UNITED STATES BANKRUPTCY COURT
FOR THE WESTERN DISTRICT OF MICHIGAN

In re:

KRISTI LYNN CARMICHAEL,

Debtor.
_____/

Case No. DL 07-09745
Hon. Scott W. Dales
Chapter 7

OPINION REGARDING MOTION OF CREATIVE WELLNESS, INC. TO DISMISS CHAPTER 7 PETITION

I. INTRODUCTION AND JURISDICTIONAL STATEMENT

This matter comes before the court upon a Motion to Dismiss Chapter 7 Petition (the "Motion") filed by Creditor Creative Wellness, Inc. (the "Creditor") against Kristi Lynn Carmichael (the "Debtor"). The Debtor timely filed a response to the Motion and I heard oral argument on May 14, 2008 in Lansing, Michigan. I commend both counsel for ably representing their clients and making incisive and courteous presentations in their papers and at oral argument.

The parties have waived the opportunity for an evidentiary hearing, and stipulated that I should decide the Motion based solely on the pleadings, schedules, and other documents reflected on the court's docket.

The court has jurisdiction pursuant to 28 U.S.C. § 1334(a). This matter is a core proceeding as described in 28 U.S.C. § 157(b)(2)(A) & (O). This opinion constitutes the court's findings of fact and conclusions of law pursuant to Fed. R. Civ. P. 52.[1]

II. ISSUE FOR DECISION

Whether the Debtor filed her bankruptcy case in a bad faith effort to prevent the Creditor from recovering an arbitrator's award arising from an employment dispute.

III. MATERIAL FACTS

On May 10, 2002, the Debtor began work for the Creditor providing holistic health care services such as massage and myofacial therapy, sports massage and similar services. The Debtor signed an Employment and Non-Compete Agreement (the "Agreement") which imposed certain employment and post-employment restrictions upon her. (Exh. C).[2] Also as a condition of her employment, the Debtor agreed to abide by the Creditor's policies reflected in the Service Providers Employee Manual for Creative Wellness, Inc. (Exh. D). Consequently, the Debtor agreed to submit employment-related disputes to arbitration before the American Arbitration Association (the "AAA").

Beginning in late February or early March 2006, the relationship between the Debtor and the Creditor started to deteriorate. They disagreed about the Debtor's responsibilities to the Creditor and the constraints of the Agreement. As a result, the Debtor resigned on March 27, 2006, and started her own business. On December 29,

[1] Federal Rules of Bankruptcy Procedure 7052 and 9014 make Federal Rule of Civil Procedure 52 applicable to this contested matter.
[2] In this Opinion, I will cite the exhibits attached to the Creditor's Motion as "Exh. __."

2006, the Creditor filed a Verified Demand for Expedited Arbitration and Motion for Temporary Restraining Order and Preliminary Injunction with the AAA.

On October 15, 2007, in response to a Motion for Summary Judgment, Thomas Cranmer (the "Arbitrator") found that the Debtor solicited three and treated twelve of the Creditor's clients, and used confidential information from two clients, thereby breaching her employment contract. (Exh. A at p. 8).

In his Interim Award, the Arbitrator directed the Creditor to supply additional information on damages because its $64,000.00 damage request was premised upon an unreasonable and unenforceable damage formula. (Exh. A at pp. 7-8). In his Final Order dated November 30, 2007, the Arbitrator found, on the merits, that the Creditor suffered $8,960.50 in actual damages flowing from the Debtor's breach. (Exh. E at p. 2). Although the Creditor asked the Arbitrator to award attorneys fees of $46,970.75, as contemplated in the employment agreement, the Arbitrator cut that proposed award in half, finding the requested fees were "excessive in light of the degree of success obtained." (Exh. E at p. 3).[3] Specifically, the Arbitrator awarded the Creditor the following amounts:

Actual Damages	$8,960.50
Attorneys Fees	$23,485.00
Costs	$11,980.21
TOTAL ARBITRATION AWARD[4]	**$44,426.21**

[3] The ultimate damage award equaled only 14% of the damages the Creditor sought to recover. Under the circumstances, I share the Arbitrator's view of the attorney fee request.

[4] The sum of the elements of the arbitration award is actually $44,425.71, but the discrepancy between this sum and the amount actually awarded is immaterial.

Before either party moved to confirm or vacate the award as contemplated in MCR 3.602, the Debtor complied with the Bankruptcy Code's credit counseling requirement and filed a voluntary Chapter 7 petition on December 31, 2007.

IV. GOVERNING LAW

A bankruptcy court has authority to dismiss a Chapter 7 petition for cause including, but not limited to, unreasonable delay, non-payment of fees, and a debtor's failure to perform statutory duties. 11 U.S.C. § 707(a).

The Creditor contends that dismissal for cause exists pursuant to 11 U.S.C. § 707(a) and that a debtor's "bad faith" in filing the petition may support a finding of "cause" for dismissal. Industrial Insurance Services, Inc. v. Zick (In re Zick), 931 F.2d 1124 (6th Cir. 1991).

"Dismissal based on lack of good faith must be undertaken on an *ad hoc* basis" and "should be confined carefully and . . . generally utilized only in those egregious cases that entail concealed or misrepresented assets and/or sources of income, and excessive and continued expenditures, lavish lifestyle, and intention to avoid a large single debt based on conduct akin to fraud, misconduct, or gross negligence." Zick, 931 F.2d at 1129. However, the Sixth Circuit noted in "a *malicious* breach of a noncompetition agreement situation," it is "permissible" to attribute a bad faith motivation to pre-petition activities of the debtor. Id. at 1129 (emphasis added). In my opinion, given the *ad hoc* nature of the inquiry, though I am *permitted* to infer bad faith, I am not *required* to do so, particularly where the moving party has not established a

"malicious" breach of contract. Indeed, though the Arbitrator found the Debtor breached the agreement, he made no finding that she did so maliciously.

