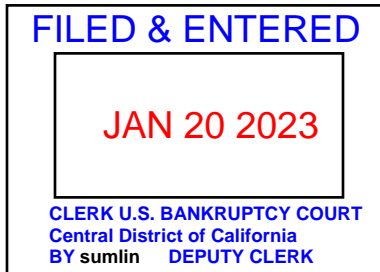


# FOR PUBLICATION



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8 **UNITED STATES BANKRUPTCY COURT**  
9 **CENTRAL DISTRICT OF CALIFORNIA**  
10 **LOS ANGELES DIVISION**

11  
12 In re:  
13 The Hacienda Company, LLC,

Case No.: 2:22-bk-15163-NB  
Chapter: 11

14 **OPINION ON MOTION TO DISMISS**  
15 **CANNABIS-RELATED CASE**

16 Debtor. Hearing Date:  
17 Date: December 20, 2022  
18 Time: 1:00 p.m.  
19 Place: Courtroom 1545  
255 E. Temple Street  
Los Angeles, CA 90012  
(and via Zoomgov per posted procedures)

20 This Bankruptcy Court has already issued an order (docket no. 71) denying the  
21 motion of the United States Trustee's ("UST") to dismiss this case (docket no. 53, the  
22 "MTD"). This Opinion memorializes and further explains this Court's reasoning.<sup>1</sup>

23 **1. BACKGROUND**

24 The above-captioned Debtor was in the business of wholesale manufacturing  
25 and packaging cannabis products under the "Lowell Herb Co." brand, a/k/a "Lowell  
26 Farms," and it ceased operations on February 25, 2021. At one time, Debtor owned

27  
28 <sup>1</sup> Unless the context suggests otherwise, a "chapter" or "section" ("§") refers to the United States Bankruptcy Code, 11 U.S.C. § 101 et seq. (the "Code"), a "Rule" means the Federal Rules of Bankruptcy Procedure or other federal or local rule, and other terms have the meanings provided in the Code, Rules, and the parties' filed papers.

1 land that was intended for use as a cannabis cultivation center, but Debtor did not  
2 achieve this goal and the vacant land was sold in 2020 to pay creditors.

3 After Debtor ceased operations, it transferred its value to a publicly traded  
4 Canadian company – allegedly by structuring the sale as one of intellectual property,  
5 not the sale of an operating cannabis business. The acquirer’s sole business is  
6 cannabis growth and sales, which apparently are legal under Canadian law. In return,  
7 Debtor received a roughly 9.4% share of the equity shares of the acquiring entity. The  
8 acquiring entity changed its name to Lowell Farms, Inc.

9 On September 21, 2022, Debtor filed this bankruptcy case. In Debtor’s initial  
10 status report, Debtor stated that it intended “to propose a plan of reorganization that  
11 provides for Debtor to sell off the shares of [Lowell Farms, Inc. that] it owns in an orderly  
12 fashion and use the proceeds from the stock to pay creditors [or] ... Debtor may elect to  
13 distribute the shares it owns to its creditors directly.” At oral argument, Debtor’s counsel  
14 elaborated that the stock of Lowell Farms, Inc. is thinly traded and therefore, to avoid  
15 flooding the market and depressing the return to creditors, “we’re talking about selling it  
16 off in chunks [over time] ....” Tr. 12/20/23 (docket no. 76), p. 16:19.

## 17 **2. JURISDICTION, AUTHORITY AND VENUE**

18 This Bankruptcy Court has jurisdiction to decide the MTD, and venue is proper,  
19 under 28 U.S.C. §§ 1334 and 1408. This is a “core” proceeding in which this  
20 Bankruptcy Court has the authority to enter a final judgment or order under 28 U.S.C.  
21 § 157(b)(2)(A) and (O). *See also Stern v. Marshall*, 131 S. Ct. 2594 (2011).<sup>2</sup>

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24  
25 <sup>2</sup> Although the UST has filed a notice of appeal, that does not divest this Bankruptcy Court of jurisdiction to issue this  
26 Opinion for two alternative reasons. First, so far as this Bankruptcy Court is aware, no appellate court has granted  
27 the UST’s motion for leave to appeal (docket no. 90). *See In re Rains*, 428 F.3d 893, 903-904 (9th Cir. 2005) (“if the  
28 order at issue is interlocutory, any appeal ... would not transfer jurisdiction to an appellate court”) (citations omitted);  
*In re Bertain*, 215 B.R. 438 (9th Cir. BAP 1997) (“The denial of a motion to dismiss is an interlocutory order”) (cleaned  
up; citations omitted). Second, this Opinion does not alter or expand any prior rulings, and instead merely provides  
further explanation, as anticipated on the record at the above-captioned hearing. *See Rains*, 428 F.3d at 904 (other  
exceptions to rule that notice of appeal divests lower court of jurisdiction).

