SO ORDERED,

Judge Jamie A. Wilson
United States Bankruptcy Judge
Date Signed: March 23, 2023

The Order of the Court is set forth below. The docket reflects the date entered.

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF MISSISSIPPI

IN RE:

RE-BUILD SEVILLE, LLC, **CASE NO. 22-01976-JAW**

DEBTOR. **CHAPTER 11**

ORDER GRANTING MOTION TO DISMISS
BANKRUPTCY CASE FOR CAUSE AS "BAD FAITH" FILING

This matter came before the Court for hearing on February 14, 2023 and March 7, 2023 (the "Hearing"), on the Motion to Dismiss Bankruptcy Case for Cause as "Bad Faith" Filing (the "Motion to Dismiss") (Dkt. #66) filed by Fairview Investment Fund V, LP ("Fairview"); the Debtor Re-Build Seville, LLC's Objection to Fairview Investment Fund V, LP's Motion to Dismiss Bankruptcy Case for Cause as "Bad Faith" Filing (the "Response") (Dkt. #80) filed by the debtor, Re-Build Seville, LLC (the "Debtor"); and the Reply in Support of Motion to Dismiss Bankruptcy Case for Cause as "Bad Faith" Filing (the "Reply") (Dkt. #82) filed by Fairview in the above-referenced bankruptcy case (the "Bankruptcy Case"). At the Hearing, Alan L. Smith represented Fairview and G. Adam Sanford represented the Debtor. One witness testified, J. Stephen Tracy ("Tracy"), who is the Debtor's manager, and twelve exhibits were introduced into evidence.[1] The

[1] The exhibits introduced into evidence are cited as "(Ex. #)".

parties stipulated to the admissibility of nine exhibits. Five of these exhibits are documents filed in the Chancery Court of Hinds County, Mississippi (the "State Court"), in Civil Action #25CH1:22-cv-00338 (the "State Court Action"), as follows : (1) the Verified Complaint for Accounting, Appointment of a Receiver, Injunctive Relief, Judicial Foreclosure, and Other Related Relief (the "State Court Complaint") (Ex. 1) filed by Fairview; (2) the Defendants' Answer to Plaintiff's Verified Complaint for Accounting, Appointment of a Receiver, Injunctive Relief, Judicial Foreclosure, and Other Related Relief; Counterclaim Against Fairview Investment Fund V, LP; and Cross-Claim Against Vulcan Industries, LLC (the "State Court Answer & Counterclaim") (Ex. 2) filed by the Debtor; (3) the Defendants' Motion to Hold in Abeyance and for Plaintiff to Provide Sum Certain Payoff (the "State Court Abeyance Motion") (Ex. 3) filed by the Debtor; (4) the Notice of Motion Hearing (the "State Court Hearing Notice") (Ex. 4); and (5) the State Court Civil Docket (Ex. 5). As to the State Court Complaint, the Debtor's counsel clarified at the Hearing on March 7, 2023 (the "March 7 Hearing") that the Debtor stipulated only that the pleading had been filed and not to the truth of Fairview's allegations contained in the pleading. (Hr'g at 1:33-1:34 (Mar. 7, 2023)).[2] The remaining four stipulated exhibits are: (1) the Appraisal Report dated April 21, 2022 (the "April 2022 Appraisal") (Ex. 6) obtained by the Debtor; (2) the Broker Opinion of Value (the "Broker's Opinion") (Ex. 7) obtained by the Debtor in February 2023; (3) an email dated September 14, 2022 from counsel for Fairview to Vulcan (Ex. 8); and (4) the proof of claim filed by Fairview in the Bankruptcy Case (the "Proof of Claim") (Cl. #1-1; Ex. 9). The Debtor introduced into evidence three additional exhibits: (1) a payoff letter from CLS to Vulcan dated September 28, 2021 (CLS's Payoff Letter") (Ex. 10); (2) the Second Mortgage Deed of Trust in favor of Vulcan (Ex. 11); and (3) a payoff statement from Fairview to Vulcan dated April 14, 2022

[2] The Hearing was not transcribed. Citations are to the timestamp of the audio recording.

(Fairview's Payoff Statement") (Ex. 12). Having fully considered the matter and being fully advised in the premises, the Court finds as follows:[3]

Jurisdiction

This Court has jurisdiction over the parties to and the subject matter of this proceeding pursuant to 28 U.S.C. § 1334. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A) and (O). Notice of the Hearing was proper under the circumstances.

Facts

On March 30, 2017, Vulcan Industries, LLC ("Vulcan") borrowed $1,387,500.00 from Bayview Loan Servicing, LLC ("Bayview"). (Cl. 1-1, Part 2). Repayment of the loan was secured by a first deed of trust on an apartment complex, known as the Seville Apartments, in Jackson, Mississippi. (Cl. 1-1, Part 3). The promissory note provided for an initial fixed interest rate of 8.75%. (Cl. 1-1, Part 2). Beginning May 1, 2022, the interest rate converted to a variable rate of 5% above the Prime Rate as published in *The Wall Street Journal* (then 3.75%). (Cl. 1-1, Part 2). After any default, the interest rate increased an additional 10%. Shortly after loaning the money, Bayview changed its corporate name and became known as Community Loan Servicing, LLC ("CLS").

Beginning January 1, 2021, Vulcan purportedly became behind in its payments on the loan. (Ex. 12). The Debtor suggested at the Hearing that CLS had placed the loan into a forbearance status during the COVID-19 pandemic. (Hr'g at 3:47-3:48 (Mar. 7, 2023)).

[3] The following findings of fact and conclusions of law are made pursuant to Rules 7052 and 9014(c) of the Federal Rules of Bankruptcy Procedure. To the extent any of the following findings of fact are determined to be conclusions of law, they are adopted, and shall be construed and deemed conclusions of law. To the extent any of the following conclusions of law are determined to be findings of fact, they are adopted, and shall be construed and deemed, as findings of fact.

