**IN THE UNITED STATES BANKRUPTCY COURT**
**FOR THE EASTERN DISTRICT OF TENNESSEE**

| | |
|---|---|
| In re<br><br>ROBERT EUGENE HOWARD<br>SS# 411-64-0186 and<br>CALLIE STEWART HOWARD<br>SS# 415-60-8870,<br><br>Debtors. | No. 96-22512<br>Chapter 7<br><br>[affirmed E.D. Tenn<br>No. 2:03-CV-361; 02-20-04]<br><br>[on appeal 6th Cir] |

**MEMORANDUM OPINION SUPPLEMENTING**
**AUGUST 12, 2003 ORAL RULING**

APPEARANCES:

ROBERT M. BAILEY, ESQ.
BAILEY, ROBERTS & BAILEY, P.L.L.C.
600 Cumberland Avenue, Suite 218
Knoxville, Tennessee 37901-2189
*Attorneys for Mary Foil Russell, Trustee*

DAVE B. JORDAN, ESQ.
Post Office Box 5215
Kingsport, Tennessee 37663
*Attorney for Robert and Callie Howard*

**MARCIA PHILLIPS PARSONS**
**UNITED STATES BANKRUPTCY JUDGE**

This case came before the court for hearing on August 12, 2003, upon the chapter 7 trustee's motion to approve compromise. The trustee requested authority to pay $2,000 from estate funds to the debtors in exchange for their agreement to dismiss an appeal and assert no further claim against the estate. That appeal, which is presently before the Sixth Circuit Court of Appeals, arose from this court's refusal to set aside the sale by the trustee of the estate's real property and subsequent affirmance of that decision by the district court. At the conclusion of the August 12, 2003 hearing, this court declined to approve the proposed compromise and entered an order on August 15, 2003, denying the chapter 7 trustee's motion. This memorandum opinion supplements the court's oral ruling rendered on the record at the August 12, 2003 hearing. This is a core proceeding. *See* 28 U.S.C. § 157(b)(A) and (N).

I.

In order to consider the merits of the proposed compromise in the proper light, a historical review of this case is necessary. The debtors, Robert and Callie Howard, filed their petition initiating this case under chapter 12 on November 4, 1996, after their previous chapter 12 case was dismissed for failure to file a plan. Both cases were filed to forestall a foreclosure by Associates Financial Services

Company ("Associates") of its deed of trust on the debtors' 79-acre dairy and tobacco farm, on which the debtors and their two adult sons, Donald and Robert, resided. The debtors' financial difficulties leading up to the foreclosure are set forth in a published decision from this court, *In re Howard*, 212 B.R. 864, 867-68 (Bankr. E.D. Tenn. 1997).

Associates and the chapter 12 trustee, C. Kenneth Still, immediately jointly moved to dismiss the case, asserting lack of good faith, an inability to reorganize, a prohibition on filing under ll U.S.C. § 109(g)(1), and chapter 12 ineligibility because the debtors were allegedly not family farmers with regular annual income. After an extensive evidentiary hearing on February 18, 1997, the court denied the joint motion. Thereafter, a hearing on the debtors' proposed second plan of reorganization and objections thereto by Associates, the chapter 12 trustee and Consumer Credit Union ("CCU") was conducted on May 13, 1997. Although confirmation of the debtors' second plan was denied, *see In re Howard*, 212 B.R. at 883; the debtors, after a modification of their plan, were ultimately able to obtain confirmation of their third amended plan on August 13, 1997.

The debtors' confirmed plan provided for full payment of Associates' claim, which at that time was $123,360.58, with Associates to retain its lien on the debtors' real property, which according to their plan had a market value of $300,000. The plan also provided for

payment in full plus 6% interest of claims held by unsecured creditors totaling $41,612.81. Because the initial plan payments were to be made from the sale of the debtors' tobacco crop in November and December, payments to creditors were not scheduled to begin until January 1998. On January 30, 1998, the debtors filed a motion asking that the time to commence payments be extended until March 1998. As a basis for the motion, the debtors stated that they had "harvested a sufficient amount of tobacco from their 1997 crop to make the payments scheduled under the plan" but did not "anticipate that they [would] be able to transport [it] to market ... before March 1, 1998." By order entered March 2, 1998, the court granted the motion over the chapter 12 trustee's objection.