1 **3. DISCUSSION**

2 **a. Legal standards**

3 As the parties acknowledge, the burden of establishing “cause” for dismissal  
4 under § 1112(b) rests with the party seeking dismissal. See *In re Rosenblum*, 608 B.R.  
5 529, 536 (Bankr. D. Nev. 2019). The movant must show such cause by “a  
6 preponderance of the evidence.” *In re Woodbrook Assocs.*, 19 F.3d 312, 317 (7th Cir.  
7 1994).

8 If the movant establishes that “cause” exists under § 1112(b)(1), then the  
9 opponent can still prevent conversion or dismissal under § 1112(b)(2) if (1) the court  
10 “finds and specifically identifies unusual circumstances establishing” that conversion or  
11 dismissal is “not in the best interests of creditors”; (2) the opponent shows that “there is  
12 a reasonable likelihood” of confirming a plan in a reasonable amount of time; (3) the  
13 opponent establishes that the grounds for conversion or dismissal include an act or  
14 omission of the debtor for which there is a “reasonable justification”; and (4) the  
15 opponent establishes that the act or omission can be “cured within a reasonable time.”  
16 See *Rosenblum*, 608 B.R. at 536-37 (summarizing § 1112(b)(2)).

17 If the debtor cannot satisfy the “unusual circumstances” elements under  
18 § 1112(b)(2), then the bankruptcy court must choose “between conversion or dismissal  
19 based on the best interests of the creditors and the estate.” *In re Nelson*, 343 B.R. 671,  
20 675 (9th Cir. BAP 2006) (citation and internal quotation marks omitted).

21 **b. Violations of nonbankruptcy law, generally**

22 A violation of nonbankruptcy law is not expressly listed as “cause” for dismissal  
23 under § 1112(b)(1) & (4), but compliance with applicable nonbankruptcy law generally is  
24 required both by statute (*e.g.*, 28 U.S.C. § 959) and under the authorities cited by both  
25 parties, so it appears to be undisputed that violations of nonbankruptcy law can be  
26 cause for dismissal. That said, there are many remedies for any debtor's violations of  
27 any law, rule, or procedure, and dismissal is one of the more extreme remedies.

28

1           There are several alternative reasons why violations of nonbankruptcy law might  
2 establish cause for dismissal. First, such violations might establish a lack of “good faith”  
3 sufficient to warrant dismissal. *See, e.g., In re Arenas*, 535 B.R. 845 (10th Cir. BAP  
4 2015) (debtors’ marijuana business, while legal under state law, was illegal under  
5 federal law, and thus the debtors could not propose a confirmable plan in good faith).  
6 *See generally In re Leavitt*, 171 F.3d 1219, 1224 (9th Cir. 1999) (“cause” for dismissal  
7 not defined by the Code, but can include “bad faith”/lack of “good faith”); *Rosenblum*,  
8 608 B.R. at 537 (listing common considerations in assessing good faith).

9           Second, violations of nonbankruptcy law might constitute “gross  
10 mismanagement” of the estate, within the meaning of § 1112(b)(4)(B), because  
11 violations of nonbankruptcy law might expose the estate to financial losses and criminal  
12 sanctions, and violating the law might constitute “mismanagement” *per se*. *See, e.g., In*  
13 *re Rent-Rite Super Kegs West Ltd.*, 484 B.R. 799, 809 (Bankr. D. Colo. 2012) (Debtor’s  
14 decision to continue leasing warehouse space to tenants engaged in the business of  
15 growing marijuana exposed Debtor to criminal liability and the risk of forfeiture which  
16 amounted to gross mismanagement).