Debtor's Purchase of the Seville Apartments

The Debtor, a Mississippi limited liability company, was formed in 2021 for the sole purpose of purchasing the Seville Apartments from Vulcan as an investment property. (Hr'g at 2:16-2:17 (Mar. 7, 2023)). Tracy, the Debtor's manager, conducted the sale negotiations with Vulcan. (Hr'g at 2:19 (Mar. 7, 2023)). Because the Debtor intended to purchase the Seville Apartments subject to CLS's deed of trust, the Debtor engaged a title company to determine the amount of the lien. (Hr'g at 2:20 (Mar. 7, 2023)). The title company sent Tracy a copy of CLS's Payoff Letter addressed to Vulcan. (Ex. 10). According to CLS's Payoff Letter, Vulcan owed $1,412,355.79, consisting of a principal balance of $1,330,608.33, regular interest through December 1, 2021 of $55,564.40, late fees of $921.03, and "[o]ther fees" of $31,121.03. (Ex. 10). CLS apparently did not charge Vulcan any interest at the default rate. (Hr'g at 3:46-3:47 (Mar. 7, 2023)). CLS's Payoff Letter contains the following disclaimer: "Note holder reserves the right to adjust these figures and refuse any funds which are insufficient to pay the loans in full or for any reason, including but not limited to error in calculation of payoff amount." (Ex. 10). CLS assigned the deed of trust to Fairview pursuant to an assignment signed by CLS on September 15, 2021 but not recorded in the land records until October 7, 2021. (Cl. 1-1, Part 4). That same day, the Debtor purchased the property for $1.7 million from Vulcan.[4]

As part of their agreement, Tracy, as the Trustee of the Seville Vulcan Industries Land Trust, signed a second deed of trust in favor of Vulcan in the amount of $1,412,355.79 (Ex. 11). That amount is based on the deed of trust debt reflected in CLS's Payoff Letter, notwithstanding the disclaimer that the payoff amount could change. (Ex. 11). The second deed of trust required the Debtor to pay six monthly payments of $15,973.53 each directly to the "Noteholder" with the

[4] It does not appear that Vulcan used any of the sale proceeds to pay Fairview.

balance due on April 7, 2022. (Ex. 11). Tracy explained that the Debtor intended to obtain third-party financing to pay off the debt within six months of the closing and that the second deed of trust would be satisfied automatically upon payment of the balance due on the first deed of trust. (Hr'g at 2:22 (Mar. 7, 2023); Ex. 11). Neither the Debtor nor Vulcan gave notice to Fairview of the sale of the Seville Apartments. (Dkt. #66 at 5).

According to the Debtor, it made its first monthly payment to Fairview on October 15, 2021 in the amount of $15,972.53, representing principal and interest at the regular rate, and escrow fees for taxes and insurance.[5] (Dkt. #87 at 19-20; Dkt. #80 at 2). Apparently aware of the assignment from CLS to Fairview, the Debtor thereafter continued making monthly payments on the loan to Fairview. (Cl. 1-1). During this time and knowing that Fairview's lien had not been satisfied, the Debtor voluntarily made repairs and improvements to some of the apartment units—all funded by Re-Build Properties, a separate but related affiliate of the Debtor. (Hr'g at 2:29-2:33 & 3:00-3:07 (Mar. 7, 2023)). The Debtor made its last payment on the loan to Fairview on March 29, 2022. (Cl. 1-1).

At some point, Fairview discovered that Vulcan had sold its collateral without its knowledge or consent. On January 27, 2022, Fairview sent Vulcan a demand letter declaring the loan in default and accelerating the entire indebtedness owed. (Dkt. #87 at 14-17). In the notice of default, Fairview asserted that "[a]n Event of Default has occurred . . . [by] the failure of Borrower to pay principal, interest, and/or other amounts due . . . beginning in the month of January of 2021." (Dkt. #87 at 15).

[5] This first loan payment was made eight days after the recordation of the assignment to Fairview. It is unclear exactly when Fairview learned about the transfer of its collateral to the Debtor, but it appears that the Debtor knew to make payments to Fairview.

State Court Action

On March 24, 2022, Fairview filed the State Court Complaint against the Debtor; Tracy, as the Trustee of the Seville Vulcan Industries Land Trust; Vulcan; and other defendants who potentially held interests in the Seville Apartments. (Ex. 1). The State Court Civil Docket identifies the nature of the lawsuit as a "Judicial Foreclosure." (Ex. 5). As relief, Fairview sought the appointment of a receiver to take possession of the property, to manage the property pending a judicial foreclosure, and to collect rent from the tenants. (Ex. 1). Fairview asked the State Court to authorize the receiver to turn over the rent payments to Fairview, less reimbursement for all reasonable costs incurred in managing the property, including compensation to the receiver for its services.

In connection with the State Court Action, Fairview provided Vulcan a copy of Fairview's Payoff Statement showing the basis for the amounts it claimed were owed as of April 18, 2022. (Ex. 12). A chart attached to Fairview's Payoff Statement shows that no loan payments were made from January 2021 until October 2021, when the Debtor purchased the property. (Dkt. #87 at 20). The payoff figure was $1,645,322.49, consisting of a principal balance of $1,344,530.73, regular interest through April 1, 2022 of $157,057.35, late fees of $5,993.52, and default interest of $99,543.31. (Dkt. #87 at 20). Fairview applied regular and default interest retroactively to the first purported missed payment on January 1, 2021. (Dkt. #87 at 20). The payoff figure of $1,645,322.49 provided by Fairview in Fairview's Payoff Statement was $232,966.70 more than the payoff figure of $1,412,355.79 in CLS's Payoff Letter prepared before the Debtor purchased the property. (Exs. 10, 12).

The Debtor filed the State Court Answer & Counterclaim denying almost all of the allegations and asserting a counterclaim against Fairview that disputed Fairview's accounting of the loan. (Ex. 2). It alleged that Fairview improperly re-aged the loan to add interest and late fees for payments

due when CLS, not Fairview, owned the loan, and then misapplied the payments made by the Debtor to the "fictitious default interest." (Ex. 2). The Debtor, while not a party to the loan, further asserted that "the loan continues to accrue an erroneous amount of daily interest during the pendency of Fairview's Complaint." (Ex. 2 at 10). The Debtor also filed a crossclaim against Vulcan seeking an injunction to prevent Vulcan from foreclosing on its second deed of trust.

