

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF WASHINGTON

KAREN A. OVERSTREET
Chief Judge

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December 1, 2008

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Re: *Court Reporting Institute, Inc.*; 06-14202
Alen Janisch; 07-15620

**COURT'S LETTER RULING ON TRUSTEE'S
MOTION FOR AN ORDER APPROVING COMPROMISE**

Dear Mr. Rigby, Ms. Ellis, Mr. Sato and Ms. McKinney:

On October 24, 2008, I held a hearing on the trustee's Motion for an Order Approving Compromise of Claims (the "Trustee's Motion"). The Trustee's Motion seeks approval of two separate settlement agreements: (i) a settlement between the trustee in the case of Court Reporting Institute, Inc. ("CRI") and the trustee in the case of Alen Janisch; and (ii) a compromise of the claims of the estate of both Janisch and CRI against Steve Fleischman, the Fleischman Family LLP, Fleischman

December 1, 2008

Page 2

Center and other entities owned or operated by the Fleischman family (collectively, "Fleischman").

I. Background and Facts.

Alen Janisch was the sole owner, director and officer of CRI. Mr. Janisch filed a Chapter 7 personal bankruptcy on November 23, 2007, Case No. 07-15620. Edmund J. Wood was appointed as trustee for the Janisch estate. CRI filed a bankruptcy petition on December 28, 2006 at Case No. 06-14202. Michael B. McCarty was appointed as trustee for the CRI bankruptcy estate. Mr. McCarty commenced an adversary proceeding against Mr. Janisch and Mr. Kai Moldskred, Case no. 07-01167, asserting several claims arising from their involvement with CRI (the "Adversary Proceeding"). Specifically, the Adversary Proceeding stated claims against Mr. Janisch for fraudulent conveyance and claims against Mr. Moldskred under both fraudulent conveyance and immediate or mediate transferee theories.

A. Partial Summary Judgment in Adversary Proceeding against Moldskred and Janisch.

On June 20, 2008, the Court granted partial summary judgment in the Adversary Proceeding in favor of Mr. McCarty. See Order of Partial Summary Judgment, docket no. 47. The Court found that from January 1, 2006 until September 7, 2006, CRI issued a series of checks made payable to Mr. Janisch in the total amount of \$487,360, which checks were negotiated by Mr. Janisch for his own benefit. The Court found that CRI received no consideration for the transfers. The Court also found that of the \$487,360 received by Mr. Janisch, \$150,000 was thereafter paid to Mr. Moldskred in payment of a short term loan made by Mr. Moldskred to Mr. Janisch. The Court found that Mr. Moldskred was the immediate transferee of the \$150,000 fraudulently transferred pursuant to Bankruptcy Code §550(b). In addition, the Court found that Mr. Moldskred was the initial transferee of \$123,000 in fraudulent conveyances in the form of a series of checks paid to Mr. Moldskred by Mr. Janisch from funds of CRI at a time when Mr. Moldskred was not a creditor of CRI, CRI having received no consideration for the transfers.

The Court's order on partial summary judgment granted Mr. McCarty judgment against Mr. Janisch in the amount of \$905,360 (the \$487,360 in cash transfers, the \$123,000 paid by CRI to Moldskred on Janisch's obligation to Moldskred and \$295,000 for the reduction and satisfaction of a promissory note owed by Janisch to CRI). Mr. McCarty was also awarded judgment

December 1, 2008

Page 3

against Mr. Moldskred for \$123,000. With regard to the \$150,000 in transfers, the Court found in Mr. Moldskred's favor that he had provided indirect benefit (consideration) to CRI for these transfers. However, the Court found there were disputes of material fact as to whether Mr. Moldskred had a complete defense to liability under Bankruptcy Code §550(b)(1) because he acted in good faith and without knowledge of the voidability of the transfers. The latter issues were reserved for trial.

B. Claims of CRI and Janisch against Fleischman.

Both the CRI and the Janisch estate may have claims against Fleischman. On behalf of the CRI estate, Mr. McCarty filed an adversary proceeding against Mr. Steve Fleischman and the Bank of America to recover \$62,000 held in an account pursuant to a letter of credit transaction (adversary case no. 08-01131). In addition, Mr. McCarty filed an adversary complaint against the Fleischman Family Limited Partnership d/b/a Fleischman Center, to recover \$150,000 which was transferred from CRI to Mr. Janisch and subsequently to Fleischman.

In the Janisch case, Fleischman has filed 3 timely proofs of claim, including Claim no. 1 for \$185,992.63 (for 16 months of lease payments on the real property located at 929 N. 130th, Seattle, which claim may be limited by 502(b)(6)), Claim no. 2 also for \$185,992.63, and Claim no. 3 also for \$185,992.63. Claim no. 3 is a duplicate of Claim nos. 1 and 2, but is filed on an official proof of claim form and has the lease attached. The lease is dated December 10, 2002, was to expire on December 31, 2007, and shows Mr. Janisch as the lessee. CRI is not obligated under the terms of the lease. Fleischman has agreed to waive this rent claim in the event the settlement and compromise are approved. Fleischman has not filed any claims in the CRI estate.

