

Bankruptcy Circuit Update
Featuring cases from September 2015

First Circuit

Sheedy v. Deutsche Bank Nat'l Trust Co., as Trustee, and J.P. Morgan Chase Bank, N.A. (In re Sheedy)
, ___ F.3d ___, 2015 WL 5104517 (1st Cir., Sept. 1, 2015).

Chapter 13 debtor attempted to avoid foreclosure of her home by asserting lender liability claims against the current note holder and its mortgage loan servicer in an adversary proceeding, trying to rescind her mortgage under TILA and asserting various state law claims. The Bankruptcy Court denied this relief, granting summary judgment in favor of the defendants, which ruling was affirmed by the District Court. Upon appeal, the Court of Appeals for the First Circuit ("First Circuit") affirmed, agreeing such claims were either time barred or without merit.

More specifically, the First Circuit held that: (1) the three-year statute of limitations on the debtor's right to rescind under TILA began to run on consummation of the refinancing transaction; (2) a time-barred TILA rescission claim could not be raised defensively by way of recoupment; (3) Massachusetts unfair and deceptive trade practices claim was also time-barred; (4) even assuming that the lender had knowingly made a false representation related to the terms of the note, the debtor could not show that she relied on this false representation to her detriment; and, (5) the debtor lacked standing to challenge the assignee/note holder's status as the grounds asserted, even if successful, would only render the assignment "voidable" and not "void".

Gray v. Tacason (In re Tacason d/b/a Cutting Edge Sports),
___ B.R. ___, 2015 WL 5674960 (1st Cir. B.A.P., Sept. 25, 2015).

Bankruptcy Court granted summary judgment in favor of creditor whose debt was then not discharged pursuant to 11 U.S.C. Section 523(a)(6), based on the issue-preclusive effect of a pre-petition state court contempt judgment entered against the debtor. This ruling was affirmed upon appeal to the Bankruptcy Appellate Panel.

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Second Circuit

Adar 980 Realty v. Sofer (In re Avraham Sofer, 1040 Management, LLC),
--- Fed.Appx ----, 2015 WL 5102527 September 1, 2015).

The Second Circuit affirmed the district court's holding that the bankruptcy court did not err in (1) denying the motion of Adar 980 Realty ("Adar") to correct the record on appeal for appeals taken from a previous decision and order, (2) dismissing Adar's adversary proceeding seeking contempt and other associated relief on the ground that Adar lacked prudential standing, and (3) declining to consider Adar's motion to covert a dismissal with prejudice filed in an adversary proceeding below into a dismissal without prejudice.

Deferring in large part to the opinions of the bankruptcy and district courts below, the Second Circuit reiterated that prudential standing remains a jurisdictional requirement. In the Second Circuit, the prudential standing rule serves to bar litigants from asserting the rights or legal interests of others in order to obtain relief from injury to themselves. Instead, a plaintiff must assert his or her own legal rights and cannot base a claim to relief on the rights or interests of third parties. Here, the Second Circuit found that the bankruptcy court had properly determined that Adar failed to demonstrate a particularized injury sufficient to demonstrate prudential standing. The Court also found the remainder of Adar's arguments to be without merit.

Hamilton v. Mark IV Industries,
--- Fed.Appx ----, 2015 WL 5315363 (September 14, 2015).

The Second Circuit affirmed the district court's judgment granting summary judgment in favor of the defendants and enjoining plaintiff Gertrude Coretta Fennell Hamilton ("Hamilton") from filing new actions in the Southern District of New York concerning her previous employment with Dayco Incorporated or concerning Dayco Incorporated's New York bankruptcy action.

The Second Circuit first restated the summary judgment standard, holding that the district court had properly granted summary judgment to the defendants in the lower court decision. The Second Circuit then considered the district court's filing injunction in order to determine whether the lower court had abused its discretion. Before imposing a filing injunction, a district court must provide a litigant with notice and an opportunity to be heard. Because Hamilton had raised the same claims in multiple other actions and venues, and because the district court had given Hamilton notice and an opportunity to be heard before imposing the filing injunction, the Second Circuit held that the district court had not abused its discretion. The Second Circuit also found that the district court had considered Hamilton's arguments and properly determined that nothing "short of a filing injunction [would] protect the courts and other parties given that several judges have detailed why [Hamilton's] claims are barred, meritless, or otherwise unavailing."

