

SIGNED.

Dated: November 5, 2012



James M. Marlar

James M. Marlar, Chief Bankruptcy Judge

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7 **UNITED STATES BANKRUPTCY COURT**
8 **DISTRICT OF ARIZONA**

9 In re:

10 GREGORY A. FRIEDMAN and JUDITH
11 MERCER-FRIEDMAN,

12 Debtors.

Chapter 11

No. 4:07-bk-02135-JMM

MEMORANDUM DECISION

13 Before the court is the Debtors' request to confirm their Second Amended Plan of
14 Reorganization, together with its modification (ECF Nos. 156, 180). An evidentiary hearing
15 was held on October 29, 2012. Appearances were noted on the record.

16 The matter, taken under advisement, is now ripe for a ruling.

17
18 **JURISDICTION**

19
20 This dispute presents a core matter over which this court has jurisdiction. 28 U.S.C.
21 § 157(b)(2)(L) (confirmation of plans).

22
23 **PROCEDURE**

24
25 The long and interesting procedural history of this case is well-known to the parties, and
26 need not be repeated at length here. Instead, the court will focus on the matter immediately
27 before it.
28

1 Prior to confirmation, the Debtors eliminated all objections to their Plan, other than that
2 of P+P, LLC, which maintains its opposition to the Debtors' Plan, and seeks to convert the case
3 to one under Chapter 7 (ECF Nos. 175, 213, 315).

4 As an individual Chapter 11 plan¹, the Debtors' Plan is straightforward. Article 8 of the
5 Plan provides:

6
7 Upon Confirmation of the Plan, all of the assets of the Debtors' estate shall be
8 vested in the Debtors and the Debtors shall continue to work in their consulting
9 and business management company. Debtors shall pay all expenses of their
10 personal life, including taxes and insurance costs, on a current basis. The
11 Debtors' disposable income shall be deposited into the Plan Fund and distributed
12 as provided herein.

13 (ECF No. 156). In a "modification" to the Plan, the Debtors detailed exactly what amounts
14 would be distributed as to their disposable income, pursuant to 11 U.S.C. § 1115:

15 1. Paragraph 1.17 of the Plan shall be modified to read as follows:

16 0.1 "Plan Fund" shall mean a fund of money to be deposited into an
17 interest-bearing deposit account for the exclusive use by the Debtors to pay Class
18 2 and 4 Claims. The Plan Fund shall be funded initially from all cash on hand as
19 of the Effective Date, less funds required to pay Claims payable as of the
20 Effective Date in accordance with the Plan. On or before the last day of each
21 month, the Debtors shall deposit their disposable income, as provided in
22 Bankruptcy Code §1325(b)(2) into the Plan Fund, provided however, that the
23 minimum deposit each month shall not be less than the sum of \$1,800 for months
24 1-20 following the Effective date and \$2,300 for months 21-60 following the
25 Effective date.

26 (ECF No. 180). As part of the modification, and consistent with the foregoing, the Debtors
27 further refined Article 8, quoted above:

28 2. Article 8 of the Plan shall be amended to read as follows:

¹ Individual plans are authorized by law. Toibb v. Radloff, 501 U.S. (S.Ct.) 157 (1991); See also, e.g., 11 USC §1115.

1 **THE LAW**

2
3 **A. Sections 1129(a)(1) and (2)--General Compliance**

4
5 **1. In General**

6
7 These sections require that the Plan and Plan proponent (here, the Debtors) have
8 complied with applicable bankruptcy law. This means that the law has been followed
9 throughout the administrative portion of the case, appropriate fees and reports have been
10 tendered, that the court and creditors have been privy to, or have not been denied access to
11 financial information, that in all respects a debtor has been transparent and candid in its
12 communications, and that it or they have materially complied with the substantive bankruptcy
13 statutes and rules.

14 Here, the administrative record supports the finding that these elements have been met.
15 All necessary professionals in the cases have been appointed by the court, fees for those
16 professionals have been disclosed and vetted, and procedures for noticing out the Debtors' Plan
17 with adequate disclosure (§ 1125) have been followed. There has been no assertion that the
18 vote solicitation process has been tainted or is otherwise improper. Therefore, it appears that,
19 in general, these provisions of the Bankruptcy Code have been satisfactorily met.