C. Claims Between the Bankruptcy Estates.

The bankruptcy estates of CRI and Mr. Janisch have competing claims against each other and against several assets. The CRI estate can only pursue its claims against the Janisch estate as a creditor in that case and is therefore barred by the automatic stay. Further, the Janisch trustee, Mr. Wood, has taken the position that he is the owner of the claims the CRI estate has made against both Fleischman and Moldskred. The Janisch estate also owns certain personal property that was assigned to Mr. Moldskred and may be recovered by the Janisch trustee, as well as avoidance claims and \$45,000 subject to a Deed of trust held by Mr. Moldskred.

D. Proposed Settlement and Compromise.

The CRI and the Janisch trustees have proposed a settlement of their claims against each other. See CRI docket, case no. 06-14202, docket entry no. 100, and Janisch docket, case no. 07-15620, docket entry no. 143. Under the terms of the proposed settlement, the two estates would each receive an equal division of all net proceeds recovered by either estate from the prosecution of avoidance claims, the sales of real and personal property, and the liquidation of assets in either estate. In addition, the CRI trustee proposes to settle his claims against Fleischman by a payment from Fleischman of \$92,000 to the CRI estate, said funds to be distributed pursuant to the terms of the above-described settlement, if approved.

A group of former students, who are also creditors of the CRI estate (the "Students"), filed an objection to the compromise of the Fleischman claims. The students contend that Fleischman knew his short-term loans to CRI were for the purpose of temporarily bolstering the year-end balance sheet of CRI in order to give the Department of Education ("DOE") a financial snapshot of CRI that would confirm its continued eligibility for the student loan funding that CRI needed in order to continue its operations. The continued operations allowed CRI to obtain more prepaid tuition from students who would never receive education or other value for their money. The students prefer to have the trustee take the \$62,000 letter of credit funds that Fleischman does not contest and use those monies to fund litigation against Fleischman to recover the alleged \$150,000 fraudulent transfer.

At the conclusion of the hearing, the Court took the matter under advisement and requested the CRI trustee to supplement the record with deposition transcripts referred to in oral argument referencing the transactions with Fleischman. The trustee submitted that additional information. See Supplemental Declaration of James Rigby in Support of Trustee's Motion for Settlement with Fleischman ("Rigby Supp. Decl."), docket no. 118. Ms. Judy McKinney also submitted supplemental materials on behalf of the Students. See docket no. 119. The Court has reviewed this supplemental material in making the ruling herein.

II. Law.

Bankruptcy Rule 9019(a) provides that the Court may approve a compromise or settlement upon motion of the trustee and after a hearing on twenty days' notice to all creditors and the United States Trustee. "The bankruptcy court has great latitude in

December 1, 2008

Page 5

approving compromise agreements." *Woodson v. Fireman's Fund Ins. Co. (In re Woodson)*, 839 F.2d 610, 619 (9th Cir. 1987). The court's discretion, however, is not unlimited; the compromise must be "fair and equitable" and "reasonable." *Id.*; *A & C Properties*, 784 F.2d 1377, 1381 (9th Cir. 1986), *cert. denied*, 479 U.S. 854 (1986). In determining the fairness and reasonableness of a proposed settlement, the court must consider: (a) The probability of success in the litigation; (b) the difficulties, if any, to be encountered in the matter of collection; (c) the complexity of the litigation involved, and the expense, inconvenience and delay necessarily attending it; (d) the paramount interest of the creditors and a proper deference to their reasonable views in the premises. *A & C Properties*, 784 F.2d at 1381. The Ninth Circuit Bankruptcy Appellate Panel has stated:

The function of compromise is to avoid litigation involving delay and expense unless there appears to be a sound legal basis for the litigation and a likelihood of substantial benefit to the estate (citation omitted). *Approval of compromise is appropriate if the court finds that the outcome of the litigation is doubtful*

Gen. Store of Beverly Hills v. Beverly Almont Co. (In re Gen. Store of Beverly Hills), 11 B.R. 539, 541 (9th Cir. BAP 1981)(emphasis added). Finally, as part of its decision, the Court may give weight to the opinions of the trustee, the parties and their attorneys. *A & C Properties*, 784 F.2d at 1384.

III. Analysis.

A. Compromise of Fleischman Claims.

In analyzing the proposed compromise of the Fleischman claims, the Court looks first at the trustee's probability of success in its litigation with Fleischman, specifically the claims for \$62,000 held in trust and for the \$150,000 Fleischman received as a subsequent transferee of CRI. The trustee contends that the \$62,000 was security for a letter of credit that has expired. Fleischman's answer (in adversary case no. 08-001131) does not dispute that he agreed to obtain a letter of credit for the benefit of CRI or that the \$62,000 was paid to him by Janisch and CRI. Fleischman contends he had a right to interest on the money but admits he must repay the principal amount. Accordingly, it would appear that the trustee is very likely to prevail on the claim against Fleischman for \$62,000.

