTS

IT IS FURTHER ORDERED that Respondent Judith K. Rogan shall immediately:

A. Repatriate to the United States all Assets and all Documents located in foreign countries held, directly or indirectly:

1. by any of the Rogan entities;
2. for the benefit of any of the Rogan entities; or
3. under the ownership or control any of the Rogan Entities, including without limitation the Peter G. Rogan Irrevocable Trust, the RPP Finance Trust, the Childrens' Trusts or any entity in which any of the foregoing holds an ownership interest;

As stated in the United States' Legal Position Regarding the Creditors' Motion to Modify the Automatic Stay, (page 2), there are three "supplementary proceedings" in the District Court for the Northern District of Illinois which are the subject of Dexia's and the United States' motions:

The three postjudgment supplementary proceedings the Creditors seek to continue pursuing — commonly referred to herein as the "Foreclosure Suit," the "Turnover Proceedings" (both before Judge Kennelly) and the "Fraudulent Transfer Proceeding" (before Judge Darrah) — arise from those judgments. . . . Each of the supplementary proceeding involve allegations that Peter Rogan fraudulently transferred to Judith Rogan assets that could be applied to the judgements.

As noted, there are two proceedings pending in the United States District Court in the Northern District of Illinois with respect to which the United States seeks relief from the automatic stay in order to proceed: (1) the United States' Petition for Relief Against Judith K. Rogan (as "Citation Respondent") in case number 02 C 3310 before the Honorable John W. Darrah; and (2) a foreclosure complaint which initiated case number 07 C 6398 before Judge Kennelly. In the former proceeding, the United States asserts fraudulent conveyance actions in two separate courts, in each of which it requests the following relief with respect to Judith (identical relief being requested in both counts):

- b) pursuant to 28 U.S.C. § 3306(a)(1), void the transfers from Peter Rogan to Judith Rogan to the extent necessary to satisfy the debts owing to the United States;
- c) pursuant to 28 U.S.C. § 3306(a)(2), issue a writ of execution so that the United States may levy on the assets of Judith Rogan to satisfy the judgment debt owed to the United States;
- d) pursuant to 28 U.S.C. § 3306(a)(3), enter judgment in favor of the United States and against Judith K. Rogan for \$5,500,000 plus prejudgment interest to the extent necessary to satisfy the judgment debt owed to the United States;

In the latter proceeding – the foreclosure action – the United States requested the following relief with respect to a condominium unit located at 55 East Erie, Chicago, Illinois:

WHEREFORE, the plaintiff, the United States of America, requests the court:

- (A) declare that the lien arising with the judgment against Peter Rogan attached to all of his property and rights to property, including to the Eric Condo.
- (B) declare that the JRK Trust hold record title to the Erie Condo as the nominee of Peter Rogan;
- (C) declare that the JRK Trust is the alter ego of Peter Rogan for purposes of and with respect to the ownership of the Erie Condo;
- (D) declare that the transfer of title to the Erie Condo to the JKR Trust was a fraudulent transfer which may be avoided by the United States as a creditor of Peter Rogan;

- (E) declare that the United States' judgment lien has attached to the Erie Condo;
- (F) foreclose the judgment lien that has attached to the Erie Condo, and that, pursuant to 28 U.S.C. § 3201(f), require the Erie Condo to be sold by an officer of this court according to law, free and clear of any right, title, lien, claim or interest of any of the parties to this action, and determine what portions of the net proceeds of the sale should be distributed to the United States for application to the judgment liabilities of Peter Rogan and to other parties;

The United States requested the following relief in that action with respect to property located at 476 Wexford Road, Valparaiso, Indiana:

WHEREFORE, the plaintiff, the United States of America, requests the court:

- (A) declare that the lien arising with the judgment against Peter Rogan attached to all of his property and rights to property, including to the Wexford Property.
- (B) declare that the JKR Trust holds title to the Wexford Property as the nominee of Peter Rogan;
- (C) declare tha The JRK Trust is the alter ego of Peter Rogan, for purposes of and with respect to the ownership of the Wexford Property;
- (D) declare that the transfer of title to the Wexford Property to the JKR Trust was a fraudulent transfer which may be avoided by the United States as a creditor of Peter Rogan;
- (E) declare that the United States' judgment lien has attached to the Wexford Property;
- (F) foreclose the judgment lien that has attached to the Wexford Property, and that, pursuant to 28 U.S.C. § 3201(f), require the Wexford Property to be sold by an officer of this court according to law, free and clear of any right, title, lien, claim or interest of any of the parties to this action, and determine what portions of the net proceeds of the sale should be distributed to the United States for application to the judgment liabilities of Peter Rogan and to other parties . . .

Dexia's proceedings were commenced by a Citation to Discover Assets to Third Party,

served on Judith (record entry #335 in case number 02-C-8288 in the United States District Court for the Northern District of Illinois), filed on June 7, 2007. This document initiated essentially an asset discovery proceeding, and was followed by proceedings initiated by Dexia in that case which resulted in the entry of a Preliminary Injunction Order With Asset Freeze and Other Equitable Relief Directed to Judith K. Rogan, on September 27, 2008. For the purpose of this decision, it is assumed that the remedies which Dexia seeks to pursue in case number 02-C-8288 against Judith essentially parallel those sought by the United States in its Petition for Relief Against Judith K. Rogan in case number 02-C-3310.

In Schedule A of the schedules which she filed in her Chapter 13 case, Judith listed an "Equitable Interest as Beneficiary of Judith Rogan Revocable Trust" in the condominium at 55 East Erie, Chicago, Illinois. In Schedule B, Judith listed the following property:

1. A bank account in "HSBC-Vancouver BC Canada" having a stated value of \$9,381.83;
2. A bank account in HSBC-Vancouver BC Canada, having a stated value of \$532,519.15;
3. Interests in various investment accounts;
4. A "Beneficial Interest of Judith Rogan Revocable Trust, established 4/19/89; Chase-Escrowed Proceeds from sale of 476 Wexford, Valparaiso, Indiana" in the stated amount of \$912,004.95;
5. An interest designated as "Peter G. Rogan Irrevocable Trust discretionary beneficiary up to \$20,000.000.00 New World Trustee's (Bahamas); Limited (aka Family Trust established Jan. 5, 1996 and in 1996 transferred beneficial interest to Debtor and other family members", in an unknown amount.

