FILED
DISTRICT OF NEBRASKA
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William L. Olson, Clerk
By ____ Deputy

IN THE UNITED STATES DISTRICT COURT FOR THE

DISTRICT OF NEBRASKA

IN THE MATTER OF:	
MAHLOCH FARMS, INC., HARVEY MAHLOCH and ALICE MAHLOCH,	CV. 85-0-107 BK. 828-669 & 670
Debtors.	MEMORANDUM OPINION

This matter is presently before the Court on appeal from an order of the United States Bankruptcy Court for the District of Nebraska entered on January 11, 1985. The appellants, C. G. Wallace, III, Trustee (hereinafter Trustee) and Saline State Bank appeal the bankruptcy court's order denying Trustee's motion to approve a compromise agreement with Saline State Bank. This Court, after carefully reviewing the record submitted on appeal and the briefs filed by the respective parties, is of the view that the January 11, 1985, order of the bankruptcy court should be reversed and remanded for proceedings consistent with this opinion.

The somewhat complex facts, as summarized, are these. During April of 1982, Harvey and Alice Mahloch filed a joint petition under Chapter 11 of the United States Bankruptcy Code in Bankruptcy Court for the District of Nebraska. Mahloch Farms, Inc., a Nebraska corporation, through which Harvey Mahloch did business, filed under Chapter 11 at approximately the same time.

Each estate was procedurally consolidated soon thereafter. The Trustee was appointed to administer the estate of Harvey Mahloch, Alice Mahloch, and Mahloch Farms, Inc., on August 31, 1982.

Saline State Bank is a major creditor of each estate with claims and assigned claims stated in the previously mentioned compromise agreement as being in excess of $9 million. The claims are alleged to be both secured and unsecured. With respect to several of the Bank's claims, a joint adversary proceeding was commenced during the early stages of estate administration by the Official Creditor's Committee and the Trustee, sounding two causes of action. The first cause of action states preferential transfers occurred between each debtor and the Bank. The second cause seeks to equitably subordinate the claims of Saline State Bank to those of various other creditors. Thereafter, the Trustee filed a separate suit against the bank in August of 1984. The suit involves additional alleged preferential transfers. The Trustee insists both adversary proceedings are complex in nature and could take up to two weeks to try.

Discovery had been conducted in both suits and the cases were proceeding towards trial when, on October 18, 1984, Saline State Bank and the Trustee entered into a compromise agreement. Therein the Trustee agreed to dismiss the litigation against the bank in exchange for Saline's agreement to withdraw

its claims against the consolidated estates. As a result, the creditor would receive close to $600,000 in settlement of its claims.

On January 11, 1985, a hearing was held on the Trustee's motion to approve the above-outlined compromise. The Trustee and Saline State Bank, through their respective counsel, argued in favor of the compromise. First National Bank of Chicago, American Ag Credit Corporation, and the Official Creditors Committee, through respective counsel, appeared in opposition to the compromise. No evidentiary hearing was held on the matter, even though one was requested by most of the parties involved. Following the hearing and oral argument on the motion to approve a compromise, the Honorable David L. Crawford, Bankruptcy Judge, denied said motion and entered his decision on the record. Thereafter, the Trustee and Saline State Bank filed a timely joint appeal which is now before this Court.

Before this Court addresses the merits of the appeal, it is prudent to state the general standard of review that guides the Court in matters such as this. Although on appeal the bankruptcy judge's findings of fact are generally entitled to stand unless clearly erroneous, where there are presented mixed questions of law and fact, the clearly erroneous rule is not applicable, In re American Beef Packers, Inc., 457 F.Supp. 313, 314 (D.Neb. 1978), and the bankruptcy judge's decision cannot be

approved without this Court's independent determination of the law. In re Werth, 443 F.Supp. 738, 739 (D.Kansas 1977), citing Stafos v. Jarvis, 477 F.2d 369, 372 (10th Cir.), cert. denied, 414 U.S. 944 (1973).

With this standard in mind, this Court must now determine whether the bankruptcy court erred in denying the Trustee's motion to approve a compromise. At the conclusion of the January 11, 1985, non-evidentiary hearing, the bankruptcy court entered its decision on the record:

> The easiest thing for me to do is to make a non-decision, by setting this for evidentiary hearing, but the fact of the matter is that that isn't going to do anybody any good at all.
>
> The only way to determine whether this is a good compromise is to try the issues, and determine who wins and who loses, and then decide whether this is a good compromise, and that's the only kind of evidentiary hearing that will be anything fruitful at all. I don't see any particular point in doing that.
>
> This is not a reorganization in the sense that there will be Mahloch Farms, reorganized. This is a liquidation and everyone seems to view it as such. The result is that we have not the catalyst of what is best for the new debtor. We are talking, very simply, about where the dollars are. The creditors think they are in litigation, and while I agree that the question of litigation with regard to solvency is always up for grabs -- well, not always, but in this case, certainly it is -- the creditors want to litigate, and I am inclined to let them litigate, at least at this point.

