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CREDITORS' COMMITTEES

(Part Two)

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This is the second half of a two-part article dealing generally with the selection, representation, and duties of Creditors' Committees. Part One (which appeared in Volume 1, Number 11 of this Newsletter) discussed the formation of a Committee and the eligibility of creditors to serve on it. Part Two discusses the duties and commensurate powers of a Committee once appointed and the responsibilities and obligations of the creditors serving on such a Committee, primarily in a Chapter 11 reorganization setting.

General Role of Committee

An appointed Creditors' Committee serves as a representative of the class of creditors from which the Committee's members are drawn and is charged with the duty of protecting the general interests of the represented class as a whole. Each creditor who serves on such a Committee has, therefore, a fiduciary obligation to ensure that the Committee's functions are exercised in a manner that promotes the constituents' interests. See H Rep No 95-595, 95th Cong 1st Sess 401 (1977). Ideally, a properly functioning Creditors' Committee will serve the purpose of affording each member of the represented class effective representation of its interests without the need for individual participation in the case. Nevertheless, because of the diverse interests that often exist even among creditors in the same class, a prudent creditor should always monitor the progress of a case notwithstanding the fact that a Committee is in place. For example, if a given creditor wants the debtor's operations to continue because of a strong prospect of future business, that creditor ought to carefully review the Committee's position if the latter is urging conversion of the case from Chapter 11 to Chapter 7. The presence of a Committee in a case does not abrogate an individual creditor's right to stand and be heard.

The extent of a Committee's role will differ from case to case depending upon various factors, such as: the size and complexity of the case, the dollar amounts involved, whether a trustee or examiner has been appointed, and whether the case is a Chapter 7 liquidation or a Chapter 11 reorganization. Nevertheless, a Creditors' Committee is recognized by the bankruptcy court as an entity holding substantial powers under the Bankruptcy Code, and the Court will seldom advocate restriction of a Committee's role once appointed. Accordingly, the members of a Committee will be required to exercise sound business and legal judgment in determining the extent to which the Committee must actively involve itself in the proceedings. Unfortunately, however, the role of a

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Creditors' Committee is often effectively restricted as a result of a lack of available financial resources.

In those relatively rare situations where one is appointed, the role of a Committee in a Chapter 7 liquidation case is necessarily limited to that of advising the trustee with regard to the marshaling and collecting of the debtor's assets. A Chapter 7 Committee will not be concerned with the relative merits of any proposed distribution, as the distributive function in a straight liquidation case becomes purely mathematical and is based the relative statutory priorities governing Chapter 7 distributions. 55 Amer Bankr L 3, p 44 (1981). In contrast, the role of a Committee in a Chapter 11 reorganization case is much more complex, since the Committee has myriad duties, including addressing the determination of assets available for distribution, determining the propriety of any proposed plan of reorganization, and often participating in the negotiation, formulation, acceptance, and confirmation of the plan. Id. The focus of this article is the relative duties and respective obligations of a Committee serving in a Chapter 11 reorganization case.

Two primary functions are generally identified as being fundamental to the role of a Creditors' Committee in a Chapter 11 case: (1) investigation of the debtor's affairs; and (2) negotiation and formulation of a plan of reorganization. See Collier's Handbook for Creditors' Committees §2.01 (1990). The investigative function serves to provide the Committee with information necessary to effectively fulfill its role of policing the activities of the debtor-in-possession or trustee and in bringing matters before the court as a party in interest. Upon being informed through exercise of its investigative function, a Committee can effectively determine the viability of a debtor's reorganization efforts and can fulfill its role as liaison or intermediary between the debtor-in-possession and other creditors. This information will further serve to promote meaningful negotiation of a feasible plan.

Duties and Powers of Committee

The primary duties and commensurate powers of an appointed Creditors' Committee are set forth in §1103 of the Bankruptcy Code. In theory, each enumerated duty implicates a separate and distinct set of corresponding rights and powers; however, the Code makes no distinction in their expression. Nevertheless, where a duty is imposed, the Bankruptcy Code undertakes to provide the Committee with the power necessary to adequately perform that duty.

It should be noted that Bankruptcy Code §1103 identifies the duties of a Creditors' Committee in permissive terms. Each of the duties enumerated is preceded by the word "may", as opposed to "must" or "shall." Thus, a Committee can tailor its involvement to the facts and circumstances of each case. Nevertheless, as set forth above, members of a Chapter 11 Creditors' Committee owe a fiduciary obligation to the class the Committee represents, and they must actively participate in the case to the extent necessary to effectively represent their constituents' interests. Moreover, the permissive word "may" in Section 1103(c) should not be deemed to limit a Committee's duties inasmuch as subsection (5) thereunder reads "perform such other services as are in the interest of those represented." Obviously, this broad language can encompass a labyrinth of duties and responsibilities which Congress has seen fit not to delineate.