Notwithstanding the foregoing, the debtors failed to make the scheduled plan payments prompting the filing on March 15, 1998, of a joint motion to dismiss by the chapter 12 trustee and Associates. The debtors responded with a second motion to extend the time to commence payments, stating that they had "arranged for their crop to be sold at market on April 9, 1998 [and] expect payment ... by April 15, 1998." At an April 14, 1998 hearing on the extension motion, the debtors withdrew their motion and filed instead a motion requesting time to file a modified plan for "partial or complete liquidation" because "their attempts to rehabilitate their farm operations ha[d] been unsuccessful" and "dismissal of the case or conversion to Chapter 7

[wa]s not in the best interest of the Debtors [or] unsecured creditors." After a hearing on the motion held on June 2, 1998, the debtors, the chapter 12 trustee and Associates entered into an agreed order which provided that the debtors would "have until October 1, 1998, to conduct an auction to include ... [the] house and farm consisting of 78.9 acres, equipment, livestock, and personalty." The order further provided that in the event the auction did not go forward, the debtors agreed to "allow immediate dismissal of their Chapter 12 case upon certification by the Chapter 12 Trustee."

Not being a party to the agreed order, CCU filed on July 22, 1998, a motion to dismiss due to lack of payments on its claim, which was secured by the debtors' cattle and certain farm equipment. At a hearing on the motion held on August 25, 1998, counsel for the debtors and CCU announced that the debtors had agreed to give CCU relief from the automatic stay and thus the motion to dismiss would be withdrawn. In a subsequent letter to the clerk of the court dated September 4, 1998, counsel for CCU advised that debtors' counsel had refused to sign an agreed order lifting the stay as announced at the August 25, 1998 hearing. Accordingly, counsel for CCU requested that the motion to dismiss be placed back on the docket for hearing.

On September 3, 1998, the debtors filed a motion to modify plan which proposed, *inter alia*, to auction the 79-acre farm except for "the house and approximately five acres" which the debtors themselves would

purchase "for a fair market value consideration of $30,000 by paying $22,500 cash and applying homestead exemption of $7,500 to the price." That motion was met by objections from Associates and CCU as well as that of the chapter 12 trustee, who also filed a motion to dismiss with prejudice based on the debtors' alleged "pattern and practice of behavior calculated to hinder, delay, and cause further prejudice to creditors." Specifically, the chapter 12 trustee noted that the proposed modification motion did not set a date by which the proposed auction would take place and that the debtors had "deliberately refused to take any affirmative action to comply" with their previous agreement to auction the farm property by October 1, 1998.

The debtors then filed an amendment to their proposed modified plan on November 9, 1998, which resolved Associates' objection. In that amendment, the debtors agreed to a November 21, 1998 auction of their entire farm with the proviso that the debtors' house and five acres would be excepted from the sale if the debtors raised $22,500 prior to November 19, 1998. The objection of CCU and its motion to dismiss were likewise resolved by entry of an agreed order entered October 5, 1998, which granted CCU relief from the stay to permit it to obtain possession of and liquidate the debtors' "livestock and farm machinery and equipment securing the obligation of the debtors." The debtors personally signed that order which also obligated them to "assist the Consumer Credit Union in locating and identifying said

livestock and farm machinery and equipment."

Thereafter, on October 22, 1998, CCU filed a motion to compel accounting of secured assets and surrender thereof because "no cows were found at the debtors' farm, and the debtor Robert Howard refused to assist the movant in locating the same" as well as "the tractor securing the obligation, and some other items of machinery were stored behind large bales of hay," rendering them inaccessible. CCU alleged that during an inspection of its collateral on April 24, 1998, the tractor, all machinery and 107 cows were all identified, but since that time the debtors had "secreted much of said collateral and now refuse[d] to account for the same and disclose its whereabouts, and have willfully refused to obey the aforesaid Order of the Court entered October 5, 1998." After notice and a hearing, the court on November 16, 1998, granted CCU's motion and directed the debtors to assemble all of CCU's collateral for repossession on November 19, 1998.

