SO ORDERED.

SIGNED this 29 day of August, 2007.

ROBERT E. NUGENT
UNITED STATES CHIEF BANKRUPTCY JUDGE

NOT DESIGNATED FOR PUBLICATION

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF KANSAS

IN RE:	)	
	)	
GARY E. KRAUSE,	)	**Case No. 05-17429**
	)	**Chapter 7**
Debtor.	)	
	)	
UNITED STATES OF AMERICA,	)	
	)	
Plaintiff,	)	
and	)	
	)	
LINDA S. PARKS, Trustee	)	
	)	
Intervener,	)	
v.	)	**Adversary No. 05-5775**
	)	
GARY KRAUSE and RICHARD KRAUSE,	)	
	)	
Defendants	)	
and	)	
	)	
DRAKE KRAUSE and RICK KRAUSE,	)	
	)	

Intervener.)
_____)

ORDER DENYING INTERVENERS DRAKE AND RICK KRAUSE'S MOTION TO STAY SANCTIONS JUDGMENT PENDING APPEAL

Interveners Drake and Rick Krause seek a stay of enforcement of the Sanctions Judgment[1] entered against their father, defendant-debtor Gary Krause in favor of the Government and the Trustee while they pursue an appeal of the same.[2] They seek a stay under Fed. R. Bankr. P. 7062 which makes Fed. R. Civ. P. 62 applicable in bankruptcy adversary proceedings.[3] The Government and the Trustee oppose the requested stay.[4]

Introduction/Background

Readers of this Order are referred to this Court's previous Memorandum Opinion on the Trustee's Motion for Sanctions for Spoliation of Evidence and the Government's Motion for Contempt and Default Judgment,[5] the Court's Order Denying Gary Krause's Motion for a Stay of the Sanctions Pending Appellate Review,[6] and the Court's Order Denying Intervener Drake Krause's

[1] Dkt. 311 and 317. Dkt. 311 is the Memorandum Opinion on the Trustee's Motion for Sanctions for Spoliation of Evidence and the Government's Motion for Contempt and Default Judgment. Dkt. 317 is the Partial Judgment on Decision emanating from the Memorandum Opinion. For ease of reference, the Court refers to these docket entries interchangeably as the "Sanctions Judgment."

[2] Dkt. 380.

[3] Fed. R. Bankr. P. 8005 contemplates that the bankruptcy court will be the primary court to stay a matter pending appeal pursuant to Bankruptcy Rule 7062. *See In re Sunset Sales, Inc.*, 195 F.3d 568 (10th Cir. 1999).

[4] Dkt. 384 and 388.

[5] Dkt. 311.

[6] Dkt. 373.

Motion for Reconsideration of the Sanctions Judgment.[7] These rulings contain the factual background giving rise to the Sanctions Judgment and the procedural history of this case. The Court will attempt to avoid repeating those matters here.

The Court is nearing final adjudication of the Government's and Trustee's claims against Gary in this adversary proceeding. Trial on the remaining claims in this case (including the validity of the Krause Children Trusts of which interveners are beneficiaries) is hard set for November 26 - December 7, 2007.

For purposes of the instant motion, interveners seek a stay of only one of the Court's discovery sanctions: defaulting Gary on the Government's and Trustee's claim that PHR, LLC is Gary's nominee, is property of the bankruptcy estate, and is subject to turnover. PHR, LLC is the putative owner of 7711 Oneida Court, Wichita, Kansas - the home where Gary and the interveners reside.[8] Interveners assert an equitable ownership interest in the Oneida property and contend that the default sanction on PHR, LLC adversely impacts them should the Trustee or Government enforce turnover of the property.

Interveners' Stay Motion

Interveners apparently proceed under Rule 62(d) and seek a waiver of the requirement that they give a supersedeas bond, citing *Dutton v. Johnson County Board of County Com'rs*.[9] *Dutton* does indeed enumerate factors for a court to consider in determining whether a stay on execution

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[7] Dkt. 377.

[8] The Court observes that Gary has recently filed a pleading in the main case styled "Notice of Provisional Claim of Homestead Exemption," asserting a provisional homestead exemption in the 7711 Oneida property. Case No. 05-17429, Dkt. 71.

[9] 884 F. Supp. 431 (D. Kan. 1995).

of a money judgment should be granted without posting a supersedeas bond.[10] The Court, however, believes that subsection (d) is inapplicable in this case because no money judgment was entered against Gary and no judgment at all was entered against interveners. *Dutton* notes that the purpose of a supersedeas bond is to protect a judgment creditor from losses that may result from staying execution of a *money judgment*.[11] The Court rejects analysis of interveners' stay motion under Rule 62(d).