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Third Circuit

In re ICL Holding Co., Inc.,

--- F.3d ----, 2015 WL 5315604 (September 14, 2015).

The Third Circuit affirmed the decision of the United States District Court for the District of Delaware, approving the sale of the Debtors' assets and attendant distributions as non-violative of the Bankruptcy Code's priority scheme. The Debtors' secured lender purchased the Debtors' assets through a credit bid of approximately 90% of the debt they were owed. No cash changed hands, but the purchaser agreed to escrow funds for the payment of professional fees and also for unsecured creditors. The U.S. Government, which held an administrative tax claim, objected to the sale on the grounds that similarly situated creditors (the professionals holding administrative claims) were being paid, while the U.S. Government's claim was going unpaid. In turn, it argued that the proposed payment to unsecured creditors violates the Bankruptcy Code's priority scheme since the U.S. Government, a senior creditor, was set to receive nothing. The Third Circuit affirmed the rulings of the Bankruptcy and District Courts and found that the escrowed payments never came through the estate and thus are not subject to the Bankruptcy Code's priority scheme.

In re New Century TRS Holdings, Inc.,

--- Fed.Appx ----, 2015 WL 5719136 (3d Cir. Sept. 23, 2015).

The Third Circuit affirmed the decision of the United States District Court for the District of Delaware, dismissing a pro se appeal for failure to prosecute. The pro se appellant filed an appeal of the Delaware Bankruptcy Court's order dismissing an adversary proceeding she had commenced. The District Court, upon the appellant's motions, granted the appellant extensions of various appellate deadlines based on the appellant's allegations of an unspecified disability. The District Court noted in its final extension order that any further failure of the appellant to timely file its required brief would lead to dismissal. Instead of submitting her brief, the appellant again moved for an extension of time, which the appellees opposed. Weighing the factors enumerated in *Poulis*, the District Court denied the requested extension and dismissed the appeal for the appellant's failure to timely prosecute. The Third Circuit summarily affirmed, finding that the responsibility to prosecute fell on the pro se appellant and the cost associated with further delay would prejudice the appellees.

In re Revel AC, Inc.,

--- F.3d ----, 2015 WL 5711358 (3d Cir. Sept. 30, 2015).

The Third Circuit reversed the decision of the District Court denying a nightclub owner's request for a stay pending appeal of Revel's section 363 sale. The Third Circuit analyzed, in

great length, the four factors commonly considered in the stay pending appeal context and found that they weighed solidly in the appellant's favor. First, the Third Circuit found the appellant likely to prevail on the merits because nothing in the record cast doubt on the validity of the lease, thereby prohibiting Revel from claiming it satisfied the section 363(f) "free and clear" standards. Second, the full loss of the nightclub's business as a result of the sale was sufficient to show irreparable harm. Finally, with respect to the balancing of harms, the Court found that Revel was unable to show its own irreparable harm even though, according to the Court, the public interest appeared to favor the denial of a stay.

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Ninth Circuit

Hughes v. Tower Park Properties, LLC (In the Matter of Tower Park Properties, LLC), --- F.3d ----, 2015 WL 5668879 (9th Cir. Sept. 28, 2015).