As the foregoing clearly demonstrates – and as both creditors admit – the property with respect to which they seek relief from the automatic stay to pursue in their actions in the United

States District Court for the Northern District of Illinois has been designated by Judith as constituting property of her Chapter 13 bankruptcy estate.²

Thus, the stage is set and so are the players. Throughout the proceedings on the creditors' motions, the court addressed to the parties its thoughts that the creditors' motions did not present the customary circumstance in which a putative creditor seeks relief from the stay in order to liquidate a claim against a debtor in a previously-pending action in a court other than the bankruptcy court. As can readily be seen from the foregoing recitation, the pending actions of both Dexia and the United States seek to determine that property included by Judith in her schedules is not in fact property of her Chapter 13 bankruptcy estate. These actions also seek to establish liens on those properties to secure judgments obtained against Peter Rogan, on various theories, particularly theories involving fraudulent conveyance assertions, and the doctrines of nominee transfer and of constructive trust. As it is permitted to do under the Federal Debt Collection Procedures Act [28 U.S.C. § 3306(a)(3)], the United States has alternatively sought a monetary judgment against Judith for the value of property which it alleges was fraudulently transferred to her by Peter.

Dexia filed claim #13-1 in Judith's Chapter 13 case, in which it asserts a claim having the value of assets allegedly transferred by Peter Rogan to Judith which may be recoverable, or recovered, by Dexia in its collection proceeding. The claim asserts that depending upon the circumstances of determination of Peter Rogan's interests in property held by Judith Rogan, its claim may be secured, and it may equal or exceed 8.7 million dollars.³ The United States

² On October 1, 2008, Judith filed a notice of appeal with respect to the preliminary injunction entered by Judge Kennelly on September 25, 2008 – an order which enjoins any transfer of these property interests.

³ It is of amusing interest to note that the claims register includes a document designated as claim #11-1, attributed to Dexia, which is comprised of a receipt issued by the "Department of Revenue – Parking in Chicago" for \$60.00 apparently paid for some form of parking violation. This claim is of no moment in this matter, and presumably Dexia will not seek

Department of Justice filed claim #15-1, as an unsecured claim, in the amount of \$5,500,000.00, based apparently upon its assertions of the value of transfers made by Peter Rogan to Judith which it deems avoidable in its action(s) in the Northern District of Illinois District Court. The claims register includes – as all do – a summary of the amounts of various classes of filed claims, stating that no claims designated as “secured” have been filed; that claims designated as “priority” have been filed in the amount of \$1,039,376.74 (comprised primarily of the priority claim of the Internal Revenue Service in the amount of \$1,035,738.64); and that claims designated as “unsecured” have been filed in the amount of \$5,892,475.73.⁴

In the customary stay relief proceeding brought by a creditor to pursue litigation pending at the time of the filing of a debtor’s case, the principal focus of the pending litigation is determination/liquidation of an indebtedness alleged by the creditor to be owed it by the debtor. This is done so that the creditor may seek to establish the amount – and at times the characterization – of an allowed claim upon which distribution may be received under a Chapter 13 plan. Indeed, at least with respect to the United States, this debt liquidation function may be served by proceedings in the United States District Court for the Northern District of Illinois with respect to that creditor’s alternative remedy provided by 28 U.S.C. § 3306(a)(3). However, there is much more at stake in the pending actions than the mere liquidation of monetary claims. If Dexia and the United States are successful in establishing the theories upon which they have asserted their respective pending actions, the result may be that certain property scheduled by Judith as property of her bankruptcy estate pursuant to 11 U.S.C. § 541(a) will be

to pursue this claim in Judith’s Chapter 13 case.

⁴ There is thus presented the interesting scenario in which the United States Department of Justice is seeking to remove property from the sphere of property of the Chapter 13 estate, which property might constitute a funding source for required payment [under 11 U.S.C. § 1322(a)(2)] of a priority claim of the United States of America asserted by the Internal Revenue Service.

determined to not be property of her bankruptcy estate subject to administration for the benefit of the creditors in her case. In addition, the result may be that Dexia and the United States will acquire liens in property removed from the Chapter 13 bankruptcy estate as a result of their pending collection proceedings. This much is clear. At this time, there has been no adjudication whatsoever that Judith Rogan owes any debt to either Dexia or to the United States in relation to the assertions of Dexia and the United States Department of Justice in relation to her. It is also clear that Judith Rogan has legal and/or equitable interests, established by written documentation, in the property with respect to which Dexia and the United States seek stay relief to establish otherwise. As a result, this is an atypical circumstance in which creditors seek relief from the automatic stay to proceed with litigation which was pending prior to the filing of the debtor's bankruptcy case. The proceedings which Dexia and the United States seek to pursue have significant ramifications upon property of Judith's Chapter 13 bankruptcy estate, and thus significant ramifications upon the landscape of any Chapter 13 plan for which Judith may seek confirmation.

The parties and the court spent a significant amount of time prior to the final evidentiary hearing establishing the court's interpretation of certain criteria for stay relief stated in its order entered on February 13, 2009 (docket record entry #114),. The court stated that the "standard to be applied to the motions for relief from the automatic stay is the three-prong standard stated in *In re Fernstrom Storage and Van Company*, 938 F.2d 731 (7th Cir. 1991), including the determination that the third prong's requirement that a creditor have a probability of prevailing on the merits would be satisfied "by a demonstration that the litigation with respect to which stay relief is sought is not frivolous". Obviously, *Fernstrom* is the controlling precedent in the Seventh Circuit for straight forward motions for stay relief "for cause" under 11 U.S.C. § 362(d)(1). The fact that the creditors' pending litigation strikes at the core of determination of property of Judith's bankruptcy estate adds another dimension to the calculus, and a very

important one at that.

