United States Bankruptcy Court
Western District of Wisconsin

Cite as: [Unpublished]

Bruce A. Schultz, individually and on behalf of the partnership, Schrank & Schultz, Plaintiff,
and
First Wisconsin National Bank of Madison, Involuntary Plaintiff,
v.
Raymond E. Schrank II, Cannon & Dunphy, S.C., William M. Cannon and Patrick O. Dunphy, Defendants
(In re Raymond E. Schrank, II, d/b/a Schrank Law Offices, f/d/b/a Schrank and Schultz, and Barbara A. Schrank, Debtors)
Bankruptcy Case No. 90-03199-7, Adv. Case. No. A91-1036-7

United States Bankruptcy Court
W.D. Wisconsin, Eau Claire Division

July 9, 1992

James W. Gardner and Bruce M. Davey, for the plaintiff.
Robert E. Shumaker, for the First Wisconsin National Bank of Madison.
Thomas G. Cannon, for defendants Cannon & Dunphy, S.C., William M. Cannon and Patrick O. Dunphy (Cannon & Dunphy).
J. Ric Gass and Leonard G. Leverson, for defendant Raymond E. Schrank II.

Thomas S. Utschig, United States Bankruptcy Judge.

MEMORANDUM OPINION, FINDINGS OF FACT, AND CONCLUSIONS OF LAW

This matter comes before the Court on a motion by the plaintiff for abstention and relief from stay. The plaintiff is Bruce A. Schultz and he is represented by James W. Gardner and Bruce M. Davey. First Wisconsin National Bank of Madison is an involuntary plaintiff in this matter; it is represented by Robert E. Shumaker. The defendants are Cannon & Dunphy, S.C., William M. Cannon and Patrick O. Dunphy (Cannon & Dunphy), all represented by Thomas G. Cannon; and Raymond E. Schrank, II, represented by J. Ric Gass and Leonard G. Leverson. The debtors in the underlying bankruptcy proceeding are Raymond E. and Barbara A. Schrank.

This matter essentially involves a dispute between former law partners over contingency fees in various personal injury cases. Plaintiff Bruce Schultz (plaintiff) and defendant Raymond Schrank II were law partners from August of 1988 to February of 1990. At some point in late 1990, defendant Schrank accepted employment at the law firm of Cannon & Dunphy, S.C. As noted, this law firm and two of its partners, William M. Cannon and Patrick O. Dunphy, are also defendants in this action.

The plaintiff raises numerous claims against the defendants collectively and individually. Against defendant Schrank, the plaintiff alleges breach of fiduciary duty of a managing partner, breach of fiduciary duty in conversion of partnership assets, breach of settlement agreement, fraud in the inducement of formation of the partnership, and providing false financial statements to Bank One. Against defendants Schrank and Cannon & Dunphy collectively, the plaintiff alleges injury to business in violation of Wisconsin Statute § 134.01 and civil conspiracy.[(1)] Against defendant Cannon & Dunphy, plaintiff alleges tortious interference with contractual relations. The plaintiff has also attached various citations to nondischargeability provisions of the bankruptcy code to several of the aforementioned state law claims, thus alleging violations of these provisions as well. These cited provisions include 11 U.S.C. §§ 523(a)(2(a), (a)(4), and (a)(6).

Aside from involving a variety of claims based on state and federal law,[(2)] this case also has a lengthy procedural history and has already generated voluminous documents, exhibits, motions and memoranda. It was originally filed in the United States Bankruptcy Court for the Western District of Wisconsin.[(3)] The federal RICO claim precipitated the withdrawal of reference to the bankruptcy court. The district court subsequently dismissed the RICO claim and referred the matter back to this Court. The plaintiff filed a motion to reconsider which was denied by the district court on March 12, 1989. See Schultz v. Schrank, No. 91-C-0202-C (W.D. Wis. March 12, 1992). Numerous motions remain outstanding in this matter. These include a motion to dismiss various counts of plaintiff's amended complaint and a motion for summary judgment filed by Cannon & Dunphy, the same two motions filed separately by defendant Schrank, a motion to compel discovery filed by the plaintiff, and the plaintiff's motion to abstain. Given the preliminary nature of this last motion, the Court will limit its decision to the abstention issue.

