Bankruptcy Circuit Update
Featuring cases from June 2018

We will be convening our next section-wide conference call on **Friday, July 27th, at 3:30 E.S.T./12:30 P.S.T.** to present and discuss notable cases from the past few months of the summaries. We are seeking volunteers to summarize significant or interesting cases. Please send an email to csullivan@diamondmccarthy.com if you are interested in presenting. The call-in information is: **dial in 866-690-2070 – code 787-594-2077**.
We hope you will join us for this call.

Second Circuit

***Wallach v. Smith* (*In re Nanodynamics, Inc.*),**
17-2410; 2018 WL 2973103 (2d Cir., June 13, 2018)

The Second Circuit affirmed the judgment of the district court affirming a bankruptcy court order dismissing the claim asserted by Mark Wallach ("Wallach"), the chapter 7 trustee of NanoDynamics, Inc. ("NanoDynamics"), for $700,000 plus interest pursuant to a prepetition stock subscription agreement.

Prior to the bankruptcy filing, David and Jennifer Smith (the "Smiths") executed a stock subscription agreement (the "Agreement") with NanoDynamics to purchase 2.5 million shares of stock at $1 per share. Under the Agreement, the Smiths would complete payment in stages by March 31, 2009, and NanoDynamics would issue a number of shares corresponding to the money paid within five business days of each receipt of funds. The Smiths failed to complete their payments by the March deadline, but did pay a total of $1.8 million in various amounts between March 9, 2009, and June 8, 2009. All but one of these payments occurred after the March deadline. Rather than terminating the Agreement or suing for breach, NanoDynamics continued to issue shares of stock within five business days of each of the three payments.

When NanoDynamics filed for bankruptcy in July 2009, a balance of $700,000 remained untendered on the Agreement, and NanoDynamics' petition listed the Agreement as an executory contract. Years later, Wallach alleged that the Smiths were in breach of the Agreement as of the contractual deadline, and were liable for the remaining balance plus interest under section 628(a) of the New York Business Corporation Law (the "BCL") and section 542 of the Bankruptcy Code. The Smiths denied liability and asserted a number of counterclaims and affirmative defenses. The bankruptcy court ultimately dismissed the claims because section 365(c)(2) of the Bankruptcy Code expressly prohibits a trustee from assuming and collecting upon a contract for the issuance of stock.

On appeal in the Second Circuit, Wallach sought the remaining balance of $700,000 plus interest as a matter of contract law, notwithstanding that performance on the contract by NanoDynamics was no longer possible. Wallach asserted that the common law rule that a trustee in bankruptcy may bring and maintain an action based on a stock subscription agreement even if

the corporation is bankrupt and cannot issue stock was codified in the BCL, which provides that a "subscriber for shares of a corporation shall be under no obligation to the corporation for payment for such shares other than the obligation to pay the unpaid portion of his subscription." BCL § 628.

The Second Circuit found such authority unavailing, noting that section 365(c)(2) of Bankruptcy Code provides in plain terms that a "trustee may not assume or assign any executory contract ... if such contract is a contract ... to issue a security of the debtor." 11 U.S.C. § 365(c)(2). The Second Circuit noted that section 365 would therefore specifically supersede any rule that would otherwise permit a trustee in bankruptcy to assume an executory contract for the sale of stock.

Wallach argued in the alternative that the proscription of section 365(c)(2) of the Bankruptcy Code did not apply to this case because the Agreement was non-executory, and the Bankruptcy Code only prevents the assumption of an executory contract. After noting that there are multiple tests for determining whether an agreement is an "executory contract" within the meaning of section 365(c) of the Bankruptcy Code, including the so-called "Countryman Test" (defining an executory contract as a contract under which the obligation of both the debtor and the counterparty are so far unperformed that the failure of either to complete performance would constitute a material breach excusing the performance of the other) and a less stringent Second Circuit test described as the "some performance due" test (defining an executory contract as one on which performance remains due to some extent on both sides).