The *Fernstrom* test is deceptively simple, stated as follows in that case:

Though § 362(a) provides for a nearly comprehensive stay of proceedings against the debtor, § 362(d) requires the bankruptcy judge “to grant relief from the stay ... for cause.” “Cause” as used in § 362(d) “has no clear definition and is determined on a case-by-case basis.” *In re Tucson Estates*, 912 F.2d 1162, 1166 (9th Cir.1990). See also *In re Makarewicz*, 121 B.R. 262, 264 (Bankr.S.D.Fla.1990); *In re Revco D.S.*, 99 B.R. 768, 777 (Bankr.N.D.Ohio 1989). Nevertheless, a number of themes emerge from the cases interpreting § 362(d)'s expansive language. As we wrote in *Matthews*, 739 F.2d at 251, “[s]uspension of [the automatic stay] may be consonant with the purposes of the Bankruptcy Act when equitable considerations weigh heavily in favor of the creditor and the debtor bears some responsibility for creating the problems.” An influential district court opinion adopts a three factor test for determining whether “cause” exists, asking whether

- a) Any great prejudice to either the bankrupt estate or the debtor will result from continuation of the civil suit,
- b) the hardship to the [non-bankrupt party] by maintenance of the stay considerably outweighs the hardship of the debtor, and
- c) the creditor has a probability of prevailing on the merits.

In re Pro Football Weekly, 60 B.R. 824, 826 (N.D.Ill.1986) (bracketed text in original, internal quotations omitted). See also *In re Bock Laundry Machine*, 37 B.R. 564, 566 (Bankr.N.D.Ohio 1984).

938 F.2d 731, 735 (7th Cir. 1991).

It must first be noted that *Fernstrom* concerns the relatively common circumstance in which a party asserting a claim against the debtor is willing to proceed entirely against insurance available to the debtor for that claim. This insurance coverage is not property of a bankruptcy estate under 11 U.S.C. § 541(a), and so long as the creditor is content to proceed in the pending case solely against the insurance proceeds available for covering an ultimately liquidated claim against the debtor, the automatic stay is really not implicated at all in the

pending action. It is in this context that *Fernstrom's* relatively simple standard must be viewed.

It is interesting to note that even in the same context, in *Holtkamp v. Littlefield*, 669 F.2d 505, 508-09 (7th Cir. 1982), the court stated:

While we agree that Congress intended that the automatic stay have broad application, the legislative history to § 362 clearly indicates that Congress recognized that the stay should be lifted in appropriate circumstances. It states:

(I)t will often be more appropriate to permit proceedings to continue in their place of origin, when no great prejudice to the bankruptcy estate would result, in order to leave the parties to their chosen forum and to relieve the bankruptcy court from many duties that may be handled elsewhere.

In re Honosky, 6 B.R. 667, 669 (D.C.S.D.W.Va.1980) citing S.Rep.No.989, 95th Cong., 2d Sess. 50, reprinted in (1978) U.S.Code Cong. & Ad.News 5836.

Holtkamp's claim that permitting the trial to go forward enabled Littlefield to gain a superior position over other creditors is belied by the facts. Holtkamp argues that by obtaining a judgment Littlefield can now enforce that judgment by securing a lien against Holtkamp's property. This contention is erroneous, for the bankruptcy's court's order expressly prohibited Littlefield from attempting to enforce his judgment. Allowing the pending action to proceed merely determined Holtkamp's liability but did not change Littlefield's status in relation to other creditors. *Brodsky v. Philadelphia Athletic Club, Inc.*, 9 B.R. 280 (Bkrtcy.E.D.Penn.1981).

Indeed, contrary to Holtkamp's assertion that the order of the bankruptcy court frustrated the policy of the Code, the lifting of the stay in this case is in complete harmony with the Code's policy of quickly and efficiently formulating plans for repayment and reorganization. The purpose of the automatic stay is to preserve what remains of the debtor's insolvent estate and to provide a systematic equitable liquidation procedure for all creditors, secured as well as unsecured, H.R.Rep.No.595, 95th Cong., 1st Sess. 340 (1977), reprinted in (1978) U.S.Code Cong. & Ad.News 6296-97, thereby preventing a "chaotic and uncontrolled scramble for the debtor's assets in a variety of uncoordinated proceedings in different courts." In re *Frigitemp Corp.*, 8 B.R. 284, 289 (D.C.S.D.N.Y.1981) citing *Fidelity Mortgage Investors v. Camelia Builders, Inc.*, 550 F.2d 47, 55 (2d Cir. 1976), cert. denied, 429 U.S. 1093, 97 S.Ct. 1107, 51 L.Ed.2d 540 (1977).

However, where, as here, the pending action is neither connected with nor interfering with the bankruptcy proceeding, the automatic stay in no way fosters Code policy. S.Rep.No.989, 95th Cong., 2d Sess. 50, 52, reprinted in (1978) U.S.Code Cong. & Ad.News 5836, 5838. Allowing the civil action to go forward did not jeopardize Holtkamp's bankrupt estate because his insurance company assumed full financial responsibility for defending that litigation.

