UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

In re: Verna B. Neilson,

Debtor.

Case No. 17-10631
Chapter 11

APPEARANCES:

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Robert E. Littlefield, Jr., United States Bankruptcy Judge

MEMORANDUM–DECISION AND ORDER

Currently before the Court is the Estate of Elena Duke Benedict's (the "Estate") motion to dismiss the Debtor's case for bad faith. The Court has jurisdiction over this proceeding pursuant to 28 U.S.C. § 157(a), (b)(1), and (b)(2).

FACTS AND PROCEDURAL HISTORY

At the outset, this Court agrees with the Westchester County Surrogate (Scarpino, S.) when he described this dispute as a "Shakespearean tragedy." (ECF No. 58; Ex. A.) Below, the Court summarizes the decades long litigation between the Debtor and her mother, now the Estate.

The Annuity Litigation

Elena Duke Benedict ("Benedict") was the daughter of Dr. Herman Kohl, a founder of Tropicana Products, Inc. Benedict had six daughters (collectively "Daughters"), including the

Debtor. In 1983, Benedict entered into an annuity agreement pursuant to which she was to receive $24,067.90 monthly for the rest of her life. In 1987, the Daughters assumed the obligation to pay the annuity to their mother in exchange for approximately $2.26 million (the "Annuity Funds"). The Daughters hired an agent to invest the Annuity Funds and make annuity payments to Benedict if the Daughters did not. As time passed, the Annuity Funds dissipated such that Benedict began receiving only partial payments in 1994.

In 1999, Benedict commenced an action against her Daughters for breach of the annuity agreement. In defense, the Debtor argued that her breach was due to gross mismanagement and self-dealing by the agent in charge of the Annuity Funds.[1] On March 31, 2014, after approximately fifteen years of litigation, the state court found the Daughters who had not already settled to be jointly and severally liable to the Estate[2] under the annuity agreement. On September 27, 2016, the state court determined the Estate's damages and, on October 25, 2016, signed a judgment in the amount of $4,237,755.03. The Debtor filed a timely notice of appeal but has not perfected the appeal. On January 31, 2017, the Estate filed a transcript of the judgment in the Columbia County Clerk's office, the county in which the Debtor owns real property.

The BDF Litigation

Benedict and 6D Farm Corporation ("6D") were equal partners in Benedict Dairy Farms ("BDF"), a partnership that has been in dissolution since 1998. The Debtor has a five-sixths interest in 6D. In 2005, the Debtor commenced an action against Benedict on the grounds that Benedict failed to make required capital contributions to BDF. The Debtor, on behalf of 6D,

[1] In 1997, the Debtor and her sister, Patricia Benedict, commenced an action against multiple defendants, including the agent in charge of the Annuity Funds, for damages arising out of the alleged mismanagement of the funds. According to the Debtor's Disclosure Statement, this lawsuit resulted in settlements of approximately $9,000,000.
[2] Benedict passed away on or about March 30, 2010.

served a claim against the Estate in the amount of $2,595,697 on September 21, 2015, based on this alleged breach. According to the Debtor, the BDF litigation remains stalled over a dispute regarding document production and has been stayed since the Debtor filed her bankruptcy case.

Pre-Petition Transfers

The Debtor lives in a 66-acre, seven-bedroom,[3] seven-bathroom, 7,500 square foot residence located at 50 Hudson Street, Kinderhook (the "Property"). (Debtor's 2004 Tr. 31:10–21, ECF No. 58, Ex. D; Adv. Proc. 17-90016, Answer 3.) According to the Debtor, the Property was appraised at $2,500,000 in 2014 (Debtor's 2004 Tr. 60:17–25), and its current estimated market value is $1,800,000 to $2,000,000. (Am. Disc. Statement 8, ECF No. 38.) On or about January 12, 2015, at which time the Debtor owned the Property solely in her own name, the Debtor transferred the Property to herself and her husband as joint tenants. (Adv. Proc. 17-90016, Answer 3.) Subsequently, on or about March 4, 2015, the Debtor and her husband transferred a seventy-five (75%) percent interest in the Property to a Trust for the benefit of their children and transferred the remaining portion of the Property to themselves as joint tenants such that they each have a twelve and a half (12.5%) percent interest. (Adv. Proc. 17-90016, Answer 3.)

The Debtor indicates that her husband was hospitalized three times during a span of twenty months and the transfers were made for estate planning purposes as a result of her husband's medical issues. (Neilson Aff. 1–2, ECF No. 77.) Further, the Debtor's disclosure statement provides that the transfers are "subject to being rescinded by the Bankruptcy Court" and indicates that she may need to commence an adversary proceeding "to recover the 87.5% of the house ownership she transferred . . . ." (Am. Disc. Statement 8.)