Tr. at 21-22.

In its brief in support of the January 25, 1985, bankruptcy court decision, First National Bank of Chicago argues Judge Crawford had sufficient information before him to disallow the compromise agreement. The Trustee, however, contends that the court had amassed an insufficient factual foundation in reaching its conclusion and thus, it was an abuse of discretion to deny the Trustee's motion to approve the compromise agreement. This Court agrees with the latter point of view.

The proposed compromise agreement was before the bankruptcy court pursuant to Bankruptcy Rule 9019(a), which allows the Court to approve compromises after Trustee's motion and hearing. The parties to this dispute correctly indicate that such a decision lies within the discretion of the bankruptcy court. **Matter of Aweco, Inc.**, 725 F.2d 293, 297 (5th Cir.), **cert. denied**, ___ U.S. ___, 105 S.Ct. 244 (1984); **In re Hallet**, 33 B.R. 564, 565 (Bankr. D. Me. 1983). An appellate court will reverse only when that discretion has been abused. **Matter of Aweco, Inc., supra**, 725 F.2d at 297; **Matter of Ocoboch**, 608 F.2d 1358, 1360 (10th Cir. 1979).

In evaluating a compromise the bankruptcy court need not conduct an exhaustive investigation into the asserted claims against the estate, nor must it conduct a mini-trial on the merits to be compromised. **See, Matter of Walsh Constr.**, 669 F.2d 1325, 1328 (9th Cir. 1982). The court, however, should consider all factors involved

to determine whether the compromise is in the best interests of the debtor's estate. In re Lakeland Dev. Corp., 48 B.R. 85, 89 (Bankr. D.Minn. 1985). In the Lakeland case, the bankruptcy judge went on to state:

> [t]he factors the Bankruptcy Court is to consider when reviewing proposed settlements or compromises have been set out by the Eighth Circuit Court of Appeals in Drexel v. Loomis, 35 F.2d 800 (8th Cir. 1929). The Drexel criteria include:
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> 1) The probability of success in litigation;
>
> 2) The difficulties, if any, to be encountered in the matter of collection;
>
> 3) The complexity of the litigation involved, and the expense, inconvenience and delay necessarily attending it;
>
> 4) The paramount interests of the creditors and the proper deference to their reasonable views in the premises.
>
> Id. at 89-90.

In his decision, Judge Crawford does not squarely address any of these four factors. Moreover, the record of the hearing does not clearly support or negate any of the above-mentioned factors. The Trustee in its oral argument and its appellate brief argues that the compromised claims involve complex issues that could take up to two weeks to try with at best a moderate chance of success for each. The creditors who opposed the agreement, however, argued that it would be in the best interests of the estate for the compromise to be

denied in that there was a high probability of success on the issue of preferences and a probability of success on the equitable subordination issue. Each argument is proper for consideration by a bankruptcy judge in evaluating a compromise agreement. Each argument fails, however, for lack of facts in support. The record sheds no light on the probability of success of the claims in question nor does it indicate how complex the claims actually are. To properly evaluate the factors set forth in **Drexel**, the bankruptcy court must collect some facts pertaining thereto.

Moreover, Judge Crawford seemed to place a great deal of emphasis on the creditors' wishes with respect to litigating the claims. Consideration of the creditors' wishes is clearly appropriate under the standard set forth in **Drexel**. Creditors' objections to a compromise agreement, however, are not controlling. Id. at 90, citing **In re Hallet, supra**, 33 B.R. at 566. The bankruptcy judge should consider creditor objections as well as the three other factors set forth in **Drexel**. Therefore, some evidence pertaining to all four factors must be heard by the bankruptcy court before a proper informed decision can be made with respect to a proposed compromise agreement. Failure to hear such evidence by the court below was clearly an abuse of discretion.

On remand, the bankruptcy judge should examine the following factors: (1) the probability of success in litigation of the claims against Saline State Bank; (2) the difficulties, if any,

to be encountered in the matter of collection, and whether this factor even applies to this dispute; (3) the complexity of the litigation involved, and the expense, inconvenience and delay necessarily attending to it; and (4) the interests of the creditors.

Accordingly, an order reversing the January 11, 1985, decision of the bankruptcy court will be entered contemporaneously with this memorandum opinion.

DATED this 28th day of August, 1985.

BY THE COURT:

C. ARLEN BEAM
UNITED STATES DISTRICT JUDGE