

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NORTH CAROLINA

FILED
U.S. BANKRUPTCY COURT

JAN - 4 1991

In Re:)

BARBARA STEIN KUMAR,)

Debtor.)
_____)

Case No. 90-31564

Chapter 11 WESTERN DISTRICT OF NC

By _____ DEPUTY

JUDGMENT

JUDGEMENT ENTERED ON JAN - 4 1991

This action was decided by the undersigned and an Order was filed on January 4, 1991. Consistent with that Order,

It is ORDERED and ADJUDGED that the Chapter 11 petition filed by the debtor is dismissed.

This the 4th day of January, 1991.



George R. Hodges
United States Bankruptcy Judge

JAN - 4 1991

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NORTH CAROLINA

WESTERN DISTRICT OF NC
DEPUTY

In Re:)
)
BARBARA STEIN KUMAR,)
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Debtor.)
_____)

Case No. 90-31564
Chapter 11

ORDER DISMISSING CASE

This matter is before the court on the Motion of United Carolina Bank ("UCB") to dismiss this case. The court has considered the record in this case, the facts stipulated to by the parties, the exhibits admitted into evidence, the testimony of the debtor, and the statements and arguments of counsel for the parties. Based upon all of that, the court has concluded that this bankruptcy case should be dismissed for the reasons that follow:

BACKGROUND

1. UCB has two secured claims in this case by virtue of it being the holder of: (1) a Deed of Trust Note dated October 17, 1986, in the original principal amount of \$400,000.00 (the "First Note"), executed by the debtor, Raj Kumar (her husband), Rajender Kumar (Raj Kumar's brother) and his wife, Veena Kumar; and (2) a Deed of Trust Noted dated June 26, 1989, in the original principal amount of \$221,770.24 (the "Second Note"), executed by the debtor and the same other individuals. Both the First Note and the Second Note are secured by a Deed of Trust dated October 17, 1986, and recorded on October 24, 1986, in Book 5344, Page 997, of the Mecklenburg County Public Registry (the "Deed of Trust"),

which constitutes a first lien on certain real property (land and commercial building) located at 4517 East Independence Boulevard, Charlotte, North Carolina (hereinafter described as the "Real Property"). The evidence offered at the hearing on UCB's Motion was that the Real Property had a market value in excess of the current balance of the encumbrances against it.

2. The Second Note represents an extension of a line of credit note in the original principal amount of \$340,000.00, dated March 29, 1988, executed by the same individuals, which matured on April 3, 1989, in order to allow those obligors additional time in which to find substitute financing on the Real Property to pay off the Second Note.

3. The debtor and her husband, Raj Kumar, own an undivided one-half interest in the Real Property as tenants by the entireties, and the other one-half interest in the Real Property is owned by Rajender and Veena Kumar as tenants by the entireties.

4. The First Note is in default for failure to pay the regular installments that have become due thereunder for the months of September through December 1990; and the Second Note is in default for failure of the debtor and the other obligors to pay the outstanding balance of principal and accrued interest at maturity on September 12, 1989.

5. As of December 21, 1990, the payoff balance of the First Note was \$320,575.81 (with interest accruing at the rate of \$90.29 per day) plus costs and attorney's fees; and the payoff

balance of the Second Note was \$228,407.44 (with interest accruing at the rate of \$69.87 per day) plus costs and attorney's fees.

6. As a result of the foregoing default under the Second Note, foreclosure of the Deed of Trust was initiated on October 25, 1989, before the Clerk of Superior Court, Mecklenburg County, North Carolina, Special Proceeding No. 89-SP-1546.

7. On November 29, 1989, the Assistant Clerk of Superior Court of Mecklenburg County, North Carolina entered an Order that found that the Second Note was in default and authorized the Substitute Trustee under the Deed of Trust to proceed with a foreclosure sale of the Real Property.