20 P+P hints that modifications to plans are impermissible. The court disagrees, and to the
21 extent that P+P has objected on this basis, will OVERRULE it.

22 Modifications of plans occur in many different ways, and in many types of factual
23 scenarios. In order for a reorganization case to function as intended--which is to move it
24 forward at a reasonable pace consistent with justice--it is necessary to consider the totality of
25 circumstances when it comes to modifications. The challenge for courts, creditors and
26 attorneys comes, with operating businesses, in the knowledge that nothing remains static, and
27 that constant adjustment is necessary to attempt to reach the correct result at the end of the case.
28 As the courts have noted, because reorganization cases are fluid, there may be shifting

1 alliances, ongoing negotiations and last-minute changes, right up to and sometimes through
2 confirmation. See In Re Woodbrook Assocs., 19 F.3d 312, 322 (7th Cir. 1994): "A special
3 aspect of the practice of bankruptcy is that it functions on a fluid set of facts, i.e., the plan can
4 always be changed. And, for the most part, bankruptcy courts permit the parties to submit
5 numerous and alternative plans. Yet, bankruptcy courts are given a great deal of discretion to
6 say when enough is enough." See also In re Henry Mayo Newhall Mem'l Hosp., 282 B.R. 444,
7 457 (9th Cir. BAP 2002) (Marlar, J., concurring) (considering "all of the fluid factors of an
8 evolving chapter 11 case"); In re Buckner, 218 B.R. 137, 149 (10th Cir. BAP 1998) (Matheson,
9 J., concurring) ("Bankruptcy proceedings are not static; they are fluid and continuing."). This is
10 the reality of a Chapter 11 practice, and it happens every day, and sometimes several times in
11 one day. This court's experience as an attorney, judge and former Ninth Circuit Bankruptcy
12 Appellate Panel judge shows this type of practice to be the rule, not the exception. Were a
13 court to be so rigid in the application of equitable principles that it required that new disclosures
14 and solicitations were needed for every change, it would be extremely difficult to achieve
15 meaningful progress on any given case. Cases would stall as the parties endlessly debated
16 evolving new issues.

17 The procedural history of the Friedman case, alone, is evidence enough to support the
18 modification based on changed circumstances.

19 P+P also argues that it has been improperly classified, because it has been placed in a
20 different class from general unsecured creditors. However, the purpose of § 1122 is to disfavor
21 only unfair discrimination. Here, the Class 5 treatment for the unsecured portion of P+P's claim
22 is that it is treated exactly as are the general unsecured creditors in Class 4:

23 The holder of the Class 5 Claim shall retain its lien on the Breckenridge property
24 to the extent of the value of Property as determined by the Court under 11 U.S.C.
25 §506 (the "Class 5 Allowed Secured Claim"), which claim shall be satisfied from
26 the proceeds (cash or credit bid) of the sale of the collateral at a foreclosure sale
27 by P+P (or a sale by the first lienholder, Washington Mutual). The amount by
28 which the Class 5 Claims exceeds the Class 5 Allowed Secured Claims shall be
allowed as the Class 5 Unsecured Claim. The Class 5 Unsecured Claims shall be
paid pro rata upon the same terms as the Class 4 Claims.

1 (ECF No. 156, Article 7.) Thus, there is no discrimination of one type of unsecured claim
2 versus another. The Ninth Circuit has noted that classifying claims differently is acceptable, so
3 long as there is a reasonable business reason for so doing. See In re Johnston, 21 F.3d 323 (9th
4 Cir. 1994). Here, the reason for different treatment is that P+P's claim was filed as partially
5 secured and partially unsecured (see Claim No. 25). That claim has never been amended.
6 Thus, the court sees no impropriety in treating this combined secured/unsecured claim in the
7 manner done in Class 5. As filed (and never amended), the P+P claim bore no rational
8 similarity to the general unsecured claims of Class 4. As a matter of fact and law, then, §1122
9 was not violated.

