This opinion is not intended for publication

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO

In re:	)	Case No. 03-12179
	)	
QUIKCAT.COM, INC.,	)	Chapter 7
	)	
Debtor.	)	Judge Arthur I. Harris

MEMORANDUM OF DECISION

Before the Court is the motion (Docket # 5) of QuikCAT.com, Inc. (QuikCAT) for dismissal of the involuntary bankruptcy petition that four former employees filed against it on February 25, 2003. For the reasons that follow: (1) QuikCAT's motion to dismiss pursuant to Bankruptcy Rule 1011 and Federal Rule of Civil Procedure 12(b) is denied; (2) the debtor shall file and serve its answer to the petition **on or before April 3, 2003**; (3) the debtor's motion to dismiss pursuant to 11 U.S.C. § 305 will be consolidated with a hearing on the merits of the petition and the debtor's answer under Bankruptcy Rule 1013; and (4) **a preliminary pretrial will be held at 11:00 a.m. on April 8, 2003,** at which time counsel shall be prepared to propose a timetable that will enable the Court to determine the issues of this contested petition at the earliest practicable time.

Under 11 U.S.C. § 303(b), an involuntary petition is commenced by the filing of a Chapter 7 or 11 bankruptcy petition

> (1) by three or more entities, each of which is either a holder of a claim against such person that is not contingent as to liability or the subject of a bona fide dispute, or an indenture trustee representing such a holder, if such claims aggregate at least $11,625 more than the value of any lien on property of the debtor securing such claims held by the holders of such claims; [or]
>
> (2) if there are fewer than 12 such holders, excluding any employee or insider of such person and any transferee of a transfer that is voidable under section 544, 545, 547, 548, 549, or 724(a) of this title, by one or more of such holders that hold in the aggregate at least $11,625 of such claims . . . .

Bankruptcy Rule 1011 directs that a debtor wishing to contest an involuntary petition must file and serve an answer or motion to dismiss within 20 days after service of the summons in the manner prescribed by Rule 12 of the Federal Rules of Civil Procedure. In the present case, the debtor filed a motion to dismiss.

In evaluating a motion to dismiss, the Court accepts as true all factual allegations contained in the plaintiff's complaint and liberally construes the complaint in favor of the party opposing the motion. *See, e.g.*, *Angel v. Kentucky*, 314 F.3d 262, 264 (6th Cir. 2002); *Herman v. Hospital Staffing Services, Inc.*, 236 B.R. 377, 380-81 (W.D. Tenn. 1999).

The debtor raises four grounds in support of its motion to dismiss: (1) the petitioning creditors are insiders and, as such, lack standing to commence an

involuntary bankruptcy proceeding against the debtor; (2) the petitioning creditors are using the Bankruptcy Code improperly by filing an involuntary bankruptcy petition against the debtor as a means to wrest control of the company from its current owners; (3) the petitioning creditors, by filing the involuntary petition, are violating the non-competition covenants to which they are bound; and (4) this Court should abstain from hearing this case pursuant to 11 U.S.C. § 305(a)(1) because the interests of creditors and the debtor would be better served by such dismissal. The court will address each of these grounds separately.

EMPLOYEES' STANDING AS PETITIONING CREDITORS UNDER § 303(B)

Debtor first contends that this petition must be dismissed because the petitioning creditors, as former employees of the debtor, purportedly lack standing under Bankruptcy Code § 303(b). In support of this argument the debtor cites *In re Runaway II*, 168 B.R. 193 (Bankr. W.D. Mo. 1994), where the court ruled on the applicability of subsection 303(b)(2) because the case involved fewer than three petitioning creditors. By contrast, this is a petition that has three or more petitioning creditors and, thus, is analyzed under the requirements of subsection 303(b)(1).

This Court believes that the correct reading of section 303(b)(1), based upon

a plain reading of the text, is that employees and insiders who are proper holders of non-contingent bona fide claims have standing to file an involuntary petition. *See In re Little Buildings, Inc.*, 49 B.R. 889, 890-91 (Bankr. N.D. Ohio 1985) (interpreting § 303(b) to mean that the claims of insiders are excluded "only from consideration in determining the number of an alleged debtor's creditors" and not "from the group of claimants eligible to file a petition"); 2 COLLIER ON BANKRUPTCY ¶ 303.03[2][c][vi] (15th ed. rev. 2003) ("Although insiders . . . cannot be included for purposes of the numerosity requirement, they can serve as petitioning creditors if they hold claims."). *See generally* Henry M. Karwowski, *Do Insiders Have Standing to File an Involuntary Petition in Small Cases?*, 21-JAN AM. BANKR. INST. J 1 (2003).

