

November 18, 2004

Barbara A. Schermerhorn
ClerkNOT FOR PUBLICATIONUNITED STATES BANKRUPTCY APPELLATE PANEL
OF THE TENTH CIRCUIT

IN RE GERALD ANTHONY VESSA,
also known as Jerry Vessa, formerly
doing business as Basin Electric, doing
business as Northern Electric, and
LORINDA ANN VESSA,

Debtors.

BAP No. WY-04-012

GERALD ANTHONY VESSA, and
LORINDA ANN VESSA,

Appellants,

v.

COMMUNITY FIRST NATIONAL
BANK OF GILLETTE,

Appellee.

Bankr. No. 03-21712
Chapter 13

ORDER AND JUDGMENT*

Appeal from the United States Bankruptcy Court
for the District of Wyoming

Before BOHANON, CORNISH, and MICHAEL, Bankruptcy Judges.

CORNISH, Bankruptcy Judge.

The Chapter 13 debtors timely appeal a final Order of the United States Bankruptcy Court for the District of Wyoming granting a “Motion to Modify

* This order and judgment is not binding precedent, except under the doctrines of law of the case, res judicata, and collateral estoppel. 10th Cir. BAP L.R. 8018-6(a).

Stay” that was filed by Community First National Bank of Gillette (CFNB).¹ The parties have consented to this Court’s jurisdiction because they have not elected to have this appeal heard by the United States District Court for the District of Wyoming.² For the reasons stated, the bankruptcy court’s Order is AFFIRMED.

I. Background

Gerald Anthony (Gerald) and Lorinda Ann Vessa (collectively, the “Debtors”) were directors and shareholders of Basin Electric, Inc. (BEI), a Wyoming corporation engaged in the commercial electronic contracting business. BEI’s only other directors and shareholders were Gerald’s brother, Ronald L. Vessa, Jr., and Ronald’s spouse, Teresa G. Vessa (collectively, the “Nondebtor Shareholders”). BEI owned and operated its business on real property located in Wyoming (Real Property). It also owned personal property, including various trenchers, trailers, and tools.

BEI borrowed \$247,000.00 from CFNB. This loan is evidenced by a Small Business Administration Note dated February 21, 2003 (SBA Note). All the Debtors and the Nondebtor Shareholders personally guaranteed the SBA Note. BEI’s obligation under the SBA Note was also secured by a Mortgage against the Real Property. CFNB was also given a security interest in BEI’s personal property and fixtures as evidenced by a Security Agreement. The specific items of personal property subject to CFNB’s security interest are itemized on a document attached to the Security Agreement (Property List). In the Security Agreement, BEI, through the Debtors and Nondebtor Shareholders, expressly represented that it owned the personal property stated on the Property List. In the security documents, BEI was required to notify CFNB of any material changes to its business structure or the ownership of CFNB’s collateral, and to maintain

¹ 28 U.S.C. § 158(a)(1); Fed. R. Bankr. P. 8002(a).

² 28 U.S.C. § 158(b)-(c); Fed. R. Bankr. P. 8001(e).

insurance on the collateral. BEI's dissolution was an enumerated ground for default under the Mortgage.

In addition to the SBA Note loan, BEI also had a line of credit with CFNB that was secured by CFNB's interest in certain personal property. But, in March 2003, that line of credit was replaced by a factoring agreement known as the "Business Manager Agreement." BEI sold its accounts receivable to CFNB under the Business Manager Agreement, and it is undisputed that CFNB was granted a security interest in, among things, all of its "present and future accounts, instruments, contract rights, chattel paper, documents and general intangibles," and the proceeds from that property.³ The Debtors and the Nondebtor Shareholders also personally guaranteed this debt. BEI, through the Debtors as corporate officers, expressly agreed that it would not assign the Business Manager Agreement without CFNB's prior written approval. It was an event of default if BEI dissolved, terminated its business, or discontinued its business as a going concern. Additionally, the Business Manager Agreement states that it is an event of default for BEI to transfer business ownership without CFNB's prior written consent.

On May 16, 2003, CFNB commenced an action in state court against BEI, the Debtors and the Nondebtor Shareholders related to the Business Manager Agreement.⁴ Subsequently, on July 10, 2003, BEI gave notice of a special meeting of its shareholders. On that same date, BEI's shareholders executed "Consent Resolutions in Lieu of Special Meeting of Shareholders," deciding to dissolve the corporation. The shareholders also resolved that they would have the

³ Business Manager Agreement ¶ 3.3, Appellant's Appendix at 163.

