UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA
ROOM 211
FEDERAL BUILDING AND U.S. POST OFFICE
225 SOUTH PIERRE STREET
PIERRE, SOUTH DAKOTA 57501-2463

IRVIN N. HOYT
BANKRUPTCY JUDGE

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October 13, 1989

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Re: Neuhauser Ranch, Inc.
Chapter 12 87-50123
Adversary 88-5005

Dear Counsel:

This letter opinion disposes of Attorney Wilbur's Rule 9011 motion for terms against Attorney William Wyman. The motion alleges that Attorney Wyman signed complaints asserting frivolous claims versus BankWest in this adversary proceeding. The sanction requested is payment for Attorney Wilbur's time and expenses incurred in defending the complaints. The Court notes that Attorney James Hurley, who is not a member of Attorney Wyman's finn, also represented the debtors/plaintiffs in this case. Attorney Hurley's participation was primarily in court hearings while Attorney Wyman primarily prepared the adversary paperwork. The motion requests no sanctions against Attorney Hurley.

The Court will begin with a very brief overview of the facts. The actions leading up to this adversary are set forth with much greater particularity in the Court's findings of fact and conclusions of law entered February 17, 1989.

Under an intricate purchase and lease back scheme, Lone Star Cattle Company leased to Neuhauser Ranch a herd of 820 cattle. BankWest possessed a first lien on the herd. At the time the adversary was brought, the cattle were leased to Todd Cowan. On March 1, 1988, the debtors filed an eight-page complaint against

Lone Star Cattle Company, Lone Star Cattle Limited Partnership, and Kenneth Jones. The complaint signed by Attorneys Hurley and Wyman, alleged that the lease to the debtors constituted a disguised security agreement which was unconscionable, tainted with undue influence, and therefore was void. The defendants responded with a motion to dismiss based inter alia on the failure to add Cowan and BankWest as indispensable parties under Rule 7019. After a stipulation was reached in a court hearing on this motion, an order proposed by Attorneys John Lovald and James Robbennolt on behalf of the defendants was entered June 27, 1988. It recited that pursuant to a stipulation, the motion to dismiss for failure to name indispensable parties was overruled and that "the first lien position of BankWest in the 820 head of cattle in question will not be challenged by plaintiffs ... ."

On June 30, 1988, plaintiffs filed a motion signed by Attorney Wyman to reconsider the above order. The motion objected particularly to the above—quoted language from the order. The defendants responded that if the plaintiffs intended to challenge the validity of the BankWest lien, then the bank should be named as a defendant in the adversary. At the August 4, 1988, hearing on the motion to reconsider, Attorneys Wyman and Hurley indicated that they would not challenge the bank's lien priority if the lien was valid, but they did not concede the validity of the lien. Based upon the parties' stipulations reached at the August 4 hearing, an order was entered the next day stating that BankWest's lien would not be challenged provided it was properly filed and valid, and that the plaintiffs reserved the right to conduct a Section 506 hearing regarding the lien. The order also recited the parties' stipulation that this Court exercise final binding jurisdiction over the adversary. See 28 U.S.C. §157(c) (2).

On September 6, 1988, a first amended complaint signed by Attorney Wyman was filed. This was a 53-page pleading oblivious to the requirement of Federal Rule of Civil Procedure 8(a)(2)'s requirement of "a short and plain statement." BankWest was named as defendant but was not served with the complaint. On September 12, 1988, Attorney Wyman signed and filed an amended motion to join BankWest as an indispensable party and defendant.

On October 14, 1988, BankWest filed a motion to dismiss for failure to state a claim. The accompanying memorandum stated that the first amended complaint requested damages against BankWest in the amount of $800,000.00 for vaguely-pleaded alleged torts, and a determination of the validity of the BankWest lien.

An Attorney Wyman-signed second amended complaint, totalling

54 pages, was filed October 25, 1988, also named BankWest as defendant. Appended to this complaint were copies of the bank's UCC-l filing which included a description of the Lone Star livestock, a continuation statement, and the South Dakota Secretary of State's certification of these copies. The second amended complaint deleted the prayer for money damages against BankWest.

On November 2, 1988, a hearing was held on the joinder and dismissal motions. At this hearing the Court inquired as to the necessity of naming BankWest as defendant. Attorney Lovald conceded BankWest's first lien. Attorney Hurley replied that the bank was added because the original defendants considered them to be indispensable and that the debtor did not know if the BankWest lien was valid at that point. Attorney Wilbur stated he would withdraw the resistance to the joinder motion based solely on the concern that if the debtors proceeded only against the original defendants and obtained a positive result, a finding that Lone Star was an agent of BankWest might have an adverse res judicata effect against the bank in a subsequent proceeding against BankWest. Attorney Wilbur also contended that the complaint was too vague to put the bank on proper notice as to the allegations against it.