In contrast to the factual circumstances of both *Fernstrom* and *Holtkamp*, the litigation which Dexia and the United States desire to pursue in the non-bankruptcy forum has significant implications with respect to determination of property of Judith's bankruptcy estate, and also with respect to which competing group of creditors (Judith's creditors in the Chapter 13 case versus the putative claims of Dexia and the United States against her) will be benefitted by the property interests which are the focus of the creditors' pending actions. Make no mistake about it: entities having fully liquidated claims with respect to Judith's legal liability to them are in direct competition with Dexia and the United States. The competition focuses on whether or not the property which Dexia and the United States seek to impress with their judgments is the property of Judith's bankruptcy estate under 11 U.S.C. § 541(a), or whether, by some legal theory or doctrine, that property – at the time of filing of her case clearly constituting property of her bankruptcy estate – is somehow divested from her bankruptcy estate by a determination which might be made in a non-bankruptcy court forum.

A more circumspect analysis, premised on *Fernstrom* but not limited to its elemental standard, was applied in *In re Comdisco, Inc.*, 271 B.R. 273, 276 (Bankr. N.D.Ill. 2002), stated as follows:

The plaintiff moved under § 362(d)(1) to modify the automatic stay "for cause." It is intuitively obvious that determining whether cause exists to modify the stay to permit a lawsuit to proceed in another court requires a balancing of the costs and benefits of maintaining the stay. See *In re Fernstrom Storage & Van Co.*, 938 F.2d 731, 735 (7th Cir.1991) (applying test that includes prejudice to the debtor or estate if stay were modified and hardship to movant if stay were maintained).^{FN5} It is also obvious

from Congress's use of the undefined word "cause" that whether the stay should be modified to permit a lawsuit to proceed depends on the facts of the specific case. Congress did choose to specify and define one cause to modify the stay in all cases where it is found-lack of adequate protection of a property interest. See §§ 361, 362(d)(1). But it did not specify anything else that would be cause in all cases in which it existed. Therefore, cause to modify the stay to permit a lawsuit to proceed "is determined on a case-by-case basis." *Fernstrom*, 938 F.2d at 735, quoting *In re Tucson Estates*, 912 F.2d 1162, 1166 (9th Cir.1990).

FN5. *Fernstrom* also lists the movant's probability of succeeding in the lawsuit as a factor, but that falls under the category of hardship resulting from the stay. If a claim is very weak, there is little hardship in staying its prosecution; if it is strong, the hardship is greater. In any event, there is no need to consider the merits of the securities fraud claim in order to decide the present motion, and this Court does not read *Fernstrom* as mandating such a consideration.

Because the inquiry must be case-specific, copying and checking off lists of "factors" from other cases that had different facts is all but useless. As the 7th Circuit has recognized, "a list of factors without a rule of decision is just a chopped salad." *In re Synthroid Mktg. Litig.*, 264 F.3d 712, 719 (7th Cir.2001). This Court has previously rejected the factor-counting approach to judicial decision-making. *Chase Manhattan Bank v. Murphy (In re Murphy)*, 190 B.R. 327, 333 (Bankr.N.D.Ill.1995) ("the fact-finding process is only clouded by copying a list of factors from other cases and weighing evidence according to how well it matches that list.") The only factors that matter are those that arise from the circumstances of the present case, and even they must be weighed in the context of all the relevant circumstances.

Although somewhat difficult to find, cases do exist in which entities have contended that property of a debtor's bankruptcy estate is actually not the debtor's property at all, based upon various theories, usually some form of constructive trust, or fraudulent conveyance, theory. We start again with the proposition that the property interests which Dexia and the United States seek to determine in the United States District Court for the Northern District of Illinois presently constitute property of Judith's Chapter 13 bankruptcy estate. Although based on multiple theories, the gist of the creditors' arguments is that the property interests at issue are

impressed with in essence a constructive trust for their benefit, and perhaps for the benefit of other creditors of Peter Rogan. While the issue of which jurisdiction's law might be applied to Dexia's and the United States' actions has not been heretofore considered in these contested matters, because Judith is a resident of the State of Indiana, the court will adopt the assumption, *in arguendo*, that Indiana law applies to determine the nature and extent of her interests in the subject property. The doctrine of constructive trust under Indiana law was stated as follows in *In re Nova Tool & Engineering, Inc.*, 228 B.R. 678, 686 (Bankr. N.D.Ind. 1998):

Accordingly, this court concludes that, under Indiana law, a constructive trust is an equitable remedy that does not confer any property interest in the "beneficiary" until a court has created it by declaring such relief.⁵

Similarly, in *In re Gurley*, 222 B.R. 124, 135-136 (Bankr. W.D.Tenn. 1998) the court discussed constructive trust issues addressed by the United States Court of Appeals for the Sixth Circuit in *In re Omegas Group, Inc.*, 16 F.3d 1443 (6th Cir. 1994) as follows:

The Sixth Circuit has not resolved the alleged conflict between sections 541(d) and 544(a). See *XL/Datacomp v. Wilson (In re Omegas Group, Inc.)*, 16 F.3d 1443, 1448-1449 (6th Cir.1994); *Craig v. Seymour (In re Crabtree)*, 871 F.2d 36, 37-38 (6th Cir.1989) (not addressing the federal bankruptcy issues because the case was decided under state law). In *Omegas Group*, however, the Sixth Circuit criticized the Fifth Circuit's analysis in *Quality Holstein Leasing* and "the vast majority of courts which have addressed bankruptcy claims based on a constructive trust." *Omegas Group*, 16 F.3d at 1449. The court reasoned: "[A] constructive trust is not really a trust. A constructive trust is a legal fiction, a common-law remedy that may only exist by the grace of judicial action." *Id.* As the court points out:

Nowhere in the Bankruptcy Code does it say, "property

⁵ *Nova Tool & Engineering* includes an excellent discussion of constructive trust doctrine in relation to property of a bankruptcy estate as addressed by the United States Court of Appeals for the Seventh Circuit (*Nova Tool, supra.*, at 683-684) which can at least be read as establishing the proposition that property subject to arguments such as those made by Dexia and by the United States clearly constitutes property of Judith's bankruptcy estate.

held by the debtor subject to a constructive trust is excluded from the debtor's estate." Title 11 U.S.C. § 541 defines the estate in bankruptcy broadly, including "all legal or equitable interests of the debtor in property as of the commencement of the case," § 541(a), and "any interest in property preserved for the benefit of or ordered transferred to the estate under [the trustee's 'strong arm' or 'avoiding' powers as provided in] section 510(c) or 551 of this title," § 541(a)(4).

