

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

In re:

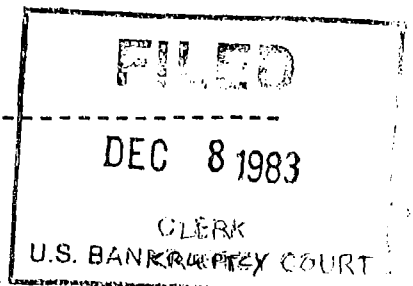
FRANK S. OSBORNE
DORIS ARLENE OSBORNE

Debtors.

In Bankruptcy:

EF7-82-00051 ✓

FINDINGS OF FACT, CONCLUSION OF LAW
AND ORDER SUBORDINATING DEBT



Bank of New Richmond, New Richmond Farmers Union Co-op Oil Company and General Feeds, Inc., by their attorney, Peter F. Herrell of Jordan, Herrell & Thiel, having filed amended applications for subordination of the claim of Production Credit Association of River Falls; and said matter coming on for trial before the Court; and the applicants appearing by their attorney; and the debtors appearing in person; and Production Credit Association of River Falls appearing by its attorney, Keith Rodli of Rodli, Beskar & Boles, S.C.; and the Court having heard the evidence of witnesses, considered the arguments of counsel and the briefs submitted thereafter, and having fully considered the entire file and record herein, makes the following FINDINGS:

(reported)

1. That the debtors, Frank S. Osborne and Doris Arlene Osborne, filed an application for relief under Chapter 7 of the Bankruptcy Code on January 15, 1982.

2. That, at all times pertinent to this matter, the debtors were involved in the beef cattle raising business.

3. That the creditors listed by the debtors included: Production Credit Association of River Falls (PCA), Bank of New Richmond (Bank), New Richmond Farmers Union Co-op Oil Company (Cenex)(for feed grinding, feed drying, gas and repairs) and General Feeds, Inc. (General)(for feed potatoes).

4. That the PCA debt was secured by collateral that included, at least, 90% of the debtors' livestock. Exhibits 5 & 6.

5. That PCA and the debtors had a business relationship dating back to, at least, late 1976 or early 1977. Transcript at 39 & 104.

6. That, in late 1976 or early 1977. James Munson, then representing PCA, told Cenex General Manager Larry Wiesenbeck that he would see to it that the debtors' accounts were paid on a regular basis. Tr. at 105. See also Tr. at 48 & 114.

7. That thereafter, from time to time, Mr. Wiesenbeck would talk with both debtor Frank Osborne (Osborne) and PCA about

Osborne's accounts and payment would be forthcoming. Tr. at 107. Occasionally, PCA would make direct payments to Cenex on Osborne's behalf. Tr. at 49 & 153.

8. That, in January 1981, Osborne began to experience continuing overdrafts at the Bank. Tr. at 30.

9. That James Munson, then of the Bank, and a representative of PCA discussed the overdraft problem. Tr. at 12, 30 & 132.

10. That, on March 3, 1981, the Bank set up a "checking reserve agreement" on Osborne's account. Tr. at 29.

11. That, in March or April, 1981, Osborne had to go to PCA on a regular basis for operating loans, tr. at 54, and PCA was aware that there was "weakness" in the Osborne loan, tr. at 121 & 150.

12. That in April or May, 1981, PCA agreed to cover the Osborne reserve account at the Bank. Tr. at 134.

13. That, in May, 1981, PCA renewed and increased the debtors' loan. Ex. 5.

14. That, in July and August, 1981, PCA made direct payments to General on Osborne's behalf. Ex. 10.

15. That, on August 19, 1981, PCA renewed and increased the debtors' loan -- but as a "controlled" loan, ex. 6 & 7,

because of concerns about the weakness of the Osborne loan, tr. at 151. A controlled loan is a loan limited to specified items. Tr. at 125.

16. That, on more than one occasion in August or September, 1981, Robert Accola of PCA met with the debtors regarding their financial situation. Tr. at 123.

17. That, during at least one of these meetings, Mr. Accola gave the debtors directions on how the funds from the PCA loan were to be spent. Tr. at 123.

18. That, at one of these meetings, Mr. Accola called Jim Munson of the Bank and asked him to "go along" with the debtors. Tr. at 15, 21, 32, 44, 68 & 124.

19. That, on September 2, 1981, the Bank went along with the debtors, i.e., took a note for \$5,000. Tr. at 25.

20. That, on September 9, 1981, PCA representatives met with General representatives. Tr. at 79, 92, 140 & 142. General had initiated the meeting because of its concerns regarding the Osborne account. Tr. at 86.

21. That PCA and General met again on October 19, 1981. Tr. 93, 139, 144.

22. That PCA expected General to seek a PCA payment on

Osborne's account at the October meeting and prepared a response. Tr. at 140, 142, 146.

23. That the planned and actual PCA response was that payment would depend upon an accurate measurement of the performance of the debtors' cattle. Tr. 94, 140, 146.

24. That General, on more than one occasion after the October meeting, called PCA regarding the Osborne account and was told that payment would be forthcoming as soon as the debtors signed some papers. Tr. at 95.

