

# In the United States Bankruptcy Court

## for the Northern District of Iowa

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J.E. ADAMS INDUSTRIES LTD.

Bankruptcy No. 98-00167-C

*Debtor(s)*

Chapter 7

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J.E. ADAMS INDUSTRIES LTD.

Adversary No. 98-9295-C

*Plaintiff(s)*

vs.

NBD EQUIPMENT FINANCE INC.

*Defendant(s)*

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### ORDER

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On May 4, 1999, the above-captioned matter came on for trial pursuant to assignment. Plaintiff appeared by Attorney Thomas Fiegen. Defendant NBD Equipment Finance, Inc., n/k/a Banc One Leasing Corp., appeared by Attorney Thomas McCuskey. Evidence was presented and the matter was taken under advisement. Briefs have been filed and this matter is ready for resolution.

### FINDINGS OF FACT

This adversary complaint was filed by Debtor J.E. Adams Industries, Inc. to enjoin the continuation of a State court lawsuit entitled NBD Equipment Finance, Inc. v. Jack E. Adams and Zakea Adams, Linn County No. LACV33865. The uncontested record establishes that J.E. Adams Industries, Ltd. filed a voluntary petition under Chapter 11 of the U.S. Bankruptcy Code on January 21, 1998. J.E. Adams Industries manufactures car wash components, custom machine parts as well as fittings and cooling fans. NBD Equipment Finance, Inc. (NBD) is a lease and finance company located in Columbus, Ohio. Over a period of time, J.E. Adams Industries and NBD entered into certain leases involving machines used in J.E. Adams Industries' business operations.

Jack and Zakea Adams are President and Vice-President of J.E. Adams Industries, Ltd. When the leases between J.E. Adams Industries and NBD were executed, both Jack and Zakea Adams signed the leases as personal guarantors. On October 11, 1998, NBD filed the pending lawsuit in Iowa District Court alleging that J.E. Adams Industries is in default on its leases. NBD seeks payment of the remaining balances on these leases from Jack and Zakea Adams under their personal guarantee.

J.E. Adams Industries filed the pending adversary on December 11, 1998 seeking injunctive relief. It asserts that Mr. Adams is intimately involved in the business J.E. Adams Industries and that if he is personally required to defend this lawsuit, it will seriously interfere with the discharge and performance of his duties to Debtor-corporation. It asserts that, if this lawsuit is not enjoined, Debtor-corporation will suffer irreparable harm in both the reorganization effort and in its ability to

consummate a plan of reorganization. The complaint also alleges that Zakea Adams' role in the corporation is critical and pursuit of the lawsuit would hamper her work for the Debtor.

Jack Adams testified that recently he has been heavily involved in sales and collection of outstanding accounts. He has traveled extensively. He testified that if he is required to defend this lawsuit, it will hamper his efforts on behalf of the Debtor-corporation. Mr. Adams is represented personally by a private attorney other than the attorney representing the Debtor-corporation. Mr. Adams testified that since the beginning of this lawsuit, he has spent about 20 minutes discussing these matters with his personal attorney. Zakea Adams did not testify.

### **ISSUE**

Debtor is seeking to enjoin the continuation of a State lawsuit in which NBD seeks to enforce personal guarantees against Mr. and Mrs. Adams. Debtor alleges that 11 U.S.C. §362 and 11 U.S.C. §105 provide the requisite authority and jurisdiction to this Court to enjoin this action. J.E. Adams Industries does not specifically state whether it is seeking temporary injunctive relief or the issuance of a permanent injunction. NBD resists the issuance of any type of injunction asserting that neither Code section provides authority under these facts to issue an injunction. The Court will discuss the application of §362 and §105 separately.

### **TEMPORARY VS. PERMANENT INJUNCTION**

Debtor is not specific whether it seeks a temporary or permanent injunction. However, testimony provided by Mr. Jack Adams indicates that it is the contemplation of J.E. Adams Industries to seek a permanent injunction. Mr. Adams testified that his busy schedule will continue after the confirmation of a plan of reorganization and that it would be extremely inconvenient to be required to defend the State lawsuit. It, therefore, appears that J.E. Adams Industries is seeking a permanent injunction.

It is the conclusion of this Court that, if any injunctive relief is available, it must be limited to a temporary injunction. Section 524(e) provides that "discharge of a debt of the debtor does not affect the liability of any other entity on, or the property of any other entity for, such debt." 11 U.S.C. §524 (e). If the Court were to grant a permanent injunction against the continuation of this lawsuit, the practical affect would be to grant a discharge to non-debtors, Jack Adams and Zakea Adams. As these individuals are non-debtors, this would violate the provisions of §524(e). No authority has been provided to the Court and the Court is aware of no authority contained in §362 or §105 which would grant to this Court the authority to alter the provisions of §524.