Here, the Second Circuit held that the Agreement was an executory contract under either test, because (1) it was undisputed that neither side tendered complete performance on the Agreement; and (2) $700,000 remained unpaid and 700,000 shares remained unissued when NanoDynamics filed for bankruptcy. The Second Circuit was also unpersuaded by Wallach's argument that the Agreement was non-executory because NanoDynamics could have rescinded the contract immediately following the payment deadline, noting that regardless of whether or not rescission was possible, NanoDynamics did not so rescind, accepting payments and issuing stock as though the Agreement were in full force and effect. Accordingly, the Second Circuit affirmed the dismissal of Wallach's claims.

***A & G Goldman P'ship v. Picard* (*In re Bernard L. Madoff Inv. Sec. LLC*), 17-51220(a), 2018 U.S. App. LEXIS 17574 (2d Cir., June 27, 2018)**

In an appeal arising from the Securities Investor Protection Act ("SIPA") liquidation of Bernard L. Madoff Investment Securities LLC ("BLMIS"), the entity through which Bernard Madoff ("Madoff") perpetrated his Ponzi scheme, the Second Circuit affirmed the judgment of the district court enjoining an action brought in Florida because it violated an injunction and automatic stay issued in the SIPA liquidation.

On May 12, 2009, Irving H. Picard, the Trustee in the SIPA liquidation (the "Trustee") filed an adversary proceeding in the SIPA liquidation against the estate of Jeffry Picower ("Picower") and several entities associated with Picower (together, the "Picower Parties")

seeking to recover $6.7 billion in withdrawals Picower made from BLMIS and bringing claims for fraudulent transfer, avoidable preferences, and turnover under both the Bankruptcy Code and New York law. The Trustee alleged that Picower benefited from BLMIS's Ponzi scheme and either knew or should have known that BLMIS's trading activity was fraudulent and fictitious, due to the closeness between Picower and Madoff and Picower's knowledge of BLMIS's operations, among other reasons.

In January 2011, the Trustee and the Picower Parties reached a settlement, pursuant to which the Picower Parties agreed to transfer over $7.2 billion to the government for distribution to Madoff's victims, $5 billion of which would be returned directly to the BLMIS estate. The bankruptcy court also issued a permanent injunction (the "Injunction"), which barred future claims against the Picower Parties that were duplicative or derivative of the claims brought by the Trustee.

In August 2014, A & G Goldman Partnership and Pamela Goldman (together, "Goldman"), former BLMIS customers, filed a complaint in the United States District Court for the Southern District of Florida (the "Florida action"), bringing a securities fraud claim under § 20(a) of the Securities Exchange Act of 1934 against the Picower Parties. The Picower Parties and the Trustee sought to enjoin the Florida action, contending that it violated the Injunction. The bankruptcy court in the Southern District of New York agreed and enjoined the Florida action, which the district court affirmed. This was Goldman's third attempt to hold the Picower Parties liable under § 20(a), and it was the third time that the bankruptcy court enjoined Goldman from proceeding under the Injunction.

The complaint in the Florida action made many of the same allegations as the prior two complaints that had been dismissed (which focused primarily on Picower's use of his own accounts at BLMIS), but further alleged two categories of conduct by Picower unrelated to his own BLMIS accounts. First, Goldman claimed that Picower what two purported loans to BLMIS totaling more than $200 million to help the Madoff Ponzi scheme avoid discovery and collapse, which the Second Circuit referred to as the "propping-up allegations." Both loan transactions were completed without formal loan documents and were not disclosed to the Financial Institution Regulatory Authority ("FINRA"). Second, in what the Second Circuit referred to as "counterparty allegations," Goldman claimed that Picower allowed BLMIS to list him in its fabricated books and records as a counterparty for a large volume of fictitious options trading, alleging that this lent credibility to Madoff's and BLMIS's fraudulent representations that they were engaged in a high volume of options trading. Finally, Goldman alleged that Picower knew that the foregoing activity would result in BLMIS's preparation and filing of false financial reports with FINRA, and that such reports would reach BLMIS customers.