December 1, 2008

Page 6

The trustee's probable success on the claim to recover the \$150,000 from Fleischman as a subsequent transferee of a fraudulent conveyance from Mr. Janisch is more uncertain. According to the facts set forth in adversary proceeding no. 08-01167, in December 2006, Fleischman transferred \$150,000 to Mr. Janisch as an interest-free loan with repayment in January, 2007. There is no documentation of the loan. On January 3, 2007, Mr. Janisch transferred \$50,000 to Fleischman via a personal check and an additional \$100,000 by personal check. The trustee alleges that Fleischman knew the purpose of the \$150,000 loan was to inflate CRI's capital account such that a "snapshot" at year end would show the DOE that CRI was in good financial standing. Mr. Fleischman denies this allegation.

The allegations against Fleischman are very similar to those made against Mr. Moldskred. In the Moldskred matter, the Court reserved for trial the issue of whether Mr. Moldskred acted in good faith and without knowledge of the voidability of the transfers at issue. Fleischman and Mr. Janisch have testified that their relationship has been that of landlord and tenant and friends, for the past 18 to 20 years. See Rigby Supp. Decl., Ex. C, p. 14, and Ex. B, p. 11. Fleischman had been making undocumented, interest-free, year-end loans to Mr. Janisch for "a few years" prior to 2005. See Rigby Supp. Decl., Ex. B, p. 15. See also Rigby Supp. Decl., Ex. C, p. 13. Mr. Fleischman claims he did not know the purpose of the loans. Rigby Supp. Decl., Ex. B, p. 15. Resolution of these issues will require a factual determination of what Fleischman knew and whether he was acting in good faith. Fleischman's counsel has indicated they will vigorously defend these claims. While the costs of litigation are never known in advance, the cost of pursuing the claims against Fleischman would likely be in line with the costs associated with the Moldskred litigation, where the Trustee indicates he has spent \$80,000 to reach the point of the current settlement and would anticipate incurring an additional \$50,000 to conclude the litigation and defend an appeal. The Court notes that Fleischman has also agreed to waive his rent claim in the Janisch bankruptcy upon approval of the settlement.

In considering the settlement of the Fleischman claims, the Court is very cognizant of the objection and interest of the Students. The Students note that under the terms of the proposed settlement, because the trustee will easily be able to recover \$62,000 from Fleischman, Fleischman is really only giving up an additional \$30,000 to settle the \$150,000 fraudulent conveyance claim. The Students would prefer to see the Trustee pursue the

claim for the \$62,000 and use the monies recovered in that litigation to pursue the remaining claims against Fleischman. However, there are risks inherent in any litigation and the trustee will need to prevail on a number of difficult factual issues in order to prevail at trial. The Court has already ruled in the Moldskred case that the determination of good faith and knowledge are factual issues that must be dealt with at trial rather than on summary judgment. Based on his experience with the Moldskred litigation, the Trustee estimates he could spend \$120,000 pursuing these claims, and still may not be successful. In addition, the trustee has argued that there are differences between the case against Moldskred and the case against Fleischman that make the case against Moldskred stronger. In particular, Mr. Moldskred was an employee at one time of CRI so knew much more about the inner workings of the company and its relationship with DOE. Mr. Fleischman was never an employee of CRI and there is no evidence he had any detailed knowledge of CRI's relationship with DOE.

By settling with Fleischman, the trustee avoids the cost of filing a summary judgment motion on the \$62,000 and any claims litigation relating to the rent claim. The settlement provides certainty as to the payment of those funds plus an additional \$30,000 to the estates. The Court is extremely sensitive to the concerns raised by the Students and to the significant harm they have suffered as a result of the actions of CRI and Janisch. Although forcing the trustee to use precious estate assets may make them feel better, on balance, the Court finds it would not be a wise use of estate resources. The Court will therefore approve the proposed compromise with Fleischman.

B. Compromise of Claims Between the Estates.

The CRI estate is holding a partial summary judgment against Mr. Janisch in the amount of \$905,360 which it cannot enforce because of the automatic stay. The CRI estate also holds a judgment against Mr. Moldskred for \$123,000 and partial summary judgment against Mr. Moldskred for \$150,000 that is recoverable if the Trustee can prove lack of good faith. Both estates have claims against Fleischman, as described above. The Janisch trustee claims ownership of the claims CRI has asserted against Fleischman and Moldskred. These estates are very intertwined and litigation between the two estates has the potential to be very expensive. No party has objected to the proposed settlement between the two estates. Accordingly, the Court finds the settlement between the two estates to be reasonable.

December 1, 2008

Page 8

Proposed orders consistent with this ruling should be noted for hearing on notice to all interested parties.

Very truly yours,

A handwritten signature in black ink, reading "Karen A. Overstreet". The signature is written in a cursive, flowing style.

Karen A. Overstreet
United States Bankruptcy Judge