

**UNITED STATES BANKRUPTCY COURT
IN AND FOR THE DISTRICT OF ARIZONA**

JAN 13 2005

UNITED STATES
BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

In re)
)
INTERNATIONAL SURFACING,)
INC.,)
)
Debtor.)

**Case No. 96-05142 PHX-CGC
Chapter 11**

**UNDER ADVISEMENT DECISION RE:
JOINT MOTION FOR
RECONSIDERATION OF FINOVA
CAPITAL CORPORATION AND
TRUSTEE JOSEPH J. JANAS**

I. Introduction

This Joint Motion for Reconsideration/Motion for New Trial ("Motion") is the latest volley in a long war among the trustees of two related bankruptcy cases (In re International Surfacing, Inc. ("ISI"), 96-05142-CGC, and In re JWJ Contracting Co., Inc. ("JWJ"), 94-06045-RTB); FINOVA Capital Corporation ("FINOVA"), a creditor of ISI's; and certain insiders, particularly Carl and Marilyn Jacobson ("the Jacobsons") and the Jacobson Family Trust ("the Trust"). The war has been fought on many fronts, most particularly in two separate bankruptcy cases before two different judges.

The multiple pieces of litigation have led to numerous settlements among the parties. In May 2004, two separate settlement agreements were reached that are inextricably intertwined. One is an agreement between JWJ and Finova, approval of which was only sought in the JWJ case ("the JWJ Settlement"). The second involves both trustees and Finova, approval of which has been sought in both cases, although substantive approval of this second agreement lies primarily here as it involves a request to modify an order previously entered in this case ("the ISI Settlement").

The background facts and circumstances have been previously set out in considerable detail in this Court's October 21, 2004, Under Advisement Decision Re: Motion to Approve Settlement Agreement and will not be extensively restated here. The Court assumes that all parties understand the facts and shorthand references to various other agreements and orders previously entered. Movants ask this Court to reconsider its October 21, 2004, Under Advisement Decision disapproving the ISI settlement agreement, and the Court has taken this opportunity to review the entire background of this case.

1 **II. Discussion**

2 As a result of its review, the Court denies Movants' Motion. Indeed, the deeper the Court dug,
3 the more troublesome the entire situation became.

4 Here is what is troubling about this ISI Settlement:

5 1. First, the real economic deal was not adequately disclosed in the ISI motion because the
6 operative economic terms are actually contained in the JWJ Settlement. A review of only the ISI
7 Settlement reveals that ISI and JWJ are agreeing to pay Finova what they had already agreed to pay (a
8 total of \$120,000, split \$100,000 and \$20,000) and the question presented is: for what? Indeed, the only
9 really significant term in the ISI Settlement is the proposed amendment to this Court's Stay Relief Order
10 ("SRO") "clarifying" that it did not effect a release of Finova's lien on the 8.5 Acre Parcel. Thus, the deal
11 appears to benefit only Finova – that is, until one reads the JWJ Settlement. In that agreement, the JWJ
12 Trustee receives 63% of the proceeds otherwise recovered by FINOVA from the 8.5 acre proceeds.

13 2. Second, when he had a direct economic stake in the outcome, the JWJ Trustee argued
14 strenuously that the SRO had in fact released FINOVA's liens, both as to ISI property and as to the 8.5
15 Acre Parcel. The JWJ Trustee's position on this could not have been more clearly stated. This appears
16 to have been for two reasons: first, if Finova had no claim to the ISI proceeds, then the JWJ estate would
17 not be liable to ISI under its agreement to reimburse \$100,000. Second, the JWJ Trustee had previously
18 obtained judgments avoiding the transfers of the 8.5 Acre Parcel from JWJ down the chain of title to the
19 Trust – thus, it had a potential claim to the 8.5 Acre Parcel proceeds if it could knock out FINOVA's lien.
20 Of course, the Insider Settlement (approved after entry of the avoidance judgment) may stand in the way
21 but that's a battle for another day.

22 3. FINOVA, meanwhile, is looking for an avenue to recover the \$1 million paid to the JWJ
23 Trustee on the Section 550 judgment. For that reason, it argues strenuously that it never intended to release
24 its lien on the 8.5 Acre Parcel until the clawback issue was resolved. But there are significant problems
25 with that position. As pointed out in the previous decision, the language of the SRO clearly contemplates
26 the eventual release of the 8.5 Acre Parcel. As pointed out before, there are ways to parse the SRO to
27 conclude that the obligation to release never ripened, but the risk was certainly there that FINOVA would
28 have no claim against the proceeds at the end of the day, an undesirable outcome for it.

1 4. Meanwhile, the JWJ Trustee wants to receive additional proceeds but he is faced with the
2 Insider Agreement as an impediment because he has agreed not to pursue the 8.5 acres in exchange for
3 payment of \$375,000. Of course, the issue whether the Finova lien survived was "preserved" under the
4 Insider Settlement so litigating that continued to be fair game; but the JWJ Trustee had already made it clear
5 through numerous pleadings that he thought FINOVA's position was bogus. So a solution presented itself:
6 1) agree to make it easier for FINOVA to prevail against the 8.5 acres by switching sides on the SRO issue;
7 2) accept without argument FINOVA's unilateral "representation and warranty" that it never intended to
8 release the 8.5 acres; 3) take the lead on getting the SRO modified; 4) receive 63% of the proceeds from
9 FINOVA as consideration; and 5) argue that none of this affects the Insiders because, after all, they owe
10 the money to FINOVA, not to the JWJ Trustee.