As such, it is the conclusion of this Court that to the extent that Debtor is seeking a permanent injunction, the same must be denied. If any authority exists to grant an injunction under the facts of this case, the same must be limited to temporary relief.

### **11 U.S.C. §362**

A petition filed under Chapter 11 of the Bankruptcy Code operates as a stay which is applicable to all entities of the continuation of any judicial action or proceeding against the debtor. 11 U.S.C. §362(a) (1). By its own terms, §362 is applicable only to debtors. There exists no provision for the extension of the automatic stay to co-debtors or other entities as is available in Chapter 13 cases. Credit Alliance Corp. v. Williams, 851 F.2d 119, 121 (4th Cir. 1988).

However, with the advent of mass tort litigation, the courts have carved out an exception to this rule under those rare circumstances where "there is such identity between the debtor and the third-party defendant that the debtor may be the real party defendant and that a judgment against the third-party defendant will in effect be a judgment or a finding against the debtor". A. H. Robins Co. v. Piccinin, 788 F.2d 994, 999 (4th Cir.), cert. denied, 479 U.S. 876 (1986).

Courts should, however, be cautious in expanding this extremely narrow exception to other types of situations including those involving guarantees or holders of guarantees. In re Vitek, Inc., 51 F.3d 530, 538 n.39 (5th Cir. 1995). Courts have been reluctant to expand the parameters of §362 beyond the narrow exception provided in mass tort litigation. They recognize that a guarantor or surety relationship differs significantly from those present in mass tort litigation. In mass tort litigation, the relationships of the parties are so intertwined that an effect upon one entity will inextricably have the same effect on other entities as well as a debtor. However, a personal guarantor is pledging property which is not part of the estate. That is the precise reason why creditors seek this type of added assurance. In re Veeco Inv. Co., 157 B.R. 452, 454 (Bankr. E.D. Mo. 1993).

Jack Adams and Zakea Adams are officers in Debtor-corporation. They are obviously closely associated with the reorganization process. However, they were sued in State court, not in their capacity as officers or stockholders of Debtor-corporation, but rather as personal guarantors. As personal guarantors, Mr. and Mrs. Adams are not automatically included within the embrace of the §362 automatic stay provided to Debtor.

It is Debtor J.E. Adams Industries which is the Plaintiff in this complaint. All issues presented here, therefore, must be examined from that perspective. The individual rights of Jack and Zakea Adams are not legally relevant to this analysis. The burden of proof is upon J.E. Adams Industries to establish not only a legal basis but a factual basis for the issuance of an injunction. In doing so, Debtor attempts to place itself within the "unusual situation" exception to §362. There is, however, no factual basis to support such a finding. The record is devoid of support for the proposition that these relationships are so intertwined that individual assets of the guarantors are synonymous with those of Debtor. The narrow exception provided for the expansion of the automatic stay under §362 is not applicable here.

Factually, Debtor must establish that the issuance of an injunction would benefit the corporation. Debtor attempts to satisfy this burden by asserting that Mr. Adams' duties on behalf of the corporation are so demanding and time consuming that he does not have time to address the State court litigation. While there is little doubt that Mr. Adams has spent an extensive amount of time with Debtor's business during the reorganization process, Debtor's assertion is not supportable. The United States Supreme Court recently had an opportunity to review the propriety of the issuance of a temporary injunction to stay civil litigation. The Court held that even the President of the United States is not entitled to the issuance of a categorical injunction against continuation of a civil lawsuit. Clinton v. Jones, 520 U.S. 681, 706 (1997). The Court held that other party's interests must also be taken into account in determining whether a stay of the civil proceedings is appropriate. The Supreme Court stated that: "We recognize that a President, like any other official or private citizen, may become distracted or preoccupied by pending litigation." Id. However, the Court held that the movant had not met his burden to establish that a stay should issue.

Likewise, it is the conclusion of this Court that J.E. Adams Industries has not established that the requirements upon its employee, Jack Adams, are so onerous as to warrant imposition of injunctive relief. This becomes more apparent when the rights of Defendant NBD are considered in the analysis. Plaintiffs in the civil lawsuit are not parties to the bankruptcy. NBD has a right to have its issues determined in State court without interference by this Court.