The Debtor filed the State Court Abeyance Motion on July 16, 2022. (Ex. 3). Although it is undisputed that there was no privity of contract between the Debtor and Fairview, the Debtor asked the State Court to compel Fairview to provide an exact payoff amount. (Hr'g at 3:21 (Mar. 7, 2021); Ex. 3). It also asked the State Court to hold the matter in abeyance for ninety days beginning from the date Fairview provided the payoff statement and to restrict interest from accruing on the loan. Fairview's request for the appointment of a receiver and the State Court Abeyance Motion were set for hearing in State Court on September 29, 2022. (Ex. 4).

Debtor's Bankruptcy Filing

On September 28, 2022 (the day before the hearing in State Court), the Debtor filed its chapter 11 petition for relief (the "Petition") (Dkt. #1). This case is a single asset real estate case within the meaning of 11 U.S.C. § 101(51B). The filing of the Petition imposed an automatic stay on the proceedings in State Court. *See* 11 U.S.C. § 362(a). A review of the State Court Civil Docket shows that all activity stopped just before that date. (Ex. 5).

In Schedule A/B of its bankruptcy schedules filed on October 12, 2022, the Debtor identified the Seville Apartments as its main asset valued at $3.9 million. (Dkt. #19 at 5). That valuation is reflected in the Debtor's April 2022 Appraisal prepared by a certified general real estate appraiser licensed in Mississippi. (Ex. 6). Other than the Seville Apartments, the assets listed in Schedule A/B included $26,803.00 in cash and deposits, $44,757.00 in accounts receivable, and $500.00 in

office equipment. (Dkt. #19 at 3-4). On February 25, 2023, before the March 7 Hearing date, the Debtor amended Schedule A/B to reduce the value of the Seville Apartments from $3.9 million to $2 million (Dkt. #100 at 4) relying on a valuation contained in a Broker's Opinion prepared that same month by a real estate brokerage firm as part of a marketing brochure. (Ex. 7). No other changes were made to Schedule A/B.

Fairview and Vulcan are the only secured creditors listed in Schedule D. (Dkt. #19 at 9). The Debtor identified Fairview as having a secured claim of $1,412,355.79 and Vulcan as having a secured claim of $0.00.[6] (Dkt. #19 at 9). In Schedule E/F, the Debtor did not list any unsecured creditors. (Dkt. #19 at 11). The Debtor later amended Schedule E/F to add Re-Build Properties as an unsecured creditor with an unsecured claim of $184,844.00. (Dkt. #52 at 2). Tracy testified that Re-Build Properties is an affiliate of the Debtor and that its claim against the Debtor is for reimbursement of the cost of renovations to the apartment units. (Hr'g at 3:00-3:07 (Mar. 7, 2023)). Tracy admitted, however, that the Debtor has no contractual obligation to pay Re-Build Properties for the cost of renovations. (Hr'g at 3:04-3:07 (Mar. 7, 2023)).

Only one creditor, Fairview, filed a proof of claim in the Bankruptcy Case. (Cl. #1-1). Fairview asserted a claim secured by the property totaling $1,849,884.38 as of the date of the Petition. (Ex. 9). Included in this amount is $388,130.37 in accrued interest at the default rate of 22.5%.[7] (Ex. 9). Fairview indicated in its Proof of Claim that it intended to file an application for post-Petition interest and fees, which would increase the total amount owed, as of January 23, 2023, from $1,849,884.38 to $2,021,145.80. (Ex. 9). The Debtor filed the Debtor Re-Build Seville, LLC's Objection to Fairview Investment Fund V, LP's Proof of Claim No. 1 (the "Objection to POC")

[6] It is unclear why Vulcan is listed as a secured creditor. In the Amended Plan, the Debtor states that Vulcan's claim totals $0.00. (Dkt. #102 at 5).

[7] Fairview's Proof of Claim shows the applicable default interest rate to be 20.50% as of September 28, 2022 and 22.50% as of January 26, 2023. (Ex. 9 at 5).

(Dkt. #87), asking the Court to reduce Fairview's claim to $1,412,355.79. The Debtor opposes the amount of Fairview's claim for the same reasons given in the State Court Answer & Counterclaim. A hearing on the Objection to POC has not yet been scheduled.

Original Disclosure Statement & Original Plan

On December 27, 2022, the Debtor filed Re-Build Seville LLC's Disclosure Statement (the "Disclosure Statement") (Dkt. #70) and Plan of Reorganization (the "Plan") (Dkt. #69). The Plan proposes to pay Fairview $1,412,355.79 over five years in sixty monthly payments of $15,000.00 with a final balloon payment due on the maturity date. According to the original Plan, interest would accrue at 2% above the Prime Rate and no pre-payment penalty applies if the debt is paid early. The Debtor amended the Disclosure Statement and Plan, which is discussed later.

Motion to Dismiss

In the Motion to Dismiss, Fairview asks the Court to dismiss the Petition as a bad faith filing under 11 U.S.C. § 1112(b) or, in the alternative, grant it relief from the automatic stay under 11 U.S.C. § 362(d).[8] According to Fairview, the Debtor did not file the Petition for a valid bankruptcy purpose but to avoid the appointment of a state-court receiver, the foreclosure of the property, and the payment of default interest. (Dkt. #66).

In its Response, the Debtor asserts that it had "no alternative" but to seek bankruptcy protection because of the "continuing accrual of the default rate of interest" and the "charging of the Debtor an exorbitant default interest rate."[9] (Dkt. #80 ¶ 28). The Debtor admits that it filed the Petition on

[8] The standards for bad faith in the context of the dismissal of a case and relief from the automatic stay are similar. *See Little Creek Dev. Co. v. Commonwealth Mortg. Corp. (In re Little Creek Dev. Co.)*, 779 F.2d 1068, 1072 (5th Cir. 1986).

