

UNITED STATES BANKRUPTCY COURT  
EASTERN DISTRICT OF TENNESSEE  
Southern Division

In re

DON WILLIAMS CONSTRUCTION CO.,  
INC.

Bankruptcy Case  
No. 91-13102

GERALD D. WHITE &  
KAREN S. WHITE,

Adversary Proceeding  
No. 94-1081

Plaintiffs

V.

JERRY FARINASH, Trustee  
In Bankruptcy, and  
FIRST TENNESSEE BANK,

Defendants

**MEMORANDUM**

Appearances: Mark E. Whittenburg, Chattanooga, Tennessee, Attorney for Plaintiffs

Richard B. Gossett, Baker, Donelson, Bearman, Adams & Caldwell, Chattanooga, Tennessee, Attorney for First Tennessee Bank

Jerry Farinash, Kennedy, Fulton & Koontz, Chattanooga, Tennessee, Attorney for the Trustee

R. Thomas Stinnett, United States Bankruptcy Judge

First Tennessee Bank ("Bank") has filed a motion to dismiss for lack of subject matter jurisdiction or for abstention if the court does have subject matter jurisdiction. For the reasons hereinafter stated, the motion is sustained and this adversary proceeding shall be dismissed.

Several months before this bankruptcy case was filed, the plaintiffs bought and paid for a subdivision lot owned by the debtor, Don Williams Construction Co., Inc. ("debtor"). The lot was subject to a deed of trust held by the Bank to secure repayment of the subdivision development loan. The debtor executed a warranty deed in favor of plaintiffs but the Bank never released its deed of trust on the lot. It is unclear whether the Bank was ever called upon to do so by the debtor. The plaintiffs do not allege they had any direct contact with the Bank regarding release of the deed of trust as to this lot.

The plaintiffs have brought suit against the Bank and the bankruptcy trustee. They argue that the Bank should be required to release the mortgage or that the Bank is estopped to enforce it. In the alternative, they ask the court to determine how much plaintiffs must pay the Bank to have the mortgage released. Only one prayer for relief concerns the trustee. The court is requested to determine the proper amount of the plaintiffs' claim in the bankruptcy case for the purposes of payment by the trustee even though the trustee has not objected to plaintiffs' claim.

Bankruptcy courts have subject matter jurisdiction of bankruptcy cases, proceedings arising in a bankruptcy case, proceedings arising under the Bankruptcy Code, and proceedings related

to a bankruptcy case. 11 U.S.C. § 1334(a) & (b). The power of a bankruptcy court to render a final decision varies according to whether a proceeding is a core proceeding or a non-core proceeding. In a core proceeding, the bankruptcy court can enter a final order subject to appeal to the district court. In related proceedings the bankruptcy court's decision is automatically reviewed *de novo* by the district court, unless the parties consent to a final decision by the bankruptcy court. 28 U.S.C. § 157(b) & (c).

The Bank contends this is not even a related proceeding, but if it is, the court should abstain. 28 U.S.C. §1334(b) and 28 U.S.C. §157(a). The Bank admits the mandatory abstention statute does not apply and suggests discretionary abstention. 28 U.S.C. §1334(c). The plaintiffs argue that this is a core proceeding, and since it is a core proceeding, the court obviously has subject matter jurisdiction and should not abstain.

#### Core or Non-core

There are several provisions in the statute that might include this dispute as a core proceeding. 28 U.S.C. § 157(b)(2) (A), (B), (K), & (O). However, these provisions cannot be extended too far. The division of proceedings into core and non-core was intended to deal with the constitutional principle set out by the Supreme Court in *Northern Pipeline Const. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 102 S.Ct. 2858, 73 L.Ed.2d 785 (1982). Core proceedings include only those disputes in which the bankruptcy court may constitutionally enter a final decision with no opportunity for an Article III judge to consider the issues except by

appellate review. The courts must construe the statutory provisions for core proceedings to abide by the constitutional principle. *Cain Partnership, Ltd. v. Pioneer Investment Services Co. (In re Pioneer Inv. Serv. Co.)*, 946 F.2d 445, 449, 22 Bankr.Ct.Dec. 118 (6th Cir. 1991); 3 DAVID G. EPSTEIN, ET AL., BANKRUPTCY §§ 12-2 & 12-3 (1992).

Whether a proceeding is core or non-core depends on both the form and the substance of the proceeding. *Michigan Employment Security Commission v. Wolverine Radio Corp.*, 930 F.2d 1132, 21 Bankr.Ct.Dec. 932, 24 Collier Bankr.Cas.2d 1702 (6th Cir. 1991). See also *Sanders Confectionery Products Inc. v. Heller Financial, Inc.*, 973 F.2d 474, 483 (6th Cir. 1992); *Cain Partnership, Ltd. v. Pioneer Investment Services Co. (In re Pioneer Inv. Serv. Co.)*, 946 F.2d 445, 449, 22 Bankr.Ct.Dec. 118 (6th Cir. 1991) (dicta).

