IN THE UNITED STATES BANKRUPTCY COURT FOR THE
DISTRICT OF PUERTO RICO

IN RE:	:	CASE NO. B95-02187(ESL)
	:	
ARIEL E. GUTIERREZ	:	CHAPTER 7
	:	
Debtor	:	INVOLUNTARY PETITION
	:	
IN RE:	:	CASE NO. B95-02188(ESL)
	:	
ENRIQUE H. GUTIERREZ	:	CHAPTER 7
	:	
Debtor	:	INVOLUNTARY PETITION
	:	

OPINION AND ORDER

Before the court is the issue of whether the petitioning creditors' claims are subject of bona fide disputes within the parameters of 11 U.S.C. §303(b)(1). At the court's direction the parties have filed briefs in support of their respective positions.

Background

These involuntary petitions were filed on April 7, 1995. The petitioning creditors in the case of Ariel E. Gutierrez are Plaza Inmaculada, SE (two claims),[1] David Efron (two claims),[2] and Bailey, Hunt and Jones.[3] The petitioning creditors in the case of Enrique H. Gutierrez are Plaza Inmaculada, SE (two claims),[4] David Efron (two claims),[5]

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[1]Claim #1 for repairs and interest in the amount of $3,030,300.00, and claim #2 for payment of fees to M. Martinez in the amount of $29,325.00.

[2]Claim #3 for payment to Banco Santander in the amount of $260,000.00, and claim #4 for note assigned by Dr. Ganapolsky in the amount of #324,000.00.

[3]Claim #5 for legal fees in the amount of $22,459.55.

[4]See footnote 1.

[5]See footnote 2.

and Bailey, Hunt and Jones.[6] Debtors filed motions to dismiss the involuntary petitions on April 13, 1995. Debtors' motion for joint administration of the cases was granted, while petitioning creditors' motion for substantive consolidation of the cases was denied. Upon consideration of debtors' motions to dismiss, the court found that the issue of bad faith is fact intensive and that it was unable to make a determination of bad faith on the pleadings and exhibits; thus, the court scheduled a hearing on an expedited basis for August 14, 1995.

At the conclusion of the evidentiary hearing, which extended over six days, the court issued an opinion and order on April 26, 1996, wherein the court declined to find bad faith on the part of the petitioning creditors. The issue of whether any of the claims are subject of a bona fide dispute remained to be considered in resolving the motions to dismiss. The court noted that although the parties had addressed the issue, it declined to determine the issue at the hearing and therefore granted the parties time to brief the issue before entering a final order on the motion to dismiss.

In its opinion and order of April 26, 1996, the court made certain findings of fact and conclusions of law. The court found that the number of petitioning creditors in each of these involuntary petitions facially meets the requirements of 11 U.S.C. § 303(b), which encompassed a finding that petitioning creditor Plaza Inmaculada, SE is a seperate and distinct entity from petitioning creditor David Efron. (dkt. #79 at p. 47). The court further found that the petitioning creditors did not file these petitions in bad

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[6]Pursuant to this court's Opinion and Order of April 26, 1996, granting B, H & J's motion to join the petition. (dkt. #79 at p. 47).

faith. (dkt. #79 at pp. 47-49).

Discussion

In the aforementioned opinion and order, the court discussed the applicable law regarding the bona fide dispute issue. Section 303(b) of the Bankruptcy Code provides that an involuntary case may be commenced by the filing of a petition "by three or more entities, each of which is either a holder of a claim against such person that is not contingent as to liability or the subject of a bona fide dispute ...." 11 U.S.C. § 303(b) (1994). The term "bona fide" is not defined in the Code, but courts have adopted an objective test for determining whether a dispute is bona fide. 1 Robert E. Ginsberg & Robert D. Martin, Bankruptcy: Text, Statutes, Rules § 2.03[B][1] at 2-34 (4th ed. 1996). The burden is initially on the creditor to establish a prima facie case that a dispute does not exist, whereupon the burden shifts to the debtor to show that a dispute does exist. Id. See also 1 William L. Norton, Jr., Norton Bankruptcy Law and Practice 2d § 21:3 at 21-8 (1994). The debtor's assertion of a counterclaim against a petitioning creditor, even a substantive one, does not make the claim contingent, nor subject of a bona fide dispute; thus, creditors with claims that may be set off by a counterclaim may still be petitioning creditors. 2 Lawrence P. King et al., Collier on Bankruptcy ¶ 303.08 at 303-27 (15th ed. 1996), citing In re Drexler, 56 B.R. 960 (Bankr. S.D.N.Y. 1986).