17           In addition, violations of nonbankruptcy law might warrant dismissal under  
18 general principles applicable to a bankruptcy court as a court of equity, pursuant to  
19 bankruptcy judges’ oath of office to uphold the law, or on other theories. *See, e.g., In re*  
20 *Johnson*, 532 B.R 53, 56-58 (Bankr. W.D. Mich. 2015) (suggesting that authorizing  
21 debtor to continue generating income from marijuana operations appears inconsistent  
22 with judicial oath to uphold the law, but concluding that Debtor could remain in  
23 bankruptcy and avoid dismissal of his case if he ceased marijuana operations). *See*  
24 *also* MTD (docket no. 53) pp. 8:18-17:11; Opp. (docket no. 59) pp. 3:6-19:26; *and* Reply  
25 (docket no. 63) pp. 7:22-11:14 (discussing authorities).

26           But the authorities cited by the parties also appear to reflect some degree of  
27 discretion. Ongoing postpetition violations are far more problematic than prepetition  
28 violations; and although indirect connections with illegal activity might violate

1 nonbankruptcy law, the degree of connection appears to be important to deciding  
2 whether to dismiss the case. See e.g., *In re Burton*, 610 B.R. 633, 637-638 (affirming  
3 dismissal as within bankruptcy court’s discretion, but holding that “the mere presence of  
4 marijuana near a bankruptcy case does not automatically prohibit a debtor from  
5 bankruptcy relief,” so a “bankruptcy court must be explicit in articulating its legal and  
6 factual bases for dismissal in cases involving marijuana”) (citations omitted); *and see*  
7 *also Garvin v. Cook Investments NW, SPNWY, LLC*, 922 F.3d 1031, 1036 (9th Cir.  
8 2019) (bankruptcy judge is not an “ombudsman without portfolio, gratuitously seeking  
9 out ‘illegalities’ . . . , a result that would be “inimical to the basic function of bankruptcy  
10 judges . . .”) (footnote, citations, and internal quotation marks omitted).

11 **c. The Controlled Substances Act, 21 U.S.C. § 801 et seq. (the “CSA”)**

12 The UST has not established any ongoing violation of the CSA by Debtor, as  
13 distinguished from any prepetition violations, either (i) by any connection to distributing  
14 cannabis or (ii) by stock ownership in a cannabis-related enterprise. Nor has the UST  
15 established that, if a chapter 11 trustee were appointed or if this case were to be  
16 converted to a chapter 7 liquidation, any trustee would have to engage in a violation of  
17 the CSA.

18 **i. No ongoing distribution of cannabis**

19 True, the CSA covers conspiracies with intent to distribute cannabis, and one  
20 way to characterize the facts might be that Debtor is effectively conspiring to continue  
21 carrying on its California-based cannabis business indirectly, through its ownership  
22 interest in a Canadian company operating under Debtor's former name. See 21 U.S.C.  
23 §§ 846 (conspiracy) *and* 856(a) (illegal to "control any place" or "profit from" a place  
24 used to manufacture, store, distribute, or use cannabis), *and* MTD p. 8:1-8.

25 Alternatively, even if (as this Bankruptcy Court finds and concludes) Debtor is *not*  
26 effectively carrying on its prepetition cannabis business indirectly, Debtor did structure  
27 its own liquidation in a manner designed to maximize the value derived from its  
28

1 connection with cannabis, which might be characterized as an indirect way to “profit  
2 from” the cannabis business.

3 On the other hand, this interpretation of section 856(a) of the CSA goes too far.  
4 Debtor's passive ownership of stock, with intent to liquidate that stock to pay creditors,  
5 will *terminate* any connection with cannabis. This appears to be the opposite of an  
6 intent to profit from an ongoing scheme to distribute cannabis, at least if Debtor does  
7 not maintain its investment in Lowell Farms, Inc. for too long a period of time (which is  
8 an issue that can be addressed in connection with confirmation of any chapter 11 plan).  
9 Therefore, the UST has not established a violation of section 856(a) of the CSA.

10 **ii. No future investment of profits from cannabis**

11 Similarly, although the UST has shown that Debtor's prepetition receipt of stock  
12 in its acquiring entity probably violated section 854 of the CSA, the UST has not  
13 established a likelihood of any postpetition violation from use or investment of cannabis  
14 proceeds. Section 854 of the CSA makes it illegal for a “person who has received any  
15 income derived, directly or indirectly, from [a relevant violation of the CSA]” to “use or  
16 invest, directly or indirectly, any part of such income, or the proceeds of such income, in  
17 acquisition of any interest in, or the establishment or operation of, any enterprise  
18 [engaged in or affecting interstate commerce].” See MTD p. 11:21-28 at n. 5 (quoting  
19 statute). Debtor does not propose, postpetition, to use any of its remaining assets to  
20 “invest” in any enterprise (cannabis-related or otherwise). Instead, Debtor proposes to  
21 sell the stock and distribute the resulting cash to creditors, or else transfer the stock  
22 directly to creditors.

