

Not Intended for Publication or Citation

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF INDIANA
FORT WAYNE DIVISION

IN THE MATTER OF:)
)
BIG HORN LAND & CATTLE CO., LLC) CASE NO. 09-10254
)
)
Debtor)

DECISION

At Fort Wayne, Indiana, on March 22, 2010.

This matter is before the court following trial of the issues raised by the Chapter 7 trustee's motion to compromise and the objections thereto filed by Rudolfo Rodriguez, a creditor and the sole member of the debtor.

Prior to bankruptcy, the debtor was involved in litigation with David and Deemia Wehner over a land sale contract by which the debtor was purchasing property located in LaGrange County. The Wehners claimed the debtor had breached that agreement and the debtor sought to rescind it, claiming fraud. The LaGrange Circuit Court ruled in favor of the Wehners, entered a judgment of foreclosure, and an appeal was taken from its decision. Before the Court of Appeals could decide the matter, the debtor filed a petition for relief under Chapter 11, staying those proceedings. The case was subsequently converted to Chapter 7 and the trustee has negotiated a settlement of the dispute. The essence of the settlement is that the property will be sold, the sale proceeds will be used to pay the costs of sale and the Wehners' secured claim; any excess will be paid to the estate, but the estate will receive no less than \$4,000. The pending appeal is to be dismissed with prejudice. By agreement of all concerned, the property has been sold; so the issue before the court concerns the sufficiency of the \$4,000 the trustee agreed to accept in settlement of the estate's claims.

While private parties may settle their disputes on any terms which may be mutually satisfactory, that is not the case in bankruptcy proceedings. In re Chicago Rapid Transit, 196 F.2d 484, 490 (7th Cir.1952). Where a settlement affects the assets of a bankruptcy estate or their distribution, the settlement must be approved by the bankruptcy court. Doing so is a matter committed to the court's discretion. In re Doctors Hospital of Hyde Park, Inc., 474 F.3d 421, 426 (7th Cir. 2007). The court should canvas the issues, familiarize itself with the attendant facts and circumstances, and "make a[n] 'informed and independent judgment' about the settlement," In re American Reserve Corp., 841 F.2d 159, 162 (7th Cir.1987), deciding "whether [it] is in the best interests of the estate." Matter of Energy Co-op., Inc., 886 F.2d 921, 927 (7th Cir.1989). As the proponent of the settlement, the trustee bears the burden of proving that it is. In re Bell & Beckwith, 93 B.R. 569, 574 (Bankr. N.D. Ohio 1988).

It is important to remember that the court is not really deciding what the terms of any settlement should be. The decision to settle, and on what basis, has already been made – in this instance by the trustee. What the court is actually doing is reviewing the propriety of the decision to settle the matter on the terms proposed. In undertaking this review, the court does not substitute its own judgment for that of the trustee. In re Martin, 212 B.R. 316, 319 (8th Cir. BAP 1988). Instead, it should determine whether the trustee adequately investigated the matter and made an informed decision when choosing between the available alternatives, see, In re Del Grosso, 106 B.R. 165, 168-69 (Bankr. N.D. Ill. 1989); if so, the court should decide whether the settlement's terms "fall within the reasonable range of litigation possibilities." Energy Co-op, 886 F.2d at 929 (quoting In re New York, N.H. & H.R. Co., 632 F.2d 955 (2nd Cir.1980)). If they do, the settlement should be approved; this remains so even if the court thinks a better deal might have been possible or that

the estate would be likely to prevail if the matter were litigated to a conclusion. See e.g., In re Austin, 186 B.R. 397, 400 (Bankr. E.D. Va. 1995) (“the settlement may be approved even if the court finds it likely that the trustee would ultimately succeed in the litigation.”).

