In the United States Bankruptcy Court

for the Northern District of Iowa

Western Division

FORT DODGE CREAMERY COMPANY
Debtor.
Debtor(s).

Bankruptcy No. X88-01550F

Chapter 7

Contested No. 2143

DECISION RE: MOTION TO COMPROMISE

Three matters are before the court for consideration: the trustee's proposed settlement of various adversary proceedings and claims; a motion to sell property of the estate, the granting of which is contingent upon approval of the settlement; and application by the attorney for the trustee seeking fees in excess of those provided by the settlement.

Katharine Doan (DOAN) and Gertrude Ambrose (AMBROSE), minority shareholders of the corporate debtor, object to the motion to compromise. Hearing was held on November 16, 1990 in Fort Dodge, Iowa. These are core proceedings under 28 U.S.C. § § 157(b) (2) (A), (B), (F), (H), (N), and (O).

The evidence presented to the court on the appropriateness of the proposed settlement consisted of the testimony of case trustee James H. Cossitt (TRUSTEE), his affidavit, summaries of information and opinion, written analysis of the potential outcome of the litigation versus the results of settlement, a stipulation of facts entered into between the trustee and the attorney for Ambrose and Doan, and the dictated and transcribed notes of attorney Maurice Stark (STARK).

Most of the evidence was directed to the likely outcome of pending litigation. The likelihood that the trustee will be successful in these proceedings is one of the court's considerations in determining whether to approve the proposed settlements. The settlement agreement resolves the trustee's disputes with various entities, including Allen R. Loomis, the estate of A. Robert (Bob) Loomis, Stark, the accounting firm of McGladrey, Hendrickson and Pullen (McGLADREY); the Internal Revenue Service (IRS); the Iowa Department of Revenue (IDOR); Plains National Bank, trustee of the Allen R. Loomis Grantor Trust; Rosedale Farms, Inc. (RFI); and First American State Bank (FASB). Counsel for most of these entities took part in the nearly two-day hearing on the proposed agreement. Many were obviously disturbed about the introduction of Stark's transcribed notes. Stark had maintained notes while in the employ of Fort Dodge Creamery Company (FDCC). The concerns may well have related to the binding effect of any of the court's resultant findings if the settlement is not approved.

The court views the dispute over settlement as a contested matter created by the objection filed by Doan and Ambrose. The dispute is fundamentally between the trustee and those shareholders. The evidence submitted was in support of their positions. The participation of other creditors and parties-ininterest helped to facilitate the court's inquiry. As creditors, they have the right to make their positions on the settlement known to the court. As to the Stark notes, the court has considered them in reaching its determination. It is understood that many of the parties disagree with statements of fact or opinion contained in Stark's notes. They take the position that there is another side to the story. Although this may be, it was Stark's version of what happened through his notes that has, in this proceeding, aided the court in considering the timing and purpose of certain events.

I.

An involuntary petition under chapter 7 of the Bankruptcy Code was filed against Fort Dodge Creamery Company on October 11, 1988. An order for relief under chapter 7 was issued February 8, 1989. James H. Cossitt was appointed trustee. The deadline for filing proofs of claim or proofs of interest was July 10, 1989.

The following entities filed proofs:

Central States Southeast and Southwest Area Health and Welfare and Pension Funds (CENTRAL STATES)	$248,248.61	UNSECURED
CENTRAL STATES	168,798.72	SECURED
CENTRAL STATES	241,892.67	SECURED
Iowa-Illinois Gas and Electric Company	1,546.25	UNSECURED
M. Gene Blackburn, P.C.	66.13	UNSECURED
Job Service of Iowa	167.89	priority UNSECURED
Jean Purkapile	3,175.03	priority UNSECURED

The following claims were filed after the claims deadline:

Maurice Stark		"unascertainable"
Rosedale Farms, Inc. (RFI)	300,000.00	priority UNSECURED
Amoco Oil Company	70.97	UNSECURED
Internal Revenue Service (IRS)	492,108.00	priority

		UNSECURED
Iowa Dept. of Revenue and Finance (IDOR)	52,135.28	priority UNSECURED

Stark's claim seeks indemnity or contribution from the estate of FDCC in the event Doan or Ambrose recovers against him in the suit pending in Webster County district court. RFI seeks indemnity from FDCC in the event Central States and others recover against it in a civil action pending in federal court in Illinois.

II.

FDCC, incorporated in Iowa in 1906, was a manufacturer of ice cream products in Fort Dodge. Some of its employees were represented by a labor union. The union and FDCC were parties to a collective bargaining agreement which required company contributions to certain pension and health and welfare funds administered by Central States. In September 1984, Central States obtained a favorable decision in a federal court action brought by Central States against FDCC for unpaid contributions to the pension and health and welfare funds. It was expected by FDCC that judgment would enter on the decision and that the judgment would be substantial.

To mitigate the judgment's damage to the company, the late Bob Loomis, an officer, director and shareholder of FDCC, began discussing with FDCC professional advisors potential protective measures. Such discussions began as early as February 4, 1985, perhaps earlier. One alternative was a corporate reorganization. Rosedale Farms, Inc. had already been incorporated in January, 1985. Through the reorganization alternative, shareholders of FDCC would exchange their stock for stock in RFI. RFI would become FDCC's parent corporation. FDCC would transfer to RFI approximately 493 acres of Iowa farmland known as Rosedale Farms. RFI would grant a mortgage on the farmland to FDCC's primary lender--First American State Bank. FASB would obtain also a security interest in the machinery, equipment and accounts of FDCC and a mortgage on the real estate where the creamery factory was located.

FASB had previously requested such liens on the farmland and other property of FDCC. Such liens were discussed when FDCC had requested an increase in its line of credit with the bank.

The reorganization, the transfer and encumbrance of the farmland, the mortgage on the factory, and the encumbrance of personalty would hopefully act as a shield against the Central States judgment. But they may also have had other purposes. The bank had wanted the security interests as the FDCC primary lender. Also, the Agricultural Stabilization and Conservation Service (ASCS) had refused the farmland's enrollment in government programs because of ownership of the land in FDCC. It was thought that if the land were owned by another entity, it could be covered by the programs.