8. After the foreclosure hearing on November 29, 1989, UCB agreed, without waiving default, to postpone scheduling the foreclosure sale of the Real Property until September 19, 1990, in order to afford Raj Kumar and the debtor additional time to obtain financing on the Real Property which would pay off the Second Note.

9. Upon the debtor's and Raj Kumar's failure to pay off the Second Note by September 19, 1990, the Substitute Trustee under the Deed of Trust scheduled the foreclosure sale of the Real Property for 11:00 a.m. on October 23, 1990.

10. This case was commenced one hour before the scheduled foreclosure sale of the Real Property, and the Substitute Trustee under the Deed of Trust has postponed the foreclosure sale of the Real Property until January 15, 1991, conditioned upon this case

being dismissed or UCB being granted relief from the automatic stay prior to the sale date.

11. The debtor's Schedule A-2 and Schedule A-3 filed in this case reflect that the only claims against the debtor are seven secured claims including the two secured claims held by UCB. The Statement of Financial Affairs and the Schedule of Current Income and Current Expenses filed by the debtor reveal that the debtor is neither self-employed nor engaged in an ongoing business and has no income.

12. Except for personal property having a value of \$2,975.00 and the personal residence which the debtor owns with her husband as tenants by the entirety, the debtor's assets consist of interests in income-producing real property held with her husband as tenants by the entirety and which they own as co-tenants with other individuals, including Rajender Kumar and Veena Kumar.

13. The real estate in which the debtor claims an interest is managed and controlled by, and all income and profits generated therefrom are paid to the debtor's husband, Raj Kumar.

14. As the result of a rift which has developed between Raj and Rajender Kumar, Raj Kumar and the debtor have initiated a special proceeding in the Superior Court of Mecklenburg County, North Carolina, Case No. 90-SP-1260, in order to force a partition sale of the Real Property.

15. The significant reason motivating the filing of the debtor's Chapter 11 petition was to stop the imminent foreclosure

sale of the Real Property. Further, the effect of the filing by the debtor alone (with out her husband joining the petition) was to shelter his other assets and business concerns from administration in a bankruptcy reorganization, and the court finds that was a conscious factor in the debtor's filing of this petition alone. The court finds these facts indicative of an improper motivation for and lack of good faith in the filing of this bankruptcy petition.

16. The debtor has no employment or income (nor did she offer any prospects of obtaining either), and by any objective measure there is no prospect for this debtor's reorganization. Any possibility of reorganization offered by the debtor is wholly dependent upon the voluntary efforts of others (particularly her husband) who are outside the control of this court, and such gratuitous possibilities (which may be withdrawn at will at any time) cannot support any reasonable prospect of reorganization of this debtor.

DISCUSSION

1. Dismissal for Lack of Good Faith

UCB has moved for dismissal of the debtor's Chapter 11 petition in part because it was not filed in "good faith." The basic framework for considering that contention was established by the Fourth Circuit in Carolin Corp. v. Miller, 886 F.2d 693, 694 (4th Cir. 1989). In Carolin, the Fourth Circuit held that:

[A] bankruptcy court may dismiss [a voluntary Chapter 11 bankruptcy] petition for want of good faith in its filing, but only with great caution and upon supportable findings both of

the objective futility of any possible reorganization and the subjective bad faith of the petitioner in invoking this form of bankruptcy protection.

Id. at 694. In establishing this principle, the Fourth Circuit acknowledged that the Bankruptcy Code does not contain a specific good faith filing requirement for Chapter 11 cases. Id. at 698. The Carolin court reasoned, however, that because of the broad policy considerations of the Bankruptcy Code and the language of several provisions of the Bankruptcy Code and of the Bankruptcy Rules, a debtor's good faith was an implicit requirement for the filing of a Chapter 11 petition. Id.