23 **iii. No showing that a future trustee would have to violate the CSA**

24 The UST raises the specter that any future bankruptcy trustee would have to  
25 engage in illegal activity. But the UST does not explain how a trustee would have to  
26 violate the CSA or any other law.

27 For example, even if Debtor still had possession of any cannabis or marijuana  
28 products (which it does not), a trustee could “ask[] the responsible federal authorities to

1 dispose of the estate’s marijuana” and then fulfill the trustee’s statutory duty to  
2 “liquidat[e] other estate property for distribution to creditors in accordance with the  
3 priorities of [§] 726.” Steven J. Boyajian, Just Say No to Drugs? Creditors Not Getting a  
4 Fair Shake When Marijuana-Related Cases are Dismissed, 36 Am. Bankr. Inst. J. 24,  
5 75 & n. 21 (Sept. 2017).

6 Moreover, it is not a foregone conclusion that the rights of any federal  
7 governmental unit to seize assets would supersede creditors’ rights. See *id.* at 75 (text  
8 accompanying nn. 28-32). Therefore, not only has the UST failed to show that a future  
9 trustee would have to violate the CSA but, to the contrary, it appears that any future  
10 trustee probably might have a duty to administer assets rather than simply turn them  
11 over to federal authorities.

12 In addition, if any future trustee were concerned about any of these issues, the  
13 trustee could seek declaratory relief or other protections to assure compliance with the  
14 law and protection from liability. Alternatively, the trustee could always seek dismissal  
15 of this case at that point.

16 For all of the foregoing reasons, the UST has not established any ongoing  
17 violation of the CSA, nor has the UST established that any future trustee would have to  
18 violate the CSA. The lack of any demonstrated illegality, now or in the foreseeable  
19 future, is one ground for denial of the MTD.<sup>3</sup>

20 **d. Alternatively, Congress did not adopt a “zero tolerance” policy under**  
21 **§ 1112(b) for any illegality**

22 Supposing for the sake of discussion that the UST could establish a violation of  
23 the CSA (which it has not done), that it not enough. Congress did not adopt a "zero  
24

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25 <sup>3</sup> To be clear, Debtor’s apparent ownership of over 9% of the stock of a cannabis business puts it in uncomfortably  
26 close proximity to the cannabis industry. Perhaps, if all the facts and circumstances were known to this Bankruptcy  
27 Court, and if this Bankruptcy Court were to engage in independent research beyond the authorities cited by the  
28 parties, Debtor’s proposed liquidation actually would be a violation of the CSA or some other criminal statute.

But this Bankruptcy Court has not been asked to render any summary judgment as to purported violations of  
criminal law, and this Bankruptcy Court’s rulings above should not be interpreted as any such summary judgment.  
Rather, on the present record and solely for purposes of the UST’s MTD, no violation of the CSA has been  
established.

1 tolerance" policy that requires dismissal of any bankruptcy case involving violation of the  
2 CSA (or other activity that might be proven to be illegal). *See Burton*, 610 B.R. at 637  
3 (no per se rule requiring dismissal when marijuana is present).

4 True, Congress has enacted the CSA and this Bankruptcy Court's duty is to  
5 follow Congressional directives. On the other hand, Congress has not specified what  
6 should be the *bankruptcy-specific* remedy for any violation of the CSA.

7 Congress could have included within the examples of "cause" in § 1112(b)(4) a  
8 violation of the CSA, or any other nonbankruptcy laws, but it chose not to do so. This  
9 implies that violations of nonbankruptcy laws do not *necessarily* constitute cause for  
10 dismissal or conversion.

