

UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA
NORTHERN DIVISION

IN RE:)
)
CALVIN JOHN GARDNER and)
JACQUELYNNE KAY GARDNER,)
)
Debtors.)
)
A. THOMAS POKELA,)
)
and)
)
FARM CREDIT BANK OF OMAHA,)
a corporation,)
)
Plaintiffs,)
)
vs.)
)
CALVIN JOHN GARDNER, JOHN F.)
KLAAS, and WHOLESALE PRODUCE)
SUPPLY CO., a Minnesota)
Corporation,)
)
Defendants.)

CASE NO. 87-10109-INH
ADVERSARY NO. 90-1005-INH
CHAPTER 12
MEMORANDUM OF DECISION RE:
MOTIONS FOR SUMMARY JUDGMENT

The matters before the Court are the Motion of Defendants John H. Klaas and Wholesale Produce Supply Company for Judgment on the Pleadings or, in the Alternative, for Summary Judgment and the Motion for Summary Judgment or in the Alternative Partial Summary Judgment filed by Intervenor Plaintiff Farm Credit Bank of Omaha and the joinders and responses thereto. These are core proceedings pursuant to 28 U.S.C. § 157(b)(2). The motions were submitted to the undersigned for consideration upon receipt of briefs. This ruling shall constitute Findings and Conclusions as required by Bankr. R. 7052.

I.

Calvin J. and Jacquelynne K. Gardner (Debtors) filed a Chapter 12 petition for debt adjustment on April 1, 1987. In their Statement of Financial Affairs, Debtors acknowledged Debtor-husband had a personal injury lawsuit pending against John F. Klaas (Klaas) and Wholesale Produce Supply Company (Wholesale Produce)

in which he sought a judgment of \$1,309,000.00.¹ On their Schedule of Personal Property, Debtors valued a personal injury lawsuit at \$30,000.00. It was not further described. Debtors did not claim any lawsuit as exempt property.

Debtors' plan was confirmed by Order entered October 15, 1987. In the plan, Debtors submitted "all or such portion of their future earnings or other future income to the supervision and control of the Trustee as is necessary for the execution of the [plan] except for those payments and earnings which may be retained or paid outside of the Trustee." Debtors also committed all of their disposable income for three years to the payment of unsecured claims. The plan did not specifically address the disposition of any lawsuit proceeds. The plan's liquidation analysis did not include any lawsuit proceeds.

Debtor-husband settled the lawsuit by a court approved stipulation of dismissal entered in the United States District Court for the District South Dakota on March 29, 1988. Debtor-husband received \$88,000. Debtors did not seek the Bankruptcy Court's approval of the settlement.

Debtors have invested some of the settlement proceeds. The remainder was used for several capital improvements and farm expenses.

On April 2, 1990, Chapter 12 Trustee A. Thomas Pokela (Trustee) commenced this adversary proceeding by filing a complaint against Debtor-husband and Klaas and Wholesale Produce, the defendants in Debtor-husband's personal injury action. Trustee seeks an order avoiding any settlement of Debtor-husband's lawsuit. He has also asked the Court to turn the lawsuit over to him so that he may determine the fairness of any settlement offer and distribute the proceeds to unsecured creditors.

Debtor-husband has answered the Trustee's complaint and argues that under 11 U.S.C. § 1227 all property of the bankruptcy estate, including the lawsuit, reverted in Debtors at confirmation, that the confirmed plan did not provide for the distribution of any lawsuit proceeds to creditors, and that the Bankruptcy Court's approval of the settlement was not needed since it occurred postconfirmation. Debtor-husband further argues that proceeds of the lawsuit

¹ Debtors' son Rob was also a plaintiff in the personal injury action. See Gardner v. Klaas, Civ. No. 86-1023, United States District Court, District of South Dakota (Northern Division).

settlement are not disposable income subject to distribution to unsecured creditors under 11 U.S.C. §1225(b)(1)(B) since the funds were not part of the bankruptcy estate at the time they were received.

By Order entered June 27, 1990, Farm Credit Bank of Omaha (FCBO) was allowed to intervene as a plaintiff. In addition to the relief sought by Trustee, FCBO seeks a modification of Debtors' plan under 11 U.S.C. § 1229 to insure distribution of any lawsuit proceeds to unsecured claim holders. FCBO also seeks costs, including attorneys' fees, incurred in this action.

Defendants Klaas and Wholesale Produce answered Trustee's complaint and FCBO's Joinder on June 29, 1990. They challenge this Court's jurisdiction over the lawsuit and argue Trustee and FCBO did not have the power to settle Debtor-husband's claim against Klaas and Wholesale Produce nor to receive any settlement funds. They seek dismissal of the action against them and request costs and expenses.

Debtor-husband answered FCBO's Joinder on July 20, 1990. The answer incorporated Debtor-husband's answer to Trustee's Complaint and discounted FCBO's interest in this proceeding.