In many respects the bankruptcy court’s review of a trustee’s decision to accept a proposed settlement involves an analysis that is very similar to that used by an appellate court in determining whether or not a trial court abuses its discretion when it is faced with discretionary choices. This is so because a trustee is not required to litigate every cause of action the estate may possess, neither is it required to challenge every competing claim to the debtor’s assets. Quite to the contrary, the trustee is given a substantial degree of prosecutorial discretion in determining whether or not such claims should be pursued or challenged or settled or abandoned. See e.g., In re Consolidated Industries, Corp., 330 B.R. 712, 715 (Bankr. N.D. Ind. 2005); In re V. Sevino Oil & Hearing Co., Inc., 91 B.R. 655, 656 (Bankr. E.D. N.Y. 1988); 3 Collier on Bankruptcy ¶ 323.03 (15th ed. rev.) (“the trustee has the authority and the discretion to prosecute, defend and/or settle, if appropriate in its judgment, causes of action which existed at the time the order for relief was entered”). In exercising that discretion, the trustee is expected to familiarize itself with the underlying facts and circumstances concerning the estate’s rights and, after analyzing the competing risks and rewards, make an informed decision as to where the estate’s best interests lie. When the trustee does so, the decision to settle is entitled to a degree of deference. In re Stone Concrete Contractors Inc., 346 B.R. 32, 49 (Bankr. D. Mass. 2006); In re Drexel Burnham Lambert Group, 134 B.R. 493, 496 (Bankr. S.D. N.Y. 1991). See also, In re Media Cent., Inc., 190 B.R. 316, 321 (E.D. Tenn.1994); In re Edwards, 228 B.R. 552, 569 (Bankr. E.D. Pa.1998). Cf., Consolidated Industries, 330 B.R. at 715 (trustee’s decisions concerning the administration of the estate are measured by a business judgment

standard). Conversely, a settlement negotiated without reference to the underlying merits of the competing claims or without an adequate inquiry into those claims should not be approved. Chicago Rapid Transit, 196 F.2d at 484; Matter of Howard Miller & Associates., 1990 WL 300918 *3 (Bankr. N.D. Ind. 1990); Stone Concrete, 346 B.R. 32, 49.

The court makes these observations concerning the trustee's responsibilities in the settlement process because of the nature of the objection to the proposed compromise. While part of the objection may be nothing more than a difference of opinion over the value of the estate's claims against the Wehners, a good part of it is directed to the adequacy of the trustee's investigation of those claims; in particular the issues presented by the appeal of the trial court's decision.

Due to a pending motion for relief from stay, the trustee believed she was faced with a tight deadline within which to complete her investigation. That investigation involved reviewing the debtor's schedules and statement of financial affairs, the motions to dismiss or convert which had been filed by the United States Trustee and the Wehners, the U.S. Trustee's notes from the meeting of creditors held while the case was pending under Chapter 11, the state court's findings of fact and conclusions of law, valuation information, some photographs, and some communications from an auctioneer and counsel for the Wehners. In evaluating all this information, she placed the greatest emphasis on the state court's decision. One thing that was not done, however, was to have a meaningful discussion with debtor's counsel in the state court proceeding concerning his perspective on the controversy, the issues presented by the pending appeal, or their merits. By not doing so, the trustee failed to make a sufficiently informed decision concerning the settlement.

Part of evaluating the adequacy of any investigation involves the amount of time available

for the investigation. Here, because of a the convergence of separate events,¹ the trustee was, at least initially, under a relatively short deadline to make some kind of decision concerning the Wehners' motion for relief from stay, and it was in connection with that motion that settlement negotiations were conducted and the decision to settle was made. But the time available for the trustee's investigation may not have been quite so limited as she perceives. A Chapter 7 trustee is entitled to a reasonable opportunity for investigation before property passes out of the estate, In re Szymanski, 344 B.R. 891, 897 (Bankr. N.D. ind. 2006), and if the time constraints she was facing did not allow her that opportunity, she could have objected to the Wehners' motion. The court also notes that the trustee and the Wehners filed two agreed motions extending the deadline for the trustee to file an objection. Under these circumstances, it does not seem that the time constraints facing the trustee were that narrow, and nothing about them suggests that they were not sufficient to give the trustee the opportunity to contact debtor's state court counsel in order to discuss the matter with him. As the attorney who represented the debtor in the state court trial and the one who filed the pending appeal, he was a relatively obvious source of meaningful information for the trustee; he could give the trustee something other than the Wehners' side of the story. See, Stone Concrete, 346 B.R. at 48-50 (interviewing only four people, three of whom were the trustee's adversaries, was not sufficient).