The issue before the Ninth Circuit in Hughes v. Tower Park Properties, LLC (In the Matter of Tower Park Properties, LLC), No. 13-5604, 2015 WL 5668879 (9th Cir. Sept. 28, 2015), was whether the sole, non-contingent beneficiary of a trust was a "party in interest" under section 1109(b) of the Bankruptcy Code such that he had standing to object to a settlement between the corporate debtor, creditor entities held by the trust (which held the bulk of the trust's assets) and the trustees of the trust. The Ninth Circuit held that, because the beneficiary lacked a legally protected interest in the settlement approval proceedings, he lacked standing to object, at least where the beneficiary's interests were adequately represented by a successor to the co-trustees of the trust. Consequently, the Ninth Court affirmed the District Court's dismissal of the beneficiary's appeal of the bankruptcy court's order approving the settlement over his objection. Factually, Alexander Hughes was the sole, non-contingent beneficiary of a trust formed by his late father, Herbalife's founder. Relevant to the appeal, the trust owned two LLCs, one of which owned undeveloped real property that was sold to the debtor and with the second LLC financed the sale becoming the debtor's largest secured creditors. Subsequently, the debtor defaulted and filed a chapter 11 case. Later, the bankruptcy court confirmed the debtor's chapter 11 plan which restructured the LLCs' debt, and one of the LLCs was to provide exit financing. Litigation ensued regarding implementation of the confirmed plan but subsequently the parties settled. Shortly after the debtor filed the 9019 settlement motion the trust beneficiary petitioned a probate court to remove the co-trustees of the trust for alleged defalcations which relief was granted a corporate entity was appointed as trustee ad litem. The beneficiary objected to the settlement (primarily as it reduced the debt owed to the two LLCs owned by the Trust that financed the sale to the debtor), and the Trustee joined but only to the extent of the request for an abatement of the hearing on the settlement motion so that it could consider the merits. The bankruptcy court approved the settlement over the beneficiary's objection; District Court dismissed the

beneficiary's appeal finding that he lacked party in interest standing. On further appeal, the Ninth Circuit affirmed, relying on In re Thorpe Insulation Co., 677 F.3d 869 (9th Cir. 2012) and In re Refco Inc., 505 F.3d 109 (2d Cir. 2007). The Ninth Circuit relied on California trust law that a trust beneficiary has no legal title or ownership in assets owned by the trust and his or her right to sue is generally limited to enforcement of trust provisions, neither of which was at play in the beneficiary's objection to the settlement agreement, that is, the beneficiary lacked a legally protected interest in the settlement. That interest, the Ninth Circuit found, was held by the co-trustees, and now the trustee ad litem who was adequately protecting the beneficiary's interests, including regarding any challenge to the settlement. The Ninth Circuit found that the beneficiary's claims against the (former) co-trustees did not belong in or should be adjudicated by the bankruptcy court. In sum, the Ninth Circuit held that the beneficiary lacked party in interest standing where his interests were being adequately protected by the trustee ad litem. Accordingly, the Ninth Circuit declined to address whether the beneficiary met Article III and prudential standing requirements, the other two prerequisites for standing to challenge the settlement.

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Ezra v. Seror (In re Ezra),

--- B.R. ----, 2015 5598944 (9th Cir. B.AP. September 22, 2015).

In *Ezra v. Seror*, the bankruptcy appellate panel affirmed the bankruptcy court's holding that the Chapter 7 trustee may avoid fraudulent transfers where the debtor's pattern of practice evidenced intent to hinder, delay, or defraud under section 3439.04(a) of the California Civil Code and section 548(a)(1)(A) of the Federal Bankruptcy Code.

Appellant Ezra first contended that the claims brought against her by Appellee Seror lacked evidentiary support to substantiate a finding of the debtors' intent to hinder, delay, or defraud creditors. The Court disagreed. A debtor's state of mind is examined under section 3439.04(a)'s disjunctive test: "[e]ither an intent to hinder or an intent to delay a creditor [] [would] suffice." The Court agreed with the bankruptcy court's inference of the required intent based on the debtors "pattern and practice of shielding their assets from creditors." Specifically, "the various transfers the debtors made affecting title to and encumbrances against their residence . . . were made for the purpose of keeping any equity in their residence as far away from their creditors as possible." The Court also factored in the debtor's experience as a real estate investment professional and the inherently litigious and nature of the real estate lending and investment business.

Appellant Ezra then asserted the claims were time-barred under the discovery rule of section 3439.09(a) and statute of repose of section 3439.09(c) under California's Civil Code

Setting appellant's failure to first address this discovery rule in bankruptcy court, the appellee was not time-barred because the discovery rule "does not commence until the plaintiff has reason to discover the fraudulent nature of the transfer" opposed to "mere discovery of the transfer itself." With respect to the statute of repose, the Court, again set aside appellant's untimely address of the issue, found that the appellee was not time-barred. According to the Court, the "seven-year statute of repose does not bar a claim under § 544(b) and Cal. Civ. Code § 3439.04 so long as the claim arose less than seven years before the debtor's bankruptcy filing."