11 In addition, such a broad reading of "cause" for dismissal could be extremely  
12 disruptive in other cases before this Bankruptcy Court, perhaps even the vast majority  
13 of all bankruptcy cases. *See, e.g., In re CWNevada LLC*, 602 B.R. 717, 728 n. 25  
14 (Bankr. D. Nev. 2019) ("bankruptcy courts have a long history of considering cases  
15 whose activities and operations have included past, present and possibly ongoing  
16 violations of applicable non-bankruptcy, civil and criminal laws") (citing examples); Hon.  
17 Keith M. Lundin (Ret.), *Up in Smoke*, Bankruptcy Workshop, Season 2, Episode 3,  
18 available at <https://lundinonchapter13.com/Content/WorkshopVideos> (last visited on  
19 January 18, 2023) (noting bankruptcy courts' and trustees' statutory mandate to  
20 administer assets, and extensive history of doing so notwithstanding some connection  
21 to illegal activity).

22 Dismissing every case that had a connection with illegal activity would be  
23 contrary to Congress' directives under the Bankruptcy Code. Consider what would  
24 happen if the doors of the bankruptcy courts were closed to any debtor who had  
25 crossed the line into illegal activity prepetition, and were attempting to wind up that  
26 activity postpetition.

27 Some of the largest business bankruptcy cases, like those of Pacific Gas &  
28 Electric Co. of "Erin Brockovich" *fame*, Enron Corporation, and Bernie Madoff, involve



1 alleged or actual criminal activity. Should those cases have been dismissed? How  
2 about cases involving sexual abuse? See *CW Nevada*, 602 B.R. at 728 n. 25 (citing,  
3 *inter alia*, NCR Staff, Catholic Diocese and Orders that Filed for Bankruptcy and Other  
4 Major Settlements, National Catholic Reporter (2018),  
5 <https://www.ncronline.org/news/catholic-dioceses-and-orders-filed-bankruptcy-and->  
6 [other-major-settlements](https://www.ncronline.org/news/catholic-dioceses-and-orders-filed-bankruptcy-and-other-major-settlements) (last visited on January 18, 2023) (listing numerous bankruptcy  
7 proceedings to address sexual abuse claims, from July 6, 2004 through approximately  
8 February 28, 2018)).

9 On a smaller scale, this Bankruptcy Court takes judicial notice that many small  
10 business bankruptcies involve restaurants or small apartment buildings, and most of  
11 those businesses have at least some ongoing level of violations of health and safety  
12 regulations. When dealing with food and shelter, although it is important to strive for  
13 perfection, realistically that goal can be extremely difficult to achieve.

14 Likewise, many individual debtors have crossed the line into illegality in ways  
15 both large and small, from engaging in criminal gang activity to failing to pay taxes or  
16 parking fines. This Bankruptcy Court takes judicial notice that individuals who are  
17 struggling financially may have difficulty paying parking fines, for example, and there are  
18 societal debates about the criminalization of nonpayment of such fines, so barring such  
19 a debtor from bankruptcy would not be a step to take lightly.

20 If all of the foregoing examples were sufficient “cause” for mandatory dismissal,  
21 this Bankruptcy Court might have to dismiss most bankruptcy cases. That would harm  
22 the constituencies that Congress attempted to protect using all of the tools of the  
23 Bankruptcy Code, including creditors, debtors, employees of debtors, and local  
24 governments and communities that depend on debtors’ ability to reorganize their  
25 finances and resume making contributions to commerce and society.

26 For example, the automatic stay of § 362(a) protects creditors from a “race to  
27 collect”: absent that stay the assets go to anyone who is able to seize them before other  
28 creditors. Insiders or other favored creditors might have an advantage in doing so,

1 contrary to Congress attempts to prevent such favoritism. See, e.g., § 547(b)(4) (longer  
2 “look back” period for preference recipients who are insiders).

3 In addition, an orderly liquidation in bankruptcy typically maximizes the value of a  
4 debtor’s assets. Bankruptcy can preserve going concern value, or can authorize a sale  
5 of assets free and clear of liens and other interests, thereby obtaining higher bids than  
6 outside of bankruptcy. See, e.g., §§ 363(f) and 1129(b)(2)(A)(ii), and see also *In re*  
7 *Olson*, 2018 WL 989263 at \*7 (9th Cir. BAP Feb. 5, 2018) (Tighe, J., concurring) (noting  
8 the usefulness of sales free and clear, even in cases connected to marijuana).