A complete reading of *Dutton* is enlightening for that portion of the opinion that interveners conveniently omit. *Dutton* involved an employee's claims under the Americans with Disability Act (ADA). The employee prevailed in a jury trial. The district court thereafter awarded back pay, fees and costs to the employee and ordered reinstatement of the employee. The district court analyzed the defendant's motion for stay of judgment pending appeal under both Rule 62(d) and Rule 62(c). It applied subsection (d) to the back pay award and subsection (c) to the order of reinstatement.

The *Dutton* court applied Rule 62(c) to the request for a stay of the reinstatement order:

> The suspension of equitable or injunctive relief ordered by a district court during the pendency of an appeal is authorized by Federal Rule of Civil Procedure 62(c).[12]

The District Court proceeded to recite the four factors frequently cited by courts, including the Tenth Circuit Court of Appeals, to obtain a stay under Rule 62(c): (1) likelihood of success on the merits of the appeal; (2) irreparable injury to the movant if the stay is denied; (3) substantial harm to other

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[10] *Id.* at 435.

[11] *Id.*

[12] *Id.* at 433.

parties if the stay is granted; and (4) the public interest favors a stay.[13]

This Court concludes that Rule 62(c) governs interveners' stay motion before the Court. Rule 62(c) states, in relevant part:

> When an appeal is taken from an interlocutory or final judgment granting . . . an injunction, the court in its discretion may suspend, modify, restore, or grant an injunction during the pendency of the appeal . . .

Here, the Sanctions Judgment, albeit by default, consists of a declaration that PHR, LLC is a nominee of Gary, is property of the estate, and is subject to turnover. In the Court's view, this declaratory judgment is in the nature of equitable or injunctive relief, notwithstanding the fact that it is not technically an "injunction" as referenced in Rule 62(c)[14] In addition, the Court notes that not all of the Government's and Trustee's claims in this adversary proceeding have been adjudicated, leading this Court to believe that the Sanctions Judgment for Gary's discovery abuses and spoliation of evidence, is not a final judgment. Rule 62(c) also applies to interlocutory relief.[15]

Analysis

Like Gary's stay motion, interveners fails to mention or address the applicable standard for a stay except for the second factor (irreparable injury). This alone is a sufficient basis for denying interveners' stay motion.[16] Because of the procedural posture of this adversary, the Court will

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[13] *Id.* These were the same standards this Court applied in determining Gary's motion for a stay of the Sanctions Judgment pending his appeal. *See* Dkt. 373, p.5, citing *Lang v. Lang (In re Lang)*, 305 B.R. 905 (10th Cir. BAP 2004).

[14] As in the instant case, the judgment sought to be stayed in *Dutton* was not an injunction.

[15] *See Waste Connections of Kansas, Inc. v. City of Bel Aire, Kansas*, 191 F. Supp. 2d 1253, 1254 (D. Kan. 2002) (The district court has discretion to enter a stay pending resolution of an interlocutory appeal under Rule 62(c).).

[16] *Id.*

nonetheless assess interveners' stay motion

Likelihood of Success on the Merits

As the Court noted when it considered Gary's request for a stay of the Sanctions Judgment, the default judgment entered by the Court on some, but not all, of the claims against him, was entered as a sanction for Gary's willful spoliation of computer evidence, Gary's noncompliance with the Court's order to produce electronic evidence and to turnover his computers, Gary's violation of the preliminary injunction, and Gary's noncompliance with the order requiring him to disclose his connections to all assets.

Interveners do not argue that the Court erred in any respect in finding that the Trustee and Government proved Gary's spoliation of evidence and contempt of the Court's discovery orders and preliminary injunction. Interveners appeared through their attorney at the evidentiary sanctions hearing and chose not to actively participate in the hearing. Nor do interveners demonstrate in their stay motion that the sanctions imposed by the Court for those offenses constituted an abuse of discretion. Interveners have not shown even a remote possibility of success on the merits of the Sanctions Judgment. This factor weighs heavily against them and is sufficient alone to deny their stay motion.[17]

Irreparable Injury to Interveners if the Stay is Denied

Interveners contend that if the Trustee and Government are permitted to enforce the Sanctions Judgment with respect to PHR, LLC (the putative owner of the family home at 7711 Oneida Court, Wichita, Kansas), they will be evicted from their home. This Court previously noted

[17] *See Lang v. Lang (In re Lang)*, 305 B.R. 905, 911 (10th Cir. BAP 2004) (affirming bankruptcy court's denial of stay on the "success on the merits" factor, without addressing the remaining factors).

