

**United States Bankruptcy Court  
Northern District of Illinois  
Eastern Division**

**Transmittal Sheet for Opinions for Posting**

**Will this opinion be published?** No

**Bankruptcy Caption:** Zarifian Enterprises, LLC

**Bankruptcy Number:** 24 B 06598

**Adversary Caption:** N/A

**Adversary Number:** N/A

**Date of Issuance:** December 17, 2024

**Judge:** David D. Cleary

**Appearance of Counsel:**

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**UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF ILLINOIS  
EASTERN DIVISION**

In re:	)	Bankruptcy No. 24 B 06598
	)	
Zarifian Enterprises, LLC,	)	Chapter 7
	)	
Debtor.	)	Judge David D. Cleary

**ORDER GRANTING MOTION TO CONVERT CHAPTER 7 CASE TO CHAPTER 11**

This matter comes before the court on the motion of Zarifian Enterprises, LLC, (“Zarifian” or “Debtor”) to convert its pending chapter 7 case to a case under Subchapter V of chapter 11 (“Motion to Convert”). An objection (“Objection”) was filed by the chapter 7 trustee (“Trustee”). Debtor filed a reply (“Reply”). For the reasons stated below, the court will grant the Motion to Convert.

**I. BACKGROUND**

On May 2, 2024, an Involuntary Petition Against a Non-Individual was filed by four petitioning creditors against Zarifian. (Dkt. No. 1). The Court entered an Order for Relief under Chapter 7 on June 5, 2024. (Dkt. No. 8). Greg Szilagyi was appointed as the Interim Chapter 7 Trustee the following day. (Dkt. No. 11). On July 10, 2024, Zarifian filed a Summary of Assets and Liabilities; Schedules A/B, D, E/F, G, H, with Declaration; and its Statement of Financial Affairs. (Dkt. Nos. 14-16). On the same day, Zarifian filed this Motion to Convert. (Dkt. No. 17). The Trustee filed a Notice of Objection the following day, and the Objection on August 7, 2024. (Dkt. Nos. 19, 32). On August 21, 2024, Debtor filed its Reply. (Dkt. No. 34).

Debtor’s Schedule A/B lists property totaling \$563,203.47. (Dkt. No. 15). Debtor lists the following assets in its Schedule A/B: (1) \$57,000 as accounts receivable; (2) \$40,000 in inventory; (3) \$16,300 in office furniture, fixtures, and equipment; and (4) \$449,903.47 in machinery, equipment, and vehicles. (*Id.*). Debtor also lists a claim of unknown value for damages resulting

from wrongful lockout from leased premises at 18505 West Creek Drive, Tinley Park, Illinois by lessor, MB Portfolio, LLC. (*Id.*). Debtor's Schedule D lists a claim against Debtor for \$29,000 secured by a purchase money security interest in a box truck worth \$25,000. (*Id.*) In Debtor's Schedule E/F, Debtor identifies seven creditors with priority unsecured claims and nine creditors holding nonpriority unsecured claims. (*Id.*).

Debtor no longer maintains its core or historical business operations as a carpentry and millwork business. (Dkt. No. 34, p.3). Similarly, Debtor no longer retains any employees, cannot operate as a carpentry and millwork business without carpenter employees, and cannot hire any such employees without the cash necessary to address the collective bargaining agreement of the carpenters' union. (Dkt. No. 32, p.6). Debtor states that it does not intend to resume its historical business operations as a carpentry and millwork, but to actively engage in liquidating its assets to pay its creditors. (Dkt. No. 34, p.3). Debtor intends to pursue this liquidation via a Subchapter V liquidating plan if its Motion to Convert is granted. (*Id.*). In addition to the assets listed in its Schedules, Debtor notes that it does maintain a bank account. (*Id.*).

## **II. DISCUSSION**

Debtor seeks to convert its case to Subchapter V of chapter 11 pursuant to 11 U.S.C. § 706(a), which provides that "[t]he debtor may convert a case under this chapter to a case under chapter 11, 12, or 13 of this title at any time, if the case has not been converted under section 1112, 1208, or 1307 of this title. Any waiver of the right to convert a case under this subsection is unenforceable."

Section 706(d), however, puts a limitation on this nearly absolute right to convert, providing that: “Notwithstanding any other provision of this section, a case may not be converted to a case under another chapter of this title unless the debtor may be a debtor under such chapter.”

**I. § 706(d) Eligibility Under *Marrama* and § 1112(b)**

Before 2007, courts did not agree on whether chapter 7 debtors had an absolute right to convert to a reorganization case. That year, the Supreme Court provided an answer. The right to convert is limited. Bankruptcy judges may immediately deny “a motion to convert filed under § 706 in lieu of a conversion order that merely postpones the allowance of equivalent relief and may provide a debtor with an opportunity to take action prejudicial to creditors.” *Marrama v. Citizens Bank of Massachusetts*, 549 U.S. 365, 375 (2007) (footnote omitted).<sup>1</sup> If a chapter 11 case would simply be reconverted to chapter 7 “for cause” under 11 U.S.C. § 1112(b), the motion to convert may be denied.

“Cause” to convert or dismiss a chapter 11 case includes a number of factual scenarios that Congress listed in 11 U.S.C. § 1112(b)(4). One of the items that constitutes “cause” is the “substantial or continuing loss to or diminution of the estate and the absence of a reasonable likelihood of rehabilitation.” 11 U.S.C. § 1112(b)(4)(A). Each of the two elements in § 1112(b)(4)(A) must be present for this ground to apply. *In re Original IFPC S'holders, Inc.*, 317 B.R. 738, 742 (Bankr. N.D. Ill. 2004). There must be (1) a substantial or continuing loss to or diminution of the estate; and (2) the absence of a reasonable likelihood of rehabilitation.