The central question in this appeal was whether the complaint in the Florida action violated the Injunction because, despite labeling their claim as a § 20(a) claim for control person liability, Goldman instead brought a disguised fraudulent transfer claim that was derivative of the Trustee's fraudulent transfer claims. The Second Circuit began its analysis by outlining the differences between the two types of claims, noting that while a fraudulent transfer is a paradigmatic example of a claim that is "general" to all creditors in a bankruptcy (and is often

brought by a trustee for the benefit of all creditors), a claim under § 20(a) is a securities fraud claim that is particularized to the injured party or parties.

The elements of a § 20(a) claim are (1) a primary violation of the securities laws by the controlled person, (2) control of the primary violator by the defendant, and (3) that the defendant was, in some meaningful sense, a culpable participant in the controlled person's fraud. Goldman claimed that the Picower Parties were liable under § 20(a) because BLMIS was the primary violator of the securities laws, Picower was a control person of BLMIS, and Picower was a direct participant in BLMIS's fraud.

The Second Circuit was not persuaded by this argument, finding that the substance of the allegations was essentially a derivative, fraudulent transfer claim, in part because Goldman failed to show that Picower had the power to direct the management or policies of BLMIS. Preliminarily, excepting the propping-up and counterparty allegations, the Second Circuit noted that the majority of Goldman's complaint centered on the withdrawals that Picower made to himself from his accounts at BLMIS, which the Second Circuit noted caused a direct injury to the estate highly emblematic of a fraudulent transfer. The Second Circuit also noted that such allegations demonstrated no control over the "management and policies" of BLMIS.

The Second Circuit was also not persuaded that the propping-up or counterparty allegations demonstrated that Picower controlled BLMIS within the meaning of § 20(a). First, Goldman asserted that Picower's contributions to the Ponzi scheme allowed the scheme to continue, and that, had he chosen not to assist BLMIS, the scheme would have collapsed earlier than it did. However, the Second Circuit noted that Goldman was only making conclusory allegations that Picower ever leveraged his allegedly important role in the scheme to direct the "management and policies" of BLMIS, holding that it was not reasonable to infer that Picower had that kind of influence merely because he could have caused BLMIS to collapse earlier than it did.

Next, Goldman contended that the propping-up and counterparty allegations demonstrated Picower's ability to direct the creation and dissemination of false and misleading trading and financial documentation because he knew his participation would result in false information being incorporated into BLMIS's financial disclosures. Again, the Second Circuit noted that such allegations demonstrated only Picower's understanding that his participation would result in the dissemination of false information, not that he actually directed that the dissemination of false information occur or otherwise had control of the primary violator of the securities laws.

Ultimately, the Second Circuit held that the "control" allegations in the complaint amounted to nothing more than an attempt to "plead around" the injunction to assert a claim for fraudulent withdrawal of assets from the estate. Because such claim was a derivative claim that was barred by the Injunction, the Second Circuit affirmed the judgment of the district court.

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Fifth Circuit

Matter of: Goodrich Petroleum Corporation
--F.3d--, 2018 WL 3149141 (5th Cir. June 27, 2018), *as revised*, June 29, 2018

In this case, the Fifth Circuit examined the interplay between the "strong arm" provision of the bankruptcy code, 11 U.S.C. § 544(a), and the Louisiana Public Records Doctrine, in the context of a mineral lease on which the debtor still owed money pursuant to separate, unrecorded agreements, that were not reflected in the terms of the lease itself.

In 2014, Fallon Family, L.P. ("Fallon Family"), entered into a settlement agreement with Goodrich Petroleum Corporation and Goodrich Petroleum Company, L.L.C. (collectively, "Goodrich"), pursuant to which Fallon Family agreed to ratify a previously disputed mineral lease in favor of Goodrich (the "Lease Ratification"), "and to release its claims against Goodrich in consideration for Goodrich's paying $650,000 within ten business days of the Settlement Agreement and executing a promissory note (the "Promissory Note") in the amount of $1,000,000." *Id*. at *1. The Lease Ratification itself did not mention either the Settlement Agreement or the Promissory Note, but simply reads that "for the promises and covenants exchanged by the Parties on or near this date, the receipt and sufficiency of which is hereby acknowledged, the Parties agree [to the listed promises and covenants]." *Id*. at *2. Pursuant to the separate Promissory Note, Goodrich was to pay $1,000,000 in biannual installments of $100,000, with the first installment due on October 15, 2015. Goodrich paid the required $650,000 under the Settlement Agreement as well as the first $100,000 installment, but, failed to pay the next $100,000 installment which was due under the Promissory Note on April 15, 2016. In March 2016, Goodrich filed a Chapter 11 bankruptcy proceeding. In those proceedings and appeals, Fallon Family argued that because Goodrich failed to make payments under the Promissory Note, the Fallon Family had the right to dissolve the Settlement Agreement on grounds of non-payment and divest Goodrich of its interest in the lease. The Fifth Circuit disagreed, holding that based on 11 U.S.C. § 544(a) and the Louisiana Public Records Doctrine, the lease as ratified could not be dissolved for nonpayment because the public record reflected that consideration had been fully paid, and a third party was not placed on notice of the remaining payments.