[3] The Estate contends that the Property has ten bedrooms. (Adv. Proc. 17-90016; Complaint 3.)

The Debtor's Case

The Debtor filed a voluntary chapter 11 petition on April 4, 2017. Beginning on July 7, 2017, significant litigation developed between the parties in this Court:

July 7, 2017	The Estate commenced an adversary proceeding (Adv. Proc. 17- 90016) objecting to the Debtor's discharge.
July 27, 2017	The Debtor commenced an adversary proceeding (Adv. Proc. 17- 90021) to avoid the Estate's judgment lien as a preference.
	The Debtor moved for a Rule 2004 examination of the Estate's executor, Patrick Carr, Esq.
July 28, 2017	The Debtor moved for sanctions against the Estate for violating the automatic stay. (ECF Nos. 39–41.)
September 12, 2017	The Estate filed this Motion to dismiss for bad faith.
October 10, 2017	The Debtor objected to the Estate's Proof of Claim for $4,590,941.03. (ECF No. 74.)

On the parties' consent, the Court entered orders assigning the matters to mediation and appointing a mediator on December 21, 2017. The parties were unable to reach a resolution and oral argument on the Motion concluded on March 28, 2018. After the parties filed additional submissions, the Court took this matter under advisement on May 2, 2018.

ARGUMENTS

The Estate argues that the Debtor filed her petition in bad faith as this case is simply a two party dispute without a bankruptcy purpose. In opposition, the Debtor claims to have filed this case to reorganize. Notwithstanding the Estate's $4 million judgment against her, the Debtor takes the position that the Estate may actually owe her money if she prevails on her appeal in the Annuity litigation and obtains a favorable result in the BDF litigation. In reply, the Estate

asserts that it is improper for the Debtor to file bankruptcy solely to continue state court litigation.

DISCUSSION

I. 11 U.S.C. § 1112(b) - Bad Faith

Pursuant to 11 U.S.C. § 1112(b), the Court may dismiss a chapter 11 case for cause. While not specifically provided for in the statute's non-exhaustive list, bad faith has long been recognized as cause for dismissal. *C-TC 9th Ave. P'shp. v. Norton Co.* (*In re C-TC 9th Ave. P'shp.)*, 113 F.3d 1304, 1309 (2d Cir. 1997). The Second Circuit articulated a factor driven test in *C-TC* to determine whether a chapter 11 case is filed in bad faith. *Id.* at 1311. Factors indicative of a bad faith include, but are not limited to, whether:

(1) The debtor has only one asset;
(2) The debtor has few unsecured creditors whose claims are small in relation to those of the secured creditors;
(3) The debtor's one asset is the subject of a foreclosure action as a result of arrearages or default on the debt;
(4) The debtor's financial condition is, in essence, a two party dispute between the debtor and secured creditors which can be resolved in the pending state foreclosure action;
(5) The timing of the debtor's filing evidences an intent to delay or frustrate the legitimate efforts of the debtor's secured creditors to enforce their rights;
(6) The debtor has little or no cash flow;
(7) The debtor can't meet current expenses including the payment of personal property and real estate taxes; and
(8) The debtor has no employees.

Id. A court should not apply the *C-TC* factors mechanically or in isolation, and may choose to consider any one or all in its effort of analyzing the totality of the circumstances. *See Pal Family Credit Co. Inc. v. Cty of Albany*, 425 B.R. 1, 5 (N.D.N.Y. 2010); *In re Loco Realty Corp.*, 2009 Bankr. LEXIS 1724 at *8–9 (Bankr. S.D.N.Y. June 25, 2009).

The present case, consisting of an individual debtor and a judgment creditor, does not lend itself to a rigid application of *C-TC*, which involved a partnership and a mortgage creditor.

Under these facts and circumstances, the Court finds it more appropriate to rely on cases involving similar two party disputes to determine whether this case should be dismissed.[4] In this regard, it is well settled law that filing for chapter 11 relief to stay state court litigation is not *per se* bad faith. *See In re Soundview Elite, Ltd.*, 503 B.R. 571, 580–81 (Bankr. S.D.N.Y. 2014); *In re Century/ML Cable Venture*, 294 B.R. 9, 34–37 (Bankr. S.D.N.Y. 2003). When a court determines that a debtor filed for a proper bankruptcy purpose, the court will generally not dismiss those cases, absent other indicia of bad faith, even though the filings may largely be designed to frustrate one creditor's efforts in state court. *See Soundview*, 503 B.R. at 580–81. Within chapter 11, it is proper for a debtor to file a case to either reorganize[5] or to achieve an orderly liquidation and, therefore, a court may be hard pressed to dismiss a case if a debtor pursues either of these purposes. *See Id.* at 581 (refusing to grant a motion to dismiss for bad faith because the Debtor sought to accomplish an orderly liquidation); *Century*, 294 B.R. at 34–37. Therefore, the Court must determine whether the case was filed to reorganize or to achieve an orderly liquidation.