In Zick, the Sixth Circuit deferred to the trial court's judgment, adopting an abuse of discretion standard of review. The trial court in Zick found that the debtor reaffirmed and rearranged obligations in a scheme designed to exclude one specific creditor from payment. In addition, the schedules in Zick contained suspicious irregularities, and the record otherwise reflected transfers or assignments of obligations to entities other than the debtor, shortly before an adverse judgment. These factors convinced the trial and appellate courts that there was "cause" to dismiss the case. Id. at 1128. Mr. Zick's lavish lifestyle in an affluent Detroit suburb and his failure to cooperate in disclosing his finances, including post-petition income, also influenced the trial court's decision. Adopting the so-called "smell test," the Sixth Circuit refused to disturb the bankruptcy court's finding that Zick acted in bad faith in filing his petition. Id. at 1127-28.

The Debtor's case shares some similarities to Zick. In both cases the primary creditor asserted rights arising out of the breach of an employment agreement, and in both cases the debtors have a modest number of creditors. However, the similarities end there.

The Debtor's counsel asserted, without contradiction, that the Debtor offered to settle the arbitration dispute for an amount that turned out to be very close to the actual damages awarded. A redacted e-mail attached as an exhibit to the Creditor's brief bolsters this assertion. (Exh. K at p. 1). Consequently, I believe the Debtor attempted in good faith to pay the Creditor's actual claim, not simply compromise it. I further note that the bulk of the Creditor's damages directly resulting from the Debtor's breach of

contract is modest compared to the Creditor's costs of enforcing its rights. In short, I find that the Creditor's aggressive litigation strategy accounted for much of its injury, and I cannot blame the Debtor for that. Moreover, having reviewed the Debtor's Schedule J, which shows a monthly net "income" of negative $606.00 and expenses that do not seem unreasonable or lavish, I do not share the Creditor's view that the Debtor should tighten her belt.

As for the suggestion that scheduling the Creditor's claim as "disputed" and "pending" somehow shows the Debtor's bad faith, I accept Debtor's counsel's explanation that the procedural uncertainty surrounding the status of an unconfirmed arbitration award -- that is whether the award is final prior to confirmation by a court of competent jurisdiction -- prompted him to schedule the Creditor's claim as he did. Checking the "disputed" box on Schedule F is consistent with the desire to preserve whatever modest right of review of the Arbitrator's award the Debtor might have had against a possible claim of judicial estoppel. In other words, the Creditor might have argued that the Debtor's failure to schedule the debt as "disputed" constituted an admission precluding her from disputing the Arbitrator's award.[5] Certainly there was no attempt to conceal the Creditor's claim – it is listed on Schedule F. Aside from the Debtor's breach of the employment agreement and covenant not to compete, and the

[5] MCR 3.602(J)(1) requires that a complaint to vacate an arbitration award be filed no later than twenty-one days after the date of the award. Because more than thirty days had elapsed between the award on November 30, 2007, and the filing of the Debtor's Chapter 7 petition on December 31, 2007, the award, although not formally confirmed, cannot be vacated. Moreover, state law governing arbitration awards provides in relevant part that "[t]he findings of fact made by the arbitrator acting within his or her powers, in the absence of fraud, shall be conclusive." MCLA § 418.864(11); Krist v. Krist, 246 Mich. App. 59, 67 631 N.W.2d 53, 57 (2001)(a binding arbitrator's factual findings are not subject to appellate review). Only those awards that contain an error of law discernible on the face of the very award itself are reviewable. "It is only the kind of legal error that is evident without scrutiny of intermediate mental indicia which remains reviewable . . ." Detroit Automobile Inter-Insurance Exchange v. Gavin, 416 Mich. 407, 429, 331 N.W.2d 418, 428 (1982). Though I need not decide the issue today, it seems quite likely that the Arbitrator's award will be conclusive in this proceeding.

Debtor's filing the petition within a month after the Arbitrator rendered his award, the Creditor has offered no other persuasive evidence of bad faith.

Granting the Creditor's Motion on the record before me would be utterly inconsistent with my obligation to "confine" the dismissal sanction to those "egregious" cases involving concealment, fraud, unfair manipulation or other hallmarks of a dishonest and undeserving debtor. Zick, 931 F.2d at 1129. The Arbitrator's award in all likelihood remains binding against the Debtor's estate, and as a practical matter has punished her for pursuing a livelihood in violation of the employment agreement. Although I do not condone the Debtor's breach of contract, I certainly understand her reasons for seeking relief in this court. As such, I do not perceive a cynical manipulation of the system, but rather a legitimate attempt to deal with a difficult creditor. Consequently, I will not punish this Debtor further for promptly availing herself of the relief Congress made available under Chapter 7. Of course, nothing in this Opinion resolves any issue in the adversary proceeding that the Creditor commenced to except its claim from the Debtor's discharge.

V. DISPOSITION

I find the Creditor has failed to establish bad faith warranting dismissal. For the foregoing reasons, I will deny the Motion and direct the Clerk to enter a separate order consistent with my decision.

Dated: May 22, 2008
at Grand Rapids, Michigan

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Scott W. Dales
United States Bankruptcy Judge