The Fifth Circuit began its analysis by concluding that Goodrich, as debtor-in-possession, "occupies the shoes of a trustee in every way" under the Bankruptcy Code, and thus its abilities as debtor in possession are defined by 11 U.S.C. § 544(a). This section of the Bankruptcy Code "creates a legal fiction affording a debtor-in-possession the abilities it would have as a bona fide purchaser of the debtor's interests in immovable property at the time the bankruptcy is filed." *Id*. at *3. The abilities of a bona fide purchaser regarding the debtor's immovable property are defined by state law. In Louisiana, the Louisiana Public Records Doctrine requires certain types of instruments affecting immovable property, including leases, to be filed in the public records in

order to be effective against third persons. Thus, because the terms of the Settlement Agreement and Promissory Note were not filed in public records, nor referenced in the ratified lease that was filed in the public records, those terms would not be effective against *third persons* under Louisiana law. The Fifth Circuit relied on its prior holding in *In re Zedda*, 103 F.3d at 1202, to conclude that 11 U.S.C. § 544(a)(3) bona fide purchasers are third persons under the Louisiana Public Records Doctrine, and so Goodrich, as a debtor-in-possession, is considered a third person acting as a bona fide purchaser for the purposes of the Louisiana Public Records Doctrines.

After determining that Goodrich qualifies as a third party, the Court turned to the question of whether a party may dissolve an agreement when it will disrupt an interest in immovable property protected by the Louisiana Public Records Doctrine. The Court held that the agreement could not be dissolved. Under longstanding Louisiana legal principles, "[n]either fraud, nor want of consideration, nor secret equities between the parties, who have placed on the public records a title valid upon its face, can be urged against the bona fide purchaser for value, who has acted on the faith of such recorded title." *Id*. at *6. Based on its previous holdings in *LeBlanc v. Bernard* and *In re Leeward Operators, LLC*, the Court held that even though Goodrich, as debtor, had not paid the Promissory Note, Goodrich, as debtor-in-possession and hypothetical bona fide purchaser of the Lease Ratification under 11 U.S.C. § 544(a)(3), may avoid dissolution because the public record indicates that consideration has been fully paid. Specifically, the Court held that the language of the Lease Ratification was inconsistent with Fallon Family's claim that consideration is insufficient. The Court held that based on the Lease Ratification language that consideration was "exchanged, […] the receipt and sufficiency of which is hereby acknowledged," a third person would understand that exchange to be complete once the Lease Ratification was effective, and would have no notice of additional payments due under the Settlement Agreement or Promissory Note.

The Fallon Family's claim for nonpayment was thus prohibited by Louisiana Civil Code article 3342, which prohibits a party to a recorded instrument from later contradicting the instrument to the prejudice of a third person. Because the recorded instrument indicates full payment, the Court held that Goodrich was shielded from dissolution and could not be divested of the lease. The Court ended its opinion by acknowledging that in bankruptcy, creditors often do not receive the full amount of their claims, but that "this is a feature, not a flaw, of the design of the bankruptcy system," and is expected and fair within the confines of bankruptcy proceedings.

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Valentine v. JP Morgan Chase Bank Nat'l Ass'n (In re Valentine),
2018 WL 3005839 (5th Cir. Jun. 14, 2018).