The result of the November 2 hearing was that the adversary would be bifurcated. Neuhausers would proceed in the first phase against the original defendants alone, and if Neuhausers were successful in the first phase then a second proceeding would be started to determine the BankWest lien issue. Attorney Wilbur indicated he would withdraw his motion to dismiss, stating that if BankWest was held in, or if the other parties stipulated that no res judicata effect would flow from the first proceeding, that he didn't "mind proving up his lien." The Court ordered that the complaint again be amended to state clear simple claims against the defendants. A third amended complaint was filed thereafter. It also did not contain a prayer for money damages against BankWest but did state that the "validity, priority and extent of the lien interests of the defendants" required resolution, and that the cattle were the plaintiff's "free and clear of any of the liens" claimed by the defendants.

Attorney Wilbur responded to the third amended complaint with a motion to strike and dismiss filed November 14, 1988. The motion alleged inter alia that the third amended complaint did not state an intelligible claim against BankWest. The Attorney Wyman-signed response to this motion stated that the second amended complaint struck the damages claim against BankWest and that the third amended complaint complied with Fed. R. Civ. p. 8. Attorney Wilbur also filed an answer and counterclaim on November 14, 1988,

generally stating that BankWest held a perfected lien. The Attorney Wyman–signed answer to BankWest's counterclaim stated that the indebtedness due BankWest on the 820 cattle was paid in full and that BankWest did not have a valid perfected security interest.

BankWest filed its motion for summary judgment November 22, 1988. On December 5, 1988, an Attorney Wyman-signed response to motion for summary judgment and corresponding affidavit were filed. These documents alleged that there was a genuine issue of fact as to whether the entities securing the BankWest security agreements had sufficient ownership interest in the cattle to allow BankWest's security interest to attach. The response also alleged that BankWest's motion for summary judgment failed to address Neuhauser's allegations that BankWest extended credit to Neuhauser and Jones/Lone Star while cognizant of the Jones/Neuhauser five-year plan, that the cattle were fully paid for, and that payments Neuhauser made to Jones/Lone Star were intended to repay the Jones/Lone Star line of credit from BankWest, but were not paid to BankWest as agreed. Attorney Wilbur the next day filed a response arguing that affidavits of participating attorneys "are improper and should not be allowed by this court."

The BankWest motion for summary judgment was granted by a stipulation of the parties at the December 7, 1988, hearing. Attorney Hurley stipulated to the grant of summary judgment on the condition that the plaintiffs would have the right to move to reconsider the summary judgment order until January 1, 1989, if the plaintiffs later discovered evidence which placed the validity of the BankWest lien in doubt. Attorney Hurley stated that any pending claims against BankWest "real or imagined" would be set aside under the stipulation reached that date regarding summary judgment. No motion to reconsider was filed. The next day a trial commenced and the Court found in favor of defendants Jones and Lone Star on all counts. Written findings of fact and conclusions of law were filed February 17, 1989.

Attorney Wilbur filed the present motion for terms ten days after the findings and conclusions were entered Attorney Wyman's written response claimed that Wilbur's motion incorrectly stated that a complaint was filed against BankWest when actually it was an amended complaint, that an October 4, 1988 letter from Attorney Wilbur to Attorney Wyman stated that Wilbur had no particular objection to litigating the validity of the BankWest lien, that BankWest withdrew its motion to dismiss and did not contest the joinder motion, and stated that Attorney Wyman followed an interpretation of the conditional summary judgment order under which "the position of the Plaintiff would have been, had a Motion

been made to the Court that the Depositions of January 9, 1989, would be taken as retroactive in accordance with the Courts [sic] Order. Mr. Wilbur reportedly attended those Depositions of Officers of BankWest; 'Wyman' did not so attend, however, the plaintiff was represented. Mr. Wilbur did not object." An April 11, 1988, hearing was held on this motion after which the Court took the matter under advisement. Attorneys Hurley, Wyman and Wilbur appeared personally at the hearing.

Rule 9011

Bankruptcy Rule 9011, modeled after Federal Rule of Civil Procedure 11, provides in most relevant part:

> The signature of an attorney or a party constitutes a certificate that the attorney or party has read the document; that to the best of the attorney's or party's knowledge, information and belief formed after reasonable inquiry it is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law and that it is not interposed for any improper purpose such as to harass, to cause delay, or to increase the cost of litigation. ... If a document is signed in violation of this rule, the court on motion or on its own initiative, shall impose on the person who signed it, the represented party, or both, an appropriate sanction, which may include an order to pay the other party or parties the amount of the reasonable expenses incurred because of the filing of the document, including a reasonable attorney's fee.