To satisfy the first prong, the loss must be substantial or continuing, but it need not be

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<sup>1</sup> The fact situation in *Marrama* involved conversion from chapter 7 to chapter 13. It applies with the same force to cases in which a debtor seeks to convert from chapter 7 to chapter 11. See *In re Irmen*, No. 07 B 03103, [2008 WL 320484](#), at \*3 (Bankr. N.D. Ill. Feb. 1, 2008).

both. *In re Ozcelebi*, 639 B.R. 365, 384 (Bankr. S.D. Tex. 2022). The loss is substantial where it is sufficiently large given the financial circumstances of the debtor as to materially negatively impact the bankruptcy estate and the interests of creditors. *Id.* Alternatively, the loss can be an ongoing issue, such as negative cash flow. *Id.* Continuing loss or diminution of the estate is established where the debtor has negative cash flow and no definite source of income. *Original IFPC S'holders, Inc.*, 317 B.R. at 742; *see also In re M.A.R. Designs & Constr., Inc.*, 653 B.R. 843, 856 (Bankr. S.D. Tex. 2023). Courts must make a full evaluation of the conditions of the estate when examining the movant's evidence for loss or diminution. *Ozcelebi*, 639 B.R. at 384.

Here, though the Trustee in his Objection contends that the continuing loss or diminution of the estate prong is met where the debtor has a negative cash flow and no definite source of income, the evidence he presents shows neither substantial or continual loss, nor diminution of the estate. Rather, the Trustee argues that Debtor will be unable to continue operating as a carpentry and millwork. Specifically, the Trustee emphasizes that the Debtor has no cash, no employees, no cash to hire new employees, no place of business to operate, and only one account receivable. While these facts are relevant to the second prong of § 1112(b)(4)(A), the absence of a reasonable likelihood of rehabilitation, they do not establish a negative cash flow or diminution of assets. The absence of positive cash flow does not make for a negative cash flow. In fact, the Debtor asserts the opposite—receivables, inventory, a lawsuit, and the sale of equipment will generate revenue for the estate. Revenue will be used to pay creditors. The Trustee has not met the burden of showing diminution of assets, or substantial or continual loss, and the first prong is not satisfied.

The second prong of § 1112(b)(4)(A), the absence of a likelihood of rehabilitation, is met

because “rehabilitation” for purposes of § 1112(b) simply does not include liquidation. *Andover Covered Bridge, LLC*, 553 B.R. 162, 175 (B.A.P. 1st Cir. 2016). Because the Debtor here intends to file a liquidating plan, a conversion to chapter 11 Subchapter V cannot lead to rehabilitation. Nevertheless, the first prong has not been met, and so Debtor will not be denied his Motion to Convert based on § 1112(b).

## **II. § 706(d) Eligibility Under § 1182(1)(A)**

The Trustee offers a second reason that Debtor is not eligible for Subchapter V relief: Debtor is not “engaged in commercial or business activities” as required by the definition of “debtor” provided in Section 1182(1)(A). Though the Trustee does not elaborate in his Objection, Debtor answers with authority in its Reply.

The definition of “debtor” in Section 1182(1)(A) “does not require a debtor to maintain its core or historical business operations on the petition date. It requires that the debtor was engaged in commercial or business activities.” *In re Port Arthur Steam Energy, L.P.*, 629 B.R. 233, 237 (S.D. Texas 2021). To determine whether a debtor “engaged in commercial or business activities,” courts must look to the ordinary meaning of the words. *See e.g., In re Port Arthur Steam Energy, L.P.*, 629 B.R. 233, 236 (Bankr. S.D. Texas 2021); *In re Offer Space, LLC*, 629 B.R. 299, 305-306 (Bankr. Utah 2021). In *In re Port Arthur Steam Energy, L.P.* and *In re Offer Space, LLC*, each court found that the debtor was engaged in commercial or business activities despite no longer actively operating a business. In each case, the debtor had filed a liquidating plan. The court in *Port Arthur* found that the debtor engaged in commercial and business activities by litigating a lawsuit, seeking to collect on outstanding accounts receivable, maintaining its facility and vehicles, and filing reports and tax returns. *Port Arthur Steam Energy, L.P.*, 629 B.R. at 236-237. The court in *Offer Space* similarly found that the debtor

engaged in commercial and business activities by “(1) having active bank accounts, (2) having accounts receivable; (3) analyzing and exploring counterclaims in a lawsuit... (4) managing the Stock, and (5) winding down its business and taking reasonable steps to pay its creditors and realize value for its assets.” *In re Offer Space, LLC*, 629 B.R. at 306.

Here, Debtor similarly no longer maintains its core or historical business operations, but remains engaged in commercial and business activities. Debtor maintains significant assets, a bank account, a 4-year commercial lease, and a claim against its landlord for wrongful lockout. Debtor would be engaged in liquidating its assets to pay its creditors had the Involuntary Petition not been filed, and it intends to file a Subchapter V plan of liquidation upon conversion. Consequently, Debtor meets the § 1182(1)(A) definition and is eligible for Subchapter V under § 706(d).

For all of the reasons stated above, **IT IS HEREBY ORDERED THAT** the Motion to Convert is **GRANTED**.

Date: December 17, 2024

A handwritten signature in cursive script, reading "David D. Cleary", written in black ink.

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DAVID D. CLEARY  
United States Bankruptcy Judge