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3 UNITED STATES BANKRUPTCY COURT
4 EASTERN DISTRICT OF CALIFORNIA
5 SACRAMENTO DIVISION
6
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8 In re)
9 JOSEPH SPRANZA,) Case No. 04-25484-A-7
10) Docket Control No. MFB-2
11 Debtor.) Date: April 25, 2005
12) Time: 9:00 a.m.
13)

14 *On April 25, 2005 at 9:00 a.m. the court considered the*
15 *motion of the chapter 7 trustee for approval of a sale as well as*
16 *a compromise between the estate and creditor Fred Bosley. The*
17 *text of the final ruling appended to minutes of the hearing*
18 *follows. This final ruling constitutes a "reasoned explanation"*
19 *for the court's decision and accordingly is posted to the court's*
20 *Internet site, www.caeb.uscourts.gov, in a text-searchable format*
21 *as required by the E-Government Act of 2002. The official record*
22 *of this ruling remains the minutes of the hearing.*

23 **FINAL RULING**

24 The debtor's request for a continuance will be denied.

25 The motion to sell property and to enter into a compromise
26 will be granted.

27 The subject property is held in a trust. There is nothing
28 in the schedules to indicate who was the settlor of the trust
that holds title to the property, who is the beneficiary, and
whether the trust is revocable.

If the debtor was the settlor and the trust is revocable,
the creditors of the debtor are permitted by state law to reach
into the trust. California Probate Code § 18200 provides: "If

1 the settlor retains the power to revoke the trust in whole or in
2 part, the trust property is subject to the claims of creditors of
3 the settlor to the extent of the power of revocation during the
4 lifetime of the settlor."

5 The court was initially concerned that the absence of
6 evidence regarding the debtor's interest in the trust prevented
7 it from determining that the bankruptcy estate had an interest in
8 the subject property. Without determining the estate's interest
9 in the subject property, the court may not approve any sale. A
10 bankruptcy court may not allow the sale of property as "property
11 of the estate" without first determining whether the debtor in
12 fact owned the property. See Moldo v. Clark (In re Clark), 266
13 B.R. 163, 172 (B.A.P. 9th Cir. 2001) (holding that "[t]he
14 threshold question, is [the property] still property of the
15 estate, must . . . be decided" before it can be sold free and
16 clear under § 363(f)); Anderson v. Conine (In re Robertson), 203
17 F.3d 855, 863 (5th Cir. 2000) ("Because the separate property
18 home of [a nondebtor] was not included or owned in indivision
19 with the property of the Debtor's bankruptcy estate, the Trustee
20 lacked authority to sell her home . . . as property of the estate
21 in which there is an interest of 'an entity other than the
22 estate' under section 363(f). . . ."); In re Coburn, 250 B.R.
23 401, 403 (Bankr. M.D. Fla. 1999) (finding it necessary to
24 determine whether an asset is property of the estate in order to
25 decide whether the trustee is entitled to sell the asset pursuant
26 to § 363(f)).

27 However, at the hearing, counsel for the debtor admitted
28 that the trust is revocable and that the debtor is its settlor.

1 Further, prior to the contribution of the land into the trust, it
2 was the community property of the debtor and his spouse. This
3 means that outside of the bankruptcy court, the debtor's
4 creditors could reach into the trust to satisfy their claims
5 against the debtor. The bankruptcy trustee may do the same. See
6 In re Barnes, 275 B.R. 889 (Bankr. E.D. Cal. 2002). And, to the
7 extent the debtor's interest in the property in that trust may be
8 community property, both his and his spouse's interest in that
9 community property is property of the bankruptcy estate. See 11
10 U.S.C. § 541(a)(2).

11 Therefore, the trustee may sell the real property.

12 The property was scheduled as having a value of \$770,000.
13 While the debtor now claims it is worth more, no admissible and
14 convincing evidence of an increased value has been offered to the
15 court. Further, no one appeared at the hearing who was willing
16 to make a higher bid for the property.

17 The property is not in ideal condition. The trustee reports
18 that it is in need of much deferred maintenance. The real
19 property taxes are not current. The improvements are not
20 insured. The mortgage is not being paid.

21 The buyer, Fred Bosley, offers to buy the subject property
22 for its scheduled value, \$770,000. He will pay sufficient cash
23 to retire all liens and security interests senior to his
24 abstracts of judgment as well as his share of the costs of sale
25 and the 5% discussed below. This portion of the offer will total
26 approximately \$225,000 in cash.

27 Mr. Bosley's claim is based on a district court money
28 judgment now totaling approximately \$750,000. The balance of the

1 purchase price will be a "credit bid" based on his judgment and
2 judgment lien. That is, his judgment, protected by a lien
3 against the subject property, will be reduced by an amount equal
4 to \$770,000 less the cash paid on account of senior liens and
5 security interests.