The issue presented to the Fifth Circuit was whether the district court's dismissal of a bankruptcy appeal, for want of prosecution, was an abuse of discretion. The Fifth Circuit affirmed the district court's decision, holding the court acted within its discretion.

Beginning in 2011, Dawna Valentine filed a number of lawsuits and initiated numerous bankruptcy proceedings to avoid foreclose and eviction from a property in Texas City, Texas. The issue on appeal derived from the relationship between the latest bankruptcy proceeding and an appeal of a judgement for possession. On January 13, 2017, a motion filed by JP Morgan Chase was granted to lift a bankruptcy stay, which Valentine appealed. On March 23rd, the district court entered a notice of deficiency notifying Valentine that certain required fees had not been paid or arranged to be paid and the failure to fix the deficiencies, within fourteen days, could result in dismissal.

On April 3rd, Valentine submitted a letter to the district court requesting the court consolidate the two cases. The letter also stated she could not afford to pay the fee, should be granted in forma pauperis status, and that all the necessary paperwork had already been submitted. Valentine's in forma pauperis status request was denied pending the completion of the Application to Proceed in District Court Without Prepaying Fees or Costs form. Valentine never submitted the required form but continued to file affidavits, judicial notice requests, and additional motions previously treated as deficient by the district court. On June 21st, the district court denied the consolidation request and warned Valentine both cases would be dismissed for want of prosecution if the deficiencies were not cured by July 7th. Instead of curing the deficiencies, Valentine filed a response restating her position and filed her first notice of appeal to the Fifth Circuit. On July 11th, the case was dismissed and all pending motions were denied as moot.

The Supreme Court has recognized a district court's "inherent power" to sua sponte dismiss cases to manage its caseload to ensure quick and efficient processing of its cases. The Fifth Circuit held that the district court acted well within its discretion.[1] Starting with the March 23rd notice, the district court provided Valentine with two options, pay the required filing fees or submit the form required to continue in forma pauperis. Instead of complying with one of the two options, Valentine chose to file additional motions and judicial notice request that did not cure the deficiencies. The court also gave Valentine numerous warnings of dismissal if the deficiencies continued to go uncured. The record of the court's continuous warnings and notifications shows that a lesser sanction did not and would not prompt diligent prosecution. Thus, the Fifth Circuit affirmed the dismissal and found no abuse of discretion.

[1] In the Fifth Circuit, dismissals will be affirmed only if there is a clear record of delay or willful conduct by the plaintiff and the district court has determined that a lesser sanction would not result in diligent prosecution or lesser sanctions were given that proved to be "futile". *In re Wood*, 199 F. App'x 328, 332 (5th Circ. 2006). Typically, when a dismissal is affirmed there has been intentional conduct causing delay, the plaintiff personally caused a delay, or a defendant has been harmed by a delay. *Id.*

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***Matter of Technicool*, No. 17-10481,**
2018 WL 3056940 (5th Cir. June 20, 2018).

In this case, the Fifth Circuit considered the confines of the "person aggrieved" standing test for bankruptcy appeals. Appellant Robert Furlough ("Furlough") owned the debtor entity, Technicool Systems. Prior to filing for bankruptcy, Technicool was sued in Texas state court by National Oilwell Varco ("NOV") for claims arising from the sale of allegedly faulty air conditioner systems. Shortly thereafter, Technicool filed for bankruptcy, and NOV lodged a $3 million proof of claim in the bankruptcy case. NOV was represented in both the state court proceeding and Technicool's bankruptcy by Stacey & Baker, P.C. ("SBPC").

In Technicool's bankruptcy case, the trustee sought to consolidate several of Furlough's related businesses and pierce their corporate veil. To that end, he filed an application to employ SBPC as special counsel under 11 U.S.C. § 327(a). Furlough objected that (1) SBPC was not a "disinterested person" as required by the statute and (2) SBPC's representation of NOV was a disqualifying interest adverse to the estate. After an evidentiary hearing, the bankruptcy court held Furlough lacked standing to object.