A. Employment of Professionals

The duty and corresponding power of a Committee to employ professionals to assist in the performance of the Committee's functions are set forth in Bankruptcy Code §1103(a). The Code provides in part that a Committee approved under §1102 "may," subject to the court's approval, "select and authorize the employment by such Committee of one or more attorneys, accountants, or other agents, to represent or perform services for such Committee." 11 USC §1103(a). This power may only be exercised "at a scheduled meeting" of the Committee "at which a majority of the Committee's members are present." Id.

Invariably, the Committee's duty to employ professionals will require retention of legal counsel almost immediately following the appointment and organization of the Committee. Decisions made during the embryo stages of a Chapter 11 case frequently have a crucial and substantial impact on the likelihood of any successful reorganization. Thus, it is incumbent upon the Committee, in light of its duty to actively serve as an advocate of the creditors in the class it represents, to promptly seek out qualified

and competent counsel to assist and guide the Committee in performing its duties.

Occasionally in a relatively modest Chapter 11 case, one encounters a Creditors' Committee attempting to function sans appointed legal counsel. In doing so, the Committee members are engaging in a very risky business in view of their potential liabilities as fiduciaries in the bankruptcy process.

An attorney or accountant employed to represent a Committee in a Chapter 11 case may not, while employed by such Committee, represent any other entity having an adverse interest in connection with the case. 11 USC §1103(b). Representation of one or more creditors of the same class as represented by the Committee does not per se constitute an adverse interest. Id. However, such representation may, over the course of the case, develop into representation of an adverse interest, in which event the attorney or accountant may be subject to removal and/or denial of compensation. See Collier's Handbook for Creditors' Committees §14.02[2]. Moreover, in view of the ambiguous language of Section 328(c) of the Bankruptcy Code, many experienced Creditors' Committee counsel endeavor to make sure that they meet the "disinterestedness" test of Section 101(14) to avoid any spurious challenges to their fees. The employment of professionals by a Committee in a Chapter 11 case may be "on any reasonable terms and conditions of employment, including a retainer, on an hourly basis, or on a contingent fee basis." 11 USC §328(a). However, such retention is almost invariably on a general retainer basis, i.e., an hourly basis. It must be kept in mind that an award of reasonable compensation to attorneys or other professionals employed by a Committee for actual and necessary services rendered must be noticed to all parties in interest and to the United States Trustee. 11 USC §330(a)(1).

B. Consultation Concerning Administration of Case

Bankruptcy Code §1103(c)(1) provides that a Committee appointed under Bankruptcy Code §1102 "may consult with the trustee or debtor-in-possession concerning the administration of the case." The Committee is duty-bound to keep itself adequately informed concerning the case administration. Nevertheless, the extent to which consultation is necessary is left to the discretion of the Committee. It is advisable that the Committee arrange for periodic meetings with the debtor-in-possession or trustee at various times throughout the administration of the case.

The consultation contemplated under Bankruptcy Code §1103(c)(1) relates to the ongoing operations of the debtor's business. Matters such as the profitability or unprofitability of the debtor's business, the conservation or dissipation of estate assets, the maintenance of adequate insurance, the prosecution or nonprosecution of causes of action, and the rejection or assumption of executory contracts have been identified as examples of those matters which generally fall under the concept of case administration. Collier's Handbook for Creditors' Committees §14.03, p 1.4-8.

The power to force the debtor-in-possession or trustee to meet with the Committee and transact business with it is defined in Bankruptcy Code §1103(d):

> (d) As soon as practicable after the appointment of a Committee under section 1102 of this title, the trustee shall meet with such Committee to transact such business as may be necessary and proper.

Additionally, as a party in interest, thee Committee has the right to request information of the debtor-in-possession or trustee pursuant to Bankruptcy Code §704(7) and §1106(a)(1).

C. Investigation of Debtor's Affairs

The duty of a Chapter 11 Creditors' Committee to investigate the affairs of a debtor is defined by Bankruptcy Code §1103(c)(2), which provides in part:

> (c) A committee appointed under section 1102 of this title may --
>
> investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business and the desirability of the continuance of such business, and any other matter relevant to the case or to the formulation of a plan.

As is apparent from the above language, the investigatory powers of a Chapter 11 Committee are very broad and extensive. This is particularly necessary when the debtor remains in possession or when ownership and management of the reorganizing business are substantially the same.