In response, debtor Robert Howard filed a motion for new trial wherein he stated that he would "testify that he has been slow to comply with Orders of this Court because he had reason to believe that he has an opportunity to acquire outside funds which will give him the ability to refinance his farm and continue farm operations." Accordingly, he requested that the time by which he be required to return the collateral to CCU be extended for two weeks so that he could explore refinancing. After a November 23, 1998 hearing, the court gave

the debtors until December 4, 1998, in which to assemble the collateral.

On January 8, 1999, a hearing was held on the chapter 12 trustee's motion to dismiss with prejudice. The debtors did not appear. Based on the evidence presented, including the testimony of CCU's representative that of the 107 cows, only 23 cows, one bull and two calves had been turned over by the debtors, the court found that debtor Robert Howard had committed fraud in connection with this case by concealing and failing to account for CCU's collateral. The chapter 12 trustee and counsel for CCU suggested that a conversion to chapter 7 instead of dismissal would be in the best interests of creditors. Accordingly, the case was converted to chapter 7 by order entered January 13, 1999.

The debtors responded by filing on January 22, 1999, a motion requesting that the January 13, 1999 order be set aside. By agreed order entered March 4, 1999, and signed by the debtors, counsel for the chapter 12 trustee, and counsel for Associates, the court's finding of fraud was vacated upon the debtors' consent for their bankruptcy case to remain as a chapter 7.

On March 9, 1999, the chapter 7 trustee, Mary Foil Russell, filed a notice of public auction of the 79-acre farm set for May 15, 1999, along with a motion for order allowing parcel and sale of the farm and a motion for order requiring the debtors to turnover the farm. In

support of the latter motion, the chapter 7 trustee filed the declaration of auctioneer David Sanders who stated that debtor Robert Howard had frustrated any attempts to have the farm surveyed and divided for sale by ordering his employees and surveyors off the property and that he had witnessed debtor Robert Howard's conversations with the chapter 7 trustee wherein he repeatedly voiced that there would be no sale of the farm. A hearing on the turnover motion was noticed for March 23, 1999. The debtors did not appear at the hearing or otherwise object to the chapter 7 trustee's request. By order entered March 24, 1999, the court directed the debtors and their sons to "vacate the Debtors' house, farm and entire premises no later than March 31, 1999." When the debtors did not comply with this order, the chapter 7 trustee filed on April 8, 1999, a motion requesting the court to find the debtors in contempt and disallow their homestead exemption as a sanction. After a hearing upon notice held on April 20, 1999, the court set April 27, 1999, as a new deadline to vacate the farm and ordered that the failure of debtors to comply would result in automatic forfeiture of their homestead exemption. The debtors apparently have remained on the premises ever since.

II.

What transpired next is the basis of the appellate litigation. On May 6, 1999, the chapter 7 trustee filed a notice of proposed

private sale or, in the alternative, amended notice of public auction. That notice recited that the debtors' son, Robert, had made a bid of $245,000 for the 79-acre farm and furnished a letter of intent from Appletree Mortgage to provide financing. The notice further provided that in the event the sale did not close by May 28, 1999, the public auction would be rescheduled for June 26, 1999. In conjunction with the proposed sale, the chapter 7 trustee filed on May 17, 1999, a motion for sale free and clear of liens. On June 17, 1999, an order granting the motion was entered authorizing a private sale of the 79-acre farm or public auction free and clear of liens with proceeds going to pay valid liens, administrative expenses, property taxes, and the balance to creditors.