[9] This assertion is not technically correct. Fairview can only charge the borrower interest pursuant to the terms of the note. The Debtor is not the borrower, Vulcan is. The Debtor purchased the property from Vulcan knowing that there was an outstanding note and deed of trust on the property and that CLS's Payoff Letter contained a disclaimer that the payoff amount could change. (Ex. 10; Hr'g at 2:20 (Mar. 7, 2023)).

the eve of a hearing in State Court but argues that avoiding a foreclosure sale is an allowable and common use of the Bankruptcy Code.

In its Reply, Fairview alleges that no foreclosure sale had been scheduled when the Petition was filed and no steps had been taken to initiate the foreclosure sale. (Dkt. #82 at 1). Fairview describes this Bankruptcy Case as a two-party dispute boiled down to the "Debtor's intense desire to avoid paying contractually mandated Default Rate interest when effecting a lien release payoff." (Dkt. #82 at 5).

Amended Disclosure Statement & Amended Plan

Days before the March 7 Hearing on the Motion to Dismiss, the Debtor filed Re-Build Seville LLC's Amended Disclosure Statement for Amended Plan (the "Amended Disclosure Statement") (Dkt. #103) and Amended Plan of Liquidation (the "Amended Plan") (Dkt. #102). In the Amended Disclosure Statement, the Debtor refers to the Broker's Opinion valuing the Seville Apartments at $2 million. The Amended Plan proposes the sale of the property and payment of Fairview's secured claim in the amount of $1,849,884.38 from the sale proceeds, thereby attempting to "cap" the amount of Fairview's security interest in the Seville Apartments.

The Evidentiary Hearing

An evidentiary hearing on the Motion to Dismiss was originally scheduled for February 14, 2023, but was continued to March 7, 2023. Counsel for Fairview began the Hearing on March 7, 2023 by asking the Court to take judicial notice of the Debtor's admissions in the stipulated exhibits. These admissions, according to Fairview's counsel, satisfy Fairview's *prima facie* burden of bad faith. In support of his argument, counsel for Fairview cited well-established case law that factual statements in pleadings constitute binding judicial admissions of the party that made them. *W.G. Yates & Sons Constr. Co. v. Hoch Assocs*., No. 3:15-CV-80, 2018 WL 315401 (N.D. Miss.

Jan. 5, 2018). He also cited a Fifth Circuit Court of Appeal's case for the proposition that admissions made in amended pleadings lose their binding force but retain their value as evidentiary admissions. *White v. Arco/Polymers, Inc.*, 720 F.2d 1391, 1396 (5th Cir. 1983). He then introduced into evidence all nine stipulated exhibits.

Tracy testified that the Debtor filed the Petition in response to a "drastic financial event" created when Fairview demanded the immediate payment of $1,645,322.49 to avoid foreclosure. (Hr'g at 2:38 (Mar. 7, 2023)). According to Tracy, this payoff amount was almost $250,000.00 more than the amount the Debtor believed was owed on the loan when it purchased the property, and the Debtor was unable to refinance the loan for that additional amount, which continued to accrue interest of $4,000.00 per diem. (Hr'g at 3:23-3:24 (Mar. 7, 2023)). In summary, the Debtor was fearful that its sizeable equity cushion was being diminished by the accrual of interest. (Hr'g at 2:38-2:39 (Mar. 7, 2023)).

Discussion

Under 11 U.S.C. § 1112(b), a bankruptcy court must convert or dismiss a chapter 11 case if the movant establishes "cause," unless it determines that the appointment of a trustee or examiner under 11 U.S.C. § 1104(a)(3) is in the best interests of creditors and the estate. *In re Roman Catholic Church of the Archdiocese of New Orleans*, 632 B.R. 593, 598 (Bankr. E.D. La. 2021). The Bankruptcy Code does not define the term "cause" but provides a non-exhaustive list of examples that would constitute "cause" for dismissal or conversion. 11 U.S.C. § 1112(b)(4). Though lack of good faith is not one of the enumerated examples in 11 U.S.C. § 1112(b)(4), there is a consensus among courts that a petition filed in bad faith is subject to dismissal under that statute. *In re Humble Place Joint Venture*, 936 F.2d 814, 816-17 (5th Cir. 1991). As explained by the Fifth Circuit in *Little Creek Development Co. v. Commonwealth Mortgage Corp. (In re Little Creek Development*

Co.), 779 F.2d 1068 (5th Cir. 1986), "every bankruptcy statute since 1898 has incorporated literally, or by judicial interpretation, a standard of good faith for the commencement, prosecution, and confirmation of bankruptcy proceedings." *Id.* at 1071. The good faith requirement "furthers the balancing process between the interests of debtors and creditors" and is "necessary to legitimize the delay and costs imposed upon parties to a bankruptcy." *Id*.

In determining whether a debtor acted in bad faith, courts must conduct an "on-the-spot evaluation of the debtor's financial condition, motives, and the local financial realities." *Little Creek*, 779 F.2d at 1072. Because a debtor is unlikely to acknowledge its own bad faith, a determination of intent requires consideration of the "totality of the circumstances" surrounding the filing of the bankruptcy case. *In re T-H New Orleans LP*, 116 F.3d 790 (5th Cir. 1997). The Fifth Circuit in *Little Creek* identified recurring patterns that appear in cases filed in bad faith. They include:

> (1) the debtor has one asset, such as a tract of real property, that is encumbered by liens;
>
> (2) the debtor has no employees except for the principals;
>
> (3) the debtor has no little or no cash flow and no available sources of income to sustain a plan or to make adequate protection payments;
>
> (4) the debtor has few unsecured creditors whose claims are relatively small;
>
> (5) the property is the subject of a foreclosure action in state court as a result of arrearages on the debt;
>
> (6) the debtor has been unsuccessful in defending the foreclosure action in state court; and
>
> (7) the debtor's financial problems involve essentially a dispute between the debtor and a secured creditor that can be resolved in a pending state court action.