Some proceedings are an integral part of the administration of the bankruptcy case. They are peculiarly bankruptcy proceedings, though the outcome may totally depend on pre-bankruptcy events and non-bankruptcy law. The court must also consider the underlying purpose and the potential effect of the proceeding relative to the bankruptcy case. Among other factors, the court should consider the nature of the parties' claims and defenses, how the dispute may affect the administration of the bankruptcy case, and whether the dispute involves the rights and liabilities of the debtor or other parties that arose out of the bankruptcy case. Cf. *Michigan Employment Security Commission v. Wolverine Radio Corp.*, 930 F.2d 1132, 1144-45 (6th Cir. 1991). The line between form and

substance is not always clear, and many types of disputes may come within the court's subject matter jurisdiction.

The plaintiffs brought this suit for the obvious purpose of freeing their property from the bank's mortgage. They did not bring suit for the purpose of determining the amount of their claim or the bank's claim in the bankruptcy case. Any effect on the claims will be incidental.

The dispute also does not involve property of the bankruptcy estate. The plaintiffs' lot did not become property of the bankruptcy estate because it was owned by the plaintiffs when the debtor filed bankruptcy. 11 U.S.C. § 541(a).

This proceeding is not peculiar to bankruptcy or an integral part of the administration of the case. It does not involve rights or liabilities arising out of the bankruptcy case. At most, the outcome may affect the administration of the bankruptcy case.

A dispute between creditors is not automatically a core proceeding simply because it may affect the amount of the creditors' claims in the bankruptcy case. The court concludes that this is not a core proceeding.

#### Subject Matter Jurisdiction

The plaintiffs argue that the court has subject matter jurisdiction because this dispute will affect their claim and the bank's claim in the bankruptcy case. The court has jurisdiction if this is at least a non-core related proceeding. 28 U.S.C. §§ 157(c) & 1334(b).

A dispute between two creditors that will affect their claims in the bankruptcy case may be within the court's jurisdiction as a non-core related proceeding. *Kaonohi Ohana, Ltd. v. Sutherland (In re Kaonohi Ohana, Ltd.)*, 873 F.2d 1302 (9th Cir. 1989); *Emerson v. Marty (In re Mark Benskin & Co., Inc.)*, 135 B.R. 825 (Bankr. W.D. Tenn. 1991); *Haden v. Edwards (In re Edwards)*, 100 B.R. 973 (Bankr. E.D. Tenn. 1989); *Churchill Cabinet Co. v. Continental Illinois Nat. Bank & Trust Co. (In re Destron, Inc.)*, 38 B.R. 310 (Bankr. N.D. Ill. 1984).

The Sixth Circuit has held that subject matter jurisdiction exists if a decision by the bankruptcy court would promote efficient and fair administration of bankruptcy cases. *Kelley v. Nodine (In re Salem Mortg. Co.)*, 783 F.2d 626, 635 (6th Cir. 1986). See also, *In re S.F. Cambridge Associates*, 135 B.R. 529 (Bankr. E.D. Tenn. 1991) (Stair); *United States v. Farmers State Bank (In re Alexander)*, 49 B.R. 733 (Bankr. D. N.D. 1985). The Sixth Circuit has also relied on the similar test of whether the outcome of the proceeding can conceivably have an effect on the bankruptcy case. *Michigan Employment Security Commission v. Wolverine Radio Corp.*, 930 F.2d 1132, 1140-43 (6th Cir. 1991); *Pacor, Inc. v. Higgins*, 743 F.2d 984 (3d Cir. 1984).

The Bank did not introduce any evidence other than the pleadings to support its motion to dismiss. This makes the Bank's motion to dismiss a facial challenge to jurisdiction. Courts have classified challenges to subject matter jurisdiction as facial or factual. *Mortensen v. First Federal Savings & Loan Association*, 549 F.2d 884 (3d Cir. 1977); *Williamson v. Tucker*, 645 F.2d 404

(5th Cir. 1981); *Mellon Bank v. Union National Bank*, 118 B.R. 31 (Bankr. W. D. Pa. 1990).