The legislative history suggests that the purpose of this requirement is to prevent creditors from using the bankruptcy court to collect legitimately disputed claims. Collier ¶ 303.08[11][c] at 303-38, citing In re Cates, 62 B.R. 179, 180 (Bankr. S.D. Tex. 1986); Ginsberg, § 2.03[C][3] at 2-41, citing In re West Side Community Hospital, Inc., 112

B.R. 243 (Bankr. N.D. Ill. 1900); In re Accident Claims Determination Corp., 146 B.R. 64 (Bankr. E.D.N.Y. 1992). Courts have formulated different standards for determining whether a debt is a bona fide dispute. Four circuits have adopted an objective standard, i.e., whether there is a genuine issue of material fact bearing upon debtor's liability, or a meritorious contention as to the application of law to undisputed facts. Collier ¶ 303.08[11][c] at 303-39, citing B.D.W. Associates, Inc. v. Busy Beaver Building Centers, Inc., 865 F.2d 65 (3rd Cir. 1989); Matter of Busick, 831 F.2d 745 (7th Cir. 1987); Bartmann v. Maverick Tube Corporation, 853 F.2d 1540 (10th Cir. 1988). See also, Ginsberg, § 2.03[B][1] at 2-34, citing In re Rimell, 946 F.2d 1363 (8th Cir. 1991), cert. denied 1992 WL 75855. This is the standard which the court indicated to the parties that it would use in the case at bar. See transcript of hearing held August 14, 1995, dkt. #48 in 95-02187 at pp. 275-276.

Thus, the court must determine whether there is a "dispute", and whether said dispute is "bona fide". In doing so, the court need not determine the outcome of the dispute. Ginsberg, §2.03[C][3] at 2-42, citing Matter of Busik, 831 F.2d 745 (7th Cir. 1987); In re Caucus Distributors, Inc., 106 B.R. 890 (Bankr. E.D. Va. 1989). See also, Norton § 21:3 at 21-8. A bona fide dispute exists when a creditor's judgment against the debtor is subject to a countervailing claim that could entirely offset the creditor's judgment. Ginsberg, id., citing In re Henry, 52 B.R. 8 (Bankr. S.D. Ohio 1985). A bona fide dispute also exists when the debtor has not admitted liability to the petitioning creditors nor have the creditors proven the debtor's liability. Ginsberg, id., citing In re Reid, 773 F.2d 945 (7th Cir. 1985). The postpetition payment or settlement of a debt

does not disqualify the creditor by rendering the dispute not bona fide because the number of petitioning creditors is determined as of the date of filing. Ginsberg, id., citing Bartman v. Maverick Tube Corp., 853 F.2d 1540 (10th Cir. 1988); In re Carvalho Industries, Inc., 68 B.R. 254 (Bankr. D. Or. 1986).

Claim #1 - Plaza Inmaculada, SE

Claim #1 in each of these involuntary cases was filed by Plaza Inmaculada, SE in the amount of $3,030,300.00. The parties agree that it arises from a construction dispute surrounding the building of phase II of the Plaza Inmaculada project and is subject of litigation pending before the Superior Court of Puerto Rico in case no. KDC 91-1048; however, they disagree as to whether the claim amounts to a bona fide dispute.

The Gutierrez' filed a civil action against Efron and Plaza Inmaculada in the Superior Court of Puerto Rico, case no. KDC 91-1048, for breach of the stock purchase agreement and collection of fees, seeking in excess of $5 million. (Ex. 14)[7]. Plaza Inmaculada filed a counterclaim for over $9,000,000.00 in damages, alleging negligence, breach of contract, and other acts by the Gutierrez. (Ex. 15). Plaza Inmaculada's claim was based upon the absence of certain "cross ties", which allegedly precluded the certification of the building for use by the Regulation and Permit Authority ("ARPE")

Petitioning creditors argue that claim #1 has already been adjudicated against the debtors. They argue that within the Superior Court litigation Plaza Inmaculada moved the court for provisional remedies in order to mitigate damages, and that the Superior

[7]Exhibit numbers refer to exhibits entered into evidence during the course of the evidentiary hearing held in August, 1995.