Little Creek, 779 F.2d at 1072-73. Each of these factors, if present, weighs against a finding of good faith. No single factor is determinative of the issue of good faith, and more weight may be given one factor over another. *In re McMahan*, 481 B.R. 901, 915-16 (Bankr. S.D. Tex. 2012).

Some courts have recognized that the *Little Creek* factors are not always suitable or helpful in assessing good faith and instead have adopted a "valid bankruptcy purpose" test. *In re Mirant Corp.*, No. 03-46590, 2005 WL 2148362, at *7 (Bankr. N.D. Tex. Jan. 26, 2005) (collecting cases). Under that test, the focus of the good faith inquiry is determining whether the debtor's "act of submitting a bankruptcy petition . . . is inconsistent with the purposes of the Bankruptcy Code or is an abuse of the bankruptcy system." *Bad-Faith Filing,* BLACK'S LAW DICTIONARY (10th ed. 2014). As to whether an act is consistent with the Bankruptcy Code, the U.S. Supreme Court has held that the purpose of bankruptcy in chapter 11 cases is to reorganize the business or to sell it as a going concern and, in either event, to maximize assets available to satisfy unsecured creditors. *Bank of Am. Nat'l Trust & Sav. Ass'n v. 203 N. LaSalle St. P'ship*, 526 U.S. 434, 453 (1999). Courts have found bad faith in situations involving a use of the bankruptcy process to obtain an unfair tactical advantage in litigation or to resolve disputes solely between two parties. *See Antelope Techs., Inc. v. Lowe (In re Antelope Techs., Inc.)*, 431 F. App'x 272, 275 (5th Cir. 2011); *In re LBJV, Ltd.*, 544 B.R. 401, 406 (Bankr. N.D. Ill. 2016).

In line with other bankruptcy courts within the Fifth Circuit, the Court adopts the following burden-shifting framework: the "movant must first establish a prima facie showing of bad faith." *Roman Catholic*, 632 B.R. at 601 (citation omitted). If the movant satisfies the initial burden to make a *prima facie* showing of a lack of good faith, then the burden shifts to the debtor to demonstrate good faith. *In re Nat'l Rifle Ass'n*, 628 B.R. 262, 270 (Bankr. N.D. Tex. 2021); 7 COLLIER ON BANKRUPTCY ¶ 1112.04[4] (16th ed. 2022). This burden-shifting framework is consistent with the text of 11 U.S.C. § 1112(b), which requires bankruptcy courts to dismiss or convert a case for cause—unless the debtor shows that unusual circumstances exist that warrant denying the relief requested by the movant.

A. Fairview's Argument That the Debtor Filed the Petition for an Improper Purpose

To attempt to meet its burden to establish a *prima face* showing of bad faith, Fairview relies on the "valid bankruptcy purpose" test and some of the *Little Creek* benchmarks. Fairview argues that a petition filed in good faith is normally filed in response to a financial crisis but that the Debtor's admissions in its pleadings establish that the Debtor was solvent and not experiencing any financial distress when it filed the Petition. For example, the Debtor admits in the Response that "[s]ince taking possession of the Real Property, the Debtor has successfully operated the Real Property as an apartment complex." (Dkt. #80 ¶ 6). Moreover, the Debtor's monthly operating reports show that the property continues to generate a positive cash flow.[10] (Dkt. #47, #51; Hr'g at 1:50-1:53 (Mar. 7, 2023)). Also, the Debtor, according to its original schedules and its own April 2022 Appraisal, has approximately $2.1 million in equity in the Seville Apartments. This figure is based on the value ($3.9 million) of the property listed by the Debtor in original Schedule A/B (Dkt. #19) and the amount of Fairview's secured claim ($1,412,355.72) in Schedule D (Dkt. #19). Although the Debtor amended Schedule A/B to reduce the value of the property to $2 million based on the Broker's Opinion[11] (Ex. 7), Fairview disputes the relevancy and accuracy of this number. Fairview contends that the Broker's Opinion is not relevant as to the Debtor's intent because it was prepared in February 2023, after the Petition date. Fairview also questions the reliability of the opinion given that it reflects a 50% decline in the value of the property in a relatively short period of time. Finally, Fairview points out that Marcus & Millichap, the brokerage firm that

[10] Fairview also argues that the Debtor's offer to pay Fairview $15,000.00 per month in adequate protection payments in the Motion to Grant Fairview Investment Fund V, LP Adequate Protection (Dkt. #55) is additional evidence that Debtor was not experiencing a financial crisis when it filed the Petition. (Dkt. #66 at 8). At the March 7 Hearing, however, the Debtor announced its intention to withdraw that motion. (Hr'g at 1:36 (Mar. 7, 2023)).

[11] The Broker's Opinion contains the following Disclaimer: "THIS IS A BROKER PRICE OPINION OR COMPARATIVE MARKET ANALYSIS OF VALUE AND SHOULD NOT BE CONSIDERED AN APPRAISAL." (Ex. 7 at 2). Tracy ultimately conceded that the April 2022 Appraisal and Broker's Opinion are two different things, used for different reasons, and that the Broker's Opinion was prepared as a marketing brochure. (Hr'g at 3:20-3:21 (Mar. 7, 2023)).

prepared the Broker's Opinion, are not appraisers or even licensed brokers in Mississippi. The absence of financial distress, according to Fairview, demonstrates that the only purpose for the bankruptcy filing was to obtain a tactical advantage in the State Court Action. (Dkt. #66 at 9).

Fairview points to the timing of the filing of the Petition in relation to the status of the State Court Action and suggests that the Debtor is forum shopping. An evidentiary hearing on Fairview's request for the appointment of a receiver was set one day after the Petition date. In the State Court Answer & Counterclaim, the Debtor "seek[s] a declaratory judgment to determine the proper amount owed to Fairview" (Ex. 2 at 9), which mirrors its assertion in the Response that "[t]his Court is fully equipped to determine the value of Fairview's allowed secured claim." (Dkt. #80 at 7).