II. The Debtor's Case was Not Filed for a Proper Purpose

[4] The Estate and the Debtor primarily rely on *C-TC* in their submissions. The Court notes that application of the *C-TC* factors, to the extent they are applicable to this case, leads to the conclusion that the case should be dismissed for bad faith:

(1) The Debtor's only undisputed significant asset is her interest in the Property;
(2) The Debtor has few unsecured creditors who are not insiders and those claims are small in relation to the Estate's claim;
(3) The Estate has a judgment lien against the Property which renders it subject to being sold a judicial sale;
(4) The case is in essence a two party dispute between the Debtor and the Estate which can be resolved in the pending state court litigation;
(5) The Debtor timed the filing of her case to attempt to avoid the Estate's judgment lien and prevent the sale of the Property;
(6) The Debtor has negative monthly net cash flow;
(7) The Debtor's DIP bank account has decreased by more than 93% since the filing of her case and she will inevitably be unable to meet her expenses; and
(8) The Debtor has no employees as she conducts no business and has not worked in thirty-five years.

[5] Within the broad category of reorganization, the Court is also referring to the category that some other courts classify as a rehabilitation.

The Court concludes that the Debtor did not file this case for a proper purpose because (1) the Debtor lacks income, (2) the Debtor refused to pursue the state court litigation, and (3) the Debtor has failed to fulfill her fiduciary duties as Debtor-in-possession ("DIP").

A. The Debtor Lacks Income

Whether a Debtor has the ability to fund a plan often determines whether a case is a proper reorganization or a case filed in bad faith.[6] For example, in *In re Texaco Inc.*, 84 B.R. 893 (Bankr. S.D.N.Y. 1988), a case cited by the Debtor at oral argument, the case proceeded as a reorganization despite its overwhelming ties to one creditor, Pennzoil. *See also Century*, 294 B.R. at 34–37. In *Texaco*, Pennzoil obtained a judgment exceeding $11 billion against Texaco in 1985, and after an appellate court largely affirmed the judgment in 1987, Texaco filed for chapter 11 relief later that year. *Texaco*, 84 B.R. at 894. After intense negotiations, Texaco and Pennzoil reached a settlement "wherein Texaco agreed to terminate [the state court litigation] and Pennzoil agreed to accept $ 3 billion in satisfaction of the Texas judgment." *Id.* at 901. Since Texaco had the ability to fund the settlement, the bankruptcy court confirmed Texaco's plan of reorganization despite the case's two-party nature.

However, where a debtor has minimal income, a court may find that such a case was filed as a litigation tactic and not in an effort to reorganize. *See In re Encore Property Management of Western New York, LLC*, 585 B.R. 22, 30 (Bankr. W.D.N.Y. 2018) (dismissing a case for bad faith where the debtor had "no cash flow and no employees" and where it seemed like the debtor's "only 'business' [was] to litigate with [the judgment creditor] . . ."); *In re Artisanal 2015, LLC*, 2017 Bankr. LEXIS 3813, at *40–41 (Bankr. S.D.N.Y. Nov. 3, 2017) (dismissing a

[6] The Court is cognizant that the Supreme Court has ruled that an unemployed individual may be eligible to be a debtor under chapter 11. *Toibb v. Radloff*, 501 U.S. 157, 161 (1991).

case for bad faith where the Debtor had no cash flow and the only purpose of the bankruptcy filing was "a hope to relitigate a state court action").

In the present case, the Debtor has not worked in 35 years and has reported $5.00 or less of income in eight of the sixteen months for which she has filed operating reports. (Debtor's 2004 Tr. 31:25–32:3). In stark contrast, the Debtor's monthly disbursements since May 2017 have ranged between $1,577.00 and $31,601.00. She meets her monthly obligations by using funds within her DIP checking account, which has decreased in value from $129,168.00 at the start of her case to $9,040.46 as of August 17, 2018. According to the Debtor's July 2018 operating report, the Debtor's net cash flow from the commencement of the case through the end of July 2018 is negative $113,070.00. Given the Debtor's reluctance to avoid transfers and sell assets, the Debtor objectively has no hope of funding a plan of reorganization. *See C-TC*, 113 F.3d at 1310 ("When it is clear that, from the date of filing, the debtor has no reasonable probability of emerging from the bankruptcy proceedings and no realistic chance of reorganizing, then the Chapter 11 petition may be frivolous.").