Almost three years later, on May 16, 2002, the debtors filed a motion requesting this court to determine the validity of the chapter 7 trustee's sale of the farm. The debtors alleged in the motion that the chapter 7 trustee sold the property at private sale on August 3, 1999, for $247,000 to Marcy Ledford; that Ms. Ledford was the daughter of the president of Appletree Mortgage Company, Shirley Harwood; that upon receiving a deed from the chapter 7 trustee, Ms. Ledford in turn transferred the property by quitclaim deed to Ms. Harwood on November 3, 1999; and that Ms. Harwood and her husband subsequently obtained loans from Washington County Bank in excess of $600,000 which were secured in part by the 79-acre farm. The debtors contended that "Marcy

Ledford was part of a conspiracy to defraud the Debtors and others by purchasing the property in fact for her mother"; that "[a]s a Mortgage Broker, Shirley Harwood owed a fiduciary duty to the Debtors"; and that "Debtors herein, the Chapter 7 Trustee and the Estate have been defrauded by Shirley Harwood and her daughter, Marcy Ledford." As relief, the debtors requested that the court "void the sale to Marcy Ledford and allow the Chapter 7 Trustee to hold a public auction in compliance with the Court's prior Order for the benefit of the Debtors, any remaining unpaid creditors in Debtor's [sic] case and any other claimants who might be entitled to share in the proceeds form [sic] the sale."

A hearing was held on the debtors' motion on June 11, 2002. At the hearing the chapter 7 trustee explained that the debtors' son, Robert, had not been able to obtain the contemplated financing from Appletree Mortgage for the purchase and that the sale had been made to Ms. Ledford in connection with an arrangement whereby the debtors and their sons would be permitted to remain on the premises while Robert sought financing to eventually purchase the farm from Ms. Ledford. Greene County Bank d/b/a Washington County Bank acknowledged that it had previously held a deed of trust against the 79-acre farm in connection with loans made to the Harwoods, but had foreclosed the deed of trust after the Harwoods defaulted in payment. Both the chapter 7 trustee and Greene County Bank urged the court to deny the debtors'

motion which the court did at the conclusion of the hearing. In so ruling, the court assumed the truth of the debtors' allegations in their motion, but noted that the property had been sold for a greater amount than originally noticed, that no allegation had been made by the debtors that Greene County Bank had not in good faith obtained the deed of trust in connection with monies lent to the Harwoods, and that the debtors had delayed almost three years before bringing this matter before the court when they obviously knew their son had not been successful in purchasing the 79-acre farm. Upon weighing the equities of the relief being sought by the debtors versus that of the chapter 7 trustee and Greene County Bank regarding the finality of the sale, the court concluded that sale should not be set aside and entered an order to this effect on June 12, 2002.

Thereafter, the debtors appealed the June 12, 2002 order to the district court which issued an order January 16, 2002, affirming this court. The district court stated that "[i]t defies all logic and reason to assume that [the debtors] never knew that their son did not complete the purchase of their home by June 1, 1999, and that his efforts to obtain financing to purchase the property through Shirley Harwood at Apple Tree Mortgage had been unsuccessful." In light of the various public records on file regarding the transfers of the property and the June 17, 1999 order allowing the sale of the property free and clear of liens, the district court concluded that the debtors' delay in

pursuing the matter and failure to obtain a stay of the order allowing the sale of the property was fatal to their motion. Thereafter, the debtors appealed to the Sixth Circuit Court of Appeals, where the appeal is at present. This is the litigation which is the subject of the chapter 7 trustee's motion to approve compromise, whereby the estate would pay $2,000 to the debtors in exchange for their agreement to dismiss their appeal and waive any further claim against the estate.

III.

In ruling upon a motion to approve a compromise, the court must determine whether the proposed compromise is fair and equitable and in the best interests of the bankruptcy estate. *See, e.g., Monus v. Lambros*, 286 B.R. 629, 636-37 (N.D. Ohio 2002). To make such a determination, courts generally consider various factors, including: (1) the probability of success in the litigation, with due consideration for the uncertainty in fact and law; (2) the complexity and likely duration of the litigation and any attendant expense, inconvenience and delay; and (3) all other matters bearing on the wisdom of the compromise. *Id.* (citing *Matter of Jackson Brewing Co.*, 624 F.2d 599, 602 (5th Cir. 1980)). The court may not simply rely upon the "trustee's word that the compromise is reasonable," but has "an affirmative obligation to apprise itself of the underlying facts and to make an independent judgment." *In re West Pointe Properties, L.P.*, 249

B.R. 273, 281 (Bankr. E.D. Tenn. 2000). The court is likewise not bound by the acquiescence of the unsecured creditors as demonstrated by their failure to object. *Id.* at 283.