Abstention is governed by 28 U.S.C. § 1334(c) which provides

> (c)(1) Nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11.
>
> (2) Upon timely motion of a party in a proceeding based upon a State law claim or State law cause of action, related to a case under title 11 but not arising under title 11 or arising in a case under title 11, with respect to which an action could not have been commenced in a court of the United States absent jurisdiction under this section, the district court shall abstain from hearing such proceeding if an action is commenced, and can be timely adjudicated, in a State forum of appropriate jurisdiction. Any decision to abstain or not to abstain made under this subsection is not reviewable by appeal or otherwise by the court of appeals under section 158(d), 1291, or 1292 of this title or by the Supreme Court of the United States under section 1254 of this title. This subsection shall not be construed to limit the applicability of the stay provided for by section 362 of title 11, United States Code, as such section applies to an action affecting the property of the estate in bankruptcy.

28 U.S.C. § 1334(c) (West 1992). Characteristic for this case, the defendants submitted lengthy memoranda containing numerous arguments against the plaintiff's motion to abstain.

Briefly summarized, defendant Schrank characterizes this action as above all else a nondischargeability action with various state law claims tacked on to it. He then notes that bankruptcy courts have exclusive jurisdiction over nondischargeability actions involving the code sections under which the plaintiff is proceeding -- 11 U.S.C. §§ 523(a)(2), (a)(4) and (a)(6). Schrank then asserts that it would be inefficient and a waste of judicial resources to try this case in state court and then later return to this Court for a second trial. He further cites numerous examples of how the elements necessary to establish a claim may differ between state law and the relevant nondischargeability provisions of the bankruptcy code. Finally, Schrank notes that it has been two years since he first sought bankruptcy protection[(4)] and laments the inevitable delay that will result in trying this matter in state court.

Defendant Cannon & Dunphy in its brief notes that it originally sought to have this matter tried in state court, which the plaintiff "vigorously opposed." Cannon & Dunphy believed that the plaintiff should pursue his claim for attorney's liens in the underlying state court personal injury actions. It then argues at length that plaintiff's "motion to abstain" is actually a motion for voluntary dismissal and the court should treat it as such. In support of this assertion, Cannon & Dunphy note that a formal determination of jurisdiction has not been made by this Court. The fact that plaintiff moved for abstention in the absence of such a determination, the argument continues, must mean that he is really seeking a voluntary dismissal. Cannon & Dunphy further cites case law for the proposition that mandatory abstention is only permissible where, among other things, the plaintiff has already filed an action in state court. Since no such action has been filed here, the argument concludes, abstention is inappropriate.

Cannon & Dunphy then asserts that the plaintiff engaged in forum shopping when he filed his case in federal court and he therefore should not be allowed to now return to state court. It further argues that, since plaintiff's motion is really one for voluntary dismissal, it is entitled to its reasonable attorney fees and costs. Cannon & Dunphy then bemoans that it has spent significant time and expense in preparing the pending motions still outstanding in this case. It accuses the plaintiff of delaying his motion to abstain until he lost his forum-shopping game. Finally, Cannon & Dunphy notes that even if the Court took plaintiff's motion as one to abstain, it still is not entitled to such because of his forum shopping and the fact that no state court action is pending.

The Court has considered the arguments of both defendants as well as the plaintiff's response to them. Having done so, the Court finds the defendants' assertions unpersuasive and decides to grant the plaintiff's motion to abstain as to the claims against defendant Cannon & Dunphy. In addition, the Court on its own motion decides to abstain as to the claims against debtor-defendant Schrank as well. The Court reaches this result for numerous reasons.