Klaas and Wholesale Produce filed a Motion for Judgment on the Pleadings, or in the Alternative, for Summary Judgment on June 29, 1990. Debtor-husband joined the Motion on July 20, 1990. FCBO filed a Motion for Summary Judgment or in the Alternative Partial Summary Judgment on July 20, 1990. Trustee joined that Motion.

A hearing was held August 21, 1990. A memorandum in support of Plaintiffs' Motion for Summary Judgment was filed post-hearing by FCBO. Responses to the memorandum were filed by Klaas and Wholesale Produce and Debtor-husband.

While the parties involved in this matter could not agree on the precise nature of the legal issues involved, the Court has determined that two questions must be resolved. First, is this Court's approval of Debtor-husband's settlement of the lawsuit required? Second, do the proceeds of Debtor-husband's settlement constitute disposable income available for distribution to unsecured creditors?

A.

Bankruptcy Rule 9019(a) provides:

COMPROMISE. On motion by the trustee and after a hearing on notice to creditors, the debtor and indenture trustees as provided in Rule 2002(a) and to such other entities as the court may designate, the court may approve a compromise or settlement.

Twenty-days' notice of a hearing on a compromise or settlement must be given to the debtor, the trustee, all creditors, and indenture trustees unless the court for cause orders that notice not be sent. Bankr. R. 2002(a)(3). The term "trustee" in the Bankr. R. 9019 incorporates a debtor-in-possession. Bankr. R. 9001(10).

The debtor retains possession of property of the estate except if he is removed as the debtor-in-possession or if a confirmed plan or confirmation order provides otherwise. 11 U.S.C. §§ 1207(b) and 1227(b). Upon confirmation, the property of the estate vests in the debtor free of any lien or creditor's claim except as provided in the confirmed plan or confirmation order unless discharge is waived or denied or a certain debt is found nondischargeable. 11 U.S.C. §§ 1227(c) and 1228(a).

A Chapter 12 trustee is not authorized to operate the business unless the debtor-in-possession is removed. 11 U.S.C. § 1202(5). While the Chapter 12 trustee is obligated to distribute funds from the debtor to creditors in compliance with the plan, 11 U.S.C. § 1226(a), he is not authorized to collect and reduce to money the property of the estate. See 11 U.S.C. § 1202. After confirmation, the court may, however, order an entity from whom the debtor is to receive income to pay all or part of that income directly to the trustee. 11 U.S.C. § 1225(c).

B.

While it is clear under Bankr. Rs. 9019(a) and 9001(10) that a debtor-in-possession is responsible for bringing settlements before the Court for

approval², the Court is unable to find that a similar obligation is placed on the debtor postconfirmation. Further, the Court finds no statute or rule that vests the Chapter 12 trustee with any authority to manage a lawsuit or negotiate a settlement, unless the debtor-in-possession has been removed. A debtor's activities after confirmation but before entry of discharge, see 11 U.S.C. § 1228(d), may receive court scrutiny if there are allegations of fraud or gross mismanagement by the debtor that is prejudicial to creditors. 11 U.S.C. §§ 1208(c)(1), 1228, and 1230. Such gross mismanagement or fraud could include an inappropriate settlement of a claim or lawsuit. The trustee's duties are sufficiently broad to allow him to file an objection to discharge, a motion to dismiss, or a complaint to revoke discharge or confirmation if there are postconfirmation problems in a Chapter 12 case.³ See 11 U.S.C. §§ 1202 and 704.

Since the settlement of Debtor-husband's personal injury suit was made post-confirmation, notice of the settlement and court approval of it under Bankr. R. 9019 were not required. This is not to say the Court now finds the settlement reasonable. That issue is not properly before the Court upon this complaint.

While Trustee and creditors have several avenues of recourse against Debtors if an inappropriate settlement was made, the Court has not found any authority that grants Trustee or creditors any recourse against Klaas and Wholesale Produce, the defendants in Debtor's lawsuit. Since there have not been any allegations by Debtors that Debtor-husband's settlement was a product of fraud by Klaas and Wholesale Produce, the Court concludes those parties should be dismissed from this action.

² The several factors that a court must consider in determining the fairness of a settlement are set forth in Lambert v. Flight Transportation Corp. (In re Flight Transportation Corp. Securities Litigation), 730 F.2d 1128, 1135-36 (8th Cir. 1984); see also Drexel v. Loomis, 35 F.2d 800, 806 (8th Cir. 1929).

³ The Court renders no opinion on whether Debtors' plan or the order of confirmation should have specifically addressed Debtor-husband's lawsuit or any potential settlement of it. While FCBO has requested that Debtors' plan be modified to allow payment of any lawsuit proceeds as disposable income under § 1225(b)(2)(B), that request was made prior to this Court's decision in In re Kuhlman, 118 B.R. 731 (Bankr. D.S.D. 1990). A restatement of a debtor's and the Chapter 12 trustee's duties governing payment of disposable income and another explanation of the available procedures under the Code for insuring disposable income is paid as set forth in Kuhlman are not needed here.