Court eventually so ordered said mitigation, further finding that the cost of the same would be assessed against the Gutierrez' if they did not prevail in overturning the decision of ARPE. (Ex. n). Plaza Inmaculada then presented a proposal to ARPE, obtained their approval of the same, corrected the alleged problem and received ARPE's certification of the building at a cost of over $3,060.000.00, the basis of claim #1.

Debtor's challenged ARPE's decisions i.e. their initial denial of certification of the building, their approval of the owner's proposed modifications and their denial of debtor's proposal, by seeking reconsideration by ARPE itself as well as review by the Superior Court of Puerto Rico and, subsequently, the Supreme Court of Puerto Rico. (Exs. Z, a - f). The petitioning creditors argue that debtors lost before each of these forums, and that therefore their claim is final, resolved within the Superior Court litigation by virtue of that court's order of August 20, 1993, as well as the orders of the Superior Court and Supreme Court affirming the decisions of ARPE. The petitioning creditors further argue that the debtor's claims (subject of the Superior Court action) which they allege may be set off against the petitioning creditor's claim, while admitedly subject to dispute, do not constitute a "bona fide dispute" in that they are merely counterclaims and do not make the claim subject to a bona fide dispute.

Debtors argue that although ARPE initially ruled against them, said ruling was a "prima facie" one, did not involve testing the building or hearing evidence, failed to consider the debtors' submissions, and is nullified by subsequent actions by ARPE and Efron, including ARPE's acceptance of debtors certification of the building in a letter dated December 11, 1995. Further, they argue that the fact that ARPE made a

determination does not mean that Plaza Inmaculada's claims in the Superior Court litigation are "liquidated and practically adjudicated"; rather, they argue that ARPE's decision was not a final ruling and that the Superior Court action is an ongoing litigation which was stayed by the filing of these involuntary petitions.

The court agrees with debtors that claim #1 is subject of a bona fide dispute. The Superior Court litigation, which was stayed after the filing of these involuntary petitions, is an ongoing proceeding, the final determination of which will affect the ultimate liability between the parties therein. It must be remembered that the Superior Court action was brought by the debtors herein; Plaza Inmaculada's claim in this bankruptcy proceeding is based upon a counterclaim in the state court action. As has been previously noted, a bona fide dispute exists when a creditor's judgment against the debtor is subject to a countervailing claim that could entirely offset the creditor's judgment. Ginsberg, id., citing In re Henry, 52 B.R. 8 (Bankr. S.D. Ohio 1985). The debtors' claims are not merely counterclaims raised against the petitioning creditor's claims herein; rather, they are independent, albeit interrelated, claims which are the basis for the Superior Court proceeding. Accordingly, claim #1 is disqualified as being subject of a bona fide dispute pursuant to 11 U.S.C. § 303(b)(1).

Claim #2 - Plaza Inmaculada, SE

Claim #2 in each of these involuntary cases was filed by Plaza Inmaculada, SE in the amount of $29,325.00. It arises from a payment made to Milton Martinez for professional fees during the course of the Superior Court litigation and the proceedings

before ARPE. The claim is based upon the Superior Court's order dated August 20, 1993, which provided that the costs of repairing the building as required by ARPE would be borne by Efron, without prejudice to him recovering the same from the Gutierrez', depending upon the outcome of the arbitration proceeding and the litigation before the court. (Ex. n)

Debtors raise two defenses to this claim which they allege renders it subject to bona fide dispute. First, they argue that a subsequent order of the Superior Court on October 21, 1993 (Ex 18), indicating that Efron and the Gutierrez' could submit seperate reports to ARPE, constitutes a reconsideration of the August 20 ruling and supercedes the same, indicates that each party should bear the cost of their own reports, and creates a dispute as to whether any fees to Martinez are owed by debtors at all. Secondly, they argue that any costs incurred would not be payable until the conclusion of the Superior Court litigation, which has not yet been resolved. Furthermore, debtors argue that the Superior Court proceeding includes many affirmative claims against Plaza Inmaculada which are unresolved and which, if found in the debtors' favor, would offset any claims awarded to Plaza Inmaculada.

As with claim #1, the court agrees with debtors that claim #2 is subject to a bona fide dispute. The Superior Court order of August 20 indicates that the recovery of Mr. Martinez' fees depends uon the outcome of the litigation, which is still pending before that court. Accordingly, claim #2 is disqualified as being subject of a bona fide dispute pursuant to 11 U.S.C. § 303(b)(1).