9 In addition, dismissal of bankruptcy cases would shield recipients of avoidable  
10 transfers (e.g., §§ 547, 548) and persons whose misdeeds might only come to light in the  
11 bankruptcy forum, with all of its mandated disclosures and investigative tools. See, e.g.,  
12 Rules 1007 & 2004; see also Boyajian, Just Say No to Drugs?, *supra*, 36 Am. Bankr. Inst.  
13 J. 24 at 75 (text accompanying nn. 22-27) (arguing that dismissal of involuntary chapter  
14 7 petition allowed “the alleged debtor to use its own federally proscribed conduct [running  
15 a marijuana business] as a shield to protect it from the collection efforts of creditors  
16 holding seemingly undisputed claims”). This Bankruptcy Court doubts that Congress  
17 intended to shield recipients of avoidable transfers, and wrongdoers, by mandating  
18 dismissal of any bankruptcy case that might be connected to violations of criminal law.

19 In fact, in many situations the victims of illegal activity are the persons who might  
20 be most severely harmed by dismissal of any bankruptcy case. This is true whether  
21 that illegal activity involves releasing carcinogens into the water supply, financial fraud,  
22 being a “slumlord,” causing food poisoning, abusing employees, child sexual abuse, or  
23 other criminal activity. The victims may be the biggest creditors, or those with the most  
24 to lose.

25 One other type of creditor who might well be harmed by any mandated dismissal  
26 of any case connected to illegal activity is any government agency charged with  
27 enforcing the law, such as the Department of Justice, which encompasses the Office of  
28 the UST itself. Such agencies’ funding, and their ability to continue policing against

1 criminal activity, might depend in part on the preservation and recovery of assets,  
2 including through bankruptcy.

3 For all of these reasons, this Bankruptcy Court does not interpret Congress'  
4 mandate that this Bankruptcy Court “shall” dismiss or convert a bankruptcy case for  
5 “cause” under § 1112(b) to mean that any violation of criminal law *requires* dismissal.  
6 Rather, this Court interprets the statute as giving discretion to determine whether  
7 dismissal is warranted based on all the facts and circumstances. *See generally Burton*,  
8 610 B.R. 633, 640 *and passim* (review of various authorities, and referring to bankruptcy  
9 courts’ “broad discretion in deciding whether to dismiss a case”).

10 Nor does this Bankruptcy Court interpret the UST's MTD to advocate for such an  
11 extreme position. *Cf. Clifford J. White III and John Sheahan, Why Marijuana Assets*  
12 *May Not Be Administered In Bankruptcy*, 36 Am. Bankr. Inst. J. 34, 34-35 (Dec. 2017)  
13 (contrasting bankruptcy cases “in which the criminal activity has already been  
14 terminated and the principal concern of the bankruptcy court is to resolve competing  
15 claims by victims for compensation” from a case involving “a company that is not only  
16 continuing in its business, but even seeking the affirmative assistance of the bankruptcy  
17 court in order to ... facilitate its violations of the law going forward”) (the authors are  
18 listed, respectively, as the director of the Executive Office for U.S. Trustees and as a  
19 trial attorney in the Office of the General Counsel).

20 In sum, this Bankruptcy Court interprets both § 1112(b) and the UST's MTD as  
21 adopting a middle ground, under which this Bankruptcy Court must exercise its  
22 discretion to determine whether, given all of the facts and circumstances, a debtor's  
23 connection to cannabis profits and any past or future investment in cannabis enterprises  
24 warrants dismissal of this bankruptcy case. Under this standard, the UST has not met  
25 its burden to establish sufficient cause for dismissal, for the reasons stated above,  
26 including (i) Debtor's indirect connection with any violation of the CSA (assuming,  
27 contrary to this Court's analysis in the prior section of this Opinion, that such a violation  
28

1 exists), (ii) Debtor's intent to liquidate its assets and pay creditors, and (iii) the benefits  
2 of a bankruptcy case for all parties in interest, including creditors.

3 **e. Alternatively, the “unusual circumstances” exception applies**

4 Congress has provided that even when there is “cause” to dismiss or convert a  
5 case, this Bankruptcy Court must not to do so under the “unusual circumstances” test  
6 described above. See § 1112(b)(2). The elements of this test have been satisfied, at  
7 least in the absence of evidence that prosecutors intend to single out Debtor for  
8 particularly harsh treatment that would undermine any ability to pay creditors and  
9 otherwise make appropriate use of the bankruptcy system.

