In the United States Bankruptcy Court

for the Northern District of Iowa

- Appealed 8/29/94;
- Remanded to Bankruptcy Court by Joint Motion of Parties 10/13/94

BOCKES BROTHERS FARMS INC.
MARY MATILDA BOCKES
Debtor(s).

Bankruptcy No. 93-60889KW

Chapter 11

ORDER

On August 11, 1994, the above-captioned matter came on for hearing pursuant to assignment. The following appearances were noted:

- Dan Childers for Debtor Bockes Brothers Farms, Inc.
- Ray Terpstra for Conrad Cooperative
- Mike Vestle for Phelps Implement Co. and Sauder Implement, Inc.
- Richard Hansen for Farm Credit Bank of Omaha
- Jeff Taylor for the Unsecured Creditors' Committee
- Ana Maria Martel for the Internal Revenue Service ("IRS")
- Joe Peiffer for First State Bank of Conrad on behalf of Dale Bockes Insurance Trust
- Eric Lam and Dean Mohr for Ag Services of America, Inc. ("ASA")
- Irvin Ness and Rod Kubat for Farmland Financial Services and Cooperative Finance Association, Inc. ("CFA")

The matter before the Court was Debtor's Motion for Approval of Compromise and Settlement. At the time of the hearing all objections to the Motion had been withdrawn except the objections by Conrad Cooperative and the IRS. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(D), (N) and (O).

STATEMENT OF FACTS

Bockes Brothers Farms, Inc., and the individual Bockeses, including Mary Bockes (hereinafter collectively referred to as "Debtor"), propose to enter into a settlement agreement with CFA and ASA. The text of the agreement is set out in Exhibit 8. The essence of the agreement is as follows: ASA shall purchase CFA's claim for $1,165,500. CFA values its claim at $2.0 million. CFA is releasing Debtor from liability for the claim. Debtor is releasing CFA for any liability for potential claims of lender liability and Deprizio-type avoidable preferences. These claims have an estimated value of approximately $500,000 to $750,000. Debtor is also releasing other general objections to CFA's claim regarding whether payments were correctly deducted, the correct rate of interest, and the

reasonableness of attorney fees. In addition, CFA and Debtor are releasing each other from all claims raised in adversary proceedings and state court actions.

In consideration of ASA's purchase of CFA's claim, Debtor is pledging to ASA certain currently unencumbered property as collateral and selling other property. The agreement contemplates that ASA will be paid in part from the sale of the property and in part over a period of time. Some of the collateral pledged to ASA includes exempt homestead property and personal property. The total Debtor will pay ASA for the CFA claim is approximately $1.3 million. The agreement also contains provisions for repayment of obligations owed directly by Debtor to ASA other than the CFA claim. The agreement specifically provides that it does not affect the priority of liens of other creditors.

Conrad Coop asserts that the agreement amounts to a sale outside the ordinary course of business which must meet the requirements of 11 U.S.C. § 363. It states that the agreement transfers unencumbered assets for the sole benefit of ASA without providing for any distribution to reduce its claim as one of the major unsecured creditors in the estate. Conrad Coop objects to the lack of specificity in the settlement agreement regarding the value of the claims against CFA which Debtor is releasing and to Debtor's payment to ASA of an amount which exceeds the amount ASA is paying to CFA.

The IRS also objects to a lack of specificity in the agreement regarding the amount of CFA's claim, the extent of the collateral securing the claim, Debtor's obligations to ASA and its collateral, etc. It asserts that the agreement provides no benefit to the estate and will leave no assets in the estate to pay the unsecured priority claim of the IRS and other unsecured claims. The IRS is concerned that the agreement calls for the transfer to ASA of property valued in excess of its claim.

In response, Debtor asserts that the compromise does benefit the estate by avoiding substantial litigation costs, estimated at approximately $500,000, and delay, in exchange for a reduction of the amount owed on CFA's claim by up to $700,000. ASA is receiving approximately $100,000 as an inducement to pay off CFA, as well as a promise of $150,000 in the event that Debtor defaults in its obligations under the agreement. Debtor notes that FFSC and CFA have heretofore been uncompromising in their position and would undoubtedly litigate the potential lender liability and Deprizio claims to the fullest. Debtor acknowledges that recovery on these claims is highly speculative. The Deprizio analysis is unresolved in the Eighth Circuit and the issue of Debtor's insolvency at the time of the transfer is disputed. The lender liability claim may be vulnerable to a res judicata defense because of dismissals filed in State Court in Grundy County.