The impetus for the bankruptcy filing, according to Fairview, is the Debtor's opposition to the payment of interest. Fairview contends that the advantage to the Debtor of having its dispute resolved here, rather than in State Court, is 11 U.S.C. § 506(b). Under that statute, Fairview holds a secured claim to the extent of the value of the Seville Apartments[12] and is entitled to post-Petition interest to the extent its claim is oversecured. The rate of that interest, because its claim arises from a contract, is the variable rate of interest set forth in the loan. *Bradford v. Crozien (In re Laymon)*, 958 F.2d 72, 75 (5th Cir. 1992). Whether Fairview is also entitled to the contractual *default* rate of interest at an additional 10%, however, depends on the equities involved in the bankruptcy proceeding. *Id.*; *see also Ultra Petroleum Corp. v. Ad Hoc Comm. of Opco Unsecured Creditors (In re Ultra Petroleum Corp.)*, 51 F.4th 138, 142 (5th Cir. 2022). Fairview argues that the Debtor could *potentially* use 11 U.S.C. § 506(b) as a tool to avoid paying any post-Petition interest at the default rate and any attorneys' fees. (Dkt. #82 at 8). The other advantage, according to Fairview,

[12] Because the Debtor is not a party to the loan, Fairview does not hold a claim against the Debtor for any difference between the amount of the loan and the value of the Seville Apartments.

is the confirmation of a plan that replaces the contractual rate of interest with the much lower *Till* rate.[13] (Dkt. #82 at 8). In the original Plan proposed by the Debtor, for example, Fairview would receive interest at 2% above the Prime Rate (9.75%) rather than the default rate at 22.5%.[14] Fairview contends that allowing the Debtor to avoid payment of contractually mandated interest would be unfair given that the Debtor has no contractual relationship with Fairview. (Dkt. #82 at 5-6).

Fairview also relies on the *Little Creek* benchmarks of a bad faith filing. Here, the Debtor owns one main asset, the Seville Apartments, which is encumbered by Fairview's and Vulcan's deeds of trust and which is the subject of a receivership and foreclosure action in State Court as the result of alleged arrearages on the loan. The Debtor has only one alleged unsecured creditor, Re-Build Properties, LLC, having a claim of $184,844.00. This alleged debt is for the costs incurred to renovate the Seville Apartments and is significantly less than Fairview's secured claim listed at $1,412,355.79. Moreover, Re-Build Properties, LLC is an insider of the Debtor, and Tracy testified at the March 7 Hearing that the Debtor is not contractually liable to pay this debt. (Dkt. #66 at 7 n.2); 11 U.S.C. § 101(31)(E) (defining insider); (Hr'g at 3:00-3:07 (Mar. 7, 2023)). Fairview asks the Court to disregard this claim for purposes of its Motion to Dismiss. Finally, Fairview insists that this matter is a two-party dispute between it and the Debtor. (Dkt. #82 at 5).

The Court finds that Fairview has established a *prima facie* showing of bad faith through judicial admissions made by the Debtor in its bankruptcy schedules, the Response, and the State Court Answer & Counterclaim and through judicial notice of the status of the State Court Action. In that

[13] In *Till v. SCS Credit Corp.*, 541 U.S. 465, 479-81 (2004), a plurality of the U.S. Supreme Court held that bankruptcy courts must calculate the cramdown interest rate in a chapter 13 case by applying the prime-plus formula. Fairview does not explain why the *Till* rate would necessarily determine the cramdown rate of interest in this chapter 11 case under these facts. *See Fin. Sec. Assurance Inc. v. T-H New Orleans Ltd. P'ship (T-H New Orleans Ltd. P'ship)*, 116 F.3d 790 (5th Cir. 1997); *Wells Fargo Bank Nat'l Ass'n v. Tex. Grand Prairie Hotel Reality, LLC (In re Tex. Grand Prairie Hotel Reality, LLC)*, 710 F.3d 324 (5th Cir. 2013) (reaffirming *T-H New Orleans Ltd. P'ship*).

[14] As of the March 7 Hearing, the U.S. Prime Rate published in *The Wall Street Journal* was 7.75%. *See Wall Street Journal Prime Rate*, BANKRATE, http://www.bankrate.com/rates/interestrates/wall-street-prime-rate.

regard, a judicial admission, as defined by the Fifth Circuit, is a "formal concession in the pleadings or stipulations by a party or counsel that is binding on the party making them." *Martinez v. Bally's La.*, 244 F.3d 474, 476 (5th Cir. 2001). In order to qualify as a judicial admission, a statement must be "deliberate, clear, and unequivocal." *Heritage Bank v. Redcom Labs., Inc.*, 250 F.3d 319, 329 (5th Cir. 2001); *see United States v. Chevez-Hernandez*, 671 F.3d 494, 501 (5th Cir. 2012) (holding that "for a statement of counsel to qualify as a judicial admission it must be made intentionally as a waiver, releasing the opponent from proof of fact").

The sworn statements of the Debtor regarding its financial affairs in the schedules, including the number of creditors and the amounts of their claims, establish that the Debtor was solvent and financially healthy when it filed the Petition. The statement of the Debtor in original Schedule A/B valuing the property at $3.9 million shows that there was substantial equity in the property. Although that statement lost its binding effect by virtue of its amendment, it still constitutes an evidentiary admission. Finally, the timing of the filing of the Petition also supports a *prima facie* case of bad faith. *See In re Delta AG Grp., LLC*, 596 B.R. 186, 195 (Bankr. W.D. La. 2019). The State Court Hearing Notice shows that the Debtor filed the Petition one day before a hearing on Fairview's request for the appointment of a receiver. Based on these red flags, the burden of proof has shifted to the Debtor to prove that it filed the Petition in good faith.