Id. at 1448. The court further explained:

The distribution of assets in a bankruptcy case is based on an identification of what assets and liabilities the debtor has "as of the commencement of the case," this being the exact moment the debtor files. A debtor that served prior to bankruptcy as trustee of an express trust generally has no right to the assets kept in trust, and the trustee in bankruptcy must fork them over to the beneficiary. However, a claim filed in bankruptcy court asserting rights to certain assets "held" in "constructive trust" for the claimant is nothing more than that: a claim. Unless a court has already impressed a constructive trust upon certain assets or a legislature has created a specific statutory right to have particular kinds of funds held as if in trust, the claimant cannot properly represent to the bankruptcy court that he was, at the time of the commencement of the case, a beneficiary of a constructive trust held by the debtor.

Id. at 1449 (citation omitted).

The Trustee argues that *Omegas Group* is not applicable in this case because in this case the Orlando bankruptcy court determined ownership of the disputed assets before the filing of Mrs. Gurley's petition. The Court notes, however, that what Judge Briskman did was to create a remedy to prevent unjust enrichment of Mrs. Gurley at the expense of Mr. Gurley's creditors. But for the Memorandum Opinion and Amended Judgment, there would be no question of the "ownership" of these assets. All records indicate that the assets are owned by Mrs. Gurley, even though Mr. Gurley exercises dominion and control over them.

Moreover, with respect to Judith's interests in real property (whatever those interests may be), it might be that the avoidance powers of 11 U.S.C. § 544(a)(3) – exercisable by the Chapter 13 Trustee in this case – will trump any attempt to impose a constructive trust or similar remedy upon those property interests; *See, Belisle v. Plunkett*, 877 F.2d 512 (7th Cir. 1989).

The potential for conflict between the bankruptcy estate's utilization of § 544(a)(3) and contentions made by Dexia and the United States clearly argue in favor of the bankruptcy court's being the appropriate forum for determination of the claims of Dexia and of the United States, and thus argue against lifting of the automatic stay.

Again, the critical concept is the fact that Judith's estate presently includes all of the property interests which Dexia and the United States seek to reach. 28 U.S.C. § 1334(e)(1) states:

(e) The district court in which a case under title 11 is commenced or is pending shall have exclusive jurisdiction—

(1) of all the property, wherever located, of the debtor as of the commencement of such case, and of property of the estate;
(emphasis supplied)

The exclusive jurisdiction of the bankruptcy court over property of a bankruptcy estate was discussed as follows in *In re Cook*, 384 B.R. 282, 296 (Bankr. N.D.Ala. 2008):

An important and beneficial attribute of bankruptcy is its inclusiveness. It gathers all assets of, and claims against, a debtor within one tribunal for administration, liquidation and adjustment. 28 U.S.C. § 157(b)(2). To maintain this inclusiveness, a bankruptcy court has a duty to exercise jurisdiction in matters arising under the Code or arising in a bankruptcy case, unless the court finds abstention is in the best interest of the parties and the estate, and will not jeopardize the rights, remedies, safeguards and legitimate expectations provided under the Code to the parties in interest. In short, a bankruptcy court should be reluctant to relinquish its jurisdiction over core proceedings, unless there is a specific showing abstention will better serve the parties in interest and the estate.

In *B & M Properties*, the District Court found the state circuit court action was only related to the underlying bankruptcy case. 342 B.R. at 632. A bankruptcy court must abstain from hearing a "related to" proceeding if there is no federal jurisdiction absent the bankruptcy case, the action is commenced in state court, and there can be a timely adjudication in state court. 28 U.S.C. § 1334(c)(2). The state court action in *B & M Properties* involved a lien claimed against property of the estate,^{FN21} and the debtor as owner of that property was a necessary party to that action. (footnote omitted) *Lily Flagg Bldg. Supply Co.*, *supra.*; *Sorsby v.*

Woodlawn Lumber Co., 202 Ala. 566, 81 So. 68 (1919); *Hughes v. Torgerson*, 96 Ala. 346, 11 So. 209 (1892). The court that determines the validity, extent and priority of the lien must inevitably determine whether the lien is enforceable. An unenforceable and, therefore, unperfected lien, is subject to avoidance by a trustee or debtor-in-possession and disallowance as a secured claim. Avoidance actions are core proceedings. 28 U.S.C. § 157(b)(2)(F), (H). If these additional factors had been addressed, perhaps the District Court in *B & M Properties* would have found the state court action involved core bankruptcy proceedings arising under the Code, potentially having a significant impact on property of the bankruptcy estate and parties in interest, and was not merely a proceeding related to the underlying bankruptcy case. (footnote omitted)

FN21. 28 U.S.C. § 1334(e)(1) provides that the district court in a bankruptcy case has exclusive jurisdiction of all the property of the debtor and the estate. The bankruptcy court is an unit of the district court. 28 U.S.C. § 151. By virtue of the Order of Reference, the bankruptcy court has the same jurisdiction as the district court under title 11 of the U.S.Code over property of the estate. 28 U.S.C. § 157(a). Unless there are compelling reasons, it is inappropriate for a bankruptcy court to abstain from adjudicating a critical issue in a core proceeding that involves property of the estate over which the bankruptcy court has exclusive jurisdiction. There are no such compelling reasons in this case, especially since Welch is not hindered by the Code from perfecting his lien.