10
11 P+P also questions whether the disclosure requirements of §1125 were met. This court
12 finds (and rules) that §1125 presented adequate disclosure, else it would not have approved the
13 disclosure statement in the first place.

14 15 **2. Sections 1129(a)(1) and (a)(2)—Conclusion**

16
17 This objection, then, as to the §§1129(a)(1) and (2) requirements, will be
18 OVERRULED.

19 The court FINDS and CONCLUDES that the Debtors have satisfied §§ 1129(a)(1) and
20 (a)(2) of the Code.

21 22 **B. Section 1129(a)(3)--Good Faith**

23
24 Good faith is an inherent requirement which runs throughout the entire Bankruptcy
25 Code. Because the bankruptcy court is a court of equity, as well as a court of law, and because
26 of the fluidity of bankruptcy proceedings, equity demands a constant balancing of the
27 competing needs of the various constituencies. It is essential that bankruptcy proceedings be
28 transparent, candid and always operate in that spirit.

1 In its most basic sense, "good faith" means honesty in purpose, faithfulness to one's
2 duty or obligation, observance of concepts of fair dealing, and the absence of intent to defraud
3 or to seek unconscionable advantage. BLACK'S LAW DICTIONARY (9th ed. 2009). The
4 bankruptcy definition most commonly applied is that the good faith, that is needed to confirm a
5 plan of reorganization, requires the plan to achieve a result consistent with the objectives and
6 purposes of the Bankruptcy Code. In re Sylmar Plaza, L.P., 314 F.3d 1070, 1074 (9th Cir.
7 2002) (citing In re Corey, 892 F.2d 829, 835 (9th Cir.1989)); In re Stolrow's, Inc., 84 B.R. 167,
8 172 (9th Cir. BAP 1988); In re Jorgensen, 66 B.R. 104, 108-09 (9th Cir. BAP 1986). In order
9 to determine good faith, a court must inquire into the totality of circumstances surrounding the
10 plan, the application of the principal of fundamental fairness in dealing with creditors, and
11 whether the plan itself will fairly achieve a result consistent with the objectives and purposes of
12 the Code. Sylmar Plaza, 314 F.3d at 1074; Stolrow's, 84 B.R. at 172; Jorgensen, 66 B.R. at
13 109; see also In re Kemp, 134 B.R. 413, 414-15 (Bankr. E.D. Cal. 1991); In re Jasik, 727 F.2d
14 1379, 1383 (5th Cir. 1984).

15 P+P raises a concern that the Debtors have not fully disclosed their interests in related
16 affiliates. It then jumps to the conclusion that the affiliates' equity, owned by the Debtors, has
17 value far in excess of what the Debtors have opined to be essentially zero. (See, e.g., P+P
18 Ex. #2.) The Debtors have proven a prima facie case that they have correctly assessed the
19 value of their equity interests in those entities.

20 P+P has failed to present any factual evidence to contradict the Debtors' valuations.

21
22 **Section 1129(a)(3)--Conclusion**
23

24 This Chapter 11 case is progressing as it should, and the court FINDS that the Debtors
25 have presented themselves in the best possible light throughout.

26 The objections on § 1129(a)(3) grounds will be OVERRULED. The Debtors have
27 satisfied this statutory requirement.
28

1 **C. Section 1129(a)(4)--Payments In Connection With the**
2 **Case or Incident to the Case Must Be Approved and Reasonable**
3

4 Typically, this Code section refers to the court's supervision over professional fees. To
5 date, all professionals who are required to do so have applied to the court for fees, or will do so,
6 and will circulate their requests to the primary constituents and the U.S. Trustee, and give
7 parties the opportunity to object. (See, e.g. DN 298, 289, 55)

8 The court has approved fees on an interim basis, and eventually, procedures will be
9 followed to allow the final entry of orders. The Plan allows the court to retain jurisdiction, for
10 this purpose, post-confirmation. (See Plan, at Article 3, ECF No. 156).