B. Debtor's Argument That It Filed the Petition in Good Faith

In its Response, the Debtor denies that it filed the Petition as a litigation strategy. (Dkt. #80 at 7). The Debtor insists that if anyone is acting in bad faith, it is Fairview. (Dkt. #80). Prior to commencing the Bankruptcy Case, the Debtor was in the midst of seeking financing to satisfy the loan but Fairview refused to provide the Debtor with a payoff amount to release its deed of trust on the

property.[15] The Debtor surmises that Fairview ignored its numerous requests for that information because it preferred to continue to accrue interest on the loan at the default rate rather than settle their dispute. According to Tracy, a representative of Fairview told him, "We are going to bleed all of your equity off, and there is nothing you can do about it." (Hr'g at 2:41-2:42 (Mar. 7, 2023)). Tracy explained why the Debtor opposed the dismissal of the Bankruptcy Case even though the Debtor had recently amended the Plan to propose a sale of the Seville Apartments: He testified that the interest on the loan is extremely high because it is based on the Prime Rate, which has tripled in the last six months, and that the cost of money per month is the same as, or even more than the amount of revenue generated by the rental income. (Hr'g at 2:42-2:43 (Mar. 7, 2023)).

The Debtor disputes Fairview's assertion that it is financially healthy. The Debtor contends that it has two outstanding deeds of trust,[16] cannot afford to pay default rate of interest to Fairview, and must bear the costs of asserting claims against the parties identified in its Disclosure Statement. Those parties include Vulcan, CLS, Farris Crisler (the closing agent), and Fairview. (Dkt. #70 at 10).

The Debtor admits that it filed the Petition on the eve of a hearing in the State Court Action but argues that avoiding a foreclosure sale is an allowable and common use of the Bankruptcy Code. (Dkt. #80 at 6). The Debtor concedes that foreclosure was not one of the matters set for hearing in State Court but argues that the State Court's appointment of a receiver would have been a first step in that direction. (Hr'g at 2:10-2:12 (Mar. 7, 2023)). Tracy's testimony, however, is contrary to the Debtor's argument. Tracy testified that he thought the Debtor might have been successful in defeating Fairview's pending request for a receiver. (Hr'g at 2:39 (Mar. 7, 2023)).

[15] Fairview asserts that it did not do so because Vulcan, not the Debtor, is the named borrower on the note and banking information is confidential. (Dkt. #82 at 8).
[16] Fairview holds the first deed of trust, and Vulcan holds the second deed of trust, as discussed *supra*.

Finally, the Debtor contends in the Response that it is attempting to save the Seville Apartments and avoid the disruption to the low-income apartment tenants that will occur if the Petition is dismissed. (Dkt. #80 at 7).

C. Court's Analysis

As a preliminary matter, the Court notes that a debtor's solvency at the time of the bankruptcy filing is not, without more, proof of an improper bankruptcy purpose. Although "[b]ankruptcy is ordinarily for the insolvent," the Bankruptcy Code does not include an insolvency requirement for chapter 11 debtors. *See Ultra Petroleum Corp.*, 51 F.4th at 142; 11 U.S.C. § 101(32) (providing definition of insolvency). Solvency and financial distress are not mutually exclusive, and a debtor should not have to face a financially hopeless situation before seeking bankruptcy relief. For this reason, a debtor that files bankruptcy to avoid a foreclosure sale is not acting in bad faith *per se*. After all, "[i]f the Court were to consider every bankruptcy filed made for the purpose of taking advantage of the automatic stay as evidence of a bad faith filing, the protection offered by the automatic stay would be meaningless." *In re Harco Co. of Jacksonville, LLC*, 331 B.R. 453, 458 (Bankr. M.D. Fla. 2005). A debtor's solvency and the imminency of foreclosure proceedings, however, are factors relevant to the analysis of good faith. *Little Creek*, 779 F.2d at 1073-74; *Roman Catholic*, 632 B.R. at 601-02.

Here, the evidence demonstrates that the Debtor was solvent and not experiencing financial difficulties when it filed the Petition. In fact, the Debtor says that it made monthly payments of $15,972.53 to Fairview from October 2021 through April 2022. (Dkt. #80 at 2). The Debtor had no obligations other than the liens on the Seville Apartments, and there was substantial equity in the property. As to these findings, the Court agrees with Fairview's analysis. First, the only unsecured creditor listed in the schedules, Re-Build Properties, is an insider of the Debtor, and Tracy

testified that no contract obligated the Debtor to reimburse Re-Build Properties for the costs of renovations. (Hr'g at 3:00-3:07 (Mar. 7, 2023)). Regardless, the amount of the insider claim ($184,844.00) is relatively small and did not render the Debtor insolvent or in financial distress.

Second, the Court places greater weight on the April 2022 Appraisal than on the Broker's Opinion. With respect to the valuation of real estate in Mississippi, a real estate brokerage firm not licensed in Mississippi is simply not on the same playing field as a Mississippi real estate appraiser. Also, the Debtor procured the Broker's Opinion on the eve of the March 7 Hearing, and its valuation contradicts the Debtor's own April 2022 Appraisal. The Broker Opinion does not assist the Court with determining value because of this disclaimer: "THIS IS A BROKER PRICE OPINION OR COMPARATIVE MARKET ANALYSIS OF VALUE AND SHOULD NOT BE CONSIDERED AN APPRAISAL." (Ex. 7 at 2).

The Court also agrees with Fairview that there was no imminent foreclosure at the time the Debtor filed the Petition. The State Court Hearing Notice shows that the hearing on September 29, 2022 was limited to Fairview's request for the appointment of a receiver and the Debtor's request for an abatement of the accrual of interest until Fairview produced an exact payoff amount. Although foreclosure may have been the end result in the State Court Litigation, that path had not yet been laid as of the Petition date. It is speculative to contend that the property would ultimately be foreclosed at this juncture in the State Court litigation. It is thus clear to the Court that the Debtor sought bankruptcy protection not because its existence was threatened by the litigation in State Court—as shown, in part, by the Debtor's proposed liquidation of the property in the Amended Plan—but because bankruptcy offered an advantage in moving the Debtor toward its ultimate goal of preventing Fairview from continuing to assess the default rate of interest to the outstanding

balance owed by Vulcan.[17] "While it is true that the filing of a bankruptcy petition often delays pending litigation due to the invocation of the automatic stay, it does so for a proper purpose—to facilitate the financial rehabilitation or liquidation of a debtor." *In re Enmon*, No. 12-10268, 2013 WL 494049, at *4 (Bankr. E.D. Tex. Feb. 7, 2013).