In pursuing the reorganization and other alternatives, Bob Loomis sought the aid of Fort Dodge attorney Maurice Stark, a well regarded Fort Dodge practitioner who practiced tax law. Their first such contact regarding the reorganization was February 4, 1985. Also involved in the discussion was Fort Dodge attorney Herb Bennett. Bennett may have provided legal services in incorporating RFI; he also represented FASB. Tax and accounting advice was furnished to FDCC by the accounting firm of McGladrey, Hendrickson and Pullen. Involved on behalf of that firm was an accountant named Dennis Craven.

A major concern related to the reorganization was the tax consequences of it. It was believed by Stark and perhaps also Craven that to avoid treatment of the land transfer as a taxable event, at least 80 per cent of the FDCC stockholders would have to approve the reorganization plan.

"On February ll, 1985 there was a meeting at First American State Bank between Messrs. A1 Loomis, Bob Loomis, [Herb] Bennett, [Maurice] Stark, and Gene Richardson [of FASB] wherein the reorganization of FDCC and the transfer and encumbrance of the farm were discussed."(1) Richardson was an officer of the bank.

"Minutes of a 'Special Meeting of the Board of Directors of the Fort Dodge Creamery Company' date 2/1/85 indicate that Allen R. Loomis and A. Robert Loomis, acting as the Board of Directors, approved the reorganization plan."(2)

Almost immediately, aspects of a reorganization were put into effect. On February 11, 1985, FDCC conveyed the farmground to RFI by warranty deed. RFI paid no money for the land. On the same date, presumably prior to the conveyance, FDCC granted FASB a mortgage on the creamery factory and the farmground. Also on February 11, FASB received a security interest in personal property of FDCC including but not limited to: inventory, accounts receivable, machinery, equipment and fixtures. The bank's interest was perfected by the filing of financing statements with the Iowa Secretary of State and the Webster County Recorder. The filings took place February 14, 1985.

"On February 11, 1985 FDCC was indebted to FASB in the principal amount of $775,000.00; on that same date, five new notes were executed by FDCC. . . ."(3) These notes replaced old notes and provided new maturity dates. A sixth note, for accrued interest through February 11, was also signed for the bank. The total indebtedness of FDCC to FASB on the newly executed notes was $801,112.59.

"All of the February 11, 1985 notes are secured by (a) the security interest granted on the same date (b) the mortgage on the Creamery building . . . and (c) the mortgage on the farm. . . ."(4)

It was hoped that the plan would be approved at an annual shareholders meeting scheduled for February 13, 1985. It was not. Although Bob and Allen R. Loomis, Bob's father, owned more than 50 per cent of the FDCC stock, there was difficulty in obtaining the assent of other shareholders sufficient to reach the 80 per cent goal.

Two shareholders who were resisting the reorganization were Katharine Doan and Gertrude Ambrose. They each owned 12.5 per cent of the outstanding capital stock of FDCC. Each was also a director and officer of the corporation. Doan had two main concerns: that the reorganization could make her liable to Central States for punitive damages for attempting to put corporate assets out of the creditor's reach, and that she would be personally liable to the IRS for any taxes arising out of the reorganization· She may have also been concerned about the loss of the farm to FASB. Ambrose also had concerns about personal liability.

A special shareholders meeting was held on March 18, 1985. The plan was discussed, along with the need for 80 per cent shareholder approval if tax problems were to be avoided. Attending were Frank and Gertrude Ambrose; Katharine Doan; Doan's attorney Terry Guinan; Fred Breen; Diane Burch; attorney Herb Bennett; Bob Loomis; A. Robert Loomis; Dennis Craven and Stark. The meeting broke up without 80 per cent approval of the plan.

Although aspects of the plan had been put into effect without such approval, it was apparently the thought of FDCC advisors that FDCC could back out of the plan without adverse tax consequences if

the 80 per cent were not obtained prior to the beginning of the corporation's next fiscal year, beginning January 31, 1986.

The proponents of the plan sought solutions. These included purchase of stock from Doan and Ambrose--all of their shares or a number of shares sufficient to give proponents of the plan the 80 per cent of shares they sought. A purchase effort did not succeed. Another alternative was to have the corporation issue additional shares of stock to the Loomises as employment compensation. This was pursued although it carried its own problems. It was discussed as a short term solution, meaning that after the reorganization had provided immediate protection from Central States, other shareholders would sometime later be put back in a status quo position regarding their ownership percentage.

"Sometime between January and May 1985, the debtor issued Allen R. Loomis and A. Robert Loomis 125 shares of capital stock of FDCC. The shares were issued without the approval of the Board of Directors and without consideration. The shares were issued in an attempt to retroactively comply with certain provisions of the Internal Revenue Code."[(5)]

The reorganization was approved by 80 per cent of the shareholders sometime in November, 1985. The vote of approval included the Loomises voting their additional shares of stock. Doan and Ambrose never voted in favor of the reorganization. Fred Breen may have. The approval was apparently considered by the corporation to be retroactive to February, 1985.

On April 15, 1985, the federal court judgments entered against FDCC in favor of Central States. They were in the amounts of $210,453.16 and $147,296,82, plus costs and interest on each judgment. FDCC and Central States later reached a settlement of their disputes. On January 1, 1986, FDCC and RFI executed a promissory note to Central States and secured it with a mortgage on the farm and the creamery site and a security interest in FDCC personalty.

The trustee and objectors believe that the evidence will show that FDCC was insolvent after the encumbrance and transfer of farmland on February 11, 1985.

"The average dollar value per acre of farmland in Webster County, Iowa on November 1, 1984 was $1,856.00/acre .... The average dollar value per acre of farmland in Webster County, Iowa on November 1, 1985 was $1,240.00/acre .... The average dollar value per acre of farmland in Webster County, Iowa November 1, 1984 and November 1, 1985 was $1,548.00 ...."[(6)]

> Rosedale Farms, Inc. presently owns the following assets:[(7)]
> (a) the Rosedale Farms:
> (b) checking account #01-7457-2 at FASB ($1,750.00);
> (c) High Yield account #60007565314 at FASB ($127,657.28);
> (d) Shearson Lehman Hutton account #461-15848-16-032 ($78,737.13);
> (e) a grain inventory (estimated value $64,267.49).