In a facial challenge, the defendant argues that the court does not in fact have jurisdiction. A court can decide a factual challenge only if the defendant introduces evidence, other than the pleadings, to show that the court does not have jurisdiction. *Titus v. Sullivan*, 4 F.3d 590 (8th Cir. 1993); *Yuksel v. Northern American Power Technology*, 805 F.Supp. 310 (E. D. Pa. 1992); *Prudential-Bache Securities, Inc. v. Lisle*, 659 F.2d 190 (N. D. Ill. 1987).

In a facial challenge the defendant argues that the facts alleged in the complaint are not sufficient to invoke jurisdiction. This is only a challenge to the complaint itself. 5A CHARLES A. WRIGHT, ET AL., FEDERAL PRACTICE AND PROCEDURE § 1350 at 211-212 (1990).

The complaint alleges jurisdiction on two grounds. The first ground is that this proceeding will affect the amount of the plaintiffs' and the Bank's claims in the bankruptcy case, and the amounts must be determined in order to complete the administration of the bankruptcy case. Second, the complaint requests the court to determine how much the plaintiffs must pay the bank for a release, and suggests that the bankruptcy trustee cannot complete the administration of the bankruptcy case without a decision on this point, because it is necessary for the trustee to evaluate the plaintiffs' claim.

For the purpose of deciding a facial challenge to jurisdiction, the court presumes that the facts alleged in the complaint

are true. *Williamson v. Tucker*, 645 F.2d 404 (5th Cir. 1981); *Prudential-Bache Securities, Inc. v. Lisle*, 659 F.2d 190 (N. D. Ill. 1987); see also *Ohio National Life Insurance Co. v. United States*, 922 F.2d 330 (6th Cir. 1992).

The complaint's allegations regarding jurisdiction fall into two categories. First are the factual allegations. They set out the facts regarding the plaintiffs' and the Bank's dealings with the debtor. These allegations also reveal that the Bank and the plaintiffs have filed claims in the bankruptcy case. Second are the allegations that the court must resolve this dispute in order for the trustee to complete the administration of the bankruptcy case.

The court is required to apply the presumption of truth to the factual allegations; however, the court is not required to apply the presumption of truth to conclusory allegations. *Sexton v. Barry*, 233 F.2d 220 (6th Cir. 1966). Plaintiffs allege the conclusion that this dispute must be resolved in order for the trustee to administer the bankruptcy case. The complaint does not allege facts to support the truthfulness of this conclusion.

The presumption that the alleged facts are true is also used for deciding motions under Rule 12(b)(6). Rule 12(b)(6) provides for dismissal on the ground that the complaint fails to state a claim upon which relief can be granted. FED. R. BANKR. P. 7012; FED. R. CIV. P. 12(b)(6). For the purposes of Rule 12(b)(6), the presumption applies only to facts alleged in the complaint and not to legal conclusions. *Briscoe v. LaHue*, 663 F.2d 713 (7th Cir.

1981) *aff'd* 460 U.S. 325, 103 S.Ct. 1108, 75 L.Ed.2d 96 (1983); *Sexton v. Barry, supra*.

For example, a complaint may allege the defendant committed fraud as defined under Tennessee law. If the defendant challenges the complaint by a motion under Rule 12(b)(6), the court cannot presume the truth of the allegation that the plaintiff committed fraud under Tennessee law. It is merely a conclusion. The facts alleged in the complaint must state a claim for fraud under Tennessee law. *Sexton v. Barry, supra*.

The same problem arises with the plaintiffs' complaint. The complaint asserts that this dispute must be resolved in order for the trustee to administer the bankruptcy case, but the facts alleged do not support this assertion.

The result is no different even if the court should presume the truth of all the allegations regarding jurisdiction, even those that are not supported by facts alleged in the complaint. At most, the allegations reveal that the Bank and the plaintiffs have filed claims in the bankruptcy case and the outcome of this dispute may affect those claims. They also reveal that the lot in question did not become property of the bankruptcy estate.

Under the most expansive reading of *Kelly v. Nodine, supra*, the bankruptcy court may have jurisdiction of a dispute between creditors if it will affect their claims in the bankruptcy case. This does not mean that the court will always have subject matter jurisdiction simply because the dispute between the creditors will affect their claims in the bankruptcy case, and certainly

does not mean that the court should always exercise subject matter jurisdiction when it may exist.

A resolution of this dispute by the court will not promote the efficient and fair administration of the bankruptcy case. The dispute may incidentally affect the parties' claims. The real purpose of the complaint is to free the plaintiffs' lot from the bank's mortgage. The lot is not and never was property of the bankruptcy estate. The issues do not involve questions of bankruptcy law. The bankruptcy trustee is named as a defendant but is essentially a bystander.

The court concludes that the allegations of the complaint are not sufficient to demonstrate subject matter jurisdiction. Normally the court would grant the plaintiffs an opportunity to amend the complaint to cure this problem. However, even if the court has jurisdiction, the court is of the opinion this is a proper case for discretionary abstention.