As stated in *In re Brown*, 22 B.R. 844, 850 (Bankr. N.D.N.Y. 1982):

As of the date of the Debtor's petition, this Court's exclusive jurisdiction includes the power to resolve competing claims to property alleged to belong to the Debtor. (citations omitted)

A dispute over the entitlement to life insurance proceeds, in which the insurance company sought relief from the stay to file an interpleader in a non-bankruptcy forum, drew this comment in *In re Grogg*, 295 B.R. 297, 307 (Bankr. C.D.Ill. 2003):

The fact that the insurance proceeds are property of LINDA'S bankruptcy estate, and that the determination of the dispute is a core proceeding, weigh heavily in favor of the bankruptcy court as the proper forum for commencement of the litigation.

Determination of competing interests in bankruptcy estate property by the bankruptcy

court is in accord with the general bankruptcy policy of considering ratable distribution as an element when equitable remedies seeking to affect bankruptcy estate property are asserted.

As stated in *In re Golden Triangle Capital, Inc.*, 171 B.R. 79, 82 (9th Cir. BAP 1994):

Determination of whether bankruptcy's policy of ratable distribution outweighs imposition of a trust depends on whether the trust arises out of intended ownership rights in the property or whether it is to be imposed as a remedy to correct a wrong. Analysis focuses on the legal relationship between the parties. If no debtor-creditor relationship exists, a trust will exclude property from the estate. This is the conclusion of *Unicom*, (property never intended for the debtor is not part of the estate); *In re Torrez*, 63 B.R. 751 (9th Cir. BAP 1986) (property held at all times in a resulting trust is not part of the estate); and *In re Anchorage Nautical Tours, Inc.*, 102 B.R. 741 (9th Cir. BAP 1989) (prepetition oral assignment of insurance proceeds effective against subsequent lienholders and bankruptcy estate).

If, on the other hand, the trust is imposed as a remedy for a claim, circumstances may warrant treating the claimant as any other creditor of the debtor, and thus subject to the policy of ratable distribution. This is the result in *In re Tleel*, 876 F.2d 769 (9th Cir.1989) (inchoate trust remedy not superior to trustee's strong-arm power); *In re Bullion Reserve of North America*, 836 F.2d 1214 (9th Cir.1988), *cert. denied*, *Bozek v. Danning*, 486 U.S. 1056, 108 S.Ct. 2824, 100 L.Ed.2d 925 (1988) (transfer of funds to debtor in exchange for right to purchase bullion creates claim based on debtor-creditor relationship); *In re Lewis W. Shurtleff, Inc.*, 778 F.2d 1416 (9th Cir.1985) (inchoate remedy of constructive trust not superior to trustee's strong-arm and policy of ratable distribution); *In re North American Coin & Currency, Ltd.*, 767 F.2d 1573 (9th Cir.1985), *cert. denied*, *Daniel A. Torres, M.D., P.C. v. Eastlick*, 475 U.S. 1083, 106 S.Ct. 1462, 89 L.Ed.2d 719 (1986) (bankruptcy court will not impose remedy of constructive trust for creditors who are no differently situated than other creditors except for timing of the transaction); *In re Foam Systems Co.*, 92 B.R. 406 (9th Cir. BAP 1988), *affirmed*, 893 F.2d 1338 (9th Cir.1990) (where no trust, but rather a security transaction, was intended by the parties, a resulting trust will not be imposed to remedy defective perfection of the security interest).

Finally, in a case construing constructive trust doctrine under both Illinois law and the law of the Seventh Circuit, the following was stated in *In re Foos*, 183 B.R. 149, 160-161 (Bankr. N.D.Ill. 1995):

The analogy to this case is obvious: we too are involved in a liquidation under a statute that provides for the distribution of assets according to specified priorities. See 11 U.S.C. § 726. It is therefore fair to conclude that an Illinois court would refuse to impose a constructive trust in this case. But the decision in *Security Casualty* supports a broader conclusion: in Illinois, constructive trust is a remedy for unjust enrichment, not the basis of a claim to ownership. The court in *Security Casualty* rejected the shareholders' claim to an ownership interest in the funds; instead, the court viewed the issue as the availability of equitable relief in the face of the distribution statute. 127 Ill.2d at 447-48, 130 Ill.Dec. at 452-53, 537 N.E.2d at 781-82.

Illinois law is therefore fully consistent with Professor's Sherwin's analysis that it is a mistake to “equate the constructive trust claimant's rights against the debtor with equitable ownership ... [as if] the claimant has an equitable interest in the property she claims, which survives the commencement of bankruptcy proceedings.” Sherwin at 315. This approach “reflects a misunderstanding of the remedial nature of constructive trusts” by assuming an ownership interest where none exists. Sherwin at 317, 339. The “mistake has been to treat the claimant's state law *remedy* as a right of equitable *ownership* for purposes of distribution in bankruptcy.... A constructive trust is not a right of ownership, but an equitable remedy against unjust enrichment.” Sherwin at 317 (emphasis supplied). Therefore, “[u]nless a court has already impressed a constructive trust upon certain assets or a legislature has created a specific statutory right to have particular kinds of funds held as if in trust,” (*Omegas Group*, 16 F.3d at 1449) the claimant has no property rights whatsoever. Rather, he merely has an unsecured claim against the debtor's estate.

This conclusion is also consistent with decisions in this Circuit. There is *dicta* in *Belisle v. Plunkett* that “[a] constructive trust ordinarily survives bankruptcy: the property may not be used to satisfy the debtor's obligations to other creditors....” *Belisle*, 877 F.2d at 513. But the authorities cited for that proposition do not support it. The Supreme Court's decision in *United States v. Whiting Pools, Inc.*, 462 U.S. 198, 103 S.Ct. 2309, 76 L.Ed.2d 515 (1983) did not deal at all with constructive trusts, though it did note that funds held in trust pursuant to statute might be excluded from the estate. *Whiting Pools*, 462 U.S. at 205 n. 10, 103 S.Ct. at 2314 n. 10. The court in *Heyman v. Kemp (In re Teltronics, Ltd.)*, 649 F.2d 1236 (7th Cir.1981) held only that the former bankruptcy act did not require a statutory receiver of the proceeds of consumer frauds to turn over those funds to a bankruptcy trustee. *Teltronics*, 649 F.2d at 1239 (“The bankruptcy rule simply does not apply to a receiver under the Consumer Fraud Act”). Here,

there is no statute creating special rights in the disputed funds. *Belisle* itself held only that a constructive trust claim was subject to the trustee's strong-arm powers to set aside certain interests under § 544(a)(3) of the bankruptcy code. Although that issue is not present in this case, the holding in *Belisle* supports the general point that there is little room for constructive trusts in bankruptcy.