The appointment of a trustee or examiner in a Chapter 11 reorganization does not supersede the investigative function of a Committee. Nevertheless, the obligation of the Committee to investigate under such circumstances will ordinarily be substantially reduced, since the Committee need not duplicate the investigatory functions performed by the trustee or examiner. To the extent that the trustee or examiner may not be developing information necessary to determine, from the viewpoint of the class the Committee represents, such things as the advisability of permitting the debtor to continue operating its business or the impact of any proposed plan, it may be inappropriate for the Committee to merely rely on the trustee or examiner's efforts. Then an independent investigation must be performed pursuant to the duties imposed by Bankruptcy Code §1103(c)(2).

The power to investigate the debtor's affairs is implemented in a substantially the same way as the Committee's power to consult with the debtor-in-possession or trustee pursuant to §1103(c)(1). The Committee holds the power to compel relevant information through reasonable request pursuant to Bankruptcy Code §704(7). In addition, as a party in interest in the case, the Committee may petition the court pursuant to Bankruptcy Rule 2004 to obtain examination of those parties necessary to an investigation.

D. Formulation of Plan

As stated above, one of the two primary roles of a Chapter 11 Creditors' Committee is to negotiate a plan of reorganization with the debtor. In imposing this duty to participate in the formulation of a plan, §1103(c)(3) of the Bankruptcy Code provides that an appointed Committee "may . . . advise those represented by such Committee of such Committee's determinations as to any plan formulated, and collect and file with the Court acceptances or rejections of a plan." To this end, the Committee must use the information and data accumulated through the exercise of its general powers and duties to fulfill its role representative of the creditors in its class.

In light of the broad powers granted a Creditors' Committee with regard to its participation in the formulation of a plan, it is unlikely that a debtor will be able to' secure confirmation of a consensual plan of reorganization without the cooperation and support of the Committee. Conversely, if a Committee (especially one representing the general body of unsecured creditors) actively opposes a plan, the likelihood of obtaining confirmation will usually be dramatically reduced. Furthermore, the Committee is empowered to file its own plan of reorganization under certain circumstances pursuant to Bankruptcy Code § 1121(c). Thus, a Chapter 11 Creditors' Committee is afforded the practical power of enforcing its right and duty to participate in the negotiation and formulation of a plan.

The basic statutory philosophy of investigation and negotiation followed by' consensual reorganization' involves the recognition and encouragement of the duty and power of a Chapter 11 Committee to participate actively in the formulation of a plan that will normally be filed by the debtor-in-possession. This philosophy, however, breaks down in cases where the debtor resorts to the cramdown provisions of §1129(b) and attempts to secure confirmation of a plan over opposition and rejection by the creditors represented by a Chapter 11 Creditors' Committee. This philosophy further breaks down where a Committee (when permitted by the Bankruptcy Code) is forced to file its own competing plan in opposition to the plan proposed by the debtor. Nevertheless, the fundamental role of representative of the class of unsecured creditors must be adhered to throughout any formulation process.

E. Request Appointment of Trustee or Examiner

Bankruptcy Code §1103(c)(4) expressly authorizes a Chapter 11 Creditors' Committee to "request the appointment of a trustee or examiner" in accordance with the provisions of Bankruptcy Code §1104. Section 1104 provides that the court shall order the appointment of a trustee:

(1) For cause, including fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by current management, either before or after the commencement of the case, or similar cause . . .; or

(2) If such appointment is in the interest of creditors, any equity security holders, and other interests of the estate. . . .

The Committee's duty to request appointment of a trustee or examiner will generally be implicated through exercise of the Committee's investigative and consultive powers. Receipt of information justifying a trustee or examiner appointment normally obligates the Committee to request of the court such an appointment if the debtor-in-possession will not accede to the same. In keeping with the Committee's duty to be active in the case, the Committee must take whatever action is proper to best represent the interests of the class it represents.

F. Duty to Perform Other Services

Section 1103(c)(5) allows an official Chapter 11 Creditors' Committee to "perform such other services as are in the interest of those represented." This provision serves as a catchall, providing a Chapter 11 Creditors' Committee with the power to perform such other services as may be appropriate to advance the interests of the class represented by the Committee. The wide scope of this language often serves to involve a Committee in many, if not all, aspects of a Chapter 11 case, e.g., analysis and objections to claims, review and recovery of voidable transfers, and abandonment and sales of assets, to mention a few. For example, a Committee of unsecured creditors has been held to be empowered to bring an action in the name of and on behalf of the debtor-in-possession to enforce a claim of the estate which the debtor-in-possession unjustifiably refuses to enforce. See In re Monsour Medical Center, 3 CBC2d 1363 (Bankr WD Pa, 1980).