The accounts and grain inventory are rents and profits of the farm.[(8)] The crops and deposits total $272,411.90 in value. RFI has incurred unpaid farm expenses in the amount of $11,500.00 from the operation of farmland.

The Central States' judgments were not the only setbacks experienced by FDCC. In the early 1980s, a farm manager embezzled substantial sums from the corporation. These were not recovered. Also, "[o] n August 22, 1986 the FDCC began voluntary product recalls of ice cream products in response to concerns about possible listeria contamination; the plant discontinued production of those products on

August 26, 1986."[(9)] Not only were there product recalls, but the listeria problem resulted in a shutdown of the plant and a loss of customers.

The creamery factory building and grounds and the machinery, equipment and fixtures therein have been abandoned by the trustee. The assets are encumbered by security interests of Central States and FASB. There was no evidence introduced as to the value of these assets.

There was no evidence to aid the court in determining the tax consequences of the sale of the farm by the estate in the event of its recovery by the trustee in the absence of settlement. There was no evidence as to the value of government program payments after the transfer of the farm to RFI. The trustee believes that all income from the farm after the transfer to RFI was used in the operation of FDCC except that income now being held by RFI.

Although the trustee and objectors may agree that the transfer and encumbrance of the farm resulted in the insolvency of FDCC, there was no evidence as to the part the reorganization played, if any, in the failure of the company.

Court costs in this case at the time of hearing were approximately $756.00. The trustee, in applications filed with the court, claims that thus far he has incurred legal fees and expenses of $60,077.47 and trustee expenses of $985.71.

As of July 25, 1990, the secured claim of FASB amounts to $354,596.00 including interest but not legal fees.

The farm transferred to RFI has a present fair market value of $1,800.00 per acre for a total value of $887,400.00. Accrued real estate taxes and drainage assessments total $17,395.00. There is no evidence as to which tax years are included. A reasonable broker's commission for the sale of the farm at the foregoing value would be five per cent, for a commission of $44,370.00.

"On August 27-28, 1986 the FDCC repaid four notes in full to Bob Loomis for a total of $62,777.46; on the same dates, FDCC repaid in fuli a note to ARL Farms, Inc. for $42,739.09 and another note to McManus, Ltd. for $32,563.11."[(10)]

Under the settlement, the estate's rights in adversary proceeding numbers X89-0158F, X89-0205F, X89-0213F, and X89-0154F (the derivative action which was remanded to state court) would be assigned to Plains National Bank, as trustee of the Allen R. Loomis Trust. The trust would dismiss these actions. Exhibit 17.

III.

THE LITIGATION

A.

Adversary Proceeding No. X89-0158F

The trustee has brought this proceeding against Allen R. Loomis; Norwest Bank, Des Moines, N.A. as executor of the estate of A. Robert Loomis; Rosedale Farms, Inc.; First American State Bank; Maurice Stark; the Internal Revenue Service and the Iowa Department of Revenue. Trustee seeks a return of the farmland to the estate and a return of profits derived from the land since its transfer. He

also seeks to avoid the mortgage of FASB and to obtain disallowance of the claims of FASB, RFI, Stark and Allen R. Loomis. If not disallowed, he asks that the claims be subordinated to a position below that provided in 11 U.S.C. §726(a) (5) (claims for post-petition interest). Finally he asks for a determination of the federal and state tax liabilities of the estate arising from the 1985 corporation reorganization of FDCC.

B.

Adversary Proceeding No. X89-0205F

This is a preference action under state and federal law. The trustee seeks the return of $601,611.07 in payments to alleged insiders during the one-year period prior to the filing of the involuntary petition and during the gap period after the petition but before the order for relief. Defendants are the Plains National Bank as trustee of the Allen R. Loomis trust, Norwest Bank as executor of the estate of A. Robert Loomis, Allen R. Loomis, McManus, Ltd., ARL Farms, Inc., Katharine Doan and Gertrude Ambrose.

C.

The Derivative Action--Webster County No. C184-0488

This shareholders' derivative action was commenced in state court by Doan and Ambrose prior to the filing of the involuntary petition. Defendants at present are Allen R. Loomis, A. Robert Loomis, Maurice Stark and the accounting firm of McGladrey, Hendrickson and Pullen. The case trustee has been substituted as the real party-in-interest. The trustee seeks recovery from the defendants for any tax liability arising from FDCC's corporate reorganization. He also prays for exemplary damages. According to the trustee, he has sought to amend the petition to add other defendants.

D.

Adversary Proceeding No. X89-0213F

This adversary proceeding, brought by the trustee against FASB has been decided. FASB must return to the estate a postpetition payment of $17,791.66. The court's judgment does not prevent FASB from later establishing secured status in the funds which it received and must return.

E.

Miscellaneous Contested Matters

The trustee has sought disqualification of counsel for FASB and counsel for Robert R. Loomis and Norwest Bank as executor for the estate of A. Robert Loomis. FASB seeks disqualification of James Cossitt as trustee and as counsel for trustee. FASB objects to Cossitt's attorney fee applications. Also, there is pending an application by the trustee that sanctions be imposed against FASB and its counsel. The merits of these matters were not at issue during the hearing on compromise. These contested matters, however, would be dismissed if the settlement were approved.

IV.

The Settlement

The trustee has reached settlement with various adversaries and other entities. Approval would result in the administration and sale of certain assets, the distribution of sales proceeds and other assets in accordance with the agreement, and a dismissal of the bankruptcy.

The parties have agreed that judgment would enter in adversary X89-0158F resulting in a return of the farmland to the estate and in a return of all profits from the farm presently being held by RFI. These include the Shearson account, the high yield account, the checking account and the 1990 crops. The real estate and crops would be liquidated at the direction of FASB. The cash proceeds, cash accounts and funds presently in the custody of the trustee would then be distributed by the trustee in satisfaction of claims in the manner provided in the agreement.