11 The court FINDS and CONCLUDES that § 1129(a)(4) has been met by the Plan and its
12 proponents.

13
14 **D. Section 1129(a)(5)--Post-Confirmation**
15 **Officers and Directors, Insiders and Compensation**
16

17 A Chapter 11 plan may not be confirmed if the continuation in management of the
18 persons proposed to serve as officers or managers of debtor is not in the interests of creditors
19 and public policy. § 1129(a)(5)(A)(ii); see In re Beyond.com Corp., 289 B.R. 138, 145 (Bankr.
20 N.D. Cal. 2003) (citing In re Sovereign Group, 1984-21 Ltd., 88 B.R. 325, 329 (Bankr. D.
21 Colo. 1988)). Indeed, continued service by prior management may be inconsistent with the
22 interests of creditors and public policy if it directly or indirectly perpetuates incompetence, lack
23 of discretion, inexperience or affiliations with groups inimical to the best interests of the debtor.
24 Beyond.com, 289 B.R. at 145 (citing In re Polytherm Indus., Inc., 33 B.R. 823, 829 (W.D. Wis.
25 1983)); In re Sherwood Square Assocs., 107 B.R. 872, 878 (Bankr. D. Md. 1989); In re SM 104
26 Ltd., 160 B.R. 202, 245-46 (Bankr. S.D. Fla. 1993) (manager who diverted rents, violated court
27 orders, made misrepresentations to secured creditors, commingled funds and maintained a
28

1 grossly inadequate accounting system, was prohibited by § 1129(a)(5) from continuing in that
2 capacity).

3 No affirmative evidence was brought forth, by any objecting party, from which the court
4 might conclude that § 1129(a)(5)'s requirements were not met. Therefore, the court FINDS that
5 the Debtors have satisfied their burden as to § 1129(a)(5).

6
7 **E. Section 1129(a)(6)--Governmental Rate Control**

8
9 This element of § 1129(a) is inapplicable to these Debtors. No creditor or class raised
10 an objection on this ground, and thus the court finds that § 1129(a)(6) does not apply.

11
12 **F. Section 1129(a)(7)--Best Interests of Creditors Test**

13
14 This section of § 1129(a) requires, with respect to each impaired class of claims or
15 interests, that each holder of a claim or interest in the class either accept the plan or receive
16 under the plan at least as much as it would receive on liquidation. In re Mid Pac. Airlines, Inc.,
17 110 B.R. 489, 491 (Bankr. D. Haw. 1990). This is commonly referred to as the "best interests
18 of creditors test." In re M. Long Arabians, 103 B.R. 211, 216 (9th Cir. BAP 1989).

19 In their Disclosure Statement, the Debtors detailed their best estimation of how creditors
20 would fare in a hypothetical liquidation. For unsecured creditors, that estimated recovery was
21 felt to be zero. (ECF No. 157 at 6-7).

22 Although objecting on this basis, P+P failed to present any evidence to contradict this
23 estimate.

24 P+P's objection, on § 1129(a)(7) grounds, will be OVERRULED.

25 The Debtors have therefore sustained their burden of proof relative to § 1129(a)(7), and
26 that element of § 1129 has been satisfied.

1 **J. Section 1129(a)(11)--Feasibility**

2
3 Feasibility is the heart of every Chapter 11 reorganization case. It is the most important
4 element of § 1129(a). Section 1129(a)(11) permits confirmation only if:

5
6 Confirmation of the plan is not likely to be followed by the liquidation, or the
7 need for further financial reorganization, of the debtor or any successor to the
8 debtor under the plan, unless such liquidation or reorganization is proposed in the
9 plan.

10 "The purpose of section 1129(a)(11) is to prevent confirmation of visionary schemes which
11 promise creditors and equity security holders more under a proposed plan than the debtor can
12 possibly attain after confirmation." In re Pizza of Haw., Inc., 761 F.2d 1374, 1382 (9th Cir.
13 1985) (quoting 5 COLLIER ON BANKRUPTCY ¶ 1129.02[11], at 1129-34 (15th ed. 1984)).

14 "A plan meets this feasibility standard if the plan offers a reasonable prospect of success
15 and is workable. . . .The prospect of financial uncertainty does not defeat plan confirmation on
16 feasibility grounds since a guarantee of the future is not required. . . . The mere potential for
17 failure of the plan is insufficient to disprove feasibility." In re Patrician St. Joseph Partners Ltd.
18 P'ship, 169 B.R. 669, 674 (D. Ariz. 1994).

