

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF:)	CASE NO. BK02-80974-TJM
)	
BROOK VALLEY IV JOINT VENTURE,)	
)	CH. 7
Debtor.)	
-----)	
IN THE MATTER OF:)	CASE NO. BK02-80973-TJM
)	
BROOK VALLEY VII JOINT VENTURE,)	
)	CH. 7
Debtor.)	

ORDER

On February 3, 2006, after a two-day trial, an order was entered in favor of the Chapter 7 trustee in each of these cases and against Robert Schropp, Leo Dahlke, and others. The order indicated that the defendants, who operated the partnership as debtors in possession, improperly bid at a foreclosure sale of bankruptcy estate property. The order found that such bidding by insiders always is a violation of a fiduciary duty. However, on appeal, the circuit court did not find that such bidding and purchase of estate property is always a violation of fiduciary duty, but did find, under the facts in this case, that the insiders violated their fiduciary duty of loyalty.

Following the entry by this court of the order in favor of the trustee, an order was entered on February 3, 2006, at Filing #83, which directed the attorneys for the debtors in possession to explain their actions which appeared to this judge to have aided the defendants in violating their duties to the bankruptcy estates.

All three attorneys filed declarations, with Mr. Biggs' being filed under penalty of perjury and Mr. Slusky's and Ms. James' declarations being filed as "true and accurate to the best of my memory, knowledge and belief."

On March 14, 2006, an order was entered acknowledging that the original order in favor of the trustee had been appealed and stating that no further action on any issues concerning Mr. Slusky, Ms. James, and Mr. Biggs would be taken until the appeal process is complete. The appeal process in federal court was complete with the entry of an opinion by the circuit court on August 6, 2007. However, at that time there was still pending in the District Court of Douglas County, Nebraska, litigation between the defendants and their bankruptcy counsel. That litigation has now been completed and so the matter is ripe for review.

I have once again reviewed all of the documents in the cases which led me to my concern about the activities of the attorneys. The documents are filed in both cases, but for this order only those appearing in Case No. BK02-80973-TJM will be discussed. Those documents include the following:

1. Motion for Approval of Stipulation and Agreed Order Granting Relief from the Automatic Stay, Filing #6, filed April 19, 2002;
2. Objection and Resistance to Motion for Reconsideration & for Appointment of Trustee, Filing #19, filed June 17, 2002;

3. Report of Trust Deed Foreclosure Sale, Filing #26, filed September 26, 2002;
4. Objection and Resistance to Motion to Set Aside Order for Relief and for Appointment of Trustee, Filing #39, filed January 3, 2003;
5. Affidavit of Robert C. Schropp, Filing #43, filed January 14, 2003;
6. Declaration of Shaun M. James, Filing #84, filed March 1, 2006;
7. Declaration of Jerry M. Slusky, Filing #85, filed March 1, 2006;
8. Declaration of William L. Biggs, Filing #87, filed March 1, 2006;
9. Status Report filed by the United States Trustee, Filing #116, including twenty-three attachments, filed May 19, 2008;
10. Supplemental Declaration of Jerry M. Slusky, Filing #125, including five attachments, filed June 10, 2008;
11. Status Report filed by the United States Trustee, Filing #140, filed February 26, 2009;
12. Status Report filed by the United States Trustee, Filing #141, filed May 22, 2009; and
13. Lange v. Schropp (In re Brook Valley VII Joint Venture), 496 F.3d 892 (8th Cir. 2007).

When I entered the original order requiring the attorneys to explain their actions, I contemplated imposing sanctions, monetary or otherwise, for what I perceived to be improper conduct directly resulting in harm to the bankruptcy estates. However, after a review of all of the above-listed materials, I conclude that no sanctions are appropriate other than the expression of my extreme disappointment concerning the communication of information between the lawyers, who, although from two different law firms, all appeared as counsel of record representing the debtors in possession in these bankruptcy estates.

The materials submitted by Mr. Slusky and Ms. James assert they believed that once relief from the automatic stay was granted, the real estate in question was no longer property of the bankruptcy estate and that under state law, anybody, including the defendants, in their own name or using an entity of some sort, were free to bid at the foreclosure sale and purchase the property for their own benefit. They also assert that their function in the cases was to deal with finance and real estate issues and that all bankruptcy matters were handled by Mr. Biggs. According to them, no one ever suggested that it was improper or a breach of fiduciary duty for the defendants to act on their own behalf and purchase the property.

Mr. Biggs claims he did not know that the defendants, with the help of Mr. Slusky and Ms. James, were setting up the purchasing entity and participating in the foreclosure sale as a purchaser. He claims that when the sale was complete, he contacted Ms. James to obtain the sale price and the name of the purchaser. He was not made aware that the purchaser was actually an entity controlled by the defendants and was not made aware that the defendants purchased the second lien rights of Darland and credit-bid those rights. As a result of his lack of knowledge, the report of sale he filed was inaccurate.

In the deposition of Mr. Slusky taken in the state court litigation, he claims Mr. Biggs knew all about the plan to put the real estate into foreclosure, set up a purchasing entity, and purchase the property. It is clear from Attachment 24 in Filing #116, a letter from Mr. Biggs to the defendants on April 2, 2002, before relief from stay was granted, that Mr. Biggs at least anticipated the process with regard to another partnership.

In the declaration filed by Mr. Biggs, he informs that once he became aware of the insider purchases, he was not concerned because of his knowledge of case law that allowed such purchase.

Giving all of the lawyers the benefit of the doubt on the "I didn't know" defense, what must be said is that the manner in which they communicated with each other and with the court in these cases is not the standard which is expected of attorneys acting as co-counsel in cases in this court. If any of the lawyers would have informed the court prior to the sale that the insiders were planning to buy the estate property there could have been a discussion about the propriety of doing so, and, perhaps, all of the litigation could have been avoided.

My original inclination to enter sanctions against the attorneys was based upon my belief that a purchase of estate property by an insider was always improper, if not criminal under 18 U.S.C. § 154. The Court of Appeals did not go that far, but did find, based upon the facts, that there had been a breach of the duty of loyalty by the defendants. Under the decision of the Court of Appeals, it is entirely possible that, given the right circumstances, insiders' purchases of estate property would not be a breach of fiduciary duty. Since it is now clear that the issue of "breach of fiduciary duty" with regard to insider purchases of estate property should be decided on a case-by-case basis, sanctioning attorneys for giving legal advice based upon their understanding of the law is not appropriate.

As far as this judge is concerned, this matter is closed.

DATED: June 8, 2009

BY THE COURT:

/s/ Timothy J. Mahoney
United States Bankruptcy Judge

Notice given by the court to:

William L. Biggs	Robert J. Bothe
Anne M. Breitzkreutz	Robert F. Craig
Shaun M. James	Rick D. Lange
Frank M. Schepers	Marion Pruss
Michael Roy Peterson	
U.S. Trustee	