The underlined portion of the Rule, sometimes referred to as the "frivolousness clause,"[1] is at the heart of this case.

Rule 11 is designed to discourage the filing of frivolous court papers or those that are legally unreasonable or without factual foundation. Hartman v. Hallmark Cards, 833 F.2d 11.7 (8th Cir. 1987). See also Kurkowski v. Volcker, 819 F.2d 201 (8th Cir.

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[1] Byrne, Sanctions for Wrongful bankruptcy Litigation, 62 Bankruptcy L.J. 109, 114 (1988).

1987). Tn Lupo v. R. Rowland & Co., 857 F.2d 482 (8th Cir. 1988) the Eighth Circuit also stated that the purpose of Rule 11 is to compensate the offended party for the expenses caused by a violation as well as to penalize the offender. The Rule is intended to be vigorously applied to curb frivolous pleadings and other papers. Adduono v. World Hockey Association, 824 F.2d 617 (8th Cir. 1987). However it is not a panacea intended to remedy all matter of attorney misconduct. Id.

Under Rules 11 and 9011, the conduct of the non-movant is to be judged under a standard of "objective reasonableness." E.E.O.C. v. Milavetz and Associates, P.A., 863 F.2d 613 (8th Cir. 1988). See also Hartman supra, Adduono supra, Kurkowski supra, and O'Connell v. Champion International Corp., 812 F.2d 393 (8th Cir. 1987). The Court does not doubt Attorney Wyman's subjective good faith in signing the documents in question. However, such good faith is not a defense under Rule 11. See Milavetz and Hartman supra. See also Robinson v. National Cash Register Co., 808 F.2d 1119 (5th Cir. 1987) and Byrne at 114.

Analysis

The Court will organize its analysis of Attorney Wilbur's motion according to what it perceived to be the three claims that Attorney Wyman at some point attempted to make against BankWest.

(a) Lender Liability Tort Claims

The first amended complaint on page 53 contained a prayer for entry of a $800,000.00 judgment against Jones/Lone Star and BankWest, jointly and severally. As noted above, the complaint was signed by Wyman as were the corresponding motions to join BankWest as defendant. A reading of the complaint revealed various vaguely stated tort and contract based lender liability theories against BankWest as well as the lien validity challenge. The prayer for damages was dropped in the second amended complaint.

At the hearing on the motion for sanctions Attorney Hurley mentioned Attorney Wilbur's October 4, 1988, letter to Attorney Wyman. The letter outlined the adverse consequences of having a bank named defendant in a lawsuit which seeks monetary damages. This letter resulted in plaintiff's withdrawal of the claim for monetary damages, thus leaving the other declaratory issues. However, withdrawing a frivolous claim may mitigate the possible sanction imposed, but it does not preclude the sanction. No showing that the damages claimed against BankWest were "well grounded in

fact and warranted" by law has been made. The Court finds Attorney Wyman did not undertake a reasonable inquiry to determine if a claim for money damages reasonably or arguably existed against the bank and concludes that Attorney Wyman's signature on the first amended complaint and related documents is sanctionable under Rule 9011.

(b) Lien Validity Issue

Under SDCL 57A-9-203(1), a security interest attaches and is valid as between the lender and debtor when the debtor signs a security agreement containing a description of the collateral, the lender extends the debtor value, and debtor has rights in the collateral. Of course in bankruptcy, perfection of the lien also becomes relevant as between the debtor and lender because of the debtor in possession lien-avoidance powers. The ordinary fashion by which one determines the existence and validity of a lien usually does not include suing the party claiming the security interest. At no time has it been explained to the Court why suing BankWest was necessary to determine the validity of its lien. Attorney Wyman has not demonstrated why the BankWest lien would be extinguished if he prevailed on the claim against Lone Star.

Attorney Hurley argued at the sanctions hearing that sanctions cannot arise from the signed documents which alleged that the lien was invalid because (1) Lone Star/Jones insisted that BankWest be added as an indispensable party; (2) BankWest withdrew its motion to dismiss the complaint brought against it and consented to joinder as defendant; and (3) the lien validity issue was dropped after post-complaint discovery proved that the lien was valid and the plaintiffs consented to entry of summary judgment against them. As to the first allegation, it is true that Lone Star/Jones orally at hearings and through written motion requested the addition of BankWest. However, Lone Star/Jones' position on this matter is most accurately stated as being that if the plaintiff challenged BankWest's lien, then the bank should be added as a defendant. It was the plaintiff's insistence that the lien may be invalid that prompted the original defendant's joinder motion. Lone Star/Jones did not claim that the lien was invalid; to the contrary, Lone Star/Jones admitted that the lien was valid at the August 4, 1988 hearing.