19 Every debtor is required to present "ample evidence to demonstrate that the Plan has a
20 reasonable probability of success." In re Acequia, Inc., 787 F.2d 1352, 1364 (9th Cir. 1986);
21 see also 7 COLLIER ON BANKRUPTCY ¶ 1129.02[11], at 1129-52, (16th ed. 2012). Section
22 1129(a)(11) "requires the plan proponent to show concrete evidence of a sufficient cash flow to
23 fund and maintain both its operations and obligations under the plan." Id. at 1129-53 (citation
24 omitted). In order to determine whether § 1129(a)(11) is satisfied, a court must "scrutinize the
25 plan to determine whether it offers a reasonable prospect of success and is workable." In re
26 Sagewood Manor Assocs. Ltd. P'ship, 223 B.R. 756, 762 (Bankr. D. Nev. 1998). Plans which
27 are based on speculation are not proper candidates for reorganization. Pizza of Haw., supra.

28 In evaluating the feasibility of a plan, the Ninth Circuit's BAP has directed courts to
consider several factors, including: (1) the adequacy of the capital structure; (2) the earning

1 power of the business; (3) economic conditions; (4) the ability of management; (5) the
2 probability of the continuation of the same management; and (6) any other related matters
3 which determine the prospects of a sufficiently successful operation to enable performance of
4 the provisions of the plan. In re Wiersma, 324 B.R. 92, 113 (9th Cir. BAP 2005), aff'd in part
5 and rev'd in part on other grounds, 483 F.3d 933 (9th Cir. 2007).

6 This Plan, proposed by individual debtors, is one which simply commits future
7 disposable income to its creditors, as § 1115 requires, and specifies what that return will be.
8 No evidence was presented to dispute the Debtors' projections.

9 The Debtors proved 11 U.S.C. § 1129(a)(11).

10 11 **K. Section 1129(a)(12)--Fees**

12
13 The U.S. Trustee has not objected on the grounds that its fees, or related fees, are
14 unpaid. No creditor has suggested that compliance with this section has not been met.

15 The court therefore finds and concludes that this provision of the Code has been
16 satisfied.

17 18 **L. Section 1129(a)(13)--Retiree Benefits**

19
20 This section is not applicable to these Debtors.

21 22 **M. Section 1129(a)(14)--Domestic Support Obligations (Alimony; Child Support)**

23
24 This section is not applicable to these Debtors.

1 In this case, the Debtors have elected not to retain their Breckinridge property, against
2 which P+P holds a lien. Thus, P+P's secured portion is to be returned to it, in full satisfaction
3 of the collateralized feature. The Plan's treatment, then, is a "fair and equitable" one.
4 Receiving collateral back is the "indubitable equivalent" of the secured portion.
5 § 1129(b)(2)(A)(iii).

6 As for the unsecured component of the P+P claim, it is to be paid in the same percentage
7 as Class 4 unsecured creditors. However, this will not be equal to 100% of the unsecured
8 portion.

9 Were this a corporate or entity case, the "absolute priority rule" would potentially defeat
10 a debtor's retention of any non-exempt property, unless the debtor infused "new value."
11 However, as we now know, the absolute priority rule does not apply to this case. In re
12 Friedman, 466 B.R. 471 (9th Cir. BAP 2012). This is because the debtors are individuals.

13
14 **CONCLUSION**
15

16 Based on the entire record in this case, the court FINDS AND CONCLUDES that
17 Debtors' Second Amended Plan (and its modification) may be confirmed.

18 Counsel for the Debtors shall present an appropriate form of order within 15 days
19 (attaching a grid or matrix as to the final iteration of class treatment).

20
21 DATED AND SIGNED ABOVE.
22

23 To be NOTICED by the BNC ("Bankruptcy Noticing Center") to:

24 Attorney for Debtors
25 Duncan E. Barber, Attorney for P+P, LLC
26 Office of the U.S. Trustee
27
28