Furlough asserted two standing arguments on appeal. First, he claimed that, but for NOV's proof of claim, he would stand to receive an estate surplus and, because of SBPC's role as counsel to NOV, it might fail to disclose any problems with the claim, robbing him of the surplus. Second, Furlough argued he had standing as a creditor of Technicool, based on a proof of claim he purchased during the appeals process.

The Fifth Circuit rejected both of these arguments, highlighting the narrow inquiry for the "person aggrieved" standing test in bankruptcy, which requires an appellant be directly and adversely affected in a pecuniary manner by the bankruptcy court's order. In short, only those with a direct financial stake in a given order can appeal it. With respect to Furlough's first argument, the Court held his allegation of harm was too speculative to confer standing because SBPC's appointment did not directly affect whether the bankruptcy court approved or denied NOV's claim. Thus, there was no direct financial impact to Furlough. The Fifth Circuit likewise rejected Furlough's second argument, explaining that—because standing is determined as of the commencement of the case when Furlough was *not* a creditor—he could not attain standing after the fact by purchasing a claim while his appeal was pending.

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Ninth Circuit

Rigby v. Mastro (In re Mastro),
585 B.R. 587 (B.A.P. June 5, 2018).

In *Rigby v. Mastro (In re Mastro)*, the debtor, Michael Mastro, and his wife fled to France with estate assets after being faced with an involuntary bankruptcy in 2009. Believing that estate assets outside his control existed, the trustee moved for an order under Federal Bankruptcy Rule 2004 and sections 521(a)(3) and (4) of the Code allowing the issuance for execution by the debtor of a consent directive. In particular, the trustee advanced several theories in support of his request. Initially, the trustee invoked Rule 2004 in connection with the debtor's duties under section 521(a)(3) and (4). Then, the trustee contended that Civil Rule 45, as applied by Rule 2004(c), authorizes consent directives. Finally, the trustee argued that Civil Rule 26, as applied by Rule 2004 by Rule 9014, authorizes consent directives. The bankruptcy court denied the motion on the grounds that the consent directive was a form of injunctive relief and entered a separate order denying the motion. The trustee moved for reconsideration and invoked an additional theory under section 105 of the Code. Treating the motion as a Rule 9023 motion, the bankruptcy court denied the motion. The trustee timely appealed but abandoned his Civil Rule 45 argument.

The issue before the Bankruptcy Appellate Panel for the Ninth Circuit was whether the bankruptcy court abused its discretion by denying the trustee's request for an order compelling a consent directive and the trustee's motion for reconsideration.

The panel held that the bankruptcy court had discretion to do so and reversed and remanded for the following reasons. First, a controlling Supreme Court decision, *Doe v. United States*, a consent directive is not testimonial in nature, and thus did not violate a signer's Fifth Amendment privilege. A signatory does not admit the existence of any account at any particular financial institution. In particular, a signatory identifies neither the contemplated recipients nor accounts in the consent directive; rather, the document generally directs any bank or other financial institution that received the consent directive to disclose any accounts held by the signatory. Second, sections 704 (a)(1) and (4) of the Code impose investigatory duties on the trustees and disclosure obligations on debtors under sections (a)(3) and (4). Third, sections 105

and Rule 2004 provide broad authority to a bankruptcy court and allow it to enter orders to carry out Code-imposed obligations. This section and rule, however, cannot operate in isolation but instead, operate in concert with the Code's investigatory and disclosure requirements. Lastly, case law allowing the use of consent directives in other contexts supports a determination that they are appropriate in a bankruptcy context. Specifically, regulatory agencies' use of consent directives bolsters the basis for the issuance of a consent directive through statutory rights and duties created by the Code.

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Wilkins v. Menchaca (In re Wilkins),
— B.R. —, 2018 WL 3197481 (9th Cir. BAP June 28, 2018)

In *In re Wilkins*, the 9th Cir BAP dismissed Debtor's appeal for lack of jurisdiction and held that the 14-day time limit of Rule 8002(a) is a mandatory jurisdictional requirement.