6 Mr. Bosley will pay five percent of the sale price to the
7 bankruptcy estate. That is, rather than credit bid the five
8 percent, it will be paid in cash to the estate but it will
9 nonetheless reduce the balance of his judgment. This amount
10 represents the consideration paid by Mr. Bosley for the
11 compromise with the estate. The estate will not challenge his
12 judgment on appeal and the estate will receive the 5% amount.
13 This compromise, however, does not affect the right of the debtor
14 to pursue an appeal to protect himself (in the event the judgment
15 is later determined to be nondischargeable) or his exempt
16 property, if any.

17 The court will not, however, approve a sale that is free and
18 clear of any unexpired leases between the debtor, his
19 predecessor(s), and/or the trust as lessor, and SDI or any other
20 party as lessee.

21 While there may or may not be grounds to terminate that
22 lease under applicable nonbankruptcy law, the bankruptcy estate
23 is limited to its remedies under 11 U.S.C. § 365. The court
24 acknowledges that there is some support in the case law for the
25 proposition that a bankruptcy trustee may sell free and clear of
26 a lessee's leasehold interest pursuant to section 363(f). See
27 Precision Indus., Inc. v. Qualitech Steel SBQ, LLC (In re
28 Qualitech Steel Corp.), 327 F.3d 537 (3rd Cir. 2003). However,

1 section 365(h) (1) grants a lessee a right to remain in possession
2 of real property after rejection of a lease by a lessor's
3 landlord. This more specific tenant protection governs the more
4 general authority to sell free and clear under section 363(f).
5 See, e.g., In re Taylor, 198 B.R. 142, 165 (Bankr. D.S.C. 1996).

6 On a motion by the trustee and after notice and a hearing,
7 the court may approve a compromise. Fed. R. Bankr. P. 9019.
8 Approval of a compromise must be based upon considerations of
9 fairness and equity. In re A & C Properties, 784 F.2d 1377, 1381
10 (9th Cir. 1986). The court must consider and balance four
11 factors: 1) the probability of success in the litigation; 2) the
12 difficulties, if any, to be encountered in the matter of
13 collection; 3) the complexity of the litigation involved; and 4)
14 the paramount interest of the creditors with a proper deference
15 to their reasonable views. In re Woodson, 839 F.2d 610, 620 (9th
16 Cir. 1988).

17 The first problem for the estate in continuing litigation
18 with Mr. Bosley is its lack of money to pay counsel. The second
19 is the fact that the debtor lost the case in the district court.
20 His only hope is a reversal on appeal. The court evaluates the
21 prospects of reversal as remote. This conclusion is based
22 principally on a review of Judge Damrell's January 9, 2004
23 memorandum and order. He noted that there was "overwhelming"
24 evidence beyond the preponderance standard justifying relief
25 under the Securities Act of 1933. He then went on to award
26 attorney's fees. To do so required that Judge Damrell conclude
27 that the debtor's defense to the suit was "without merit." He
28 characterized that defense as "bordering on the frivolous." He

1 also noted that the debtor ignored the "obvious evidence" against
2 him and his attempts to settle the suit unnecessarily protracted
3 the litigation. As a result, Judge Damrell awarded over \$200,000
4 in attorney's fees to Mr. Bosley.

5 This court is charged with determining the probability of
6 success on the merits. The fact that the district court has held
7 against the debtor after a trial on the merits and concluded that
8 his defense was without merit, is an excellent barometer of the
9 merits of the debtor's defense to Mr. Bosley's claim. The appeal
10 is likely to go nowhere.

11 The litigation, at least what is left of it, if not settled,
12 will require the trustee to retain a special counsel well-versed
13 in securities law. This is a burden the estate cannot afford.

14 While the debtor may offer to take the laboring oar in the
15 appeal, given Judge Damrell's conclusions about his conduct
16 before and during the trial, the trustee is no position to cede
17 his fiduciary responsibilities to the debtor and his
18 professionals.

19 In this regard, the court notes that in a prior case, Case
20 No. 01-30805, the debtor's son filed a chapter 13 petition with
21 the goal of protecting the subject property from foreclosure.
22 The court concluded that the prior case had been filed and
23 prosecuted by the son for Joseph Spranza's benefit. The fact
24 that the subject property is now an asset of Joseph Spranza
25 indicates to the court that it was correct in its prior
26 conclusion.

27 This prior case, and the debtor's complicity in its abuse,
28 reinforces the court's conclusion that the trustee cannot rely

1 upon the debtor to protect the estate's interest in the appeal.

2 Therefore, the court concludes that the compromise is fair
3 and equitable and in the best interests of the creditors and the
4 estate. The motion, insofar as it seeks authority to enter into
5 a compromise, will be granted.