10 Specifically, the unusual circumstances in this case are as follows. First, Debtor  
11 has divested itself, prepetition, of any direct involvement in the cannabis business.  
12 Second, unlike most dismissals by this Court, which generally involve situations such as  
13 a pending foreclosure of fully-encumbered property and no realistic possibility of a  
14 distribution to unsecured creditors, in this case any dismissal would undermine a very  
15 realistic possibility of a substantial payment to creditors. That successful outcome  
16 appears to be very likely because the only thing for Debtor to do is to sell its stock in the  
17 Canadian company, which appears to be legal and feasible under Canadian law, and  
18 then to use the proceeds to pay creditors; or alternatively to distribute the stock to  
19 creditors.

20 These facts also establish the other elements of the “unusual circumstances”  
21 test: conversion or dismissal is not in the best interests of creditors; there is a  
22 reasonable likelihood of confirming a plan in a reasonable amount of time; even if  
23 Debtor’s acts and omissions in seeking to divest itself of its assets and pay creditors  
24 somehow violated the CSA or other law, and would otherwise mandate dismissal,  
25 Debtor’s attempt to maximize value and pay creditors establishes a “reasonable  
26 justification” for such acts and omissions; and, so long as Debtor’s process of selling or  
27 distributing its stock in the Canadian company does not take too long, any violation of  
28

1 law can be “cured within a reasonable time.” *Rosenblum*, 608 B.R. at 536-37 (reviewing  
2 elements of § 1112(b)(2)).

3 In addition, this Bankruptcy Court is mindful of the fact that there are many other  
4 tools to address any wrongful or illegal conduct by any debtor in possession of the  
5 bankruptcy estate. For example, in appropriate circumstances a trustee or examiner  
6 can be appointed (§ 1104), or sanctions can be imposed. See, e.g., Rule 9011. The  
7 availability of such alternatives reinforces a more flexible interpretation of § 1112 as just  
8 one of many possible tools, not a tool that this Bankruptcy Court has to use regardless  
9 of the consequences.

10 In addition, this Bankruptcy Court notes that there are many non-bankruptcy tools  
11 that can be used to address any illegal activity. Remedies can be sought, in appropriate  
12 situations, by prosecutors, private attorneys general, class action representatives,  
13 individual plaintiffs, and others, such as local, state, and national governments, to  
14 address any violations of nonbankruptcy law in a more nuanced and targeted manner  
15 than the blunt tool of dismissing bankruptcy cases. Again, the availability of such  
16 alternatives reinforces this Bankruptcy Court's interpretation of § 1112(b) as providing  
17 some discretion: dismissal is not the only remedy.

18 **f. No intent to condone illegal activity**

19 To be clear, nothing in this Opinion should be interpreted as condoning illegal  
20 activity. Illegal activity can be cause for dismissal in appropriate circumstances, both as  
21 a matter of interpreting Congress' directives in § 1112(b) and, more generally, to  
22 preserve the integrity of the bankruptcy system and the bankruptcy courts that  
23 Congress has established. See, e.g., *In re Mattiace Industries, Inc.*, 76 B.R. 44, 47-48  
24 (Bankr. E.D.N.Y. 1987) (dismissing chapter 11 bankruptcy case because debtor's  
25 continued violations of state environmental regulations endangered public health and  
26 conversion was inappropriate due to difficulties a trustee would face in managing  
27 debtor's hazardous waste site with limited estate resources)

28


1 But this Bankruptcy Court would be overstepping its role, and acting contrary to  
2 Congress' directives within the Bankruptcy Code, if it were to deny creditors, debtors,  
3 employees, equity investors, and other constituencies the benefits and protections of  
4 bankruptcy based on the facts and circumstances presented. In general this  
5 Bankruptcy Court should defer to prosecutors, and all of the other types of persons  
6 mentioned above, to use their discretion about whether and how to address any  
7 violations of nonbankruptcy law. See *Cook Investments*, 922 F.3d 1031, 1036 (rejecting  
8 "ombudsman" role of bankruptcy court). Such parties can pursue remedies in a more  
9 nuanced and targeted manner, rather than using the blunt tool of dismissal, which on  
10 the record presented is contrary to the best interests of creditors and the estate.

11 **4. CONCLUSION**

12 For all of the foregoing reasons, the MTD has been denied by separate order.

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24 Date: January 20, 2023

  
Neil W. Bason  
United States Bankruptcy Judge