The third argument has been discussed to a large degree above under heading (a). contrary to Attorney Hurley's assertions, it is not a defense that the challenge to the validity of the lien was withdrawn after discovery established the lien's validity. "What

Rule 11 and Rule 9011 forbid are 'expeditionary pleadings,' filed with nothing but the hope that discovery will yield some basis for the position taken." Byrne at 114-115 (footnotes omitted). This observation applies with equal force to the lender liability claims.

The Court finds that Attorney Wyman's signatures on the complaints and other documents challenging BankWest's lien were not objectively the product of a reasonable inquiry nor well grounded in fact or warranted by law and concludes that these documents were signed in contravention to Rule 9011.

(c) Request for 506 Valuation

Some documents signed by Attorney Wyman refer to the need for a Section 506 valuation of the bank's lien. This request is of no impact as to the present motion. It was rarely brought up at any of the hearings and doubtless resulted in very little, if any, time expended by Attorney Wilbur. The Court observes, however, that the 506 motion was relevant only (1) if BankWest had an unassailable lien, the position contrary to that taken by plaintiffs, and (2) if the plaintiffs succeeded on their claim versus Lone Star/Jones and were found to be the owners of the cattle.

Conclusion

This Court generally has been hesitant to grant Rule 9011 motions. However, counsel's actions in this case meet the high threshold required by the Rule. The cases of Mary Ann Pensiero, Inc. v. Lingle, 847 F.2d 90 (3rd Cir. 1988) and United States v. Hawley, 768 F.2d 249 (8th Cir. 1985) cited by Attorney Wyman at the hearing on this motion do not aid his cause. Hawley is a criminal case in which the Eighth Circuit noted in passing that defense counsel's tactics would have violated Rule 11. In Pensiero, the Third Circuit enacted "a requirement that all motions requesting Rule 11 sanctions be filed in the district court before the entry of a final judgment. Where appropriate, such motion should be filed in earlier time — as soon as practicable after discovery of the Rule 11 violation." However, the Court's research does not reveal the existence of a similar rule in the Eighth Circuit.

The Court also notes Attorney Wilbur's September 28, 1988, November 10, 1988 and January 3, 1989 letters to Attorney Wyman which indicated Wilbur's intention to bring a Rule 9011 motion.

According to Byrne "to establish a foundation for recovering the costs incurred in bringing the dispositive motion, the adversary should formally demand withdrawal of the complaint and state an intention to seek sanctions prior to filing the motion." Id. at 124.

Attorney Wyman was given ample opportunity to explain and amend his signed. documents in order to state or attempt to state valid or meritorious claims against BankWest. However, at no time throughout the course of this adversary proceeding did he establish an intelligible claim against the bank.

Since a Rule 9011 motion can arise only within a bankruptcy proceeding the Court concludes that the present matter is a core proceeding under 28 U.S.C. §157(b). The Court shall enter an appropriate order granting Attorney Wilbur's motion. Attorney Wilbur is directed to submit proposed findings of fact and conclusions of law consistent with this opinion.

Very truly yours,

Irvin N. Hoyt
Chief Bankruptcy Judge

INH/sh
CC: Bankruptcy Clerk

UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA

IN RE: NEUHAUSER RANCH, INC., Debtor. NEUHAUSER RANCH, INC., Plaintiff, v LONE STAR CATTLE LIMITED PARTNERSHIP, a/k/a LONE STAR CATTLE COMPANY, a South Dakota Limited Partnership, and its General Partner, KEN JONES; and KENNETH JONES, a/k/a KEN JONES individually; and DOUBLE K CATTLE COMPANY, a/k/a KK CATTLE COMPANY, a sole proprietorship of KENNETH JONES; and WESTERN GENERAL CORPORATION, a/k/a GENERAL WESTERN CORPORATION, a South Dakota Corporation; and BANKWEST, INC., formerly, BANKWEST, N.A. , Pierre, SD, Defendants.	CASE NO. 87-50123 ADVERSARY NO. 88-5005 CHAPTER 12 ORDER GRANTING SANCTIONS UNDER BANKRUPTCY RULE 9011

Pursuant to the letter opinion executed this same date,

IT IS HEREBY ORDERED that Attorney William A. Wyman shall pay from his personal assets the sum of $2,571.13 in attorney's fees, sales tax, and costs to Attorney Brent A. Wilbur.

Dated this 13th day of October, 1989.

BY THE COURT:

Irvin N. Hoyt
Chief Bankruptcy Judge

ATTEST:

PATRICIA MERRITT, CLERK

By: ____________________
Deputy

(SEAL)