Although recognizing a bankruptcy court's authority to dismiss a Chapter 11 bankruptcy petition for lack of good faith in filing, the Fourth Circuit in Carolin admonished bankruptcy courts to use great care and caution in exercising the power to dismiss. Id. at 700. The Fourth Circuit warned bankruptcy courts to remember that the Bankruptcy Code provides creditors of Chapter 11 debtors with remedies such as relief from stay, adequate protection, and dismissal or conversion under 11 U.S.C. § 1112(b), and that courts should not use dismissal for lack of good faith in filing as an easy alternative to creditors' other post-petition statutory remedies. Id. The Fourth Circuit recognized that by using dismissal as an alternative to the statutory remedies, courts would be subverting the reorganization scheme envisioned in the Bankruptcy Code. Id.

The Fourth Circuit in Carolin adopted a two-pronged test for bankruptcy courts to apply in considering whether to dismiss a

Chapter 11 petition for lack of good faith in filing. Id. at 700-01. The Carolin court required a showing of both objective futility and subjective bad faith in filing before a court properly could dismiss a Chapter 11 petition for lack of good faith. Id. The court noted that in applying the two-pronged test, a court should attempt to determine whether allowing the Chapter 11 petition to proceed past filing would further the purposes of the Bankruptcy Code. Id. at 701. In adopting the two-pronged test, the Fourth Circuit noted that courts should inquire into objective futility to insure that the bankruptcy proceeding will in some way be related to revitalizing a financially troubled debtor. Id. at 701. The Carolin court directed courts to focus on determining whether there exists a going concern to preserve and whether there exists any hope of rehabilitation. Id. The Fourth Circuit noted, further, that courts should inquire into the debtor's subjective bad faith to insure that the debtor actually intends to use the provisions of Chapter 11 to reorganize an existing enterprise or to preserve going concern values of an existing business. Id. at 702. The Fourth Circuit in Carolin stated that the subjective bad faith inquiry would allow courts to determine whether the debtor's real motive in filing a Chapter 11 petition was to abuse the reorganization process and to delay creditors through the automatic stay without any intent or ability to reorganize its activities. Id.

The Fourth Circuit in Carolin noted that in applying the two-pronged test, courts should inquire into the totality of the

circumstances surrounding the filing. Id. at 701. The Fourth Circuit also stated that courts should not rely on any list of factors and that no single factor necessarily would lead to a finding of lack of good faith in filing. Id.

Courts other than the Fourth Circuit have considered the dismissal of a Chapter 11 petition for lack of good faith in filing and have recognized that courts should consider the totality of the circumstances surrounding the filing of the bankruptcy petition. See Little Creek Devel. Co. v. Commonwealth Mortgage Corp. (In re Little Creek Devel. Co.), 779 F.2d 1068 (5th Cir. 1986); In re L'Puente Ltd. Partnership, 104 Bankr. 503 (Bankr. S.D. Fla. 1989); In re Mill Place Ltd. Partnership, 94 Bankr. 139 (Bankr. Minn. 1988); In re Krilich, 87 Bankr. 178 (Bankr. M.D. Fla. 1988); North Central Devel. Co. v. Landmark Capital Co. (In re Landmark Capital Co.), 27 Bankr. 273 (Bankr. Ariz. 1983).

The many factors considered by these courts include, inter alia, the number of assets belonging to the debtor; the degree to which the debtor has encumbered its assets; the number of employees of the debtor, excluding its principals; the adequacy of the debtor's cash flow; the number and amount of the debtor's unsecured claims relative to its secured claims; the existence of a foreclosure proceeding on the debtor's encumbered assets; and the realistic possibility of an effective reorganization.

In applying these principles to the facts of this case, the court can conclude only that the debtor's petition is subject to dismissal for lack of good faith because (a) first, the objective

futility of any possible reorganization and (b) the debtor's subjective bad faith in filing her petition.