The agreement on such payments is set out at this point verbatim:

PAYMENT OF CLAIMS

1. All unsecured creditors of the FDCC estate other than Central States, the United States, the IDOR, and the Plains National Bank (which creditors and their claims are listed on Exhibit A hereto) shall be paid in full (without interest);[(11)]

2. Central States shall be paid $470,000 on its claim for contributions; Central States' withdrawal liability claim (presently estimated at $333,000) shall be paid at $75,000; remaining payments (if any) are governed by paragraph 9 (sic).[(12)]

3. First American shall initially be paid $300,000 on its claim, subject to the provisionsof paragraphs 10 and 11, below.

4. The parties to this Agreement recommend that the Court allow James Cossitt $46,000 in full satisfaction of his administrative claims for trustee fees and expenses, attorney for trustee fees and expenses and any fees or expenses incurred by Mr. Eide on behalf of the trustee. As part of this recommendation, Mr. Cossitt agrees to provide the following additional services:

(a) preparation and noticing of one Motion for Approval of the Settlement Agreement and one Application to Sell Real Estate Free and Clear of Liens;
(b) attendance for one day at any hearing on the Motion for Approval of the Settlement Agreement;
(c) preparation of the reports required by the U.S. Trustee to close the case.

In the event the parties to this Agreement desire Mr. Cossitt to perform any additional services in obtaining approval for the Agreement or its' (sic) implementation, beyond those specifically described, any additional services shall be paid, in an amount determined by the Court, from the settlement proceeds, after normal application, notice and hearing on any such application.

5. The United States has asserted claims arising out of the 1985 corporate reorganization and/or arising out of the sale of the assets of RFI and/or FDCC contemplated by this agreement (including but not limited to the real estate and crops). FDCC denies any and all liability for tax, interest or penalty arising out of the 1985 corporate reorganization, but in order to avoid the burden and expense of further litigation and without admitting any liability or such tax, interest or penalty, however, the following agreement has been

reached: The United States shall be paid $220,000.00 and the United States agrees to accept the amount in full satisfaction of the claims described, including any tax, interest, or penalty arising out of the 1985 corporate reorganization and/or the sale of the assets of RFI and/or FDCC contemplated by the Agreement (including but not limited to the real estate and crops). The United States shall not be paid less that (sic) $220,000.00, and none of the $220,000.00 is subject to refund.

6. The IDOR has asserted claims arising out of the 1985 corporate reorganization and/or arising out of the sale of the assets of RFI and/or FDCC contemplated by this agreement (including but not limited to the real estate and crops). The FDCC denies any and all liability for tax, interest and penalty arising out of the 1985 corporate reorganization, but in order to avoid the burden and expense of further litigation the following agreement has been reached: the IDOR shall be paid $20,000.00 and the IDOR agrees to accept this amount in full satisfaction of the claims described, including any tax, interest or penalty arising out of the 1985 corporate reorganization and/or the sale of the assets of RFI and/or FDCC contemplated by this Agreement (including but not limited to the real estate and crops).

7. The accountant for the Trustee shall be paid any additional fees for work necessary to close the estate which the Court approves after normal application, notice, and hearing on any such application.

8. The Trustee's Court costs (not more than $1,000) shall be paid.

9. The Trustee shall file a notice of dismissal and execute mutual releases as to defendants Stark and McGladrey in Adversary Claim number X-89-0154F, the claims against these defendants being of no significant value to the estate. Adversary Claim Numbers, X-89-0158F, X-89-0205F, and X-89-0213F and the remainder of claim number X-89-0154F shall be assigned to the Plains National Bank in satisfaction of its claim against the estate.

10. To the extent that liquidation of the assets described above nets less than the amount required to make all of the payments set forth above, First American will accept less than $300,000, reducing its recovery on a dollar-for-dollar basis.

11. To the extent that liquidation of the assets described above nets more than the amount required to make all of the payments set forth above, First American shall receive the overage on a dollar-for-dollar basis until it receives its principal, interest, attorney's fees and costs up to July 25, 1990. Thereafter, First American and Central States will share dollar-for-dollar in any additional overage until they have received all additional interest on unpaid principal balances of secured promissorynotes, attorney's fees and costs accruing on and after July 25, 1990. Thereafter, Central States and the shareholders of FDCC will share dollar-for-dollar in any additional overage until their claims are satisfied.

12. Central States and First American will release of record their liens on the FDCC buildings and equipment, which have been abandoned by the estate.

Although the settlement provides for a dismissal of the bankruptcy, the parties to the proposal agree that the company could remain in bankruptcy if the court considered it necessary to approval of the

agreement. Also, although the agreement limits court costs to $1,000.00, FASB has consented to full payment of court costs out of its share of the settlement. It also has consented to the trustee's most recent legal fee application. Doan and Ambrose recently applied for the allowance of their legal fees as an administrative expense. Objections to the allowance were filed. A settlement, recently approved by this court, grants Doan and Ambrose an administrative claim for legal fees to the extent of $5,000.00.

Trustee acknowledges that as part of the compromise, the estate would release any claims against Stark and McGladrey. Likewise, Stark and McGladrey would release the trustee and the estate from any pre- or post-petition claims which either may hold. The trustee would dismiss any pending actions against Stark or McGladrey prior to the assignment of claims to Plains National Bank.

V.

THE STANDING OF DOAN AND AMBROSE TO OBJECT

Central States, which supports the proposal, argues that Doan and Ambrose have no standing to object to the settlement as they are not creditors of the estate. Central States points out that Bankr. R. 9019 requires notice of compromises to creditors but not to equity security holders and that equity security holders are not creditors of the estate. Furthermore, Central States argues that regardless of the outcome of any litigation there would be no distribution by the trustee to shareholders, as any distribution of surplus estate property would be made to the debtor corporation pursuant to 11 U.S.C. § 726(a)(6).