Turning first to the probability of the debtors' success on their appeal, debtors' counsel stated that the debtors have already executed a settlement agreement with Greene County Bank whereby the bank quitclaimed the debtors their home and seven acres and the debtors in turn quitclaimed the remaining acreage to the bank. That having been accomplished, the court fails to comprehend why the appeal has not been rendered moot. The relief sought from this court in their motion which is the subject of the appeal was "to void the sale to Marcy Ledford and allow the Chapter 7 Trustee to hold a public auction in compliance with the Court's prior Order for the benefit of the Debtors, any remaining unpaid creditors in Debtor's [sic] case and any other claimants who might be entitled to share in the proceeds form [sic] the sale." Obviously, the debtors cannot have both the sale set aside so as to allow the chapter trustee to auction the 79-acre farm and yet keep a portion of the property, that being their house and seven acres subsequently deeded to them by Greene County Bank, for which they have not paid the estate. The debtors' quitclaim of their interest in the farm acreage and settlement with Greene County Bank simply can not be reconciled with the debtors' request in their motion that the sale by the chapter 7 trustee be voided and the farm auctioned.

Furthermore, even if appeal has not been rendered moot, the court remains convinced that the grounds upon which this court denied the motion and on which the district court affirmed are correct and highly unlikely to be overturned by the Sixth Circuit Court of Appeals. For these reasons, the court concludes that the debtors' appeal is without any merit and therefore the possibility of their success thereon extremely remote.

The chapter 7 trustee indicates that she expects to incur approximately $3,000 more in legal fees while the debtors exhaust their appeal before the Sixth Circuit and the estate risks the possibility that the matter may be remanded for an additional hearing or further findings which would require the additional expenditure of attorney fees. The matter on appeal is not complex and in fact could very well be dismissed for mootness on a motion by the chapter 7 trustee. In any event, when compared against the payment of $2,000 to the debtors, $3,000 in attendant expenses to defend the appeal is relatively insignificant. Moreover, any delay associated with the appeal would be negligible considering the already lengthy history of this case. Although the chapter 7 trustee indicates that the debtors in exchange for the $2,000 will also make "no further claim on the bankruptcy estate," the court is unaware of any claim by the debtors against the estate other than the now moot request that the sale be voided. Certainly, the debtors do not have a homestead claim since it was

forfeited as a sanction for their contempt of this court's April 23, 1999 order directing the debtors to vacate their residence and turn it over to the chapter 7 trustee. The debtors did not appeal that order and it is now final.

Lastly, when considering the other matters bearing on the wisdom of approving the proposed compromise, the court cannot in good conscience approve the settlement. A report of sale filed by chapter 7 trustee on May 22, 2002, indicates that of $247,000 in sale proceeds, Associates received $175,000 in payment of its claim. When the debtors' chapter 12 plan was confirmed, Associates was owed less than $125,000. Thus, over $50,000 equity in the property dissipated while the debtors repeatedly sought to delay and frustrate any sale and otherwise contemptuously refused to vacate the property as ordered to permit the chapter 7 trustee to prepare the property to achieve the best sales price. That amount would have assured a substantial, if not full, payment to all the unsecured creditors. As it stands now, the chapter 7 trustee is doubtful that any distribution will be made to such creditors. The debtors have in effect bested the system by receiving a discharge of their indebtedness while at the same time frustrating the sale of estate property in such a manner as to enable them to keep a portion of their property. For this court to authorize an additional award of $2,000 in estate funds to the debtors under these circumstances would indeed be a travesty of justice. For these

reasons, the court finds the proposed compromise to be unfair, inequitable and not in the best interests of this estate.

FILED: October 3, 2003

BY THE COURT

_____
MARCIA PHILLIPS PARSONS
UNITED STATES BANKRUPTCY JUDGE