⁴ The Debtors have included a copy of CFNB's state court complaint in the record on appeal. There is no record that this complaint was introduced into evidence before the bankruptcy court and, therefore, we will not consider it. But, we accept as true the Debtors' statement that CFNB commenced an action on May 16, 2003.

first right and option to acquire right, title and interest of BEI in and to its remaining assets (Option). CFNB was not notified of these resolutions and actions.

On July 28, 2003, Gerald exercised the Option, thus acquiring the personal property listed on an attached Schedule A, subject “to the security or priority right therein of any creditor having a security interest or other priority interest.”⁵ Schedule A to the Option includes some of CFNB’s personal property collateral. The Option states that Gerald assumed “for his account the payment obligation of the corporation to its creditor or creditors having a security interest or other priority in each such asset.”⁶ A Bill of Sale was also executed on July 28th, under which BEI sold the personal property listed on Schedule A to Gerald for “valuable consideration.”⁷ Gerald tendered no monetary consideration to BEI in exchange for the transfer of assets, but rather acquired them in exchange for his agreement to assume the corporation’s debt. It thus appears Gerald agreed to assume a debt he was already obligated to pay under the guaranty agreement. On July 30, 2003, Articles of Dissolution of BEI were filed with the Wyoming Secretary of State. It is undisputed that CFNB was not notified of the Option, the transfer evidenced by the Bill of Sale, or of BEI’s dissolution.

In addition to the personal property transfer, BEI transferred the Real Property subject to CFNB’s Mortgage to Gerald in August 2003.⁸ Gerald also took title to the Real Property subject to the Mortgage. CFNB was not notified of this transfer.

⁵ Option at 1, Appellant’s Appendix at 118.

⁶ Option at 1, Appellant’s Appendix at 118.

⁷ Bill of Sale at 1, Appellant’s Appendix at 130.

⁸ A quitclaim deed dated August 20, 2003, was entered into evidence below, but it is not included in the appellate record. That this transfer took place, however, is not contested.

Immediately after BEI was dissolved, Gerald began doing business as Northern Electric (NE).⁹ Like BEI, NE is an electrical contracting business. BEI formerly performed large industrial jobs; now NE engages in small consumer service jobs. BEI had thirty-six employees, and NE has three, including the Debtors. NE uses the Real Property and some or all of the personal property subject to CFNB's liens. Gerald made no payments to CFNB under the Business Manager Agreement after July 2003.¹⁰

On August 27, 2003, the Debtors filed their Chapter 13 petition. In their "Second Amended Chapter 13 Plan" (Plan), the Debtors proposed to pay approximately 2.2% of claims held by general unsecured creditors whose claims were undisputed and liquidated. Since CFNB's claims are disputed, they are not included in the calculation of this percentage. According to the Plan, CFNB had a claim in the amount of \$245,969.21 secured by fixtures, equipment and office furniture. Of that claim, \$6,560.50, the fair market value of CFNB's collateral, is to be paid, with the remaining disputed unsecured portion being treated as an unsecured deficiency claim. The Plan also proposes to cure a \$5,007.00 arrearage on the SBA Note through pro rata payments made by the trustee. By making this cure, the Debtors state that their default under the SBA Note would be waived. Finally, the Debtors propose to "strip off" the unsecured portion of CFNB's Mortgage claim. They would directly pay CFNB according to the terms of the SBA Note and Mortgage. However, the total amount paid would be the fair market value of the Real Property, \$129,000.00, and not the principal sum due which the Debtors admit exceeds \$240,000.00. The Debtors state that the difference between the amount owed to CFNB and the amount to be paid to it will be treated as a disputed unsecured claim. Despite their proposal to make direct

⁹ See Statement of Financial Affairs, Appellant's Appendix at 225.

¹⁰ Transcript at 56, Appellant's Appendix at 83.

payments to CFNB on the SBA Note, several postpetition payments have not made.¹¹

In November 2003, CFNB filed its “Motion to Modify Stay” (Stay Motion). The Stay Motion sought relief from the automatic stay under 11 U.S.C. § 362(d)¹² to “permit [it] to repossess and foreclose its security interest in” the Real Property and undefined “accounts receivables [sic], inventory, equipment and general intangibles.”¹³ CFNB first argued that the automatic stay did not apply because the property in question was BEI’s property, not property of the Debtors’ estate. Alternatively, CFNB asserted that relief from stay was appropriate under § 362(d) because the Debtors had failed to offer adequate protection for its interests. CFNB further argued that the Debtors had no equity in the collateral, and that BEI’s transfer of CFNB’s collateral to Gerald was in violation of the applicable loan agreements.