Bankr. R. 9019(a) does provide that the court may designate entities to receive notice of settlements. Doan and Ambrose are entities under the Code. 11 U.S.C. § 101(14). Moreover, the settlement affects their interest in the company. It is their position that if all litigation were pursued to a likely successful conclusion, there would be sufficient assets in the estate to make the debtor solvent. This would give their stock in the debtor value. Although any surplus would be distributed to the debtor corporation, the court concludes that the objecting shareholders nave a pecuniary interest in the outcome of the settlement contest. Even if they did not, the court would consider their arguments. The court has an independent duty to determine the advisability of compromise. Matter of Aweco, Inc., 725 F.2d 293, 299 (5th Cir. 1984), reh'g. and reh'g. en banc denied (1984). The participation and arguments of Doan and Ambrose have aided the court in the fulfillment of its duty.

VI.

In determining whether a proposed compromise should be approved, the bankruptcy judge must apprise himself "of all facts necessary for an intelligent and objective opinion of the probabilities of ultimate success should the claim be litigated. Further, the judge should form an educated estimate of the complexity, expense, and likely duration of such litigation, the possible difficulties of collecting on any judgment which might be obtained, and all other factors relevant to a full and fair assessment of the wisdom of the proposed compromise." Protective Committee for Independent Stockholders of TMT Trailer Ferry, Inc. v. Anderson, 390 U.S. 414, 424 (1968).

In fulfillment of this standard, the Eighth Circuit Court of Appeals has required consideration of four factors:

> (a) The probability of success in the litigation; (b) the difficulties, if any, to be encountered in the matter of collection; (c) the complexity of the litigation involved, and

> the expense, inconvenience and delay necessarily attending it; (d) the paramount interest of the creditors and a proper deference to their reasonable views in the premises.

Drexel v. Loomis, 35 F.2d 800, 806 (8th Cir. 1929).

Said another way, the court must determine "whether the settlement 'fall[s] below the lowest point in the range of reasonableness.'" Cosoff v. Rodman (In re W. T. Grant Co.), 699 F.2d 599, 608 (2nd Cir. 1983) citing Newman v. Stein, 464 F.2d 689, 693 (2nd Cir.), cert. denied sub nom. Benson v. Newman, 409 U.S. 1039 (1972).

DISCUSSION

Adversary No. X89-0158F

The trustee seeks a return of the 493 acres of farmland from RFI and a return of the profits of the land still in the possession of RFI. These profits total $272,411.90. Trustee relies on state law by virtue of 11 U.S.C. § 544(b). The trustee contends in his suit that the conveyance to RFI was fraudulent. The trustee's ability to avoid the transfer to RFI is dependent on the existence of an actual creditor against whom the transfer is voidable. Certainly, Central States come to mind. The evidence presented indicates that Central States was the object of the scheme. While there may have been other motives to the transfer, an important and perhaps primary motive was to shield the farm from the impending Central States' judgment. To succeed, the trustee need only show it was one motive of the transfer. Matthews v. Thompson, 186 Mass. 14, 71 N.E. 93, 96 (1904). But Central States and the debtor may have settled any grievance Central States may have had as a result of the transfer. It took a note, mortgage and security interest from debtor in January, 1986. Doan and Ambrose have not pointed to any other creditor in whose stead the trustee could attack the transfer. Besides Central States and FASB, there are few unsecured creditors in the case and objectors have not shown that any existed at the time of the transfer or that the transfer was aimed at them as potential future creditors.

Although this problem with the trustee's suit exists, the court will assume that the trustee may rely on an ability of Central States to set aside the transfer. There is both direct evidence and circumstantial evidence tending to prove the corporation's intent to defraud, to hinder or to delay Central States. The transfer was for no consideration. It was made to a related corporation and the profits from the land continued to be used in FDCC's business. The trustee believes the debtor was insolvent as a result of the transfer. The court believes there is a fair likelihood that the trustee will prevail on the merits and obtain return not only of the land but of the profits of the land presently in possession of RFI. If the profits are returned to the estate, the estate should pay the accrued farm expenses of $11,500.00. These will be treated as an administrative expense.

Trustee also seeks to avoid the mortgage of FASB in the farmland. Although the mortgage secured valid antecedent debt, trustee contends it was given to hinder, delay or defraud Central States.

There is some evidence of this. A mortgage to the bank was proposed as part of the overall reorganization plan and separately as a method to protect the farm from Central States. Gene Richardson, an officer of the bank, was told of the plan. However, there is also some evidence that the bank had wanted a mortgage on the farm before the union problem arose to protect its claim against FDCC. The outcome of trustee's effort is far from certain. Iowa law does provide for an avoidance of the mortgage of a creditor who knowingly participated in a conveyance intended to defraud others. Wilson v. Horr, 15 Iowa 489, 492 (1864); Mulvaney v. Buckler, 190 Iowa 1119, 181 N.W. 395, 397 (1921). The former case also supports trustee's claim that the creditor participating in the fraudulent

transfer may have his claim subordinated to the claims of other creditors. No one, however, particularly Doan or Ambrose, has cited to the court any authority for the proposition that FASB's claim would be subordinated to minority shareholders of the debtor corporation which participated in the transaction. For the purposes of the proposal before the court, it will be assumed that trustee would be successful in avoiding bank's mortgage in the farmland, the creamery site and the personal property of the debtor. Such avoidance would render FASB an unsecured creditor in the case.

The evidence shows that the secured claim of FASB as of July 25, 1990 including interest was $354,596.00. There is no evidence as to the amount of the claim on the date of the involuntary petition. Avoidance of the bank's mortgage would result in a preservation of the bank's lien for the benefit of the estate. 11 U.S.C. § 551; In re Blanks, 64 B.R. 467, 468 (Bankr. C.D. N.C. 1986). Preservation of the bank's lien would place the bankruptcy estate in a secured position superior to Central States. Interest would continue to accrue onthe preserved lien until payment of the secured claims against the land. This would continue to erode the value of the Central States' lien.