in ruling on Gary's motion, that the impact on a debtor's family of personal disruption and emotional distress caused by the IRS's seizure of the family home to satisfy debtor's tax liability is not irreparable injury.[18]

Much of what the Seventh Circuit Court of Appeals said in *Carlson* is applicable here. The fact pattern is not unlike that in the case at bar. The debtor in *Carlson* was a lawyer who failed to pay income taxes of $150,000 for the years 1990, 1991 and 1992. During the period that the debtor was contesting his tax liability, he sought bankruptcy protection under chapter 11. The bankruptcy court eventually dismissed the debtor's case because he could not submit a confirmable plan. The debtor sought a stay of collection proceedings by the IRS (to enforce its tax lien) pending his appeal to the district court. Both the bankruptcy court and the district court denied his stay request.

> Carlson [debtor] maintains that because stay was denied, the IRS is free to seize and liquidate his home to satisfy its tax claim. . . . if the IRS were to seize assets for payment of taxes, penalties, or interest, and a court later ruled that the taxpayer was not liable for some or all of the payment, the damage could be undone by a simple order requiring repayment with appropriate interest. Carlson urges us here to recognize an exception to that principle, because of the heightened interest he has in his home. . . . He concludes that, to the extent this case is about the IRS's power to seize his home for satisfaction of his tax liabilities, it's now or never for him.
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> * * *
>
> The real problem Carlson faces is that he offers absolutely no authority for the proposition that homes are somehow exempt from tax liens. This is not surprising, because it is not uncommon for the IRS to turn to precisely that asset for payment. [citations omitted.] The Carlsons are typical in that their home represents one of their largest assets. We are not unaware of the disruption this imposes on individuals, but this is a problem Carlson brought upon himself. We therefore conclude that the substantial personal grief that the family would experience if the IRS follows through pending this appeal and seizes the house is nonetheless not the kind of irreparable

[18] *See* Dkt. 373, at p. 7, *citing In re Carlson*, 224 F.3d 716 (7th Cir. 2000).

injury . . . require[d].[19]

So too, here, the interveners' potential loss of the Oneida property to the Trustee or the Government through enforcement of the Sanctions Judgment does not constitute irreparable injury. If the appellate court reverses this Court's Sanctions Judgment, the Trustee and Government will be required to return the property (if still in their possession) or the proceeds from its sale back to PHR, LLC.

Every day, this Court is faced with the seemingly harsh impact of court orders on innocent family members of debtors – debtors, who like Gary, voluntarily sought bankruptcy protection. Stay relief is routinely granted to mortgage creditors during a bankruptcy so that the creditors can foreclose their mortgages and satisfy their claims. Debtors in bankruptcy are commonly forced to surrender their home to creditors to obtain a "fresh start." Pre-petition transfers by debtors to family members are sometimes avoided as preferences or fraudulent transfers. Such actions undoubtedly adversely impact the family of the debtor and put innocent children out of their home, but that fact does not warrant this Court's ignoring the law. Intervener Drake is attending college in Lawrence, Kansas and has already moved out of the Oneida property. His brother Rick is in his last year of high school and likely soon to be out on his own too. In the meantime, nothing is presented by interveners to suggest that their father Gary is incapable of providing other suitable housing for himself and his sons, given his last reported monthly income of $8,000. In the Court's experience, very few chapter 7 debtors before this Court earn this amount of monthly income or enjoy the standard of living that Gary and interveners enjoy, even while in bankruptcy.

Interveners also assert an equitable ownership in the Oneida property. They do not clearly

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[19] 224 F.3d at 718-19.

delineate the basis for that ownership but the Court assumes it arises by virtue of their beneficial interest in the Krause Children Trusts, which in turn purport to own PHR, LLC. The elimination of the interveners' equitable ownership of the Oneida property as a result of their father's misdeeds does give the Court pause, particular if, as it turns out, the Krause Children Trusts and PHR, LLC are legitimate trusts and entities and duly hold legal title to the Oneida property. Given what the Court has heard to date regarding the creation of PHR, LLC and the transactions regarding the Oneida property, it is highly skeptical of a determination favorable to interveners and Gary. Those very transactions are what led this Court to grant a preliminary injunction and freeze the assets of PHR, LLC nearly two years ago.

Interveners have not demonstrated that they will suffer an irreparable injury if a stay pending appeal is denied.