Conclusion

It is almost universally acknowledged that an aggressive, active and well-represented Creditors' Committee is a vital and essential element in the reorganization process. Congress recognized this when, in Section 1102(a)(1) of the Bankruptcy Code, it made the appointment of an Unsecured Creditors' Committee mandatory. Unfortunately, Congress never figured out how to require creditors to serve on Committees or how to get them to work with dedication and sacrifice on a sometimes extended endeavor that is essentially a labor of love. For this reason, the value of a Committee's role, and thus the success or failure of the Chapter 11 mechanism, is often intricately related to experience and competence of the professionals (particularly the attorneys) retained by the Committee -- for it is those professionals who translate the Committee's powers, duties, and functions into reality and substance on a day-to-day basis.

RECENT BANKRUPTCY DECISIONS

The following are summaries of recent court decisions that address important issues of bankruptcy law and procedure. These summaries were prepared by Jahel H. Nolan with the assistance of Larry Ver Merris.

In re Blue Grass Ford-Mercury Incorporated, Case No. 90-6121 (6th Cir. August 20, 1991). This case, authored by Judge Ralph B. Guy, Jr., involves a preference action. In 1977, Farmers National Bank of Cynthiana entered into a floor-plan financing arrangement with the debtor's predecessor, Blue Grass Ford. Under that arrangement, Blue Grass Ford financed the purchase of automobiles from the manufacturer. At that time, the bank took a security interest in Blue Grass Ford's automobile inventory and perfected it.

In 1979, Blue Grass Ford sold the dealership to the debtor. The parties used the old security agreement for a while. In 1981, the debtor began having financial problems. It got a Small Business Association guaranteed loan from the bank. To secure the loan, the bank took a new security interest in the debtor's inventory and other assets, although automobiles were not specifically mentioned. That security interest was also perfected.

In 1982, the debtor filed bankruptcy under Chapter 11. The bank sought preferred status as a security creditor. The bankruptcy and the district courts denied the bank that status. It appealed, claiming that it was a perfected secured creditor and payments made to the debtor could not be avoided as preferences. The bank claimed that both the financing statement filed in 1977 and the one filed in 1981 served to protect its interest in the inventory.

The court first assumed that the bank's security interest in the inventory continued after the transfer of the inventory to the debtor. Despite this assumption, the bank still did not prevail on its argument because the court found that the 1977 statement was unable to perfect any security interest in the debtor's 1981 automobile inventory because the inventory did not exist in 1977.

The 1981 statement was also ineffective to protect the bank even though it purported to cover all inventory of the debtor. The court stated that as a rule the collateral description in a valid security agreement controls and no extraneous materials could be considered. The court noted that at first glance it would appear that the word "inventory" included floor-plan vehicles because the security agreement did not exclude them from its collateral description. However, the section following the collateral description on the security agreement stated that the debtor warranted that it was the absolute owner and held legal and beneficial title to the collateral. However, the debtor was not the absolute owner free and clear of all liens of the floor plan vehicles. Thus, they could not, under the terms of the security agreement, be collateral for the 1981 note. The court also stated that the entire purpose of the bank's security interest was to secure the Small Business Association guaranteed loan. The security agreement, in defining the security interest, failed to state that its function was to secure anything in addition to the loan. Therefore, the bank's perfected security interest did not flow from the security agreement and financing statement executed in connection with the SBA loan and extend to the floor plan notes executed afterwards.

In addition, the bank claimed that even if was an unsecured and unperfected creditor, the debtor had failed to prove all of the elements of a preferential transfer, specifically that the debtor was insolvent during the preferential period and that the transfers allowed the bank to receive more than it would have under a Chapter 7 liquidation. The court stated that Section 547(f) of the Bankruptcy Code provides that debtors are presumed to have been insolvent on or during the 90 days immediately preceding the date of the filing of the petition. Thus, the bank was required to present evidence to rebut this presumption. Even though the bank attempted to do this, the findings of fact with regard to the debtor's assets and liabilities during the preference period could only be reversed if clearly erroneous. The court stated that in light of the testimony and supporting documentation, the court could not conclude that the bankruptcy court's determination was clearly erroneous.

In regard to the bank's argument that the debtor failed to prove that it had received more than it would have in a Chapter 7 liquidation, the court found that unsecured creditors would have received nothing under Chapter 7. Thus, because the bank was an unsecured creditor, it would not have received any payments under Chapter 7, therefore any payments it did receive were in excess of the amount to which it was entitled.