The Debtors objected to CFNB’s Stay Motion. They argued that relief from the stay was inappropriate because the Personal Property and the Real Property were necessary for an effective reorganization. The Debtors also asserted that they were affording CFNB adequate protection by making their plan payments to the Chapter 13 trustee.

At an evidentiary hearing, Gerald testified that some of CFNB’s collateral had not been transferred to him when BEI dissolved; that this property was located at the Real Property; and that it was uninsured.¹⁴ He also stated that at least one of the trailers on the Property List had been sold, but the trustee had to

¹¹ Transcript at 56, Appellant’s Appendix at 83.

¹² All future statutory references in the text of this Order and Judgment are to title 11 of the United States Code.

¹³ Motion to Modify Stay at 2, Appellant’s Appendix at 191.

¹⁴ Transcript at 34, 36, 38-39, Appellant’s Appendix at 61, 63, 65-66.

collect the proceeds. He stated that CFNB had not been notified of the sale.¹⁵

The bankruptcy court, after hearing evidence, entered its Order granting the Stay Motion as to the Real Property and a portion of the personal property.¹⁶ It held that CFNB was required to obtain relief from the automatic stay because the Real Property and the personal property that BEI transferred to Gerald was property of the Debtors' estate. The bankruptcy court then held that "cause" existed to modify the automatic stay. BEI's prepetition property transfers to Gerald were improper because CFNB was not notified and they were accomplished to thwart CFNB's foreclosure efforts. It also concluded that the Debtors's Plan did not afford CFNB adequate protection.

The bankruptcy court's Order has now been stayed pending appeal.

II. Discussion

Upon the filing of a bankruptcy petition, § 362(a) automatically stays certain acts related to the debtor and its property. Relief from that stay may be granted under § 362(d) which states, in relevant part, that:

- (d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay—
 - (1) for cause, including the lack of adequate protection of an interest in property of such party in interest[.]¹⁷

A bankruptcy court's order granting relief from the automatic stay for "cause"

¹⁵ *Id.* at 39, Appellant's Appendix at 66.

¹⁶ The bankruptcy court stated that CFNB could pursue its remedies to repossess and foreclose its interests in "[a]ll trenchers, trailers and tools listed on attached Exhibit A[.]" Order on Community First National Bank of Gillette's Motion for Relief From Stay at 7, Appellant's Appendix at 25. In the Order, the court stated that it had inconclusive evidence regarding CFNB's interest in vehicles and accounts that allegedly secured its claims against the Debtors. *Id.* at 3-4, Appellant's Appendix at 21-22. CFNB has not appealed that portion of the Order.

¹⁷ 11 U.S.C. § 362(d)(1).

pursuant to § 362(d)(1) is reviewed for abuse of discretion.¹⁸ “Under the abuse of discretion standard ‘a trial court’s decision will not be disturbed unless the appellate court has a definite and firm conviction that the lower court made a clear error of judgment or exceeded the bounds of permissible choice in the circumstances.’”¹⁹

“Cause” for relief from the stay is not defined in the Bankruptcy Code, but it is well-established that it is determined on a case-by-case basis, taking into account all of the circumstances of each case.²⁰ “Cause” for modifying or terminating the automatic stay has, therefore, been found to exist when a case is filed in bad faith.²¹ Bad faith and, thus, “cause” may exist when a debtor has acted improperly in some way toward the movant-creditor during the prepetition period and when a petition is filed to thwart foreclosure efforts.²²

¹⁸ *Franklin Sav. Ass’n v. Office of Thrift Supervision*, 31 F.3d 1020, 1023 (10th Cir. 1994); *Pursifull v. Eakin*, 814 F.2d 1501, 1504 (10th Cir. 1987); *In re Busch*, 294 B.R. 137, 140 (10th Cir. BAP 2003); *Carbaugh v. Carbaugh (In re Carbaugh)*, 278 B.R. 512, 517 (10th Cir. BAP 2002).

¹⁹ *Moothart v. Bell*, 21 F.3d 1499, 1504 (10th Cir. 1994) (quoting *McEwen v. City of Norman*, 926 F.2d 1539, 1553-54 (10th Cir.1991)).

²⁰ *See, e.g., Pursifull*, 814 F.2d at 1506 (citing cases); *Busch*, 294 B.R. at 140; *Carbaugh*, 278 B.R. at 525.