B. The Debtor's filing is designed to stall state court litigation indefinitely

Notwithstanding her negative monthly net cash flow, the Debtor argues she can reorganize. The Debtor's Plan proposes a three tiered approach dependent on varying outcomes in state court. In the first instance, if she wins in all respects, she contends that she may be able to fund the plan in full using only the cash which she has on hand. Second, if all does not go in her favor, she proposes to sell her twelve and a half (12.5%) percent interest in the property. Finally, if she does not succeed in either the Annuity or BDF litigation, the Debtor proposes to commence an adversary proceeding against her husband and her son, as executor for the trust, to recover the entirety of the property for the benefit of the estate.

From the Debtor's Plan it is clear that the Debtor believes the success of her bankruptcy case depends largely, if not entirely, on changing the landscape in state court. However, her actions after the commencement of her bankruptcy case show a concerted effort to avoid the litigation altogether. On February 3, 2017, the Appellate Division, Second Department denied the Debtor's motion for a stay pending appeal in the Annuity litigation. (ECF No. 58; Ex. E.) Once the Debtor filed her bankruptcy case, the Second Department indicated that her bankruptcy filing stayed the appeal and that she would need to obtain an order lifting the stay for her to perfect her appeal.[8] Even though the Debtor's case has been pending since April 4, 2017, the Debtor has not filed a motion seeking that relief.[9] By filing bankruptcy and not pursuing an order lifting the automatic stay, the Debtor not only used the Bankruptcy Code as a shield and substitute for a state court stay pending appeal, but also as a sword in the Annuity litigation since this approach allows her to keep the Annuity litigation in state court purgatory without resolution or consequence.

The same can be said for the BDF litigation which, despite the Debtor's position that it is her most valuable asset and is central to her bankruptcy case, similarly remains stayed. On one hand, the Debtor attempts to defeat the Estate's motion by relying on this alleged asset while, on the other hand, she chooses not to pursue the action. The Debtor's conduct as it relates to both

[8] As a general matter, the Court notes that the automatic stay created by the filing of a bankruptcy case would ordinarily not apply to the debtor's prosecution of an appeal as an appellant.

[9] Facing dismissal on March 28, 2018, Debtor's counsel orally requested permission for the Debtor to file a motion to lift stay in order to prosecute the state court litigation. At the time that Debtor's counsel made this request, the case was just one week short of being a year old. The Court indicated that the Debtor may file the motion but that the filing of such a motion might wait until the adjourned hearing date on the dismissal motion. To accommodate further briefing by the parties, the Court adjourned the matter to May 2, 2018 as opposed to April 11, 2018, as was originally indicated on the record. Further, the Debtor also waited to make this request for approximately eight months from the filing her Disclosure Statement on July 27, 2017. It is clear that on that date, the Debtor understood the importance of her pursuit of the state court litigation as the Disclosure Statement provides, "The Debtor believes that her appeal can be decided within the next year (she will need to lift the automatic stay in the Bankruptcy Court to allow the appeal to go forward and she will do so)." (Am. Disc. Statement 8.)

the Annuity and BDF litigation undermines her arguments that her case should not be dismissed and cements that this case is a two party dispute that belongs in state court. *See In re Purpura*, 170 B.R. 202, 207 (Bankr. E.D.N.Y. 1994) (dismissing for bad faith where "the filing for relief represented a litigation tactic to stall and impede the enforcement of legal rights against the debtor . . ."); *In re Wally Findlay Galleries, Inc.*, 36 B.R. 849, 851 (Bankr. S.D.N.Y. 1984) ("The debtor filed its petition herein to avoid the consequences of adverse state court decisions while it continues litigation. This court should not, and will not, act as a substitute for a supersedeas bond of state court proceedings.").