CONCLUSIONS OF LAW

The decision whether to approve a settlement is committed to the sound discretion of the Bankruptcy Court. In exercising its discretion, the Court must make an informed and independent judgment. In re Flight Transp. Corp. Sec. Litig., 730 F.2d 1128, 1135 (8th Cir. 1984), cert. denied 469 U.S. 1207 (1985); In re Cox, No. A-86-1718S, slip op. at 14 (Bankr. N.D. Iowa June 8, 1990). The Court should approve the settlement unless it falls below the lowest point in the range of reasonableness. In re New Concept Hous., Inc., 951 F.2d 932, 938 (8th Cir. 1991). The Court may approve a settlement over the objections of some parties so long as it is in the best interests of the estate as a whole. Flight Transp. Corp., 730 F.2d at 1138.

The Eighth Circuit has stated that the trial court must determine whether a settlement is fair, reasonable and adequate under all the circumstances. In making that determination, the Eighth Circuit has adopted a broadly accepted four-factor test. Those factors are:

> (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.

Flight Transp. Corp., 730 F.2d at 1135, quoting Drexel v. Loomis, 35 F.2d 800, 806 (8th Cir. 1929).

The second factor, i.e. difficulties in collection, is not an issue in this case. It does not appear to be disputed that ASA is financially able to pay for CFA's claim. The parties appear to be willing and able to enter the necessary releases.

A. Likelihood of Success on the Merits.

The Court and the parties need not precisely assign a value to each claim. In re Energy Coop., Inc., 886 F.2d 921, 928 (7th Cir. 1989). The world of settlements does not read like a balance sheet, nor should it. Id. The Court must determine that the value of the compromise is reasonably equivalent to the value of the potential claim. Id. The reviewing court need not conduct its own investigation but may credit and consider the opinion of the debtor-in-possession and counsel. In re Purofied Down Prods. Corp., 150 B.R. 519, 522 (S.D.N.Y. 1993). The court need not conduct its own mini-trial to determine the merits of the underlying litigation. Id.

Debtor's brief candidly outlines the merits of its potential claims against CFA. In order for Debtor to be successful in the Deprizio preferential transfer claim, it must prove that it was insolvent at the time the transfer was made. This would be highly disputed by CFA. Although this Court has embraced the Deprizio analysis. the Eighth Circuit Court of Appeals has not yet ruled on the issue. See In re McGregor Harbor, Inc., No. L-92-00234D, Adv. No. 92-2239LD, slip op. at 4 (Bankr. N.D. Iowa May 28, 1993). Considering the parties' litigious history, it is likely that litigation of Debtor's Deprizio claim would involve eventual appeal to the Eighth Circuit. Thus, the outcome of the Deprizio claim is uncertain.

As to the lender liability claim, Debtor acknowledges that CFA has a colorable defense of res judicata regarding the 1992 crop year based on dismissals entered in State Court. CFA also asserts that no agreement was made regarding the 1993 crop year which would preclude recovery. The Court is very familiar with numerous cases of lender liability in Iowa courts which have resulted in little, if any, recovery for the plaintiffs. This Court generally agrees with the analysis that in the emerging area of lender liability, the possibility of success for plaintiffs is ordinarily remote. In re Hanson Indus., Inc., 88 B.R. 942, 948 (Bankr. D. Minn. 1988).

The Court concludes that consideration of Debtor's probability of success in the litigation militates in favor of the conclusion that settlement is in the best interests of the estate. Both of the outlined claims appear to be of marginal value in the circumstances. Without conducting a mini-trial on the merits of the two claims, it appears that the proposed settlement is the estate's best option.

B. Expense, Inconvenience and Delay of the Litigation

The complexity of the litigation and the expense, inconvenience and delay necessarily attending it is the third of the Drexel factors. Settlement is favored when the law of the claim is little developed and unsettled, requiring major factual and legal development for adjudication. In re Hancock-Nelson Mercantile Co., 95 B.R. 982, 995 (Bankr. D. Minn. 1989). Settlement can offer some hope of minimal payment to unsecured creditors without taking a gamble on litigation which can drag out and drain assets of the estate. Hanson Indus., 88 B.R. at 950.

Debtor's uncontroverted estimate of litigation costs is $500,000. Significant non-monetary benefits also attend settlements such as quick distribution of funds rather than paying for legal fees. Energy Coop., 886 F.2d at 927. Any fund potentially available to creditors may be substantially depleted by the costs of litigation. In re Miller, 148 B.R. 510, 525 (Bankr. N.D. Ill. 1992).