(a) Objective Futility of Reorganization

Congress designed Chapter 11 of the Bankruptcy Code "to prevent the waste and reduction in asset values that result from unnecessary liquidation. Congress meant to encourage financial restructuring and to reestablish efficient business operations." In re Sirius Systems, Inc., 112 Bankr. 50, 52 (Bankr. D.N.H. 1990) (quoting In re Schlangen, 91 Bankr. 834, 837 (Bankr. N.D. Ill. 1988)). The essence of Chapter 11, thus, is business reorganization. Id. (quoting In re Harvey Probber, Inc., 44 Bankr. 647, 650 (Bankr. D. Mass. 1984)). The inquiry into the possibility of reorganization must ascertain the existence of a going concern needing preservation and the realistic hope of rehabilitation. Carolin, 886 F.2d at 701; see Little Creek, 779 F.2d at 1073.

Even after giving the debtor the benefit of all doubts, the court cannot find that there is any realistic possibility of a successful reorganization of this debtor. The debtor is an individual with no employment, no income, and no prospects for either (except upon voluntary help from others). There simply is nothing here to reorganize, no entity that can be reorganized, and even if there were, there are no means in this case with which to effect a reorganization.

The debtor's tentative proposal for reorganization was to sell the Real Property securing UCB's debt in order to satisfy

her debts -- in other words to liquidate that asset. The court, finds that this possible reorganization plan would be futile. The Fourth Circuit's language in Carolin focuses on a reorganiza-
tion for continued operations. See Carolin, 886 F.2d at 701-03. The Carolin decision does not purport to limit use of Chapter 11 for such reorganizations, and Chapter 11 often properly is utilized to effect the liquidation of an entity. But, even assuming that liquidation is a viable "reorganization," it appears futile here because the debtor does not control this Real Property. The debtor owns an interest by the entirety in an undivided interest in the Real Property. It appears that the four owners are not able to cooperate in a sale of the Real Property as indicated by the State Court partition action. Moreover, there has been no effort to sell the Real Property until immediately prior to these proceedings, and to date, no prospects have been identified nor any offers made on the property. Further, it appears that this debtor's entirety interest in an undivided interest in the Real Property is not itself capable of being severed and sold, and even if it was, it would not appear that that interest alone would be sufficient to fund a feasible reorganization. Consequently, assuming that liquidation would be a proper use of Chapter 11, liquidation of the Real Property here appears futile.

Any suggestion that reorganization of the debtor might be funded by assistance from her husband is insufficient to support any prospect for reorganization. Any such assistance would be wholly voluntary on his part, would be outside of any control by

the court, and could be terminated at his will at any time. Consequently, the court finds and concludes that, by any objective standard, there is no prospect of reorganization by this debtor and that any purported reorganization of this debtor is futile.

(b) Subjective "Bad Faith"

In addition to finding that the debtor has no objective and realistic possibility to reorganize successfully, the court must find that because this debtor did not file its Chapter 11 petition for a proper purpose consistent with the purposes of Chapter 11 of the Bankruptcy Code, the debtor's filing of this Chapter 11 petition was in "bad faith," or not in "good faith."

Carolin, Little Creek, Landmark and the other cases discussed previously set out principles relevant to this issue. First, although the term "bad faith" may produce images of malfeasance, there is no moral element to that standard in these circumstances. So, the court may find subjective "bad faith" even in the absence of any element of moral turpitude in the debtor's motivation. Here, the debtor appeared to be honest and forthright in every respect. There was nothing evil or unlawful in any of the debtor's actions. The debtor was motivated by her own self-interest, which is understandable. This self-interest, however, does not comport with the proper purposes of the filing of a Chapter 11 petition in the circumstances of this case.

Second, to support a finding of subjective bad faith, the court necessarily must find that the Chapter 11 petition was

filed for a purpose other than one that is consistent with the goals of the Bankruptcy Code. See Carolin, 886 F.2d at 702. The fundamental purpose of Chapter 11 is to serve as a debt collection device that solves the "common pool" problem of multiple creditors having claims against a debtor with insufficient assets fully to satisfy all of their debts.¹ So, the fundamental goal of Chapter 11 is to optimize the benefits to creditors. In this case, the only significant creditor is UCB, and there is no real "common pool" problem to be solved by the bankruptcy.