Substantial Harm to the Government and Trustee if the Stay is Granted

As this Court observed in denying Gary's stay motion, some of the harm visited upon the Government and the Trustee if a stay of the Sanctions Judgment were granted, is a further delay in marshaling assets of the estate and collecting Gary's $3 million tax liability. Like Gary, interveners offer no security to the Trustee or Government to protect their interest in the Sanctions Judgment during the pendency of the appeal.[20] To the contrary, interveners assert that no supersedeas bond should be required. Interveners (and Gary) propose to live in the Oneida property (property which Gary has steadfastly maintained he does not own) for free while they proceed with their appeal.

[20] For example, interveners have not come forward with proof of insurance on the Oneida property nor offered to name the Trustee as the loss payee on the policy of insurance. The Court is mindful that in a previous hearing in this matter, the 2005 tax appraisal of the Oneida property was $392,000. *See* Dkt. 22, Ex. A.

As noted in *Carlson*:

> The district court has the discretion to waive this [bond] requirement, but waiver is appropriate only if the appellant has a clearly demonstrated ability to satisfy the judgment in the event the appeal is unsuccessful and there is no other concern that the appellee's rights will be compromised by a failure adequately to secure the judgment. [citations omitted.] This case presents the polar opposite of a situation in which waiver is appropriate. There is every reason to lack confidence that Carlson will pay up eventually; to the contrary, just two days after a prior IRS collection effort, Carlson signaled his intent to evade his obligations by transferring a piece of real estate to his son at no charge. *Carlson*, 126 F.3d at 919. Nor has Carlson subsequently demonstrated anything but obstinance in this matter since our last opinion.[21]

The same is true in the instant case. While the Oneida property is a substantial asset, it will hardly satisfy Gary's tax liability if and when liquidated. Even if the Trustee and Government prevail on their claims, the assets in the various trusts and entities (assets that were frozen by the preliminary injunction) will fall far short of satisfying Gary's $3 million tax debt. The Government has spent the last two years in this Court alone trying to ascertain the extent of Gary's assets. Gary has resisted at every turn. As the Court found in the Sanctions Judgment, Gary has already shown his propensity to defy this Court's orders by destroying computer evidence and violating the preliminary injunction.[22] And as the Government established at the hearing on the preliminary injunction, Gary caused PHR, LLC to be created July 29, 2005 and transferred the Oneida property to it on August 5, 2005 within thirty (30) days of being served with the IRS collection summons.[23] In short, Gary, and now the interveners, have taken every step to delay the gathering of assets of the estate and paying Gary's creditors. This Court has grave concerns that the Trustee's and Government's rights may be

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[21] 224 F.3d at 719.

[22] *See* Dkt. 311 at pp. 31-32.

[23] *See* Dkt. 80 at pp. 4-5, 7, 10-11.

further compromised by the lack of security and the continued delay.

And more importantly, interveners do not and cannot restore the computer evidence that Gary destroyed when he intentionally wiped the hard drives before their turnover to the Trustee. Interveners cannot alleviate the prejudice inflicted upon the Trustee and the Government by the spoliation of evidence – evidence that may have supported their nominee theory and other claims.

In the Court's view, the only way to lessen the harm to the Trustee and Government is to proceed with dispatch to a trial of the remaining claims in this adversary proceeding. The Court intends to do so on November 26, 2007.

Public Interest

Interveners have identified no public interest that would be advanced by granting a stay of enforcement of the Sanction Judgment on the Oneida property. The Court does not believe that interveners' potential loss of the Oneida property as a result of their father's misconduct offends the public interest. Nothing precludes interveners and their father from establishing a new place of residence. And as noted above, interveners are or near the age of majority and emancipation. Further, for the reasons stated in the Court's order denying Gary's stay motion, this factor weighs heavily in favor of the Government and the Trustee.[24]

Summary

Interveners fail to address or satisfy the four factors for obtaining a Rule 62(c) stay pending appeal. Interveners' motion for a stay pending appeal of the Sanctions Judgment is therefore DENIED. The temporary stay entered by this Court on August 23, 2007 is hereby lifted[25] and the

[24] *See* Dkt. 373 at p. 9.

[25] Dkt. 393.

Trustee and Government shall be permitted to enforce the Sanctions Judgment, including the Trustee's right to proceed with enforcement of turnover of property. To the extent assets of the various entities and trusts named in the Sanctions Judgment were frozen by this Court's preliminary injunction entered December 5, 2005, the preliminary injunction is modified to permit their turnover to the Trustee.

IT IS THEREFORE ORDERED THAT Interveners Drake and Rick Krause's Motion to Stay Enforcement of Sanctions Judgment Pending Appeal is DENIED.

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