Considering the speculative nature of Debtor's claims and the costs of litigation, the Court concludes that the expense, delay and inconvenience of litigation also militate in favor of settlement. Considering the costs of litigation and the potential lengthy delay, even if Debtor was successful in its claims, very little would be gained by protracted litigation. Inveterate gamblers might prefer the risk of no distribution against the prospect of a larger one. Hancock-Nelson Mercantile, 95 B.R. at 999. In these circumstances, however, the gamble is not in the best interests of the estate.

C. Due Deference to the Views of Creditors

The fourth factor, giving due deference to the views of creditors, also supports the Court's approval of the settlement agreement. Approval of a settlement is strengthened by the fact that most creditors support it. Flight Transp. Corp., 730 F.2d at 1137. The views of all creditors need not be given the same weight, just "proper deference." In re Sassalos, 160 B.R. 646, 654 (D. Or. 1993). While the Court must give deference to the reasonable views of creditors, objections do not rule. In re Lee Way Holding Co., 120 B.R. 881, 890 (Bankr. S.D. Ohio 1990).

Objections were withdrawn by Sauder Implement, Phelps Implement, Farm Credit Bank of Omaha, First State Bank of Conrad as Trustee of the Dale Bockes Insurance Trust and the Unsecured Creditors' Committee. The Court has given ample consideration to the objections of the IRS and Conrad Coop. The IRS seeks further clarification of the values and obligations covered by the settlement agreement. The Court concludes that the record is sufficient to determine the effect of the settlement agreement and whether it is in the best interests of the estate.

Both the IRS and Conrad Coop argue their position based upon the premise that the agreement strips Debtor of all property and of any ability to reorganize. This, however, is not the correct analysis. Debtor will retain control of some of the property transferred or pledged as collateral in the settlement agreement. Debtor can maintain its farming operation through its several farm leases. It will also be able to continue in its bean processing business. Although no plan of reorganization has been filed, reorganization is not precluded by the settlement agreement. To the contrary, avoiding litigation with CFA may well promote effective reorganization.

The IRS objects to Debtor's pledge of exempt homestead and personal property which it may be able to attach under 26 U.S.C. § 6334(e). The Court concludes that the IRS's ability to reach such exempt property is uncertain. Its rights are not being violated by Debtor's offer to ASA of exempt property as security.

Conrad Coop argues that the settlement constitutes a sale outside the ordinary course of business and must comply with the requirements of 11 U.S.C. § 363. That section requires that the sale of assets be

fair and reasonable and in good faith. In re Apex Oil Co., 92 B.R. 847, 866 (Bankr. E.D. Mo. 1988). It requires a sound business reason for a pre-confirmation sale of assets. In re Sovereign Estates, Ltd., 104 B.R. 702, 704 (Bankr. E.D. Pa. 1989).

The Court concludes that the § 363 requirements are much like the requirements for approval of settlement and are met in these circumstances. Debtor's proposal of the settlement evidences sound business judgment because it reduces CFA's potential $2.0 million claim to approximately $1.3 million by compromising claims against CFA which are of uncertain value. Unsecured creditors such as Conrad Coop could be more at risk of receiving nothing if the settlement is not approved given the costs and delays attendant to protracted litigation. Approving the settlement promotes Debtor's financial health which should result in benefits to unsecured creditors through an effective plan of reorganization. As in Apex Oil, the agreement preserves a core of vital assets around which Debtor can reorganize. 92 B.R. at 869.

D. Conclusion

"The law favors compromise." In re Lawrence & Erausquin, Inc., 124 B.R. 37, 39 (Bankr. N.D. Ohio 1990) (considering whether to approve settlement of a claim). Giving due consideration to all factors, the Court finds that approval of the settlement is in the best interests of the estate. CFA's claim is significantly reduced and treacherous litigation is avoided. The majority of creditors have not objected to the settlement. The settlement agreement falls well above the lowest point in the range of reasonableness.

The Court has examined Debtor's proposed Order Approving Compromise and Settlement. The proposed Order is accurate in its recitation of the facts and conforms with the Court's independent analysis and conclusions. Therefore, the Court shall adopt the Order Approving Compromise and Settlement proposed by Debtor upon presentation to the Court of an executed copy.

WHEREFORE, Debtor's Motion for Approval of Compromise and Settlement is GRANTED.

FURTHER, the objections of the IRS and Conrad Coop are OVERRULED.

FURTHER, the Court hereby approves the Settlement Agreement set out in Exhibit 8.

FURTHER, the Court shall adopt Debtor's proposed Order Approving Compromise and Settlement upon presentation to the Court of a fully executed copy.

SO ORDERED this 18th day of August, 1994.

Paul J. Kilburg
U.S. Bankruptcy Judge