In the Matter of IPG Holdings, Inc. v. Loree Ltd., Case No. 89-19586-G (E.D. Mich. May 8, 1991). This case, authored by Judge Bernard A. Friedman, addressed appeals from two orders of the bankruptcy court. The first action involved an appeal from the bankruptcy court's order stating that the trustee still retained the right to take over the case if he believed that the cause of action belonged to the estate (the 90-71157 action). The second action involved an appeal from the bankruptcy court's order lifting the stay, which stated that no party could execute on any judgment against the debtors without further order of the bankruptcy court (the 90-71464 action).

In analyzing its jurisdictional authority in the 90-71464 action, the court noted that the Sixth

Circuit has held that a bankruptcy court's lifting of an automatic stay is final and therefore immediately appealable. The Sixth Circuit suggested that an immediate appeal was permitted even if the order in question was not technically final when it was necessary to avoid causing serious harm by delaying the appeal. Judge Friedman stated that although the bankruptcy court had lifted the stay, no party was threatened by the kind of serious harm necessary to render lifting the stay immediately appealable. This condition on the order meant that the district court lacked jurisdiction to entertain the appeal in the 90-71464 action.

The court also found that it did not have jurisdiction to hear the appeal on the 90-71157 action as that appeal sought to determine a statement in the bankruptcy court's order that did not conclusively determine any rights or appear to be in any sense final within the meaning of Section 158(a).

Finally, the court determined that the appellants may not have standing to appeal. A person or entity may appeal a bankruptcy court order only if it is a person aggrieved by the order. To be aggrieved, the party must have a financial stake in the bankruptcy court's order. Standing did not exist just because the appellants in the 90-71464 action would have to expend professional fees. The appellants in the 90-71157 action did not explained how they stood to be directly affected by the bankruptcy court's decision that the trustee could take over the case if he believed the cause of action belonged to the estate.

In re Brace, Adv. Proc. No. 89-0389 (Bkrtcy. W.D. Mich. September 11, 1991). This opinion, authored by Judge Laurence E. Howard, involved a determination of the award of interest in an action under 11 U.S.C. §523(a). The case arose out of the sale of a home by the debtors to David and Mary Payne. After the purchase, the basement walls began to cave in, causing damage to the basement and the rest of the house. After the debtors filed their bankruptcy petition, the Paynes brought an adversary proceeding pursuant to 11 U.S.C. §523(a)(2), stating that the debtors knowingly and fraudulently made false representations to them about the quality, structural soundness, and defects present in the house. The court found the debt to be nondischargeable and awarded damages of approximately $29,000.

In determining the amount of interest allowed for the periods both pre- and post-petition, the court stated that prejudgment interest was appropriate as compensation for the lost use of money in order to place the aggrieved party in the same position as if the damage had not occurred, even if the claim is unliquidated. The court also stated that Michigan law mandates the award of prejudgment interest in civil cases in which a money judgment is rendered. The court concluded that awarding prejudgment interest would fully compensate the Paynes for their loss.

The appropriate starting point for the accrual of prejudgment interest would be the filing of the state court action. The fact that the debtors were in bankruptcy had no effect on the ability to recover interest once a finding under 523(a) had been made. There being no federal statute governing the application of prejudgment interest, Judge Howard adopted the reasoning of the Sixth Circuit and determined that both pre- and post-judgment interest would be based on 28 U.S.C.A. §1961(a). Therefore, the federal judgment rate of 6.26 percent was applicable, and the Paynes were awarded that amount for both pre- and post-judgment interest.

In re Bush, Case No. 91-82109 (Bkrtcy. W.D. Mich. September 4, 1991). This opinion, authored by Judge Jo Ann C. Stevenson, addresses the court's concern with routine requests by attorneys for a $1,000 fee for representing Chapter 13 debtors. On April 13, 1991, Daniel M. and Ann C. Bush filed their Chapter 13 petition. A proposed order confirming the debtor's Chapter 13 plan and approving attorney fees of $1,000 was submitted and signed, but the fees were allowed in the reduced amount of $600.

The court stated that it has an obligation to examine the priority of fees and expenses requested even if no objections are raised. This obligation is especially important in Chapter 13 cases, where the

debtor has no motivation to object. According to the court, most Chapter 13 consumer bankruptcies are generally repetitious and the work required does not change substantially with the particular facts of the case. The only documents filed with the court were counsel's completed form schedules and the plan.

Debtors' attorney charged over $500 for sending or receiving routine letters and phone calls. He spent 36 minutes reviewing two proofs of claim which the court believed could have been charged at 6 minutes total.