C. Violation of Fiduciary Duties

Additionally, the Court cannot otherwise conclude that the Debtor filed this case for a proper purpose because such a holding would also condone the Debtor's dereliction of her fiduciary duties to creditors and the estate as DIP. As it relates to creditors, "[t]he job of a [DIP] remains under the Code as that described by Judge Friendly – to get the creditors paid." *In re Pied Piper Casuals, Inc.*, 40 B.R. 723, 727 (Bankr. S.D.N.Y. 1984) (quoting *Grayson-Robinson Stores, Inc. v. Sec. & Exch. Comm'n*, 320 F.2d 940 (2d Cir. 1963)); *see also In re Ionosphere Clubs, Inc.*, 113 B.R. 164, 169 (Bankr. S.D.N.Y. 1990). While a chapter 11 DIP is not under a statutory duty to liquidate assets, the DIP must maximize the value of the estate for creditors. *See In re Breitburn Energy Partners LP*, 582 B.R. 321, 355 (Bankr. S.D.N.Y. 2018); *In re Ancona*, 2016 Bankr. LEXIS 4114, at *32–33 (Bankr. S.D.N.Y. Nov. 30, 2016); *see also In re Reliant Energy Channelview LP*, 594 F.3d 200, 210 (3rd Cir. 2010).

This duty requires, among other things, the DIP to pursue avoidance actions and "to sell when the [DIP] is worth more dead than alive." *Breitburn Energy*, 582 B.R. at 355; *see also Wolf v. Weinstein*, 372 U.S. 633, 649–51 (1963); *In re Casco Fashions, Inc.*, 490 F.2d 1197,

1201 (2d Cir. 1973); *Ionosphere Clubs, Inc.*, 113 B.R. at 169. Given the Debtor's lack of income, the Debtor can only pay creditors by selling property and avoiding transfers – this is the Debtor's nonnegotiable fiduciary duty in chapter 11. *See Commodore Int'l v. Gould (In re Commodore Int'l Ltd.)*, 262 F.3d 96, 99 (2d Cir. 2001) (holding that "[t]he [debtor in possession] has an obligation to pursue all actions that are in the best interests of creditors and the estate.").

Failure to exercise these duties may be grounds for dismissal or conversion under 11 U.S.C. § 1112(b), or appointment of a trustee pursuant to 11 U.S.C. § 1104. *See Canadian Pac. Forest Prods. v. J.D. Irving, Ltd. (In re Gibson Grp.)*, 66 F.3d 1436, 1442 (6th Cir. 1995); *United Phosphorus, Ltd. v. Fox (In re Fox)*, 305 B.R. 912, 915–16 (B.A.P. 10th Cir. 2004); *Ancona*, 2016 Bankr. LEXIS 4114, at *32–33 ("If a debtor-in-possession defaults in its responsibilities, the debtor may be dispossessed of control of its business and a chapter 11 trustee should be appointed."); *In re AdBrite Corp.*, 290 B.R. 209, 217 (Bankr. S.D.N.Y. 2003) (holding that "[a] debtor-in-possession's dereliction of its fiduciary duty to creditors" is a ground for dismissal or conversion pursuant to § 1112(b)).

As more fully set forth above, it is clear that the Debtor only intends on exercising her fiduciary duties once she exhausts all of her rights in the Annuity and BDF litigation. Since the Debtor has minimal income, the only way for the Debtor to maximize the estate's value is to avoid preferences, recover transfers, and to sell, or otherwise extract value from, her assets. Under the facts of this case, refusing to recover the Property until state court litigation concludes is a violation of her fiduciary duty as the obligation to pay creditors cannot wait until a time that suits the Debtor. The litigation history between the parties makes clear that the Debtor's proposal would result in significant delay since it took seventeen years for the annuity litigation

to be reduced to a judgment, which is now on appeal, and the BDF litigation has been pending since 2005 without a judgment, which too will surely be appealed whenever it is entered.

In summary, this filing was designed to further delay agonizing family litigation stretching nearly twenty years. The Debtor has negative monthly income and has not made any effort to proceed with the Annuity litigation appeal or the BDF litigation despite conceding that success in state court is vital to her bankruptcy case. The Debtor does not cite to a single case which would support her ability to stay in chapter 11 while proceeding in this manner. For all of these reasons, the Court concludes that the Debtor did not file this case for the proper purpose of reorganizing but rather for the improper purpose of relitigating and continuing to litigate. *See Encore*, 585 B.R. at 30; *Artisanal*, 2017 Bankr. LEXIS 3813, at *40–41; *Purpura*, 170 B.R. at 207; *Wally Findlay Galleries*, 36 B.R. at 851. If the Court were to find that this case was filed for a proper purpose, it would legitimize a "wait and see" approach that permits the Debtor to use the bankruptcy process as a litigation tactic and prejudicially delay creditors, all under the guise of reorganization.

CONCLUSION

For all of the foregoing reasons, the Estate's Motion is granted and the Debtor's case is DISMISSED.

It is SO ORDERED.

Dated: August 31, 2018
Albany, New York

/s/ Robert E. Littlefield, Jr.
Robert E. Littlefield, Jr.
United States Bankruptcy Judge