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11th Circuit

Tucker v. Mukamal

---Fed.Appx. ---, 2015 WL 5166276 (11th Cir. Sept. 4, 2015).

The Eleventh Circuit affirmed the district court's order affirming the bankruptcy court's denial of the debtor's motion to recuse the bankruptcy court judge and closure of the bankruptcy case.

Debtor filed a chapter 7 bankruptcy in 2004. Two years later, the Debtor and the Trustee (Mukamal) entered into a court-approved settlement agreement to settle certain debts against the estate in exchange for his discharge. The agreement required the Debtor to make certain payments by November 20, 2007, and upon default the Trustee was entitled to seek revocation of his discharge. The Debtor subsequently defaulted, so in 2011 the Trustee moved to revoke the debtor's discharge, which the bankruptcy court granted. The Debtor filed a motion to recuse the bankruptcy judge, which the judge denied.

Two years later, the Trustee filed a motion to close the bankruptcy case since the adversary, which did not involve the Trustee or the estate, had been ongoing for ten years and could continue for some time without a resolution. The court granted the Trustee's motion over the Debtor's objection and the Debtor appealed.

A judge is not "recusable for bias or prejudice when his knowledge and the opinion it produced were properly and necessarily acquired in the course of the proceedings." While the judge made half a dozen or so comments about the Debtor's demeanor and litigation tactics over a ten year period of litigation, there were no facts on appeal showing favoritism or antagonism that warranted recusal.

Since only a "person aggrieved" may file appeal a bankruptcy order and the Debtor was not a "person aggrieved"—a person with "a financial stake in the order being appealed"—the Debtor lacked standing to object to Trustee's motion to close the case.

In re PSN USA, Inc.,

--- Fed.Appx. ---, 2015 WL 5167803 (11th Cir. Sep. 4, 2015).

The Eleventh Circuit affirmed the district court's order affirming the bankruptcy court's granting the defendant's motion for partial of summary judgment.

The Debtor's confirmed Chapter 11 plan established a liquidating trust to pursue chapter 5 causes of action. The Liquidating Trustee filed an adversary proceeding to recover payments that the debtor made pursuant to a contract signed by debtor's corporate parent under a constructive fraud theory. The bankruptcy court held that the debtor received reasonably equivalent value for two reasons: (1) the debtor received and used the contracted services; and (2) the parent and the debtor shared an identity of interests, such that any benefit the parent received under the contract also indirectly benefited the debtor. In affirming, the Eleventh Circuit stated that reasonably equivalent value is given if the debtor shares in the enjoyment of or use of a good or service.

In re Moore,

--- Fed Appx. ---, 2015 WL 5204615 (11th Cir. Sep. 8, 2015).

The Eleventh Circuit affirmed the bankruptcy court's final judgment in favor of the debtors on a §727(a)(5) adversary proceeding brought by creditors.

The debtors' LLC entered into an agreement to perform interior decorating services and provide certain goods for the creditors. When the LLC was unable to perform under the contract, the creditors sued in state court and received a judgment against the debtors and the debtors LLC. Shortly thereafter, the debtors filed bankruptcy. Earlier in the year the LLC received monies from a consignment shop that sold assets belonging to the LLC. At issue was whether the bankruptcy court erred in determining that a debtor does not have an obligation to explain the loss of funds under 11 U.S.C. § 727(a)(5) when the funds belong to a single-member LLC. The bankruptcy court made factual findings that the assets of the corporation were never owned by the debtors and were not at any time available to them for their use and were, therefore, not within reach of a creditor. Further the district court reasoned that, if the bankruptcy court erred in its decision, the error was harmless because the debtor explained the disposition of the corporate assets to the satisfaction of the bankruptcy court. It was shown that all moneys paid to LLC were deposited in the corporation's accounts, were never the personal property of the debtors, and were used to pay corporate liabilities.

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