Debtor filed a single notice of appeal related to three orders in her Chapter 7 case. The notice of appeal was untimely as to all three orders. After a motion to dismiss, the BAP sua sponte requested briefing on whether the 14-day deadline for filing a bankruptcy appeal was jurisdictional or a mandatory claim-processing rule subject to waiver or forfeiture in light of *Hamer v. Neighborhood Hous. Servs. Of Chicago,* 138 S.Ct. 13 (2017).

The BAP reasoned that under *Hamer* a rule is jurisdictional "[i]f the Legislature clearly states that a threshold limitation on a statute's scope shall count as jurisdictional" and although Congress' intent must be clear, it need not be explicit.

The BAP held that 28 U.S.C. §158(c)(2) implements a congressionally mandated time constraint by referring to "the time provided by Rule 8002(a)" and plainly states that bankruptcy appeals "shall be taken in the same manner as appeals in civil proceedings" to the courts of appeals. Finally, the BAP held that public policy considerations favor a strict construction of the 14-day deadline to give finality to the bankruptcy process.

Ultimately the BAP held that *Hamer* does not require a departure from binding 9th Circuit precedent that the 14-day time limit of Rule 8002(a) is jurisdictional.

***Schnitzel, Inc. v. Sorensen (In re Sorensen)*,**
— B.R. —, 2018 Bankr. LEXIS 1849 (9th Cir. BAP, June 15, 2018)

In *In re Sorensen*, the 9th Circuit BAP affirmed the Bankruptcy Court's order prohibiting pawnbroker R&J from disposing of Chapter 13 Debtor's pawned jewelry.

In March 2016, Debtor pledged five pieces of jewelry to R&J as collateral for five pawn loans which had a termination date of November 2016. In August 2016 Debtor filed a Chapter 13 bankruptcy listing R&J as a secured creditor and proposing to pay the claim through the plan. Consistent with California law, R&J provided a notice of termination in November 2016 providing a 10 day right of redemption. Debtor did not redeem the jewelry and instead filed an adversary complaint seeking injunctive relief and a TRO to prevent R&J from disposing of the jewelry which Debtor contended was part of the estate.

R&J opposed the TRO request on the basis that the jewelry was excluded from the estate under §541(b)(8) because Debtor failed to redeem the property within the 10 day redemption period. R&J did not object to the plan which was confirmed prior to the hearing on the TRO request.

The BAP affirmed the Bankruptcy Court's holding that the notice of termination was violative of the automatic stay and was therefore void ab initio. As a result, §541(b)(8)(C) was not satisfied because under California law the Debtor has a right to redeem until 10 days after valid notice of termination. Because the notice was void, Debtor's right to redeem did not expire, R&J never took title to the jewelry, and §541(b)(8) did not remove the jewelry from the estate.

The BAP noted that varying state laws governing pawn transactions could lead to different results and distinguished cases applying state laws that automatically terminate a right of redemption. Because the BAP affirmed the Bankruptcy Court's ruling that the jewelry was not removed from the estate under §548(b)(8), it did not reach the issue of whether R&J was bound by the terms of the confirmed plan.

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Tenth Circuit

MAY

In Derma Penn, LLC v. 4EverYoung, Ltd.,
No. 17-4105, 2018 WL 2684268 (10th Cir. June 5, 2018)

The Tenth Circuit affirmed the denial of a motion to vacate civil contempt orders against Michael Anderer, a creditor (and former shareholder) of Derma Penn. Factually, Derma Penn sued 4EveryYoung for trademark infringement, and 4EveryYoung counter-claimed to enforce its right to purchase the Derma Pen trademark upon termination of the parties' agreement. That trademark, and the rest of Derma Pen's assets, secured a loan Anderer made to Derma Pen which subsequently filed for bankruptcy. Anderer made a DIP loan to Derma Penn in its chapter 11 case and, as part of that loan, Derma Penn stipulated to the validity and (first) priority of Anderer's liens. After dismissal of Derma Penn's chapter 11 case, Anderer obtained a state court judgment against Derma Penn which assigned its trademark to Anderer and registered it with the U.S. Patent Office. On 4EveryYoung's motion, the district court enjoined Derma Penn and then Anderer (who was subsequently joined as a defendant to the lawsuit) from transferring the trademark except in connection with a foreclosure action based on the DIP financing provided by Anderer. Despite the injunction, Anderer proceeded with a foreclosure sale, purchased the trademark himself and assigned it to a third party limited liability company in which he held a minority interest. This led to entry of orders holding Anderer in civil contempt; however, after the underlying injunction orders had been vacated due to sanctions imposed on 4EveryYoung for failing to secure replacement counsel by a deadline set by the court, Anderer moved to vacate the resultant contempt orders and release the injunction bond he had posted. The district court denied both motions. While it agreed that generally speaking civil contempt sanctions cannot stand if the order that was disobeyed was reversed by the issuing court or by an appellate court, the Tenth Circuit affirmed because termination of the violated order was unrelated to the merits. In other words, because there had been no determination by the district court that the injunction orders as to Anderer were erroneously entered, the fact they were vacated on non-merits grounds did not serve as a basis to vacate the contempt orders.