Finally, J.E. Adams Industries has not established that the burden of the civil litigation is so great that Mr. Adams could not perform his obligations as an employee of the corporation. He testified that he has spent approximately 20 minutes since the commencement of the civil action on this litigation. Mr. Adams has a private attorney who is conducting this litigation on his behalf. While obviously some input from Mr. Adams is necessary to prepare this case, it is not, by its nature, an extremely complex type of litigation. No showing has been made why Mr. Adams could not conduct his ordinary business obligations and simultaneously proceed with the civil litigation.

It is the conclusion of this Court that Debtor has failed to show that the very narrow exception provided to the extension of the automatic stay under §362 should be applicable to either Jack Adams or Zakea Adams. Additionally, the Court concludes that no factual showing has been made to warrant the application of injunctive relief even if a legal basis exists.

### 11 U.S.C. §105

Debtor, alternatively, asks the Court to invoke the Court's general powers under 11 U.S.C. §105 to enjoin the State lawsuit. The Code, under §105(a), provides that: "The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." This section has been interpreted to provide the Court supplemental powers to implement other provisions of the Bankruptcy Code. However, the Bankruptcy Court's power under §105(a) should be exercised sparingly. In re Wengert Transp., Inc., 59 B.R. 226, 231 (Bankr. N.D. Iowa 1986).

An injunction issued under 11 U.S.C. §105 must be consistent with the remainder of the Bankruptcy Code. In re Oxford Management, Inc., 4 F.3d 1329, 1334 (5th Cir. 1993). An injunction issued under this section cannot alter other provisions of the Bankruptcy Code and does not authorize a bankruptcy court to create rights not otherwise available under applicable law. In other words, §105 "does not authorize the bankruptcy courts to create substantive rights that are otherwise unavailable under applicable law, or constitute a roving commission to do equity." United States v. Sutton, 786 F.2d 1305, 1308 (5th Cir. 1986). "The broad latitude afforded bankruptcy courts in fashioning remedies should not be used in a way that tramples on the rights of dissenters among creditors or non-parties to the proceedings." In re Vitek, Inc., 51 F.3d at 538 n.39.

To be entitled to relief under §105(a), a debtor must satisfy the usual requirements governing injunctions and must show a necessity for the relief sought. These elements include proof of: 1) irreparable harm; 2) the likelihood of success of debtor's reorganization; 3) minimal harm to others; and 4) protection of the public interest. In re National Cattle Congress, Inc., 179 B.R. 588, 599 (Bankr. N.D. Iowa 1995).

First, the purported harm involves the amount of time which Mr. Jack Adams would be required to be away from his duties as President and Chief Executive Officer of the Debtor-corporation. The evidence does not support such a finding. From the time the State lawsuit was filed until the hearing on this injunction, Mr. Adams' time spent on the lawsuit has been minimal. The lawsuit is not complex litigation and it is not fair to conclude that excessive amounts of time are required to defend this lawsuit. Second, the success or failure of the reorganization of Debtor-corporation does not appear to have a significant impact on this issue.

Third, in balancing the harm that granting an injunction would inflict on others, a balancing of the equities requires the Court to reject the entry of a temporary injunction. Creditor NBD has rights against Jack and Zakea Adams, who are not debtors in bankruptcy, under their guarantees. Mr. Adams asserts that the reason for seeking the injunction is to allow additional time for his business

operations. However, it is as equally compelling to conclude that Mr. and Mrs. Adams have a personal interest in delaying this lawsuit so they may not be required to honor their personal guarantees. Presumably, if an injunction were issued, Debtor-corporation would benefit because it would have the unrestricted access to Jack Adams' time. Defendants in the State lawsuit, Mr. and Mrs. Adams, would benefit because they would not have to respond to NBD's claim of liability under their personal guarantees. Only NBD would suffer adverse consequences because it would be required to forego collection efforts under the guarantees. Under any weighing of equities, the balance tips unfairly in favor of J.E. Adams Industries, Jack Adams, individually, and Zakea Adams, individually. The Court must conclude that the stated reasons of Debtor are insufficient to warrant the issuance of an injunction.

**WHEREFORE**, the Application for an Injunction by J.E. Adams Industries, Ltd. and against Defendant NBD Equipment Finance, Inc. seeking a stay of the State action captioned NBD Equipment Finance, Inc. v. Jack E. Adams and Zakea Adams, Linn County No. LACV33865, must be and is hereby DENIED.

**SO ORDERED** this 13th day of May, 1999.

Paul J. Kilburg  
U.S. Bankruptcy Judge