Debtors' attorney also billed 1 hour for attending a confirmation hearing on a day when the court's entire 29-matter morning calendar, which included the confirmation hearing, was completed in one hour. In addition, counsel appeared on behalf of three clients during that hour. The court estimated that the Bushs' uncontested confirmation hearing was concluded in no more than 5 minutes. Likewise, counsel billed 1 hour for attending a 341 meeting where he appeared on behalf of six debtors in 1 hour and 20 minutes. The court concluded that these charges were clearly excessive and should have been apportioned among the debtors represented by the attorney.

In addition, the court would not reimburse Debtors' attorney for 1 hour spent on the preparation of his bill, finding the charge to be excessive. The document was neither requested nor required but was voluntarily prepared by counsel for his own benefit.

The court did not recognize a $1,000 minimum base fee to be routinely requested or allowed without consideration of the actual legal work performed. The requested and awarded fee must be based on a number of factors including but not limited to the legal work actually, reasonably, and necessarily performed; the type and amount of debts scheduled; and the complexity of the work involved.

In the Matter of Haworth Inc. v. Sunarhauserman Ltd./Sunarhauserman Ltee, Adv. Proc. No. 91-8454 (Bkrtcy. W.D. Mich. September 3, 1991). This opinion, authored by Judge Laurence E. Howard, addresses a motion to transfer a case originally commenced in state court to the Bankruptcy Cou for the Northern District of Ohio. Sunarhauserma Ltd./Sunarhauserman LTEE ("Sunar") was a Canadian corporation engaged in the manufacture and sale of office furniture. It filed bankruptcy in Canada. Sunar is a wholly owned subsidiary of Sunarhauserman Inc., an Ohio corporation, and a wholly owned subsidiary of Hauserman, Inc., also in Ohio. Both Hauserman and Sunarhauserman ("Hauserman") filed for Chapter 11 relief in the United States Bankruptcy Court for the Northern District of Ohio on October 5, 1989.

Haworth purchased the "RACE" line of office furniture from both Sunar and Hauserman out of bankruptcy. The sale was embodied in two agreements that were virtually identical. Due to certain trademark disputes, Haworth refused to make the last installment payment under the contract. Hauserman filed an adversary proceeding against Haworth in Ohio claiming that Haworth had breached its payment obligation. Haworth filed an action against Sunar in Kent County Circuit Court claiming breach of contract, breach of warranty, fraud, and misrepresentation. The action filed by Haworth was removed to the Bankruptcy Court for the Western District of Michigan pursuant to 28 U.S.C. § 1452(a). Sunar sought dismissal, stay, or transfer of the action. In response, Haworth asked for remand to the state court or abstention. The Canadian trustee for Sunar sought to have the proceedings against him dismissed. The court first determined that the adversary proceeding was properly before the court and that it had jurisdiction to decide the motions presented. The court reasoned that the Haworth suit was related to the Hauserman Chapter 11 case because the outcome of the proceeding could conceivably have an effect upon the estate being administered in bankruptcy. The parties also conceded that there was, at a minimum, a "related-to" jurisdiction present in the case.

Judge Howard also determined that the motion for transfer should be granted. The court delineated six factors that should be considered in determining whether transfer to another district was in the interest of justice and the convenience of the parties, the most important of which was whether the

transfer would promote the economic and efficient administration of the estate. Since all of the parties involved in the dispute, including the plaintiff, were already before the bankruptcy court in Ohio, efficiency was served by having this matter transferred there. In addition, the Ohio bankruptcy court had already begun the adversary proceeding and had made rulings with respect to the case.

Last, the court found justice strongly favored transferring the case to the forum where the debtor was located because the proceeding was related to the Hauserman bankruptcy. The parties in Ohio were going forward with an action substantially similar to the one before the court in Michigan. Transferring the proceeding would place all of the disputes arising out of the bankruptcy sale before the court that had originally approved the sale.

Having decided to transfer the case, the court stated that the trustee's motion to dismiss need not be decided.

As for Haworth's motion for mandatory abstention and remand, the court found that equity favored that the proceeding be litigated in Ohio due to that court's being prepared to handle the issues raised in the dispute. It also had jurisdiction over all the necessary parties. Relying on his decision in DC Equipment Co., 1990 Bkrtcy. LEXIS 569, the court stated that although this matter was only related to a case under Title 11, mandatory abstention was improper as the state court proceeding was filed after the bankruptcy in Ohio had commenced.