III.

A.

The definition of property of the estate in a Chapter 12 case is very broad. It includes all property specified in 11 U.S.C. § 541, which applies to all bankruptcy cases, **plus**:

- (1) all property of the kind specified in [§ 541] that the debtor acquires **after** the commencement of the case but before the case is closed, dismissed, or converted to a case under Chapter 7 of this title, whichever occurs first; and
- (2) earnings from services performed by the debtor after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7 of this title, whichever occurs first.

11 U.S.C. § 1207(a) (in pertinent part, emphasis added). Causes of action belonging to a debtor when a case is commenced are included within the definition of property of the estate found in § 541. Mixon v. Anderson (In re Ozark Restaurant Equipment Co.), 816 F.2d 1222, 1225 (8th Cir.), cert. denied, 484 U.S. 848 (1987). Accordingly, causes of action arising "after the commencement of the case but before the case is closed, dismissed, or converted" are included in Chapter 12 property of the estate.

Disposable income is defined as:

- income which is received by the debtor and which is not reasonably necessary to be expended--
- (A) for the maintenance or support of the debtor or a dependent of the debtor; or
 - (B) for the payment of expenditures necessary for the continuation, preservation, and operation of the debtor's business.

11 U.S.C. § 1225(b)(2). Income is not defined. However, every Chapter 12 plan must "provide for the submission of all or such portion of future earnings **or other future income** of the debtor to the supervision and control of the trustee as is necessary for the execution of the plan[.]" 11 U.S.C. § 1222(a)(1) (emphasis added). Therefore, Congress clearly intended the term "income" in Chapter 12 to encompass more than just "earnings."

B.

The Court concludes that Debtor-husband's receipt from the settlement of his personal injury lawsuit constitutes income that Debtors must make available

for plan payments under § 1222(a)(1) and that may constitute disposable income under § 1225(b)(2). This conclusion is consistent with the broad definitions of Chapter 12 "property of the estate" and "disposable income" and the purpose of § 1222(a)(1). The Court finds no other statute or rule that allows Debtors to shield this non exempt property from being made available for plan payments.

The Court does not render herein a decision on whether the settlement proceeds should be made available to unsecured creditors as disposable income. That question was not reached on these summary judgment motions and is more appropriately addressed in an objection to discharge or motion to dismiss by Trustee or a creditor for failure to make all plan payments. See Kuhlman, 118 B.R. at 735-39.

An order granting Defendants' motion for summary judgment and denying Plaintiffs' motion for summary judgment will be entered. The order will not prejudice Trustee's and FCBO's right to object to discharge or seek dismissal of the case on the grounds that Debtors have failed to make all plan payments, including payments of disposable income, or that Debtors have committed fraud or grossly mismanaged their business affairs.

Finally, the Court concludes that the novel issues of law presented here and the unsettled case law in this District on the role of a Chapter 12 trustee preclude any award of costs. An order will be entered denying Trustee's, FCBO's, and Klaas' and Wholesale Produce's requests for costs.

So ordered this 15th day of February, 1991.

BY THE COURT:

Irvin N. Hoyt
Chief Bankruptcy Judge

ATTEST:

PATRICIA MERRITT, CLERK

By _____
Deputy Clerk

(SEAL)

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)	ADVERSARY NO. 90-1005-INH
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JACQUELYNNE KAY GARDNER,)	CHAPTER 12
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Debtors.)	
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A. THOMAS POKELA,)	
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FARM CREDIT BANK OF OMAHA,)	ORDER RE:
a corporation,)	MOTIONS FOR SUMMARY JUDGMENT
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CALVIN JOHN GARDNER, JOHN F.)	
KLAAS, and WHOLESALE PRODUCE)	
SUPPLY CO., a Minnesota)	
Corporation,)	
)	
Defendants.)	

In recognition of and in compliance with the Memorandum of Decision Re: Motions for Summary Judgment entered this day,

IT IS HEREBY ORDERED that the Motion of Defendants John H. Klaas and Wholesale Produce Supply Company for Judgment on the Pleadings or, in the Alternative, for Summary Judgment is GRANTED and the Motion for Summary Judgment or in the Alternative Partial Summary Judgment filed by Intervenor Plaintiff Farm Credit Bank of Omaha is DENIED without prejudice to Trustee A. Thomas Pokela's or other parties in interest's right to object to discharge or seek dismissal of the case for, inter alia, Debtors' fraud, gross mismanagement, or failure to make all plan payments, including payments of disposable income; and

-2-

IT IS FURTHER ORDERED that requests for costs by Trustee A. Thomas Pokela, Farm Credit Bank of Omaha, and John H. Klaas and Wholesale Produce Supply Company are DENIED.

So ordered this ___ day of February, 1991.

BY THE COURT:

Irvin N. Hoyt
Chief Bankruptcy Judge

ATTEST:

PATRICIA MERRITT, CLERK

By _____
Deputy Clerk

(SEAL)