²¹ *See, e.g., Laguna Assocs. Ltd. Partnership v. Aetna Casualty & Surety Co. (In re Laguna Assocs. Ltd. Partnership)*, 30 F.3d 734, 737-38 (6th Cir. 1994) (“cause” to terminate stay exists where case was filed in bad faith) (citing numerous cases); *In re Pacific Rim Investments, LLP*, 243 B.R. 768, 772 (D. Colo. 2000) (“cause” to terminate stay existed where debtor filed Chapter 11 case to avoid state court foreclosure litigation); *cf. Udall v. FDIC (In re Nursery Land Dev., Inc.)*, 91 F.3d 1414 (10th Cir. 1996) (debtor filed Chapter 11 petition in bad faith where it acquired property on eve of foreclosure and then filed petition to frustrate foreclosure).

²² *See, e.g., Laguna Assocs.*, 30 F.3d at 738 (listing improper prepetition conduct as grounds for bad faith in dismissing case or granting relief from stay), *cited with approval in Nursery Land*, 91 F.3d at 1416 (sanctions imposed against Chapter 11 debtor’s principal and attorney affirmed; debtor’s case filed in bad faith where debtor acquired property and filed its petition to frustrate foreclosure); *see also In re Kolberg*, 199 B.R. 929, 934 (W.D. Mich. 1996)

(continued...)

Based on the record in this case, we do not have a definite and firm conviction that the bankruptcy court made a clear error of judgment or exceeded the bounds of permissible choice under these circumstances. Therefore, its Order granting CFNB relief from stay as to some of its collateral must be affirmed. BEI, acting through the Debtors and Nondebtor Shareholders, assigned its CFNB debts and transferred CFNB's collateral to Gerald and then dissolved without notifying CFNB. These acts violated the parties' agreements and resulted in default of the agreements.

That this conduct took place shortly after CFNB filed its state court action and just before the Debtors filed their Chapter 13 petition further justifies the bankruptcy court's "cause" finding. The bankruptcy court's finding of "cause" is further supported by the facts that some of CFNB's collateral is not insured in violation of the agreements, and Gerald, who assumed BEI's debt under the Business Manager Agreement, did not make prepetition payments to CFNB. Despite Gerald's assumption of the SBA Note and his Plan proposal to make payments on that debt directly to CFNB, several postpetition payments were not made. The totality of all of the circumstances therefore support the bankruptcy court's finding of "cause" to lift the automatic stay.²³

The Debtors next argue that "cause" does not exist because it was not improper for Gerald to assume BEI's debt and take title to the collateral since he had personally guaranteed BEI's debt. This argument misses the mark. CFNB contracted with BEI, basing its lending decision on the existence of collateral and the Debtors' and other guaranties. BEI was a corporate entity doing business with

²² (...continued)
(creditor may receive exemption from operation of the automatic stay when debtor has acted improperly).

²³ Affirming that "cause" exists based on the totality of the circumstances, we need not address the "new debtor syndrome" mentioned by the bankruptcy court.

thirty-six employees on large industrial electrical contracting jobs. The Debtors could not unilaterally decide that Gerald, not BEI, would owe the debt. This is made clear by the relevant agreements, all of which require notice and CFNB's consent for transfers and assignments. The need for a secured lender to be notified of an assignment of its debt is illustrated here, where assignee-Gerald, doing business as NE, has greatly changed the type and scale of business performed from that of assignor-BEI.

The Debtors are correct that filing a bankruptcy petition while a foreclosure proceeding is pending is not at all unusual or per se improper, but the law outlined above shows that timing is relevant in determining whether "cause" exists for lifting the automatic stay. Here, the relevant events – the transfers and assignments, BEI's dissolution and the filing of the Debtors' Chapter 13 petition – all took place shortly after CFNB filed its state court action. The timing of these events coupled with the fact that CFNB, BEI's primary lender, was not notified of the corporate activity, support the finding of "cause" for lifting the automatic stay.

Finally, the Debtors argue that the acts did not amount to "malfeasance." To the extent that malfeasance contains an element of evil intent, the Debtors are correct in arguing that there was no evidence of such intent. From Gerald's testimony it is clear that he is distraught at his distressed financial situation and the financial collapse of BEI. While he in large part blames CFNB for his plight, there was no evidence that any of his actions were done to intentionally harm CFNB. This being said, however, the totality of all the evidence demonstrates that the bankruptcy court did not abuse its discretion in allowing CFNB to pursue its collateral at this time.

III. Conclusion

The bankruptcy court is AFFIRMED.