However, trustee also seeks disallowance of the FASB claim pursuant to 11 U.S.C. § 502(b)(1) which permits disallowance of claims if the claims are unenforceable under state law. Trustee seeks such relief based on First National Bank of Council Bluffs v. One Craig Place, Ltd., 303 N.W.2d 688 (Iowa 1981). In that case, the Iowa Supreme Court refused to enforce a corporation's promissory note to a bank because it found that the bank had aided and abetted a breach of the trust owed by the corporation's promoters to the corporation and its minority shareholders. Id. at 697.

Doan and Ambrose contend that the trustee would be successful in his effort to obtain disallowance of the FASB claim. This is not certain. There is an important distinguishing feature between the FDCC situation and the circumstances of One Craig Place. In the latter, the loan and resultant note were created as part of the breach of trust. In contrast, the FDCC indebtedness to FASB existed long before the reorganization and mortgage. The trustee concedes that the money was legitimately loaned by FASB to FDCC. The court does not find any evidence that the loans were part of a scheme to defraud. Nonetheless, for purposes of the settlement, the court will consider that the claim of FASB will be disallowed. If disallowed, the preservation of the avoided mortgage would be worthless to the estate, and the mortgage of Central States would remain senior.

Count IV of the complaint seeks a return of the value of 250 shares of stock in debtor corporation issued to A. Robert Loomis and Bob Loomis. The shares were allegedly issued to increase the Loomises' percentage ownership of the company in order to obtain an 80 per cent affirmative vote for the reorganization. There is evidence to support the theory that this transfer was fraudulent. There is little evidence of the value of the shares. $tark's notes do include a calculation of value of FDCC shares at a time when Loomises had considered buying out Doan and Ambrose. At that time, a share was thought perhaps to have a book value of $74.27. Exhibit B, page 51. When the issuance of stock to Loomises was discussed, each share was though perhaps to have a fair market value of $32.00 per share. Exhibit B, page 54. For purposes of consideration of settlement, the court finds the shares issued to the Loomises have a per share value of $74.27 for a total value of 250 shares of $18,567.50. The court will presume the trustee will recover this amount for the estate.

Adversary No. X89-0213F

The court has previously decided this proceeding by the trustee against FASB. FASB must return to the estate a postpetition payment of pre-petition debt in the amount of $17,791.66. If the settlement proposal is approved, the bank will retain the payment. If the settlement is not approved, there is no certainty whether this judgment will add anything to the estate for distribution. There certainly will be

further litigation as FASB claims a security interest in the funds as proceeds of personal property collateral. If, however, the trustee can show that the bank's lien on personalty was given to defraud other creditors, the bank would be relegated to an unsecured claim. Trustee claims that bank's claim should be disallowed or treated as unsecured and subordinated to other unsecured debt. As previously stated, although the outcome is far from certain, there is authority to support such remedies, so in considering the settlement, bank's claim will be projected as disallowed. The returned payments will be treated as part of the estate available for distribution.

Adversary No. X89-0205F

This adversary proceeding seeks recovery of more than $600,000.00. Little evidence was introduced on the likelihood of success against the various defendants. Theories of recovery are threefold. The trustee seeks to recover $4,923.32 from Plains National Bank as trustee of the Allen R. Loomis trust and from Allen R. Loomis as avoidable post-petition payments. There are few defenses to such suits. The court will presume success.

Trustee also seeks to recover from the same defendants $21,696.11 in pre-petition preference payments. For $5,019.34 of that amount, the trustee would have the benefit of a presumption of insolvency of FDCC. For the balance, he would not and would have to prove that FDCC was insolvent each time debt repayment took place between October 21, 1987 and June 12, 1988. Again the court will presume that the trustee would be successful, despite the lack of evidence that this would be so.

Count II seeks recovery of allegedly preferential payments made to A. Robert Loomis. Trustee would have to show insolvency at the time of each of the five payments which totaled $3,077.98. The court will presume the trustee's success on this count.

The remaining counts of the suit seek recovery of payments made by the debtor to alleged insiders prior to bankruptcy. The counts are premised on state law which considers as improperly preferential those payments by an insolvent corporation to satisfy pre-existing debt owed to a controlling shareholder. Boyd v. Boyd & Boyd, Inc., 386 N.W. 2d 540, 544 (Iowa App. 1986). Nearly all of the subject payments were made to Allen R. Loomis, Bob Loomis or to entities which they allegedly controlled. Trustee would have to prove insolvency at the time of the transfers. Some of the payments took place as early as January, 1985. Despite the lack of evidence as to success on the merits, the court will presume the trustee's success on most of the 25 counts based on this-theory. The court will not presume such success as to counts 25 through 28 lodged against Doan or Ambrose. There has been no evidence to show the trustee would be successful in showing control over the corporation by these shareholders.

In summary, the court will presume that the trustee will be successful in recovering $570,000.58. The court will also consider that the entities returning the money will be treated as unsecured creditors pursuant to 11 U.S.C. S 502(h).

The Derivative Action and Adversary X89-0158F

The Determination of Taxes and Indemnification

In the pending adversary X89-0158F, trustee seeks a determination of federal and state income taxes arising out of the FDCC corporate reorganization. If the estate is liable for the taxes, trustee seeks indemnification for them.

The IRS claims the transfer of the land to RFI was a taxable event and that taxes, penalties and interest to the date of bankruptcy total $492,108.00. Exhibit 13. IRS also claims post-petition interest. The Iowa Department of Revenue and Finance has filed an amended proof of claim for $52,135.28 for taxes attributable to the transfer.

If the bankruptcy court determines some or all of these taxes are owed, trustee would hope to recover what the estate must pay from Loomises and from Stark and McGladrey, the corporation's tax advisors.

There is evidence tending to show that under the direction of Bob Loomis, the corporation transferred the land before 80 per cent shareholder agreement on the reorganization was obtained and that even when 80 per cent approvalwas obtained, it was rigged through an issuance of stock. There is also evidence that the transfer was intended to hinder or delay Central States. Trustee contends that if the scheme was not tax free, the tax burden should fall on the Loomises and the tax advisors.

What is their liability for taxes if the transfer were not tax free? There is substantial evidence that while the advisors knew they could not predict with certainty the tax ramifications if 80 per cent approval were obtained, they did warn the corporation of the potentially dire consequences of approval of the reorganization at less than 80 per cent. The decision to go forward was not theirs. However, they did give advice regarding the issuance of shares to Loomises to reach the 80 per cent level.

