

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF:)
)
FRANK & HUCK TRADING COMPANY,) CASE NO. BK01-41308
)
Debtor(s).) CH. 12

MEMORANDUM

Hearing was held in Lincoln on July 2, 2001, on Platte Valley Ag Company's Motion to Dismiss this case (Fil. #7) and Objection by the debtor (Fil. #13). Arlan Wine and Randy Eckhardt appeared on behalf of the debtors. John Selzer represented the movant. Jerry Jensen represented the United States Trustee. This memorandum contains findings of fact and conclusions of law required by Fed. R. Bankr. P. 7052 and Fed. R. Civ. P. 52. This is a core proceeding as defined by 28 U.S.C. § 157(b)(2)(A).

The motion to dismiss challenges the ability of Frank & Huck Trading Company to be a debtor as defined by the Bankruptcy Code. The debtor characterizes itself as a business trust, which is an entity that may be a debtor under the terms of the Bankruptcy Code, but the moving creditor here suggests that Frank & Huck Trading Company does not meet the definition of a business trust as contemplated by Title 11.

The case was filed under Chapter 11 and subsequently converted to a Chapter 12. Under 11 U.S.C. § 109, only a "person" who may be a debtor under Chapter 7 may be a debtor under Chapter 11, and only a "family farmer" may be a debtor under Chapter 12. Under the definitional provisions of § 101, "family farmer" includes individuals, partnerships, or corporations which meet certain requirements. § 101(18). A "person" may be an individual, a partnership, or a corporation. § 101(41). A corporation includes

- an association having a power or privilege that a private corporation, but not an individual or a partnership, possesses;
- a partnership association organized under a law that makes only the capital subscribed responsible for the debts of such association;

- a joint-stock company;
- an unincorporated company or association; or
- a business trust.

§ 101(9)(A).

Thus, a business trust may be a debtor, but any other type of trust may not.

The Bankruptcy Code does not define a business trust, however, so courts have interpreted the section as reflecting a Congressional intent to offer bankruptcy protection to those entities which have the attributes of a corporation, but not to trusts in general. Accordingly, a number of characteristics have been identified to distinguish business trusts from non-business trusts. The foremost factor seems to be whether the trust was created and is maintained "for a business purpose." Additional distinguishing factors include title to the property held by a trustee; centralized management; continuity uninterrupted by death of the beneficial owners; transferable certificates of interest; and limited liability. In re Betty L. Hays Trust, 65 B.R. 665, 668 (Bankr. D. Neb. 1986) (citing the tax case of Morrissey v. Commissioner, 296 U.S. 344 (1935)). See also Lewis v. Haworth (In re Haworth), 253 B.R. 478, 481-82 (Bankr. D. Wyo. 2000); In re Owners Family Preservation Trust, No. 91-00004, 1991 WL 408009, at *1 (D. N. Mar. I. May 13, 1991); In re Constitutional Trust #2-562, 114 B.R. 627, 631 n.12 (Bankr. D. Minn. 1990); In re Margaret E. DeHoff Trust I, 114 B.R. 189, 191 (Bankr. W.D. Mo. 1990).

A trust created to transact business for the benefit or profit of investors holding transferable certificates representing interests in the trust is likely a business trust. Put another way,

The business trust is a voluntary pooling of capital by a number of people who are the holders of freely transferrable certificates evidencing beneficial interests in the trust estate. The holders are entitled to the same limitation of personal liability extended to stockholders of private corporations. Because of the similarity, Congress has afforded the business trust the same privileges in bankruptcy as a private corporation.

In re Nellie M. Hurst Trust, No. 97-1-4562-PM, 1997 WL 412168, at *3-4 (Bankr. D. Md. June 23, 1997) (quoting In re Morgantown

Trust No. 1, 155 B.R. 137, 143 (Bankr. N.D. W.Va. 1993)).

The court deciding the Hurst Trust case consulted Am. Jur. for a definition of "business trust":

Indeed, the profit-making function is one of the most significant characteristics of the business trust. Title to the capital of the organization is vested in trustees, who usually manage the affairs of the trust. The beneficial interests in the trust estate and in the profits are evidenced by transferable certificates, similar to corporate shares, and the existence or life of the organization is not affected by the death or disability of a member or shareholder or by the sale or transfer of his interest.