Most importantly, case-law precedent addressing abstention by bankruptcy courts supports this result. Numerous courts list the following factors as ones which courts should consider when deciding whether to abstain:

> (1) the effect or lack thereof on the efficient administration of the estate if a Court recommends abstention, (2) the extent to which state law issues predominate over bankruptcy issues, (3) the difficulty or unsettled nature of the applicable law, (4) the presence of a related proceeding commenced in state court or other nonbankruptcy court, (5) the jurisdictional basis, if any, other than 28 U.S.C. § 1334, (6) the degree of relatedness or remoteness of the proceeding to the main bankruptcy case, (7) the substance rather than form of an asserted "core" proceeding, (8) the feasibility of severing state law

> claims from core bankruptcy matters to allow judgments to be entered in state court with enforcement left to the bankruptcy court, (9) the burden of [the bankruptcy court's] docket, (10) the likelihood that the commencement of the proceeding in bankruptcy court involves forum shopping by one of the parties, (11) the existence of a right to a jury trial, and (12) the presence in the proceeding of nondebtor parties.

See, e.g., Christensen v. Tucson Estates, Inc. (In re Tucson Estates, Inc.), 912 F.2d 1162, 1167 (9th Cir. 1990) citing with approval Republic Reader's Service, Inc. v. Magazine Service Bureau, Inc. (In re Republic Reader's Service, Inc.), 81 B.R. 422, 429 (Bankr. S.D. Tex. 1987); All American Laundry Service v. Ascher (In re Ascher), 128 B.R. 639, 646 (Bankr. N.D. Ill. 1991). Most of these factors weigh in favor of the Court's abstention in this case. First, in spite of defendant Schrank's assertion to the contrary, this case is not mainly a nondischargeability action. Rather it is a case in which state law issues clearly predominate. Even those causes of action in which plaintiff has included one or more of the nondischargeability provisions of 11 U.S.C. § 523 are essentially fraud claims under state law.[(5)] Defendant Schrank implicitly argues this point as to several of plaintiff's claims when he correctly notes in his brief that the fiduciary duty requirement under 11 U.S.C. § 523(a)(4) has consistently been interpreted very narrowly to mean an express trust relationship. The characterization of what are in reality state law fraud claims as nondischargeability actions is stretching the parameters of those provisions of the bankruptcy code. This analysis establishes the existence of a second factor from the aforementioned list -- the substance rather than the form of an asserted "core" proceeding. As noted by the court in In re Republic Reader's Service, Inc., "often a proceeding, cast in the language of a core proceeding, merely shrouds state law actions under the guise of a bankruptcy issue." 81 B.R. 422, 427 (Bankr. S.D. Tex. 1987). This is the case here -- what is in reality a garden variety of state law fraud claims is labeled as a garden variety of nondischargeability claims under the bankruptcy code.

The Court is aware that "[t]he mere presence of state law issues is not enough to warrant abstention since 'virtually every issue which arises within the context of a bankruptcy case involves state law to at least some degree.'" In re Ascher, 128 B.R. 639, 647 (Bankr. N.D. Ill. 1991) citing with approval In re Republic Reader's Service, Inc., 81 B.R. 422, 427 (Bankr. S.D. Tex 1987). Nevertheless, the presence of many of the other aforementioned factors in addition to the presence of state law issues warrants abstention in this case.

A third factor weighing in favor of abstention is the nature of the state law claims involved here. Causes of action involving civil conspiracy, breach of settlement agreements, tortious interference with contractual relations, injury to business, and breach of fiduciary duty in the context of a partnership are not the types of claims which this Court routinely adjudicates. In addition, several of the causes of action are grounded on relatively novel or unsettled issues of state law -- namely the tortious interference and civil conspiracy claims. As noted by the plaintiff, the defendants have raised defenses involving the ethical duties of an attorney pursuant to the rules of professional responsibility. Conflicts between a lawyer's fiduciary duty to a partner and that lawyer's ethical responsibility to a client involve unsettled issues of state law about which little or no statutory or common law precedent exists. A state court would be better suited to address such issues and render judgment consistent with state law and state court precedent. "State courts afford the best forum for deciding issues whose resolution turns on interpretation of state law . . . ." In re Republic Reader's Service, Inc., 81 B.R. 422, 427 (Bankr. S.D. Tex 1987).