25. That, on November 6, 1981, PCA representatives went to the Bank to deliver a check for \$3,500 to the Bank on Osborne's behalf and to discuss PCA's obligations regarding Osborne's debts. Tr. at 16-20 & 152.

26. That, on the same day, PCA representatives went to Cenex to tell Mr. Wiesenbeck that PCA could provide no more funds for Osborne's account than \$1,000. Tr. at 153. See also Ex. 18.

27. That, on November 20, 1981, in response to a threat to stop delivery of feed to Osborne made to PCA by General, PCA agreed to forward a check to General on Osborne's behalf. Tr. at 88 & 96. See Ex. 11. And that such a check was issued on November 30, 1981. Ex. 10.

28. That, in late December, 1981, PCA took possession of, and sold, the debtors' herd. Tr. at 121.

29. That, at least until November of 1981, the applicants looked to PCA for payment of Osborne's accounts. Tr. at 26 & 42-43 (Bank); findings of fact 6 & 7 (Cenex); and findings of fact 20-24 (General).

30. That PCA induced the applicants, by silence or otherwise, see, e.g., tr. at 109, to continue to extend credit to the debtors after it became aware of the debtors' troubled financial situation. See findings of fact 11 & 29.

31. That, given the transactions and relationships between the applicants, the debtors and PCA, PCA had actual or constructive knowledge that Cenex and General would feel compelled to continue to extend credit to the debtors' livestock operation after October and November of 1981 (the Bank did not extend credit after that time, tr. at 36). See Tr. at 109-110 (Cenex) & 89 (General).

32. That the applicants argue for equitable subordination under 11 U.S.C. sec. 510(c)(1982).

33. That subordination is an appropriate remedy when the Court is satisfied that the following conditions are met:

- (1) The claimant must have engaged in some type of inequitable conduct;

- (2) The misconduct must have resulted in injury to other creditors or conferred an unfair advantage on the claimant;
- (3) The subordination must not be inconsistent with the Bankruptcy Code.

In re All Products Co., 32 B.R. 811 (Bankr.E.D.Mich. 1983) (applying In re Mobile Steel Co., 563 F.2d 962, 700 (5th Cir. 1977) to the Bankruptcy Code).

34. That PCA argues that, as the applicants have not shown that it was an insider in breach of fiduciary duty or that it was a non-insider guilty of gross misconduct, the applicants have not shown that it had engaged ⁱⁿ inequitable conduct. See In re Teltronics Services, Inc., 29 B.R. 139, 169 (Bankr.E.D.N.Y. 1983).

35. That "the bankruptcy court has the power to sift the circumstances surrounding any claim to see that injustice or unfairness is not done in administration of the bankrupt estate." Pepper v. Litton, 308 U.S. 295, 308, 60 S.Ct. 238, 84 L.Ed.2d 281 (1939).

36. That the transactions between the debtors and PCA demonstrated more than an arms-length debtor-creditor relationship. And that these transactions, given the nature of PCA's collateral

(livestock that required daily care to preserve value), approach the status of a joint venture.

37. That the transactions between the applicants and PCA demonstrated more than arms-length unsecured creditor-secured creditor relationships. And that these transactions put PCA in a position approaching -- if not actually reaching -- that of a guarantor.

38. That PCA's October and November, 1981, attempts to extricate itself from any obligation to the applicants do not shield it from responsibility. Cf. 57 Am.Jur.2d Negligence sec. 46 (1971) (one who renders aid may have a duty to continue to assist) and 57 Am.Jur.2d Negligence sec. 227 (1971) (one who's conduct leads to rescue by another may be liable to the rescuer).

39. That PCA's October and November, 1981, attempts to extricate itself from any obligation to the applicants do not shield it from subordination. Cf. Wis. Stats. sec. 409(504(1)(a) (reimbursement of cost of holding secured property has priority in distribution of proceeds of sale).

40. That, while PCA may be neither an insider in breach of fiduciary duty nor a non-insider guilty of gross misconduct, it is

certainly something in between and has engaged in inequitable conduct.

41. That PCA's inequitable conduct resulted in injury to other creditors, i.e., unpaid debts of the debtors.

42. That PCA's inequitable conduct resulted in an unfair advantage to itself, i.e., preservation of its collateral at the expense of other creditors.

43. That, given the enactment of sec. 510(c), equitable subordination is consistent with the Bankruptcy Code.

CONCLUSION OF LAW

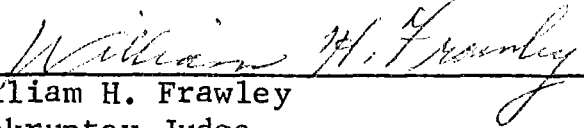
The claim of Production Credit Association of River Falls in the above captioned matter should be subordinated to the claims of Bank of New Richmond, New Richmond Farmers Union Co-op Oil Company and General Feeds, Inc.

NOW, THEREFORE, IT IS ORDERED that the claim of Production Credit Association of River Falls filed in this Court against the bankruptcy estate of debtors Frank S. Osborne and Doris Arlene Osborne should be, and the same hereby is, subordinated to the claims

of Bank of New Richmond, New Richmond Farmers Union Co-op Oil
Company and General Feeds, Inc., without costs.

Dated: December 8 , 1983.

BY THE COURT:



William H. Frawley
Bankruptcy Judge