In re Three Lakes Cocktail Lounge & Restaurant, Case No. 89-00123 (Bkrtcy. W.D. Mich. September 3, 1991). This case, authored by Judge Laurence E. Howard, involves conflicting interests claimed by each party in Resort Class C and SDM liquor licenses. Clarence Lindstrom and his wife owned and operated a bar known as Tiny's. They also possessed the liquor licenses that were the subject of this proceeding.

During its first years of operation, the bar experienced financial trouble, and Lindstrom called upon Clarence Sartory for help in running the business and to infuse capital. Lindstrom and Sartory formed the corporation Three Lakes Cocktail Lounge and Restaurant. During the incorporation process, the Lindstroms apparently agreed to transfer the liquor licenses to the new corporation along with their interest in the business. Various loans were entered into by both Sartory individually and by the corporation. On December 31, 1987, Three Lakes entered into a series of transactions with First National Bank & Trust Co. of Hermansville, Michigan. These included signing a security agreement covering all assets of the corporation and entering into a pledge of the liquor licenses. The bank properly filed its security agreements with the Secretary of State, except as to the liquor licenses.

With the liquor licenses owned by the debtor and the bankruptcy estate, both the bank and the trustee claimed a security interest in them. The court stated that through Section 544(a) of the Bankruptcy Code, the trustee is clothed with the status of a judicial lien creditor and can preserve the estate's interest in the debtor's property that is inferior to his status. Section 544(a)(1) empowers the trustee to avoid any transfer to the debtor or any obligation incurred by the debtor that is voidable by a creditor possessing the status of a judicial lien creditor under state law.

State law priority rules govern what interests are avoidable. Under Michigan's adoption of the U.C.C., an unperfected security is subordinate to the rights of a person who becomes a lien creditor before the security interest is perfected. Judge Miles has ruled definitively for the Western District of Michigan that a liquor license is a general intangible subject to the perfection provisions of Michigan law. A creditor must perfect its interest in a liquor license by filing its financing statement with the Secretary of State in order to gain the priority of a secured creditor in bankruptcy. Since the bank failed to properly file a financing statement, it possessed an unperfected interest in the license as of the commencement of the case. Therefore, the bank's interest was subordinate to the trustee's status as a judicial lien creditor.

STEERING COMMITTEE MEETING MINUTES

A meeting was held on September 20, 1991 at noon at the Peninsular Club. **PRESENT:** Brett Rodgers, Peter Teholiz, Mark Van Allsburg, Janet Thomas, Larry Ver Merris, Thomas P. Sarb, David Doran (for Pat Mears), Thomas Schouten, Robert Wright, Robert Sawdey.

1. 1992 FBA Seminar. A motion was approved to hold the 1992 FBA Bankruptcy Seminar on August 13 to 15, 1992 at the newly renovated Park Place Hotel in Traverse City, Michigan. An Education Committee consisting of Bob Wright, Chair, Tom Schouten and Peter Teholiz was formed to plan the educational program and to select a keynote speaker.

2. Report on 1991 FBA Bankruptcy Seminar. Attendance at the 1991 FBA Bankruptcy Seminar increased to 141 people from the 115 people attending the 1990 Seminar. The 1991 program showed revenues of $15,735.00, total expenses of $8,313.64, and a net profit of $7,421.36 for the Federal Bar Association.

3. FBA Matching Funds for Attorney Conference Room. Brett Rodgers reported that the FBA Executive Committee has agreed to provide matching funds for furnishing the attorney conference room at the Bankruptcy Court in the amount of $2,600.00. Discussion was held with regard to further needs for the attorney conference room, including phones and fax machines. The Committee members will review such needs and report back at a future Steering Committee Meeting.

4. New Newsletter Editor. Larry Ver Merris reported that Tom Sarb will be taking over as editor of the monthly newsletter. Any announcements, articles, or new case summaries should be directed to Tom Sarb's attention.

5. Election of Steering Committee Members and Officers. The Committee approved a motion to increase the size of the Steering Committee to members. Steve Rayman and Janet Thomas were elected to one year terms on the Steering Committee. Bob Mollhagen was elected to a two year term on the Steering Committee, and Marcia Meoli was elected to a three year term on the Steering Committee. Tom Schouten, Brett Rodgers, and Jim Engbers were re-elected to three year terms on the Steering Committee. Therefore, the Steering Committee Members and the dates on which their terms expire are as follows:

TERMS EXPIRING		
1992	1993	1994
Tim Curtin	Robert Sawdey	Tom Schouten
Pat Mears	Colleen Olsen	Brett Rodgers
Peter Teholiz	Bob Wright	Jim Engbers
Steve Rayman	Bob Mollhagen	Marcia Meoli
Janet Thomas		

Brett Rodgers was re-elected chairman. Finally, the Steering Committee discussed that it would consider terminating membership of any member of the Steering Committee if that member or the member's proxy misses more than four meetings per year.