That advantage, as perceived by the Debtor, was to stay the State Court Litigation, abate the accrual of interest which was siphoning off the Debtor's equity in the property, and force Fairview to the negotiating table. In that regard, 11 U.S.C. § 362(a) stays the continuation of judicial proceedings and 11 U.S.C. § 502(b)(2) bars claims for unmatured interest.[18] These provisions of the Bankruptcy Code assume the existence of a good-faith bankruptcy filing and, therefore, are reserved for use only where the benefits of those laws do not create an injustice. *Little Creek*, 779 F.2d at 1073.

The Debtor proposes an Amended Plan that ends the operations of its business. The Bankruptcy Code allows for a distribution of a debtor's estate pursuant to a valid plan of liquidation. 11 U.S.C. § 1123. The Bankruptcy Code, however, cannot be used to facilitate the liquidation of assets that does not maximize the value of the Debtor for creditors but simply liquidates assets on terms favorable to the Debtor's equity owners. *See 203 N. LaSalle*, 526 U.S. at 453 (characterizing one purpose of chapter 11 as "maximizing property available *to satisfy creditors*"). The Debtor's Amended Plan seeks to cap Fairview's security interest. In the absence of any creditors but Fairview and the presence of substantial equity in the property, the sale of the Seville Apartments in a

[17] Tracy testified that the Debtor had purchased a title insurance policy excepting Fairview's deed of trust and the Debtor had relied on the payoff amount provided to it by the title agent, not Fairview. (Hr'g at 2:20-2:21 (Mar. 7, 2023). However, according to Tracy, the "deal" with Vulcan was that the note would be paid in full within six months. Since the Debtor opted to close the transaction without satisfying the underlying loan, it incurred the risk: (1) that CLS would continue to hold the note and not transfer or assign it and (2) that the payoff amount provided by the title agent would not change. Tracy testified that the Debtor purchased the Seville Apartments without reading the promissory note. (Hr'g at 3:47 (Mar. 7, 2023)).

[18] A claim for post-petition interest may be recoverable under 11 U.S.C. § 506(b) from the date of the petition through the confirmation date if the creditor is oversecured.

bankruptcy proceeding pursuant to the Amended Plan benefits no one other than the Debtor's members.

Here, the Debtor has used the bankruptcy process as a litigation tactic in what is essentially a two-party dispute between it and Fairview. *Investors Grp., LLC v. Pottorff*, 518 B.R. 380, 383-84 (N.D. Tex. 2014) (affirming dismissal of bankruptcy petition for being filed in bad faith based on court's finding that primary purpose was to gain an unfair advantage in pending litigation); *In re First Fin. Enters., Inc.*, 99 B.R. 751, 755-56 (Bankr. W.D. Tex. 1989) (finding cause for dismissal under 11 U.S.C. § 1112(b) because "obvious purpose" of bankruptcy case was "to use the Chapter 11 filing as a litigation strategy and leverage" in order to defeat appointment of a receiver). The Debtor asserts that it had no alternative but to file bankruptcy, but the Debtor's predicament is one of its own making. It was the Debtor's decision to purchase the property from Vulcan, and so it must accept the risk associated with its business judgment.

In any event, the State Court is better suited to determine the issues raised by the Debtor in the pending State Court Litigation where Fairview, a non-debtor, is suing not only the Debtor but also non-debtor defendants and where the issues involve the adjudication of state law rights. This Court's jurisdiction and Constitutional authority are limited, and it could not afford a full and final resolution of all issues as to all parties.

At the March 7 Hearing, counsel for the Debtor asked the Court to view the Bankruptcy Case differently from cases involving multi-district litigation. (Hr'g at 2:12-2:15 (Mar. 7, 2023)). For example, the bankruptcy court in *Roman Catholic* concluded that the debtor, although solvent, was experiencing financial distress because of the proliferation of lawsuits against it and the high probability that it would be held liable for numerous claims. *Roman Catholic*, 632 B.R. at 601-11. The Court agrees with counsel for the Debtor that a finding of financial distress does not necessarily

require evidence that a debtor faced multi-district litigation as of the petition date. Here, using the guide rails in *Little Creek* and considering the "totality of the circumstances" surrounding the filing of the Bankruptcy Case, the Court concludes that cause exists for dismissal.

Although the Court finds cause to dismiss the Bankruptcy Case, 11 U.S.C. § 1112(b)(1) provides an exception if the Debtor demonstrates that unusual circumstances exist showing that dismissal is not in the best interests of the creditors and the estate. In that regard, Tracy testified that the Debtor's loss of the Seville Apartments would adversely affect the tenants and the surrounding community. (Hr'g at 2:36-2:37 (Mar. 7, 2023)). He asserted that the renovations made the apartment units as well as the surrounding neighborhood safer, the Debtor contemplates making even more repairs, and the loss of the property would halt that progress. Other than Tracy's testimony, the Debtor produced no evidence to support these contentions. In any event, they are moot given that the Debtor now proposes to sell the Seville Apartments in its Amended Plan.

Conclusion

To allow the Debtor to remain "clothed" in the protection of the Bankruptcy Code under these circumstances where the Debtor is solvent, is not experiencing financial distress, and is not a party to the loan would contravene the principles of good faith as set forth in *Little Creek* and would condone an abuse of the reorganization process in this two-party dispute. For the above reasons, the Court finds that the Motion to Dismiss should be granted. The dismissal of the Bankruptcy Case renders it unnecessary to decide if Fairview is entitled to relief from the automatic stay pursuant to 11 U.S.C. § 362(d).

IT IS, THEREFORE, ORDERED that the Motion to Dismiss is hereby granted and the Petition is hereby dismissed.

##END OF ORDER##