The courts in Carolin, Little Creek and the other cases cited above, give extensive, non-exclusive lists of factors which further support this determination. Although not meeting all of those factors, this case does involve enough of them to substantiate further the debtor's subjective bad faith in filing this Chapter 11 petition. This is in effect a single-asset bankruptcy and almost exclusively a two-party dispute. No other significant creditors exist or have expressed any interest whatsoever in this proceeding. The debtor has virtually no cash and no income from any employment or "operations." The timing of the bankruptcy filing immediately before a scheduled foreclosure sale demonstrates a purpose of delay. The last minute filing of a bankruptcy petition alone ordinarily may not be sufficient to demonstrate an improper purpose. See Carolin, 886 F.2d at 703. In

¹ There are other related purposes such as preserving jobs for employees and generally benefiting the local community by preserving the existence of an employer. Those factors are not factors here.

light of the circumstances of this case, however, that conclusion is inescapable.

The court can conclude only that the debtor filed this bankruptcy petition to stay, delay and frustrate UCB's efforts to enforce its rights in the debtor's Real Property. That is not proper purpose for filing a Chapter 11 petition. For all of these reasons, the court finds and concludes that the debtor filed her Chapter 11 petition in bad faith.

Based upon its findings of futility of reorganization and bad faith in filing, the court concludes that this case should be dismissed.

II. Dismissal Pursuant to Section 1112(b)

This case also merits dismissal pursuant to the provisions of the Bankruptcy Code on account of several of the factors noted above. Section 1112(b) provides for dismissal of a Chapter 11 case "for cause, including -

- (2) inability to effectuate a plan;
- (3) unreasonable delay by the debtor, that is prejudicial to creditors...."

11 U.S.C. § 1112(b) (1988). The court finds and concludes that the futility of the debtor's reorganization and her delay of UCB's exercise of its rights in the Real Property constitute sufficient bases to justify dismissal of this case pursuant to 11 U.S.C. § 1112(b)(2) and (3).

III. Dismissal for Ineligibility For Chapter 11 Relief

A number of courts have held that Chapter 11 is designed for business reorganizations and that persons who are not engaged in business are not eligible for Chapter 11 relief. In re Toibb, 902 F.2d 14, 14-15 (8th Cir. 1990); Wamsqanz v. Boatmen's Bank of DeSoto, 804 F.2d 503, 504-05 (8th Cir. 1986); In re Little Creek Dev. Co., 779 F.2d 1068, 1073 (5th Cir. 1986); In re Winshall Settlor's Trust, 758 F.2d 1136, 1137 (6th Cir. 1985); In re Wentworth, 83 Bankr. 705, 705-06 (Bankr. D.N.D. 1988); In re Rowland, 77 Bankr. 265, 267 (Bankr. D. Mont. 1987); In re Lange, 75 Bankr. 154, 156-57 (Bankr. N.D. Ohio 1987); In re Bendig, 74 Bankr. 47, 48 (Bankr. D. Conn. 1987); In re Ponn Realty Trust, 4 Bankr. 226, 230-32 (Bankr. D. Mass. 1980). Other courts have not so restricted Chapter 11 relief and have permitted filings by persons not engaged in business. Gonzales v. Parks, 830 F.2d 1033, 1034 n.1 (9th cir. 1987); In re Moog, 774 F.2d 1073, 1074-75 (11th Cir. 1985); In re Cook, 98 Bankr. 624, 625-26 (Bankr. D. Mass. 1989); In re Fernandez, 97 Bankr. 262, 263 (Bankr. E.D.N.C. 1989). Given the conclusion that this case should be dismissed for other reasons, it is not necessary for the court to deal with the conflicting decisions on this issue. It is sufficient here to note that there is no entity in this case that is capable of reorganization, and in that circumstance, the debtor is not eligible for Chapter 11 relief.

It is therefore ORDERED that the Chapter 11 petition filed by the debtor is dismissed.

This the 4th day of January, 1991.



George R. Hodges
United States Bankruptcy Judge