IN THE UNITED STATES BANKRUPTCY COURT
FOR THE WESTERN DISTRICT OF WISCONSIN

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IN RE JOHN S. OTTEMAN, (Chapter 7)

Debtor. Case Number: 02-10332

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MEMORANDUM DECISION

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Debtor, John Otteman filed a voluntary chapter 7 petition on January 18, 2002 and received a discharge on April 29, 2002. The case has been reopened twice, most recently when the trustee, William Rameker, learned of a lawsuit that Otteman had initiated against Securities Service Network, Inc. ("SSN"), a securities brokerage. Otteman claims in excess of $100,000 for overtrading.

The trustee pursued the lawsuit to settlement for $12,000—enough to pay all of the unpaid allowed claims in the estate. When the trustee sought court approval of the settlement, the debtor objected and made a slightly higher offer to buy back the lawsuit. At the hearing, the trustee and SSN cited the debtor's prior bad conduct as among the grounds for approving the settlement.

The debtor submitted an affidavit from his attorney in the lawsuit (prior to the trustee taking over) that claimed that the debtor's account "had an annual turnover in excess of 20 times . . . [which is] 3 times more aggressively than the level most courts says [sic] creates a conclusion of excessive trading." Stoltmann Aff. at ¶ 2. He states that "[t]he aggressive and reckless trading in the account is the most egregious I have

reviewed in approximately seven years of private practice and having represented well in excess of 300 investors." Id. at ¶ 4. He calculates that the debtor's "account needed to return well in excess of 20% annually in order to cover the margin interest, costs, fees and commissions from the trading activity," making it impossible to earn money. Id. at ¶ 5-6.

SSN responded that the debtor directed all trades on his account in person. He identified (in writing) his objective in opening the SSN account as "very speculation" and "new issue." Klimas Aff. Ex. A at 2. He traded penny stocks, which SSN says its broker had no interest in overtrading because there were no commissions paid to brokers on penny stock transactions. Id. SSN sent Otteman 23 separate letters (Id. Ex. C) alerting him to the risky trading in his account and detailing the number of trades and amount of commissions which had occurred in the prior 30 days. SSN claims that Otteman's aggressive margin positions were taken against the advice of the broker who managed his account. SSN was concerned enough about this trading at the time it occurred to require Otteman to sign a letter indicating that he was trading against his broker's advice. Id. Ex. D.

The trustee and SSN contend that the debtor failed to disclose the existence of the claim against SSN on two separate occasions, failed to disclose the source of $20,000 that he invested with SSN post-petition, and failed to disclose a bank account in his bankruptcy. Otteman responds that he only became aware of the claim against SSN in August 2004, when he saw a law firm's television commercial and began speaking with attorneys about his claim. SSN alleges that Otteman still was required to disclose the lawsuit when the case was reopened. Otteman contends otherwise. D. Aff. at ¶¶ 3-5. As

to the $20,000 check that he sent to SSN, Otteman says that he does not fully recall where it came from, but that

> approximately $6,000.00 came from the proceeds of stock and approximately $2,500.00 from the proceeds of the sale of a boat, both of which are disclosed in Schedule B. . . . approximately $6,000.00 came from a distribution from my mother's probate estate which was disclosed to the Trustee and is reflected in the Stipulation dated January 2004 . . . the remaining funds may have come from Unemployment Compensation which I began to receive after I filed my bankruptcy and possibly a payment from my mother's probate estate which I became entitled to for acting as personal representative of that estate.

Id. at ¶ 7. Finally, he claims that he did disclose the bank account on his schedules as a savings account instead of a checking account, likely leading SSN to overlook it when trying to find the account on Schedule B. Otteman attaches to his affidavit documents that appear to support his contentions.

A chapter 7 trustee is required to "collect and reduce to money the property of the estate for which such trustee serves, and close such estate as expeditiously as is compatible with the best interests of parties in interest." 11 U.S.C. § 704(a) (2006). When the estate owns causes of action against others, the trustee can reduce them to money either by litigating or settling. If the trustee chooses to settle, § 363(b)(1) of the Bankruptcy Code gives the trustee the authority to do so. 11 U.S.C. § 363(b)(1) ("The trustee, after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate"); In re Telesphere Communications, Inc., 179 B.R. 544, 552 n.7 (Bankr. N.D. Ill. 1994) ("The settlement of a cause of action held by the estate is plainly the equivalent of a sale of that claim. There is no difference in the effect on the estate between the sale of a claim (by way of assignment) to a third party and a settlement of the claim with the adverse party").