Claim #3 - David Efron

Claim #3 in each of these involuntary cases was filed by David Efron in the amount of $260,000.00. It arises from a payment made by Efron to Banco Santander on behalf of an obligation inherited from his father, Jose Efron, who had guaranteed a $500,000.00 loan given by the bank to Advisors Investment Group ("AIG"), a corporation wholly owned by the Gutierrez'. (Ex. N). (The debt to AIG was also guaranteed by the Gutierrez' themselves. (Ex. J)). Subsequent to David Efron's partial payment on the obligation to the bank, the bank disbursed the same amount to debtors, returning the obligation to its original amount. Efron brought an action against the bank in Superior Court, case no. KAC 91-0072; said action was consolidated with the Gutierrez' action, KDC 91-1048, and Efron subsequently obtained a judgment against the bank upon a motion for summary judgment (Ex. G). Upon entry of said judgment the bank delivered the notes and guarantees, endorsed to Efron, as ordered by the court.

Debtors argue that this claim is intertwined with the issues pending in the Superior Court litigation and that their claims may serve to offset the same. Further, they argue that Efron is not a holder in due course because the note was acquired after maturity, and is therefore subject to all defenses they may assert against Santander.

The court agrees with the petitioning creditors that this claim is not subject of a bona fide dispute. Even though the claim may be related to the issues pending in the Superior Court litigation, it is based upn a judgment which is final and unappealable. Accordingly, claim #3 is a qualifying claim under the requirements of 11 U.S.C. § 303(b)(1).

Claim #4 - David Efron

Claim #4 in each of these involuntary cases was filed by David Efron in the amount of $324,000.00. It arises from a promissory note in the amount of $300,000.00 which was executed by Villa Marina Village, personally guaranteed by the Gutierrez', and assigned to Efron by Dr. Israel Ganapolsky. According to petitioning creditors, when Efron gave notice of the transfer of the note the Gutierrez' filed an action for declaratory judgment in the Superior Court of Puerto Rico, case no. KAC-94-1315. (Ex. 30). According to petitioning creditors, this action has a motion for summary judgment pending (Ex h) which was unopposed by the Gutierrez', despite the fact that the court ordered them to answer and granted additional time to do so. Furthermore, according to petitioning creditors, the Gutierrez' moved the Superior Court to stay the proceedings when this involuntary petition was filed, and have requested that the court abstain from entertaining the summary judgment issue, arguing that it should be resolved by this court.

Debtors argue, as with the previous claim, that this claim is intertwined with the Superior Court Plaza Inmaculada litigation, as well as subject of its own proceeding, that the note subject of the claim was acquired after maturity and Efron is therefore not a holder in due course and subject to any defenses the debtors may raise against Ganapolsky, and that their affirmative claims against Efron may offset any award to him on this claim.

The court agrees with debtors that claim #4 is subject of a bona fide dispute. Even though a summary judgment motion is pending, as petitioning creditors themselves

admit, no final judgment has been entered in the Superior Court action, which is stayed.[8] Accordingly, claim #4 is disqualified as being subject of a bona fide dispute pursuant to 11 U.S.C. § 303(b)(1).

Claim #5 - Bailey, Hunt & Jones

Claim #5 in each of these involuntary cases was filed by the law firm of Bailey, Hunt & Jones in the amount of $22,459.00, and is based upon a claim of legal fees owed by the involuntary debtors to the firm for legal representation in an action in Florida. The petitioning creditors argue that the debtors have admitted to a debt with the firm, illustrated by their proposed settlement of the debt for $15,000.00 with a payment plan. They further point to letter sent post-petition by the debtors' former counsel to the firm indicating that their claim could not exceed $10,000.00. (Ex. E). The petitioning creditors argue that this is an admitted debt, and that any dispute as to the exact amount owed does not disqualify the creditor as a petitioner under 11 U.S.C. § 303.