11 5. But the problem is that FINOVA is using JWJ Trustee's new found acquiescence as a means
12 of solidifying its claims against the 8.5 Acre proceeds, while at the same time both assert that the Insiders
13 lack any say in the matter. Arguing that the Insiders were not parties to the SRO, FINOVA and the JWJ
14 Trustee claim they have no standing. Purely in the context of the ISI case this is correct and the Court so
15 held. But the context is broader than that, as both of these parties know. The clear intent of FINOVA (and
16 JWJ Trustee, now that he has a 63% beneficial interest in the proceeds) is to take the "clarified" SRO and
17 give it to the JWJ Court as ammunition against the Trust's claim in its declaratory judgment action by
18 asserting that this Court has already decided what the SRO means. Of course, that is what the Trust also
19 wants to do, so long as the original October 21 order remains intact. Indeed, it already has done so when
20 it asked the JWJ Court to take judicial notice of the October 21 order at hearing on the FINOVA/JWJ
21 compromise. And, one believes, FINOVA is likely very much aware of its risk since it has agreed to
22 undertake the litigation against the Insiders and only keep 37% of the proceeds. Although there is no factual
23 record before this Court on how the allocation was reached, these percentages do not suggest that
24 FINOVA thought it had the better of the argument. While this fact may not be admissible in another
25 proceeding under Rule 408 where the matter compromised is at issue, it is relevant here to whether this
26 settlement ought to be approved.

27 6. FINOVA complains that it is being unfairly taken to task for seeking to clarify the SRO, but
28 its protestations ring hollow. FINOVA's underlying theme is that it was not sued under 11 U.S.C. section

1 550 until after the SRO was entered, so there was no basis to protect itself against the early release of its
2 lien on the 8.5 Acre Parcel. Thus, its clawback provisions kicked in later and revived the claim and the lien.

3 There are two problems with this argument. First, there is no clawback provision in the deed of
4 trust; even in the lengthy motion for reconsideration that proposition was not challenged. Second, and more
5 importantly, at the time the SRO was presented to this Court for signature, FINOVA was clearly on notice
6 that the JWJ Trustee would be looking to it as a source of recovery for the preferences paid on ISI's behalf
7 by JWJ. As early as November of the previous year, the JWJ Trustee had so informed FINOVA. In
8 January, the JWJ Trustee advised that he would not object to the SRO so long as his Section 550 rights
9 against FINOVA were unaffected. FINOVA admitted the truth of both of these statements in response to
10 the Statement of Facts relating to the Motion for Summary Judgment in Adversary Proceeding 01-119. In
11 addition, as pointed out in other orders, the SRO was certainly less than a model of clarity on the issues of
12 whether FINOVA's agreement to release its lien on the 8.5 Acre Parcel was inoperative if it was pursued
13 the Trustee under Section 550. Indeed, the total lack of any language relating to the issue is the very reason
14 the "clarification" of the SRO is a major cog in this proposed settlement.

15 7. The ISI Trustee is largely a bystander to this little drama. For the most part, he simply
16 wants everything resolved. He had previously agreed to pay FINOVA net \$20,000 in exchange for
17 FINOVA's waiver of any further claims against his proceeds and he is still happy to do that.

18 The Court finds this entire dance distasteful. Litigation is supposed to be conducted on the merits,
19 not by stealth. Taken separately, these two settlements seem fair enough. Thus, it seems reasonable enough
20 that the parties to a dispute should be able to carve up the spoils in a way that reflects their perceived risks
21 – that's what happened in the JWJ Bankruptcy before Judge Baum. In this case, it seems reasonable
22 enough to resolve a dispute by a stipulated "clarification" of an order previously agreed to by the same
23 parties while insisting that parties who are strangers to the SRO, i.e., the Insiders, have no standing to
24 complain. Both of these propositions are reasonable on their face, until it becomes clear that 1) the purpose
25 of the "clarification" is to pre-empt the issue in another adversary proceeding (where the Insiders are
26 plaintiffs and do have standing) so as to be able to state to the other judge, "See, this is what the judge who
27 entered the order thinks the order means; that should be the end of it," and 2) that the division of the spoils
28 in the one case is what is driving the request for "clarification" in the other.

1 The SRO is what it is. The Insider Settlement is what it is. A forum exists to resolve disputes
2 swirling around those matters in the old fashioned way – through presentation of evidence and argument
3 where all interested parties are present and participate.

4 The bottom line here is that pending before Judge Baum is the adversary proceeding, newly
5 transferred from Judge Murguia, that squarely presents the two remaining issues: 1) does FINOVA still have
6 a lien on the proceeds from the sale of the 8.5 Acre Parcel and (2), if not, who wins between the JWJ
7 Trustee (asserting the avoidance judgment as his trump card) and the Insiders (asserting their settlement with
8 the JWJ Trustee as their trump card). Let that be decided on the evidence, not on language concocted by
9 the parties in another proceeding in another context or, for that matter, by language in an order where the
10 matter was not directly presented. Neither the “clarified” SRO nor the Under Advisement Decision should
11 be conclusive on this issue.

12 For the forgoing reasons, the Court will not approve a settlement that provides for modification of
13 the previous SRO.

14 Motion to reconsider denied.

15 So ordered.

16 DATED: January 13, 2005

17
18 
19 Charles G. Case II
UNITED STATES BANKRUPTCY JUDGE

20 Copy of the foregoing hand-delivered and/or mailed
21 this 13th day of January, 2005, to:

22 Hon. Redfield T. Baum

23 Joseph Janas, Trustee
24 2434 East Patrick Lane
Phoenix, Arizona 85024

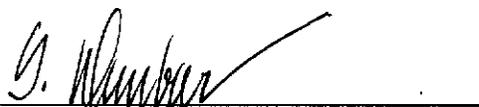
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