In re Nellie M. Hurst Trust, 1997 WL 412168 at *2 (quoting 13 Am. Jur. 2d Business Trusts § 3 (1964)).

In fact, the Bankruptcy Act's definition of "corporation" is substantially similar to § 101(9)(A), but instead of "business trust," it refers to "any business conducted by a trustee or trustees wherein beneficial interest or ownership is evidenced by certificate or other written instrument." Associated Cemetery Mgmt., Inc. v. Barnes, 268 F.2d 97, 100-01 (8th Cir. 1959).

"[A] basic distinction between a business trust and other trusts is that business trusts are created for the purpose of carrying on some kind of business, whereas the purpose of a non-business trust is to protect and preserve the res." Shawmut Bank Conn., N.A. v. First Fid. Bank (In re Secured Equip. Trust of Eastern Air Lines, Inc.), 38 F.3d 86, 89 (2d Cir. 1994).

However, business activity by the trust, without more, does not mean that the trust is a business trust. Such a determination is based on a fact-specific analysis of the trust at issue. Id.

In this case, the debtor states that its entire function has been to engage in the business of custom haying, and that its trust document was purposely drafted in vague terms to permit flexibility.

The trust agreement in evidence displays very few of the

characteristics of a business trust. The trust property, at least at the time the trust was created, consisted of cash, to be held, managed, invested and reinvested by the trustee for the benefit of Erik and Derik Eckhardt. The trust will terminate upon the death or the 100th birthday of either beneficiary. The trust contains a spendthrift provision to prevent the transfer or encumbrance of the trust property by a beneficiary.

The language of the trust document does not express an intent to conduct a business or commercial activity. The trust does not continue uninterrupted by the death of a beneficiary. The beneficiaries' interests in the trust are not transferable, and there are no "freely transferable certificates" representing the beneficiaries' ownership rights.

In the Secured Equipment Trust of Eastern Air Lines case, a group of investors formed a trust to fund the purchase of the airline's fleet of aircraft and lease the fleet back to the airline. The income from the lease of the airplanes was expected simply to cover the investment, with any excess amounts to be returned to the airline. Upon payment in full by Eastern of the trust's investment, title to the fleet would be reconveyed to Eastern and the trust would be dissolved. Eastern ultimately filed bankruptcy and defaulted on its lease. The trust then began actively managing, maintaining, marketing, leasing and liquidating the fleet. Three investors in the trust subsequently filed an involuntary Chapter 11 petition against the trust.

The Second Circuit Court of Appeals affirmed the dismissal of the trust's bankruptcy because the trust was not eligible to be a debtor. It reasoned that the trust "was established merely to secure the repayment of the [investors'] loans to Eastern. As such, its purpose was to preserve the interest that the certificateholders has already been guaranteed, not to generate it." 38 F.3d at 90 (emphasis in original). Moreover, the court said, "[a]ny business activities that the Trust is currently engaged in are incidental to the Trust's sole responsibility of protecting the certificateholders' security interest." Id.

Therefore, even if a trust engages in business activities, it may not be a business trust if it was not established for the purpose of transacting business. Where, as here, the trust's purpose is the protection and preservation of the trust property, even though business activities may be part and parcel of doing so, it is not a business trust.

Despite the debtor's argument here that a lender should know it is a business trust because it borrowed working capital to conduct the farming operation, there is no evidence that the lender knew or should have known what type of trust the debtor is, or that the lender had reason to believe the trust was anything other than a traditional trust.

The Frank & Huck Trading Company appears to be designed to preserve the trust res for its beneficiaries. It does not meet the requirements of a business trust, and it cannot be a debtor under the Bankruptcy Code.

IT IS ORDERED Platte Valley Ag Credit Company's Motion to Dismiss (Fil. #7) is granted.

Separate journal entry to be filed.

DATED: August 6, 2001

BY THE COURT:

/s/Timothy J. Mahoney
Timothy J. Mahoney
Chief Judge

Copies faxed by the Court to:

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Arlan Wine, Atty. for Debtor, (308)345-4353

Copies mailed by the Court to:

United States Trustee
Richard Lydick, Chap. 12 Trustee

Movant (*) is responsible for giving notice of this journal entry to all other parties not listed above if required by rule or statute.

Movant (*) is responsible for giving notice of this journal entry to all other parties (that are not listed above) if required by rule or statute.