Debtors argue that they owe nothing to the firm, and that they have always maintained this position. Nevertheless, they admit to acquiesing to the settlement agreement and forwarding $5,000.00 to the firm to "avoid any conflict". They argue that the existence of the settlement agreement does not establish that the claim is not subject of a bona fide dispute, and contend that insufficient evidence has been presented on the matter. Debtors go on to note that they have made provisions for the resolution of the firm's claim, in the event that the court determines that it is not subject of a bona fide

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[8]The court notes that case no. KAC-94-1315 is not an action automatically stayed by 11 U.S.C. § 362.

dispute, by depositing the full amount of the claim with their current attorneys. They argue that the firm thus no longer faces risk of non-payment and should therefore be disqualified as a petitioning creditor because their claim should be deemed satisfied.

Debtors have clearly acknowledged the existence of this debt, as evidenced by various testimonies and submissions to this court; accordingly, the court agrees with petitioning creditors that claim #5 is not subject of a bona fide dispute within the meaning of 11 U.S.C. § 303(b)(1). The fact that debtors have provided for the resolution of this claim does not disqualify it; as has been previously noted, the post-petition settlement of a debt does not disqualify the creditor by rendering the dispute not bona fide because the number of petitioning creditors is determined as of the date of filing. Ginsberg, § 2.03[C][3] at 2-42, citing Bartman v. Maverick Tube Corp., 853 F.2d 1540 (10th Cir. 1988); In re Carvalho Industries, Inc., 68 B.R. 254 (Bankr. D. Or. 1986).

Joinder of Creditors

As this court previously noted in its Opinion and Order of April 26, 1996 (dkt. #79 in case no. 95-02187), an involuntary petition which is defective because it has an insufficient number of petitioning creditors, or because one of their claims is disqualified, may be subject to cure as of right. Norton § 21:8 at 21-14, citing In re Crown Sportswear, Inc., 575 F.2d 991 (1st Cir. 1978) ("[i]ntervention is a matter of right unless the Bankruptcy Court finds the petition was made in bad faith"). The Bankruptcy Code provides that creditors may join in the petition with the same effect as if they were a

petitioning creditor. 11 U.S.C. § 303(c).[9] If the claim of one of the petitioning creditors is found to be subject to a bona fide dispute, disqualifying that creditor, the court may permit the remaining creditors to seek an additional creditor to join the petition. Collier, ¶ 303.08[11][b] at 303-35, ¶ 303.33 at 303-115; Ginsberg at 2-52, citing In re Kidwell, 158 B.R. 203 (Bankr. E.D. Cal. 1993); In re Johnston Hawks, Ltd., 49 B.R. 823 (Bankr. D. Hawaii 1985). However, for joinder to be permitted, the initial petition had to be filed in good faith. In re LaRoche, 131 B.R. 253 (D.R.I. 1991), aff'd 969 F.2d 1299 (1st Cir. 1992). See also 8 Lawrence P. King, et al., Collier on Bankruptcy ¶ 1003.05 at 1003-13. This court indicated in the aforementioned Opinion and Order that it may allow time for additional creditors to join the petition if it finds that one or more of the claims upon which the petitions were filed is subject of a bona fide dispute.

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[9]Section 303(c) provides: "[a]fter the filing of a petition under this section but before the case is dismissed or relief is ordered, a creditor holding an unsecured claim that is not contingent, other than a creditor filing under subsection (b) of this section, may join in the petition with the same effect as if such joining creditor were a petitioning creditor under subsection (b) of this section." 11 U.S.C. § 303(c).

Conclusion

Petitioning creditors' claims #1, #2 and #4 are subject of bona fide disputes and therefore may not be the basis for the filing of these involuntary petitions in bankruptcy pursuant to 11 U.S.C. § 303(b)(1), which prohibits the same. Accordingly, Plaza Inmaculada, SE is disqualified from being a petitioning creditor in these petitions as both of its claims have been found to be subject of bona fide disputes. This leaves only two petitioning creditors, David Efron and Bailey, Hunt & Jones, an insufficient number of creditors under 11 U.S.C. § 303(b)(1).

The court hereby orders the involuntary debtors to answer the petitions within a period of twenty (20) days from the date of entry of this order, and to comply with the requirements of Fed. R. Bankr. P. 1003(b). Pursuant to said rule, if the answer to the petition avers the existence of twelve (12) or more creditors, the court grants the remaining creditors a period of fifteen (15) days from the date of filing of the answer to find an additional creditor(s) to join the involuntary petitions.

SO ORDERED.

In San Juan, Puerto Rico, this 22nd day of November, 1996.

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ENRIQUE S. LAMOUTTE
Chief, U.S. Bankruptcy Judge