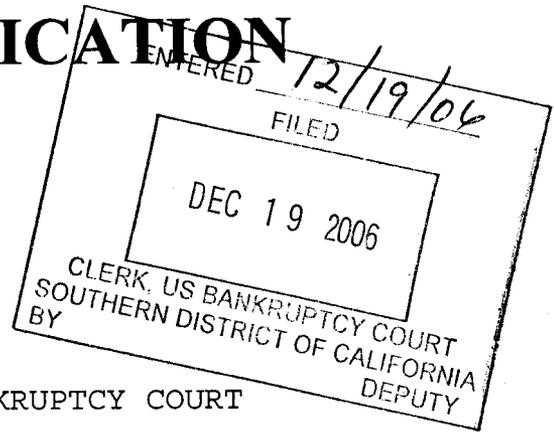


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# NOT FOR PUBLIC



UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF CALIFORNIA

In re

RICHARD HOUGHTON,

Debtor.

Bankruptcy No. 04-09161-JM7

Memorandum Decision

The Court heard argument on November 9, 2006, as to whether an order for relief should be entered on the involuntary petition filed by the California Corporations Commission ("Commission"), Kenneth Burns ("Burns") and Paul W. Liscom ("Liscom"). The Bankruptcy Appellate Panel previously ruled that Burns and Liscom did not have individual claims under the consent judgment ("Consent Judgment") entered into between the alleged debtor and the Commission. On remand, the Panel instructed this Court to determine if Burns and Liscom had claims against the alleged debtor which would qualify them as petitioning creditors under Bankruptcy Code Section 303(b)(1).

The Commission asserts that Burns and Liscom would have independent claims for fraud in the sale of the securities. See Cal. Corp. Code § 25503. The difficulty with this argument is that the

1 statute of limitations has expired on any such claims. The Commission  
2 contends, however, that the statute of limitations was tolled by the  
3 Consent Judgment. It argues that the alleged debtor acknowledged the  
4 debts owed to Burns and Liscom when he entered into the Consent  
5 Judgment.

6 The alleged debtor counters that there was no acknowledgment of  
7 debts owed to Burns and Liscom in the Consent Judgment. He also  
8 points out that pursuant to the language of the Consent Judgment,  
9 he did not admit to any of the allegations in the Commission's  
10 complaint. He also argues that the existence of the issue over the  
11 statute of limitations demonstrates that there is a bona fide dispute  
12 as to the claims of Burns and Liscom.

13 The burden is on the petitioning creditors to show that no bona  
14 fide dispute exists. In re Vortex Fishing Systems, Inc., 277 F.3d  
15 1057, 1064 (9<sup>th</sup> Cir. 2002). In Vortex, the Ninth Circuit Court of  
16 Appeals adopted the objective test for determining if a bona fide  
17 dispute exists. Pursuant to that test, "if there is a genuine issue  
18 of material fact that bears upon the debtor's liability, or a  
19 meritorious contention as to the application of law to undisputed  
20 facts, then the petition must be dismissed." Vortex, 277 F.3d at 1064  
21 (quoting In re Lough, 57 B.R. 993, 996-97 (E.Mich. 1986)). Courts  
22 have explained that Congress intended to disqualify a creditor  
23 whenever there is any legitimate basis for the debtor not paying the  
24 debt, whether that basis is factual or legal, because it did not  
25 intend to require a debtor to pay a legitimately disputed debt simply  
26 to avoid the stigma of bankruptcy. In re BDC 56 LLC, 330 F.3d 111 (2d  
27 Cir. 2003).

28 Based on the record provided by the Commission, this Court

1 determines that any claims held by Burns and Liscom are subject to a  
2 bona fide dispute. It is not clear that the Consent Judgment was an  
3 acknowledgment of a debt owed by the alleged debtor to Burns and  
4 Liscom. An acknowledgment must be an admission of a debt existing to  
5 the creditor in question. First Nat. Bk. of Park Rapids v. Pray, 86  
6 Cal.App. 484 (1927). The Bankruptcy Appellate Panel characterized the  
7 Consent Judgment as follows:

8       Though the Consent Judgment expressly requires Debtor to  
9       pay restitution to the Commission in the form of a money  
10       judgment, it is absent of any language indicating to whom  
11       the restitution award is payable to other than the  
12       Commission. The language in the Consent Judgment would  
13       provide a future court with no indication that Burns and  
14       Liscom were victims.

15       An acknowledgment may be made to an agent of the creditor or to  
16       some person authorized to receive it. Western Coal and Mining Co. v.  
17       Jones, 27 Cal.2d 819 (1946). However, as pointed out by the Panel,  
18       there is no reference in the Consent Judgment, or for that matter in  
19       the Commission's complaint, to Burns and Liscom. The Commission has  
20       filed the declaration of Michelle Lipton, wherein she explains how she  
21       calculated the amount sought in the complaint and Consent Judgment.  
22       But, at best, this merely raises a genuine issue of material fact as  
23       to the effect of the Consent Judgment and whether it was a proper  
24       acknowledgment of any debt owed Burns and Liscom. Since any  
25       independent claims held by Burns and Liscom are subject to a bona fide  
26       dispute, Burns and Liscom are not eligible to join in as petitioning  
27       creditors.

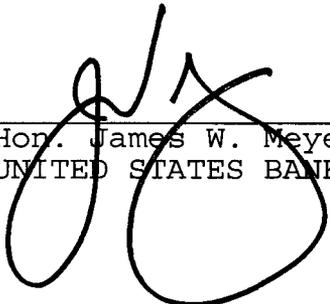
28       The involuntary petition must be DISMISSED because the petition

1 fails the Section 303(b)(1) three-petitioner requirement for debtors  
2 with twelve or more creditors.

3       The Court will schedule a status conference at which time it will  
4 discuss the appropriate form of order. Additionally, at that hearing  
5 the parties will be asked to address any remaining matters to be  
6 resolved in this case.

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8 Date: DEC 19 2006

  
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Hon. James W. Meyers  
UNITED STATES BANKRUPTCY JUDGE

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