The evidence is not sufficient for the court to predict with any certainty what the outcome of the state court proceeding would be. This is so as to liability for taxes and for punitive damages. For purposes of the settlement motion, the court will presume that the estate will be liable to the United States and to Iowa for the taxes claimed and that the trustee will recover a like amount from the defendants in the state court suit.[(13)]

ASSETS OF THE ESTATE

In light of the foregoing presumptions and findings, these would be the assets of the estate:

Proceeds of sale of farmland	$ 887,400.00
Rents and profits of farm, 1990	272,412.00
Cash in possession of trustee (Exhibit 4)	30,288.00
Repayment of post-petition transfers by FASB	17,792.00
Recovery from preference suit	570,001.00
Recovery from stock distribution	18,568.00
Indemnification recovery, state action (state and federal taxes)	544,243.00
Total assets	$2,340,704.00

ESTIMATED ADMINISTRATIVE EXPENSES

Trustee fees on the foregoing total would be approximately $70,041.00. The trustee has already incurred expenses of $985.71. As attorney for the trustee, James Cossitt has already applied for $60,077.47 in fees and expenses. Based upon an examination of the case file and upon examination of

contested matters and adversary proceedings where no outside counsel is expected to be employed, the court finds that Cossitt's allowed attorney's fees and expenses for the case would reach at least $100,000.00. It is expected that outside counsel would be employed for adversary X89-0205F and the state court action. The court finds that a one-third contingency fee would be reasonable for the pursuit of such litigation. In each case, $1,000.00 in non-taxable costs and expenses would be reasonable if not conservative. Doan and Ambrose have been allowed legal fees in the amount of $5,000.00.

With regard to the sale of the farmland, the trustee estimates a five per cent sales commission to obtain the expected sales price. He also estimates unpaid but accrued real estate taxes and drainage assessments on the real estate which would have to be paid. The trustee also estimates $5,000.00 in accountant fees for the estate. Total court costs for the case are estimated at $2,500.00. Objectors have not contested these estimates, and the court finds them reasonable.

There is insufficient evidence for the court to estimate income taxes to the estate for the sale of the farmland or for the sale of 1990 crops. These expenses will not be included in the administrative expenses.

The court estimates administrative expenses as follows:

Trustee fees	$ 70,041.00
Trustee's expenses	986.00
Trustee attorney expense (Cossitt)	100,000.00
Trustee attorney expense (preference action)	190,000.00
Trustee attorney expense (state action)	181,414.00
Legal expense (preference and state)	2,000.00
Accountant	5,000.00
Court costs	2,500.00
Sales commission on land	44,370.00
Unpaid farm expenses	11,500.00
Attorney's fees for Doan and Ambrose	5,000.00
Total estimated administrative expenses:	$612,811.00

SECURED CLAIMS

From the land sale proceeds, the trustee would have to pay the real estate taxes and drainage assessments and the mortgage of Central States. Central States would be entitled to interest and attorneys' fees related to its secured claim so long as the value of the real estate exceeded the amount of the claim.

On July 25, 1990, Central States' secured claim was $470,000.00. Trustee estimates $91,000.00 in legal fees and two more years of interest before payment in the amount of $112,800.00. As of July 25, 1990, Central States had incurred nearly $67,000.00 of the expected fees. Little evidence was introduced to support these estimates. However, Doan and Ambrose do not dispute them. For purposes of this proceeding, the court will estimate allowed legal fees of $75,000.00 as part of Central States' secured claim and interest until payment of $56,400.00. The trustee's estimate of interest was based on his expectation that litigation including appeals would continue at least two years from July

25, 1990. This period would also include the time necessary to sell the real estate and to obtain permission to pay the secured creditor. The estimate is probably not unreasonable. The court, however, prefers a more conservative estimate of one year's interest.

Although they are not administrative expenses, the following amounts must be deducted from the sales proceeds of the land, and thus the total assets of the estate, before a distribution to unsecured creditors can be calculated.

Central States' secured claim (7/25/90)	$470,000.00
Interest and attorney fees added to Central States' claim	131,400.00
Real estate taxes and drainage assessments	61,765.00
Total	$663,165.00

When one deducts these claims and administrative expenses of $612,811.00 from the assets of the estate, the remainder for distribution to unsecured creditors is $1,064,728.00.

UNSECURED CLAIMS

Timely filed unsecured claims include:

Central States	$248,248.00
Iowa-Illinois Gas	1,546.00
Blackburn, P.C.	66.00
Iowa Job Service	167.00
Purkapile	3,175.00
Total	$253,202.00

New unsecured claims would arise from the avoidance of the alleged preferences. 11 U.S.C. § 502(h). These claims would share with timely filed claims against the estate. Payment of such claims would increase timely filed unsecured claims to $823,203.00 ($253,202.00 + $570,001.00). Distribution to these creditors would leave a remainder in the estate of $241,525.00 ($1,064,728.00 - $823,203.00). Section 726(2)(c)(ii) or 726(3) would then permit payment to creditors with late-filed claims:

Amoco Oil Co.	$ 71.00
IRS	492,108.00
Iowa Dept. of Revenue	52,135.00
Total	$544,314.00

Late-filed claims would thus not be paid in full. There would be no distribution to the debtor under 11 U.S.C. § 726(a)(6). Even if the claims arising out of preference avoidance were disallowed, there would be little if anything left over for the debtor. If such claims were disallowed, and if timely and untimely unsecured claims were paid in full as of the date of the petition, there would remain a balance of estate funds of $267,212.00 ($1,064,728.00 - $253,202.00 - $544,314.00). Interest could then be paid to unsecured creditors pursuant to 11 U.S.C. S 725(a)(5). The interest would be paid on the unsecured claims from the date of the filing of the involuntary petition to the date of payment.