Here, no constructive trust was judicially or statutorily imposed before bankruptcy. Yet the only entitlement to these funds asserted by Skadden is as the beneficiary of a constructive trust to remedy the Debtor's unjust enrichment. The Court concludes, based on the foregoing analysis, that Skadden has no equitable or other property interest in these funds. Its interest is indistinguishable from that of the other creditors, and that interest is really an interest in the estate, which is represented by the Trustee.

3. The Availability of the Constructive Trust Remedy Post-Bankruptcy

Even viewing constructive trust as a remedy, rather than a form of property right, however, it might still be appropriate to allow intervention to give Skadden a chance to convince this Court to impose that remedy. But intervention is not appropriate because this Court lacks the authority to grant that relief in a bankruptcy case. Alternatively, even if that authority existed, it should not be exercised in this case.

Chapter 7 provides for the distribution to creditors of the proceeds of the liquidation of estate assets in accordance with stated priorities among various classes of creditors. See 11 U.S.C. § 726. As we have seen, the imposition of a constructive trust creates a right in favor of the trust claimant to specific property. When property is removed from a bankruptcy estate, the effect is to give the trust claimant a super-priority, so that its claim is satisfied before those of other similarly situated creditors, and outside the statutory priority scheme. *In Matter of Haber Oil*, 12 F.3d 426, 436 (5th Cir.1994) (“Because the constructive trust doctrine can wreak such havoc with the priority system ordained by the Bankruptcy Code, bankruptcy courts are generally reluctant ‘to impose constructive trusts without a substantial reason to do so’ ”) (quoting *Neochem Corp. v. Behring Int'l, Inc. (In re Behring Int'l, Inc.)*, 61 B.R. 896, 902 (Bankr.N.D.Tex.1986)).

Nothing in the bankruptcy code authorizes the super-priority treatment of creditors whose only claim to such treatment is that they would be entitled to the remedy of the imposition of a constructive trust outside of bankruptcy. As a general rule,

bankruptcy courts may not alter the statutory priorities. *Shapiro v. Saybrook Mfg. Co., Inc. (In re Saybrook Mfg. Co., Inc.)*, 963 F.2d 1490, 1495-96 (11th Cir.1992) (“Section 507 of the Bankruptcy Code fixes the priority order of claims and expenses against the bankruptcy estate. Creditors within a given class are to be treated equally, and bankruptcy courts may not create their own rules of superpriority within a single class”) (citations omitted); *Transamerica Commercial Fin. Corp. v. Citibank, N.A. (In re Sun Runner Marine, Inc.)*, 945 F.2d 1089, 1094 (9th Cir.1991) (“To [pay certain pre-petition unsecured claims in full while other remain unpaid] would impermissibly violate the priority scheme of the Bankruptcy Code”); *In re FCX, Inc.*, 60 B.R. 405, 409-11 (E.D.N.C.1986) (court cannot alter distribution priorities absent inequitable conduct by claimant); *In re Baldwin-United Corporation, D.H.*, 43 B.R. 443, 457 (S.D. Ohio 1984) (“It is ... beyond travail that the most significant policy in bankruptcy jurisprudence is equality of treatment of like-situated creditors”).

Courts that understand the significance of the bankruptcy filing have refused to impose constructive trusts post-bankruptcy. These courts recognize that the imposition of a constructive trust “creates a mechanism by which a creditor may attain a position roughly equivalent to a perfected security interest in proceeds without complying with the usual statutory formalities, ... and thus tends to undercut the statutory scheme.” *Auto-Train*, 810 F.2d at 275. *Accord Omegas Group*, 16 F.3d at 1452 (“The equities of bankruptcy are not the equities of the common law. Constructive trusts are anathema to the equities of bankruptcy since they take from the estate, and thus directly from competing creditors, not from the offending debtor”); *Oxford Organisation v. Peterson (In re Stotler and Co.)*, 144 B.R. 385, 388 (N.D.Ill.1992) (Aspen, J.) (“a constructive trust is fundamentally at odds with the general goals of the Bankruptcy Code”). *North American Coin & Currency*, 767 F.2d at 1575 (courts “necessarily act very cautiously in exercising such a relatively undefined equitable power in favor of one group of potential creditors at the expense of other creditors, for ratable distribution is one of the strongest policies behind the bankruptcy laws”).⁶

The foregoing cases are not cited to express the court’s position on the assertion of constructive trust, or similar, theories in relation to property of a debtor’s bankruptcy estate. Rather, the cases are addressed to emphasize the critical difference between litigation which

⁶ Previously in this decision, the court assumed, *in arguendo*, that Indiana law would apply to Dexia’s and the United States’ constructive trust contentions. As stated in *Foos*, Illinois and Seventh Circuit law appear to be parallel to Indiana law.

seeks solely to determine a monetary claim, and litigation which seeks to determine the scope of bankruptcy estate property. Because of its exclusive jurisdiction over § 541(a) property, the bankruptcy court is both statutorily empowered and perhaps statutorily required to retain and exercise control over determinations which affect claims to estate property, and as a result affect distributions to creditors in a bankruptcy case.