Rule 9019 of the Federal Rules of Bankruptcy Procedure governs the contents of the hearing required by § 363 to approve a proposed settlement.

> **(a) Compromise.** On motion by the trustee and after notice and a hearing, the court may approve a compromise or settlement. Notice shall be given to creditors, the United States trustee, the debtor, and indenture trustees as provided in Rule 2002 and to any other entity as the court may direct.

Fed. R. Bankr. Proc. 9019(a) (2006). The burden of proof under § 363(b) is on the trustee; however, the "objectant . . . is required to produce some evidence respecting its objections." In re Lionel Corp., 722 F.2d 1063, 1071 (2d Cir. 1983).

"A bankruptcy judge may approve a settlement in a liquidation proceeding if the settlement is in the estate's best interests." In re Am. Reserve Corp.), 841 F.2d 159, 161 (7th Cir. 1987).

> This step requires the court to estimate both the value of the proposed settlement and the likely outcome of litigating the claims proposed to be settled. However, a precise determination of likely outcomes is not required, since an exact judicial determination of the values in issue would defeat the purpose of compromising the claim.

Telesphere, 179 B.R. at 553 (citing In re Energy Co-Op., Inc., 886 F.2d 921, 929 (7th Cir. 1989)) (internal marks omitted). "A challenged settlement fails this test only if it falls below the lowest point in the range of reasonableness." Energy Co-Op., 886 F.2d at 929 (internal marks and citations omitted). Still, the inquiry can be extremely detailed, as it requires consideration of (1) the likelihood of obtaining a particular recovery, (2) the litigation costs the trustee would incur, (3) the portion of any recovery that would be returned to the debtor because it exceeds the filed claims, (4) any impact of the recovery on the estate's right to pursue other defendants, and (5) the risk of noncollection from each potential settling party. Telesphere, 179 B.R. at 554; see Protective Comm. for Indep. S'holders of TMT Trailer Ferry, Inc. v. Anderson, 390 U.S. 414, 424-25, 88 S.Ct.

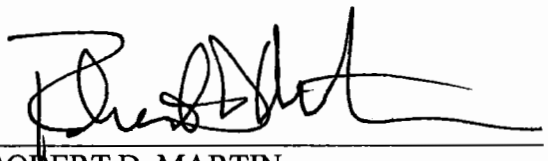
1157 (1968) (requiring "an educated estimate of the complexity, expense, and likely duration of such litigation, the possible difficulties of collecting on any judgment which might be obtained, and all other factors relevant to a full and fair assessment of the wisdom of the proposed compromise").

Generally, the existence of a higher bid for the estate's cause of action, which presents an equal likelihood of full payment, is sufficient grounds for disapproving a settlement proposal. However, the trustee expressed reservations on the likelihood of receiving payment from Otteman. No source of funds for Otteman's payment was disclosed at the hearing. It appears certain to me that the trustee has fairly valued the proposed settlement under the standards for consideration set out in Telesphere. His preference for the SSN offer is well above the lowest range of reasonableness. In fact, it appears to me to be a prudent and appropriate way in which to obtain full benefit for the estate.

The reported cases do not specify equitable doctrines as part of the settlement approval analysis, but equitable doctrines are always available if demanded by the facts. For example, in In re Louden, 106 B.R. 109 (Bankr. E.D. Ky. 1989), the bankruptcy court applied the doctrine of equitable estoppel to dismiss a lawsuit brought by the debtor which the debtor had not disclosed in two previous bankruptcy proceedings. The district court in Kunica v. St. Jean Financial, Inc., 233 B.R. 46, 58 (S.D.N.Y. 1999) (and citing cases), reached the same conclusion because "repeated failure to adequately disclose the Claims asserted here amounts to the assertion of inconsistent positions within the meaning of the judicial estoppel doctrine." The presence of a potential equitable defense

is an appropriate consideration in the trustee's valuation of the lawsuit. Otteman's objection to the settlement is overruled. The trustee's motion may be granted.

Dated: November 8, 2006



ROBERT D. MARTIN
UNITED STATES BANKRUPCY JUDGE