More than two years has already passed since filing. Given the extensive litigation in this case, if all matters were litigated, it is a reasonable estimate that four years would pass from petition to payment. The most recent federal rate of interest on judgments is 7.28 per cent. The court will use this rate. Four years of interest on unsecured claims of $797,516 is $232,236. After payment of this interest, approximately $35,000 would remain in the estate. This could be paid to the debtor under 11 U.S.C. § 726(a)(6).

However, such payment to the debtor presumes that there would be no state or federal income taxes payable by the estate on account of the income from the sale of 1990 crops, the sale of the farmland, or from the interest income from estate funds held on deposit during administration. It also presumes no further real estate taxes have accrued. Although there is no evidence to enable the court to calculate what such taxes might be, the court considers it likely that some such taxes would be payable.

SUMMARY

It is unlikely that even if the trustee were successful in recovery on nearly all the estate claims in all the pending litigation that there would be a significant distribution to the debtor absent the assessment of exemplary damages in the state court action. It is difficult to assess the likelihood that the state court judge will assess such damages against the defendants. The state court could not award the trustee exemplary damages against Norwest as the executor of the estate of Bob Loomis. Any claim to punitive damages against Bob Loomis would be cut off by his death. Wonder v. Rahm, 249 N.W.2d 630, 632 (Iowa 1977).

The outcome of litigation is always somewhat of a gamble. It is one which the creditors, especially Central States, do not wish to take. Central States believes that if the case is not settled and litigation continues, there is a likelihood that its legal costs and potential adverse outcomes could reduce its recovery to an amount below that for which it has settled. The minority shareholders wish to take the gamble, but in a sense they want to gamble with the money of the unsecured creditors.

Settlement may not leave the minority shareholders at a total loss. The corporation may obtain some value from the creamery siteand the machinery and equipment. Also, Doan and Ambrose will retain any personal claims they may have against any third parties.

The views of the unsecured creditors on whether these proceedings should be compromised are important, especially the views of Central States, the one large creditor whose claim is not in some way disputed and who, after all, was the creditor at whom the reorganization scheme was allegedly aimed. It desires that these cases be put to rest, that it recover a portion of its claim and that it recover the payment soon. Doan and Ambrose argue that the integrity of the judicial system cries out for the trial of these proceedings and that justice requires that the wrongdoers be punished. However, this court fears that it cannot take a "pound of flesh" from any alleged wrongdoer without taking "blood" from the innocent Central States.[(14)]

There are other important factors which militate in favor of settlement. Trial of all the proceedings would delay distribution to creditors. It is the duty of the trustee to liquidate the estate as "expeditiously as is compatible with the best interests of parties in interest." 11 U.S.C. § 704(1). Approval of the settlement agreement would provide a more expeditious distribution to creditors. Second, compromise of litigation should be encouraged by the courts. Aaker v. Aaker, 338 N.W.2d 645, 647-648 (N.D. 1983).

Finally, when the court considers the delay and expense which would be engendered by the continuance of the actions, it comes to the conclusion that the cost and delay are simply not worth it to the estate. This settlement may not be the best settlement, but it is a good settlement. It is one which the trustee, the other parties to the litigation and certain creditors of the estate have hammered out over a long period of time. They are satisfied with the result, and the court is not offended by it. The settlement should be approved, but with some qualifications or conditions. The case should not be dismissed. The trustee has administered assets. He is required by the agreement to do more. He must liquidate assets and distribute funds to creditors in accordance with the payment plan. No one has offered a reason that this needs to be done outside of bankruptcy. Retention by the court permits continued scrutiny of the efforts of the parties to consummate the agreement. Second, court costs must be paid in full, regardless of their amount. Third, there is no judicial economy inherent in a settlement which assigns the actions to be settled to a third party which could then pursue them. Plains National Bank, according to its letter (Exhibit 17), intends to dismiss the actions. This will be a condition of approval.

ORDER

IT IS ORDERED that the trustee's Motion to Compromise will be granted and the Settlement Agreement approved on the following conditions: (1) the case in chief shall not be dismissed, (2) all court costs shall be paid in full, and (3) Plains National Bank, trustee of the Allen R. Loomis Trust, shall, as assignee of certain claims of the estate, dismiss with prejudice the following proceedings: Adversary X89-0158F, Adversary X89-0205F, Adversary X89-0213F and civil action No. C184-0488 pending in the Iowa District Court for Webster County.

IT IS FURTHER ORDERED that unless either a party to the agreement or Plains National Bank rejects these conditions within 14 days from the date of this Order, the motion to compromise will be granted and the Settlement Agreement will be approved. If any of the parties to the agreement or the bank rejects the conditions within such period of time, further hearing shall be held to determine the validity of the rejection.

IT IS FURTHER ORDERED that if the agreement is approved, the trustee shall have 14 days from its approval to submit to the court a proposed order granting the Motion for Partial Summary Judgment in adversary number X89-0158F; a proposed order granting the trustee's Motion to Sell Property of the Estate Free and Clear of Liens; and a proposed order granting the application of James H. Cossitt for administrative expense.

SO ORDERED ON THIS 26 DAY OF DECEMBER, 1990.

William L. Edmonds
Bankruptcy Judge

1. Stipulated Facts by Trustee and Objectors, (Hereinafter "Stipulation"), page 2, ¶ 11.

2. Stipulation, as amended by Trustee, exhibit 14, page 3.

3. Stipulation, page 3, ¶ 14.

4. Stipulation, page 4, ¶ 21.

5. Stipulation, page 4, ¶ 23.

6. Stipulation, page 4, ¶ 24, ¶25, and ¶ 26.

7. Stipulation, page 5, ¶27; Exhibit 4.

8. Stipulation, page 5, ¶ 28.

9. Stipulation, page 5, ¶ 29.

10. Stipulation, page 5, ¶ 30.

11. Listed creditors to be paid in full are Purkapile, Iowa-Illinois Gas & Electric, Blackburn, Job Service of Iowa and Amoco Oil Co.

12. Parties agreed at the hearing that this should have been a reference to paragraph 11.

13. The court will use the amount of the IRS and IDOR claims as of the date of the petition and not try to calculate interest to a date certain.

14. William Shakespeare, The Merchant of Venice.