Because the current petition was filed by three or more creditors, it satisfies the numerosity requirements of subsection 303(b)(1). Whatever qualifying language may exist for the numerosity of petitioners under subsection 303(b)(2) simply does not apply. Furthermore, although some petitioning creditor-insiders might have an improper purpose for pursuing an involuntary bankruptcy proceeding, the Bankruptcy Code already has other means of policing such bad conduct without barring all creditor-insiders from ever petitioning under

section 303. *See, e.g.*, 11 U.S.C. §§ 303(e) (allowing the court to require the petitioners to post a bond for amounts that petitioners may later be required to pay under subsection 303(i)), 303(i) (granting the court authority to award to the debtor costs and attorneys' fees if the involuntary petition is dismissed, and damages or punitive damages if the petition was filed in bad faith), and 305 (permitting a court to dismiss or suspend a case when abstention is appropriate). Therefore, there are no policy reasons for preferring the strained interpretation of section 303 sought by the debtor in this case.

The practice of excluding employees and insiders for counting purposes apparently dates back to the Bankruptcy Act of 1898, when Congress adopted Section 59, the predecessor provision to Section 303 of the Bankruptcy Code. Back in 1898, members of Congress apparently feared that through connivance with friendly creditors an insolvent debtor "might be able unfairly to hamstring one or two large creditors." *In re Skye Marketing Corporation Corp.*, 11 B.R. 891, 897 (Bankr. E.D. N.Y. 1981), *quoting In re Gibralter Amusements Ltd.*, 291 F.2d 22, 25 (2d Cir. 1961). Thus, the historical context behind this statute also provides no support for interpreting the language of subsection 303(b)(2) as barring all employees and insiders from ever being petitioning creditors.

Because the debtor does not dispute that these four petitioners have non-contingent bona fide claims in the aggregate of at least $11,625, the debtor's motion to dismiss based upon this first ground is denied.

PETITIONERS' ALLEGEDLY IMPROPER PURPOSE

The debtor's second argument is that the petition should be dismissed because the petitioners allegedly have an improper purpose in bringing this involuntary petition. Even if true, however, this assertion is not a proper basis for a motion to dismiss the petition under Federal Rule of Civil Procedure 12(b)(6), as made applicable by Bankruptcy Rule 1011. In evaluating a motion to dismiss under 12(b)(6), the court must accept the petitioning creditors' allegations as true and cannot look to evidence beyond the pleadings. *See* FED. R. CIV. P. 12(b) ("If . . . matters outside the pleading are presented to and not excluded by the court, the motion shall be treated as one for summary judgment and disposed of as provided in Rule 56"). Therefore, while this argument may be relevant to whether an order of relief is ultimately appropriate under section 303, and perhaps also to whether abstention is appropriate under section 305, it is not a proper basis for a motion to dismiss the petition under Federal Rule of Civil Procedure 12(b)(6) or Bankruptcy Rule 1011.

ALLEGED VIOLATIONS OF COVENANTS NOT TO COMPETE

Debtor's third argument is that this action must be dismissed because the petitioning creditors, by pursuing their involuntary petition, are allegedly violating a covenant not to compete. This argument fails for the same reason as the debtor's second argument–namely, that, even if true, this assertion is not a proper basis for a motion to dismiss the petition under Federal Rule of Civil Procedure 12(b)(6) or Bankruptcy Rule 1011.

MOTION FOR ABSTENTION

Debtor's final argument is that this action should be dismissed under 11 U.S.C. § 305 as being in the best interest of the debtor and its creditors. Even if true, however, such argument would not be a proper basis for a motion to dismiss the petition under Federal Rule of Civil Procedure 12(b)(6) or Bankruptcy Rule 1011 and, by itself, should not excuse the requirement to file an answer contesting the petition under Bankruptcy Rule 1011 and Federal Rule of Civil Procedure 12(a)(4)(A). The Court will therefore consolidate debtor's motion for abstention under 11 U.S.C. § 305 with a hearing on the merits of the petition and debtor's answer under Bankruptcy Rule 1013.

CONCLUSION

For the foregoing reasons: (1) QuikCAT's motion to dismiss under Bankruptcy Rule 1011 and Federal Rule of Civil Procedure 12(b) is denied; (2) the debtor shall file and serve its answer to the petition **on or before April 3, 2003**; (3) QuikCAT's motion to dismiss under 11 U.S.C. § 305 will be consolidated with a hearing on the merits of the petition and debtor's answer under Bankruptcy Rule 1013; and (4) **a preliminary pretrial will be held at 11:00 a.m. on April 8, 2003,** at which time counsel shall be prepared to propose a timetable that will enable the Court to determine the issues of this contested petition at the earliest practicable time.

/s/ Arthur I. Harris 03/24/2003
Arthur I. Harris
United States Bankruptcy Judge