JUNE

***In re Dee's Foodservice ABQ, Inc.*, No. 16-11560-j11,**
2018 WL 3025284 (Bankr. D. N.M. June 15, 2018),

The court held that it lacked jurisdiction over claims concerning unclaimed funds (i.e., funds the debtors unsuccessfully attempted to distribute to creditors) arising post-dismissal in the absence of a confirmed plan such that it would overrule the UST's objection contemplating that the debtors be required to deposit unclaimed funds into the court's registry. The court explained that, after dismissal of a bankruptcy case a court retains jurisdiction over "core" proceedings but while it can retain post-dismissal jurisdiction over "related" matters ordinarily those matters are dismissed with the underlying bankruptcy case. The court confirmed that a bankruptcy court lacks jurisdiction over "related" non-core proceedings commenced after dismissal of the underlying bankruptcy case. Continuing, the court explained that, in a structured dismissal of a

chapter 11 case where no plan is confirmed, claims to funds only arise post-dismissal and are not governed by the Code and, therefore, such claims are non-core matters. The court explained that neither Code Sections 347(b) nor 1143 apply where there is no confirmed chapter 11 plan.

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Eleventh Circuit

Weakley v. Eagle Logistics,
— F.3d —, No. 17-14022, 2018 WL 3188663, at *1 (11th Cir. June 29, 2018)

The Eleventh Circuit reviewed the district court's grant of summary judgment against Weakley in favor of several defendants in litigation cases Weakley failed to disclose in his bankruptcy case. The district court reasoned that Weakley not only failed to disclose the litigation claims on his initial schedules, but also on the six subsequent amendments. Indeed, he only disclosed the claims *after* the defendants sought to apply judicial estoppel to bar the claims. The court determined that Weakley's disclosure of lesser-value claims, in conjunction with his failure to disclose the potentially high-value claims, evidenced a motive to conceal.

In 2017, the Eleventh Circuit *en banc* retreated from part of its prior judicial estoppel precedent, holding that courts cannot automatically infer a plaintiff's intent to mislead based solely on the plaintiff's failure to disclose a civil claim in a bankruptcy proceeding. *See Slater v. United States Steel Corp*., 871 F.3d 1174 (11th Cir. 2017). In *Weakley*, the appellate court applied the standards it announced in *Slater* to affirm the district court's grant of summary judgment because the district court "made its determination based on the facts and circumstances relating to the bankruptcy filings and nondisclosure." *Weakley*, at *2. The court also noted that Weakley's dismissal of his bankruptcy proceeding "after his duplicity was found out" did not negate the district court's application of judicial estoppel.

Slater v. U.S. Steel Corporation,
891 F.3d 1329 (11th Cir. 2018)

This ruling follows the Eleventh Circuit's *en banc* decision in *Slater v. United States Steel Corp*., 871 F.3d 1174 (11th Cir. 2017), which remanded the case to the panel to further consider the district court's judicial estoppel ruling in light of the *en banc* decision.

The panel found that the district court, bound by the prior precedent, did not consider the factors enunciated by the *en banc* court in applying judicial estoppel. This decision does not add

much precedential value beyond the *en banc* decision, but it does contain a concise recitation of the factors district courts should consider in deciding these kinds of judicial estoppel issues.

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