A fourth factor relevant in this case is the "feasibility of severing state law claims from core bankruptcy matters to allow judgment to be entered in state court with enforcement left to the bankruptcy court." Here it is very feasible to sever the state law claims from the core bankruptcy matters. As already noted, even those claims labeled as core nondischargeability claims are rooted in state law fraud provisions. Allowing such claims to be first adjudicated to final judgment in a state court and then returned to the bankruptcy forum is a common occurrence among bankruptcy courts. As noted by one such court, "[s]ection 1334 supports the duality of allowing a claim to be adjudicated to final judgment in state court while preserving the issues of the status and enforceability of the claim in the bankruptcy court." In re Tucson Estates, Inc., 912 F.2d 1162, 1167 (9th Cir. 1990) citing with approval In re Republic Reader's Service, Inc., 810 B.R. 422, 427 (Bankr. S.D. Tex. 1987). See also In re Comer, 723 F.2d 737 (9th Cir. 1984); Osai v. Tabuena (In re Ozai), 34 B.R. 764 (Bankr. 9th Cir. 1983). See generally 1 Collier on Bankruptcy ¶ 3.01 at 3-74 (15th ed. 1982). It is therefore appropriate that the Court allow the numerous state law claims at issue here to be adjudicated to final judgment in state court and then returned to this Court for a nondischargeability determination if necessary.

Both defendants, moreover, have filed summary judgment motions and make repeated assertions that most, if not all of the plaintiff's claims are baseless. If this is indeed the case, then no state court judgment will ultimately result, and the matter will end there; further adjudication by this Court will be unnecessary. It is therefore quite possible that the Court's decision to abstain at this juncture could result in a more efficient administration of this matter -- another of the factors listed by the Tucson Estates court. Even if state court judgments do result as to some of the issues, the subsequent hearing in this Court would not need to involve a retrial as to all of the issues heard in state court. The elements for establishing a claim under §§ 523(a)(2)(A), (a)(4), or (a)(6) are relatively narrow and well defined. Such matters are dealt with expeditiously by this Court and do not usually necessitate protracted hearings. Recent Supreme Court and lower court decisions, moreover, indicate support for a more liberal application of collateral estoppel where prior judgments for fraud have already been obtained. See, e.g., Grogan v. Garner, 112 L. Ed. 2d 755, 767 (1992). See also Northern Pipeline Construction Co. v. Marathon Pipe Line Co., 458 U.S. 50 (1982); United States Life Title Ins. Co. v. Dohm, 19 B.R. 134 (N.D. Ill. 1982); Elmore v. Davis (In re Davis), 23 B.R. 639 (Bankr. W.D. Ky. 1982).

Yet another factor supports the notion that abstention will likely result in a more efficient administration of this matter. The plaintiff here has requested a jury trial. He has not filed a claim in the debtor's bankruptcy case, thus he has not waived his right to one. See Granfinanciera, S.A. v. Nordberg, 492 U.S. 33 (1989). Whether and under what circumstances a bankruptcy court can conduct a jury trial is currently a hotly debated question throughout the country. See generally Gibson, Jury Trials and Core Proceedings: The Bankruptcy Judge's Uncertain Authority, 65 Am. Bankr. L.J. 143 (1991); Shelton & Harris, Bankruptcy Jurisdiction and Jury Trials: The Constitutional Nightmare Continues, 8 Bankr. Dev. J. 469 (1991). Retention of this case in federal court would undoubtedly necessitate yet another return to the district court to answer the jury trial question. Given the history of this case, whichever way that court would decide, its decision would likely be appealed to the Seventh Circuit and possibly further. The defendants make much of the delay that has already occurred in this matter. Given the jury issue, however, retaining this case in federal court would likely result in even greater delay than would occur in allowing a state court to adjudicate it.