The question arises as to the interface of the foregoing analysis with the *Fernstrom* criteria. Putting aside the begged question of whether *Fernstrom* exclusively applies in a context such as that at issue in this case (see, *In re Comdisco, supra.*), as contrasted to the relatively straight forward context of a party proceeding solely against insurance proceeds, the foregoing discussion falls comfortably into the first prong of the *Fernstrom* test, i.e., consideration of whether “any great prejudice to either the bankruptcy estate or the debtor will result from continuation of the civil suit”. Prejudice in this context is not focused on outcome, but rather upon an analysis of the relative expertise, focus, and jurisdiction of competing courts to address the issues at hand, and on the impact of addressing those issues on the administration of a bankruptcy estate. While certainly the judges of the United States District Court for the Northern District of Illinois have expertise in matters relating to fraudulent conveyances, nominee titleholders, constructive trusts and the like, because of the nature of the cases before it, the expertise of this court in those areas at least equals that of judges of the United States District Court for the Northern District of Illinois. The court also notes, solely for the sake of noting its background familiarity with potentially applicable law, that the undersigned was a principal instructor for the United States Department of Justice in its programs of attorney and agency education when the Federal Debt Collection Procedures Act was initially passed and implemented. This court, unlike a district court, has particularized expertise in the bankruptcy arena with respect to concepts of law which may or may not apply under applicable precedent to determine issues relating to the imposition of constructive trusts or similar

remedies, and the potential utilization of § 544 or other avoidance powers. This court, unlike the district courts, is statutorily imbued with the responsibility for balancing the interests of all creditors and parties-in-interest whose claims may be affected by a determination of property interests. Given the issues that foreseeably will arise with respect to the matters asserted by Dexia and the United States, this court is quite comfortable in determining that significant prejudice may arise to the interests of the estate and/or the debtor if the assertions of Dexia and the United States are determined in a non-bankruptcy forum. Thus, the first *Fernstrom* factor weighs in favor of denying the requested relief.

With respect to the second *Fernstrom* factor, the issue is really where litigation will be conducted, not if it will be, and in this context the hardship to Dexia and the United States by maintenance of the stay is roughly equivalent to the hardship which may be experienced by the debtor if the stay is lifted. If the court denies the stay relief motions, a ready forum is available in this court for determination of Dexia's and the United States' claims and/or interests, through the mechanism of litigation which both Dexia and the United States may commence. It should also be noted that Dexia and the United States have both filed claims in Judith's case, the respective determinations of which involve the issues pending in the Northern District of Illinois, and which will generate "core proceedings" under 28 U.S.C. § 157(b)(2)(B), if those claims are challenged by the debtor. Because of the proximity of Chicago, Illinois to Hammond, Indiana, the court perceives no prejudice to either party by having to travel to, and present matters in, either venue. Because the Chapter 13 Trustee is inevitably involved in issues concerning interests of the debtor in property and seeking to advance the interests of creditors of the debtor through those interests, maintaining jurisdiction in the United States Bankruptcy Court in Hammond, Indiana weighs slightly in favor of denying the motions for relief from stay, albeit very slightly. Dexia and the United States have sought to make the argument that extensive discovery has already been undertaken in the Northern District of Illinois, and that this is a

factor in their favor. Discovery is discovery, and to the extent it has been undertaken and concluded, the parties already have the information which the discovery was designed to provide. To the extent they don't have that information, continued discovery in either forum is a neutral factor. As to the contention that judges who have determined the underlying liability of Peter Rogan and others, and are therefore extensively familiar with the schemes of those persons or entities – have a leg up over this court, the court responds first that those courts are limited to a record made in prior proceedings, a record which this court is more than capable of determining. Moreover, whether or not Dexia and/or the United States can succeed in their actions depends in significant part upon concepts of tracing of property into the hands of those whom it is alleged are not entitled to it. That evidence is just as easily presented here as it is in proceedings in Chicago. Whether or not those claims can be successfully made depends in large part on the extent to which Judith can establish sources of funds for assets in which she has an interest which arose from her and her husband's legitimate employment, an issue which is just as easily determined by this court as it would be by a trial court in the underlying fraud actions against Peter Rogan, et al. in which those issues – from the court's review of the dockets in the underlying cases – were not significantly addressed previously. Given that the second prong is that the hardship to Dexia and to the United States must considerably outweigh the hardship to the debtor, this factor weighs in favor of the debtor.

The final factor – whether or not Dexia and the United States have a probability of prevailing on the merits – will in large part depend upon whether or not their actions can be undertaken to defeat the interests of the bankruptcy estate. It should be apparent by now that these issues are not at all clear, and that the law applicable to their determination is much more within the realm of expertise of the bankruptcy court than it is of the district court. Given that the standard for “prevailing” is essentially the assertion of an action that is not frivolous, it is beyond question that the record before the court establishes significant issues as to the origin

of the property of Judith which at this time constitutes property of her bankruptcy estate. Thus, Dexia and the United States have satisfied this prong. However, the determination of their actions can be as easily accomplished in the bankruptcy court by means of an adversary proceeding under Fed.R.Bankr.P. 7001(1), (2), (7) and/or (9) as it can by proceeding with the presently pending actions in the Northern District of Illinois.

Based upon the foregoing, the court determines that Dexia and the United States have failed to establish "cause" under 11 U.S.C. § 362(d)(1) with respect to their requests for lifting of the automatic stay to proceed with pending actions in the United States District Court for the Northern District of Illinois. The motions filed respectively by those creditors are therefore denied.

IT IS ORDERED that the Motion to Modify Automatic Stay filed by Dexia Credit Local is denied.

IT IS FURTHER ORDERED that the Motion to Join Dexia's Motion to Modify Stay filed by the United States of America is also denied.

Dated at Hammond, Indiana on July 23, 2009.

/s/ J. Philip Klingeberger
J. Philip Klingeberger, Judge
United States Bankruptcy Court

Distribution:
Debtor, Attorney for Debtor
Trustee, US Trustee
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