#### Abstention

The statute allows a court to abstain "in the interest of justice, or in the interest of comity with state courts or respect for state law." 28 U.S.C. §1334(c)(1). Though the statute refers to the abstention by the district court, the question has in effect been referred to the bankruptcy court. 28 U.S.C. § 157(a); FED. R. BANKR. P. 5011.

The courts have listed numerous factors that may be relevant when deciding whether or not to abstain. *See, e.g., Republic*

*Reader's Service, Inc. v. Magazine Service Bureau, Inc. (In re Reader's Service, Inc.)*, 81 B.R. 422, 429 (Bankr. W. D. Tex. 1987); *Christensen v. Tucson Estates, Inc. (In re Tucson Estates, Inc.)*, 912 F.2d 1162, 1166-1167 (9th Cir. 1991).

In the *Salem Mortgage* case, the Sixth Circuit said:

The degree to which a related proceeding is related to the bankruptcy case, as a practical matter, will doubtless be an important factor in the decision whether to abstain.

*Kelley v. Nodine (In re Salem Mortg. Co.)*, 783 F.2d 626, 635 (6th Cir. 1986). See also, *Duvoisin v. Foster (In re Southern Industrial Banking Corp.)*, 809 F.2d 329 (6th Cir. 1987).

Other courts have abstained from lawsuits brought by creditors to determine large unliquidated claims against the debtor and the bankruptcy estate. See, e.g., *Christensen v. Tucson Estates, Inc. (In re Tucson Estates, Inc.)*, 912 F.2d 1162 (9th Cir. 1992); *Bright v. Southern Technical College, Inc. (In re Southern Technical College, Inc.)*, 144 B.R. 421 (Bankr. E. D. Ark. 1992); *Southmark Prime Plus v. Southmark Storage Associates Limited Partnership (In re Southmark Storage Associates Limited Partnership)*, 132 B.R. 231 (Bankr. D. Conn. 1991).

This proceeding is even more appropriate for abstention. The dispute is only slightly related to the bankruptcy case. It is not a suit to establish the plaintiffs' or the Bank's claim against the bankruptcy estate. It is a dispute between two creditors over the Bank's mortgage on the plaintiffs' subdivision lot. The dis-

pute may affect their claims in the bankruptcy case but only incidentally.

The complaint raises only state law issues. The parties are all local. The state courts are as convenient for the parties as this court, and there is no need for the longer reach of the bankruptcy court's personal jurisdiction. The plaintiffs have not pointed out any barrier to their bringing suit in state court. The motion to dismiss was filed early so that this proceeding has not progressed too far. Abstention should not impose extra work on the parties or cause any delay.

On the other hand, this court's subject matter jurisdiction is in doubt. Because this appears to be a non-core related proceeding, a final decision requires action by another court—*de novo* review by the district court—with the added delay (assuming the parties do not consent to a final decision by the bankruptcy judge). 28 U.S.C. § 157(c). Nothing suggests the Bank would consent.

Abstention is justified in the interest of justice, comity with the state courts, and respect for state law. *Brooklyn Jenapo Federal Credit Union v. Shain (In re Shain)*, 47 B.R. 309 (Bankr. E.D. N.Y. 1985); *In re Jodan's Pro Hardware*, 49 B.R. 976 (Bankr. E. D. Wis. 1985); *Geschke v. CLDC Management Corp. (In re CLDC Management Corp.)*, 58 B.R. 176 (Bankr. N. D. Ill. 1985); see also *Gabel v. Engra, Inc. (In re Engra, Inc.)*, 86 B.R. 890 (S. D. Tex. 1988); *In re Esteves Excavation, Inc.*, 56 B.R. 802 (Bankr. D. N.J. 1985).

This memorandum is the court's findings of fact and conclusions of law. FED. R. BANKR. P. 7052. The court will enter an order.

At Chattanooga, Tennessee.

BY THE COURT

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R. Thomas Stinnett  
U. S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT  
EASTERN DISTRICT OF TENNESSEE  
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GERALD D. WHITE &  
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Plaintiffs

V.

JERRY FARINASH, Trustee  
In Bankruptcy, and  
FIRST TENNESSEE BANK,

Defendants

**ORDER**

For the reasons stated in a Memorandum Opinion filed contemporaneously herewith,

It is ORDERED that the motion of First Tennessee Bank is sustained and this adversary proceeding is dismissed.

ENTER:

BY THE COURT

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R. THOMAS STINNETT  
UNITED STATES BANKRUPTCY JUDGE

[entered January 13, 1995]