The jury issue raises another of the aforementioned factors in deciding whether to

abstain -- the right to a jury trial. The plaintiff here has requested a jury trial and he may well have a right to one. An additional factor present in this case is the presence of a nondebtor party. One of the defendants, Cannon & Dunphy, is such a party. Finally, the presence of a nondebtor party in this proceeding makes yet another factor relevant -- the degree of relatedness or remoteness of the proceeding to the main bankruptcy case. Even though the debtor is a codefendant, the presence of a nondebtor law firm and certain of its principals as defendants renders this matter more remote from the main bankruptcy case than would be the case if the debtor were the sole defendant. Only four of the plaintiff's eight claims, moreover, are alleged to be causes of action grounded in the bankruptcy code; and as already shown, even those are essentially state law fraud actions.

In summary then, eight of the twelve factors identified by the court in In re Republic Reader's Service, Inc. weigh in favor of abstention. Although certain of the other factors admittedly may weigh in favor of retention of this matter -- such as the possibility that the plaintiff engaged in forum shopping -- the balance tilts decisively in favor of abstention.

The Court therefore decides to grant the plaintiff's motion to abstain as to the issues against the nondebtor defendant Cannon & Dunphy. It then becomes clear that a decision sua sponte to abstain as to the remaining issues against the debtor-defendant is warranted as well. The claims against both defendants are closely interrelated and the factual bases which underlie those claims are in many respects the same. Concerns of judicial economy and efficiency mandate that this matter be heard in one forum. On the basis of the preceding analysis of relevant factors -- especially the fact that the claims against the debtor are essentially state law fraud claims -- it is clear that the appropriate single forum is a Wisconsin state court.

One final consideration is worthy of note. The defendants lament the fact that a great deal of work has been invested in preparing the documents and memoranda underlying the various motions currently outstanding in this matter. The implication is that abstaining in this matter would necessitate a "reinvention of the wheel" -- all of this work would have to be performed again in state court. If this is indeed the implication, then it is in error. The parties will merely need to refile the relevant documents and memoranda in state court. The underlying argument and analysis remains the same whether presented in a state or federal forum.

The Court therefore abstains on the basis of 28 U.S.C. § 1334(c)(1) as to all issues presented by this matter. Accordingly, relief from stay is granted to the plaintiff to proceed against the debtor-defendant in state court as to the claims presented. The enforcement of any ultimate judgment against the debtor-defendant is stayed pending further order of this Court. Finally, all costs in this matter are denied pending further order.

This decision shall constitute findings of fact and conclusions of law pursuant to Bankruptcy Rule 7052 and Rule 52 of the Federal Rules of Civil Procedure.

END NOTES:

1. An additional cause of action -- that the defendants violated the federal Racketeer Influenced and Corrupt Organizations Act (RICO) and the Wisconsin counterpart thereof, the Wisconsin Organized Crime Control Act (WOCCA) -- was dismissed by the U.S. District Court for the Western District of Wisconsin on January 3, 1992. The basis for the dismissal was failure to state a claim upon which relief can be granted. See Schultz v. Schrank, 91-C-0202-C (W.D. Wis. Jan. 2, 1992). The

district court further found that count 9 of the plaintiff's complaint -- providing false financial statements to Bank One -- has no federal basis but is rather a state-law fraud claim. See id.

2. The district court in its decision of January 3, 1992, referred to the "[m]iasma of bankruptcy, bankruptcy fraud, and state law issues of this case." See Schultz v. Schrank, No. 91-C-0202-C at 22 (W.D. Wis. June 2, 1992). The Random House dictionary defines "miasma" as "noxious exhalations from putrescent organic matter; poisonous effluvia or germs infecting the atmosphere." Random House Dictionary 843 (Revised edition 1982).

3. In re Raymond E. Schrank II, d/b/a Schrank Law Offices f/d/b/a Schrank & Schultz and Barbara A. Schrank, Case No. MM7-90-03199.

4. Schrank first filed a petition under Chapter 11 on March 26, 1990. This case was dismissed on application on August 22, 1990. The debtor-defendant then filed a petition under Chapter 7 shortly thereafter -- on November 15, 1990.

5. The district court recognized as much as to one of the claims -- that defendant Schrank provided false financial statements to Bank One. The court noted that this is a "private cause of action . . . for fraud, a state law claim." Schultz v. Schrank, No. 91-C-0202-C at 21 (W.D. Wis. Jan. 2, 1992).