6. The next meeting of the Steering Committee will be held at the Peninsular Club on Friday, October 18 at noon.

LOCAL BANKRUPTCY STATISTICS

The following is a summary of the number of bankruptcy cases commenced in the United States Bankruptcy Court for the Western District of Michigan (Lower Peninsula) during the period from January 1, 1991 through August 31, 1991. These filings are compared to those made during the same period one year ago, and two years ago.

	1/1/91 - 8/31/91	1/1/89 - 8/31/89	1/1/88 - 8/31/88
Capter 7	3,416	2,210	1,871
Chapter 11	113	63	61
Chapter 12	20	9	25
Chapter 13	1,177	809	790
Totals	4,726	3,091	2,747

EDITOR'S NOTEBOOK

Effective this issue, I have succeeded Larry Ver Merris in the editorship of the Bankruptcy Newsletter. On behalf of the members of the Bankruptcy Section of the Federal Bar Association, I would like to extend our deepest appreciation to Larry for all of the many hours he has devoted to this enterprise over the last few years. The Newsletter has been timely, informative, and interesting. I will do my best to maintain the quality of the Newsletter to which the Bankruptcy Section has become accustomed during Larry's tenure.

As this issue went to press, we became aware of a decision of the Sixth Circuit in the case of In re Mansfield Tire & Rubber Company, 1991 U.S. App. LEXIS 201541 (6th Cir. August 28, 1991), holding that the federal government is entitled to priority in bankruptcy on its minimum funding pension excise tax claim. In that case, The Sixth Circuit also held that a tax owed to the federal government may not be equitably subordinated to other claims unless it is shown that the federal government engaged in inequitable conduct. A more complete summary of this case will appear in next month's edition.

In another recent case of note outside of the Sixth Circuit, the Second Circuit addressed in In re Chateaugay Corporation, et al., 1991 U.S. App. LEXIS 20949 (2d. Cir. Sept. 6, 1991) (the LTV bankruptcy case) the conflict between the Bankruptcy Code and the Super Fund law. In Chateaugay the Second Circuit affirmed the decision of the District Court that certain "response costs" incurred by the EPA were pre-petition "claims" dischargeable in bankruptcy, regardless of when such costs were incurred, as long as they concerned a release or threatened release of hazardous substances that occurred before the Debtor filed. The Second Circuit also affirmed the judgment to the extent that it held that the Debtor's obligations to operate and maintain facilities it owns or operates as required by environmental laws, regardless of when the offending condition arose, is not dischargeable and that CERCLA response costs incurred during the bankruptcy at sites owned or operated by the Debtor constitute expenses of administration and are entitled to priority. The decision on the first issue, however, is much less favorable to Debtor corporations than it appears at first blush, for the Court ruled that a

"clean up order that accomplishes the dual objectives of removing accumulated wastes and stopping or ameliorating ongoing pollution emanating from such waste is not a dischargeable claim." Id. at page 14. The Court ruled that an order to clean up a site, to the extent that it imposes obligations distinct from any obligation to stop or ameliorate ongoing pollution, is a "claim" dischargeable in bankruptcy. But as the Court noted, "[w]e recognize that most environmental injunctions will fall on the non-'claim' side of the line." In ruling that response costs incurred during the administration of the case are administrative expenses, the Court relied upon the decisions of the Sixth Circuit in In re Wall Tube and Metal Products Company, 831 F.2d 118 (6th Cir. 1987) and of this district in In re Peerless Plating Company, 70 B.R. 943 (Bankr. W.D. Mi. 1987).

In a related context, the September, 1991 edition of Michigan Lawyers Weekly summarizes the case of Niecko v. Emro Marketing Co., decided by Judge Rosen of the United States District Court for the Eastern District of Michigan, which held that a purchase by plaintiff of a piece of real property purchased "as is" from the defendant, where both buyer and seller were aware that the property had formerly been operated as a gas station, insulated the seller from liability to the purchaser for the clean up of toxic hydrocarbons that contaminated the soil. The purchase agreement expressly made no representations or warranties about the property, including soil conditions. Further, there was no evidence that the defendant had actual knowledge that the soil was contaminated prior to sale.

In closing, let me request that any reader who wishes to submit an article for possible publication in subsequent editions of the Newsletter submit it to my attention at 800 Calder Plaza Building, Grand Rapids, Michigan 49503. All articles are welcome.

Thomas P. Sarb