One of the reasons it was so important for the trustee to have contacted debtor's state court counsel is because some of the issues on appeal have to do with the way in which the state court's

¹This case began as a Chapter 11 and was subsequently converted to Chapter 7, as the result of motions filed by both the Wehners and the UST. The Wehners had also filed a separate motion for relief from stay and abandonment. All three motions were heard on the same day. The orders from those proceedings converted the case and gave the Chapter 7 trustee (who did not exist at the time of the hearing) twenty-one days to object to the stay motion. Orders dated April 24, 2009.

findings of fact and conclusions of law came to be. The trustee gave that decision the greatest emphasis in her evaluation of the controversy; yet, rather than being the independent work product of the state court judge, it appears that the state court simply adopted the Wehners' proposed findings and conclusions verbatim, right down to the typos. While doing so is not prohibited, it is frowned upon and may subject the trial court's decision to more scrutiny by the appellate court than one might otherwise expect. See, Prowell v. State, 741 N.E.2d 704, 708-09 (Ind. 2001). See also, Parks v. Delaware County Dept. of Child Services, 862 N.E.2d 1275, 1278 (Ind. Ct. App. 2007); Maloblocki v. Maloblocki, 646 N.E.2d 358, 361-62 (Ind. Ct. App. 1995). By failing to contact debtor's state court counsel, the trustee never learned that the origin of the very document she relied upon most heavily might very well be among the estate's strongest arguments on appeal. She was never able to consider that argument in her evaluation of the case or of the estate's prospects for a successful appeal.

The court recognizes that a trustee's investigation does not have to be exhaustive: the trustee need not turn over every stone before making a decision to settle. The investigation does, however, have to be reasonable or appropriate to the circumstances. Furthermore, a party will not be able to defeat a proposed settlement simply by identifying just any issue and then arguing that the trustee failed to consider it. It must be a meaningful issue: one that matters. Del Grosso, 106 B.R. at 168. It must also be one that would have been discovered in the course of a reasonable (time permitting) investigation of the matter and which, if pursued, would have produced information that should have been taken into consideration in making the decision to settle. The arguments raised in opposition to the proposed settlement concerning the trustee's failure to sufficiently investigate the issues on appeal satisfy all these criteria.

In the trustee's defense the court will acknowledge that debtor's state court counsel never approached the trustee and volunteered any of his information. It is not as though he was beating down her door and frantically trying to get her attention, while she studiously ignored him. Apparently, it was not until the last day of the deadline for objections to the motion to compromise that he brought his information to the trustee's attention, through the objection which was filed on Rodriguez's behalf. Of course, by then it was too late: the proposed settlement had already been negotiated. We will never know what might have happened had counsel been a bit more pro-active and sought out the trustee soon after conversion, and there is no reason he could not have done so. Despite the fact that one might wish opposing counsel had done more while there was still time to influence the trustee's decision, it is the trustee who had the affirmative obligation to investigate the issues associated with the administration of the estate and the compromise of claims belonging to it; it was not the other way around. Debtor's state court counsel was an obvious source of information concerning the claim against the Wehners and the pending appeal, and by neglecting that source the trustee failed to make an adequately informed decision concerning the settlement.

The objection is sustained and the motion to approve compromise will be DENIED. An order doing so will be entered.

/s/ Robert E. Grant
Chief Judge, United States Bankruptcy Court