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SPV OSUS, Ltd. v. UBS AG

United States Court of Appeals for the Second Circuit

June 14, 2017, Argued; February 9, 2018, Decided

Docket No. 16-2173

Reporter
2018 U.S. App. LEXIS 3088 *; 882 F.3d 333; 65 Bankr. Ct. Dec. 60; 2018 WL 798291

SPV OSUS LTD., Plaintiff-Appellant, v. UBS AG, UBS (LUXEMBOURG) S.A., UBS FUND SERVICES (LUXEMBOURG) S.A., UBS THIRD PARTY MANAGEMENT COMPANY S.A., AIA LLC, ACCESS PARTNERS (SUISSE) S.A., ACCESS MANAGEMENT LUXEMBOURG S.A., ACCESS PARTNERS S.A. (LUXEMBOURG), PATRICK LITTAYE, ACCESS INTERNATIONAL ADVISORS LTD., THEODORE DUMBAULD, Defendants-Appellees.[1]

Prior History: SPV Osus Ltd. is the putative assignee of Optimal Strategic U.S. Equity Ltd (collectively, "SPV"). Optimal invested money directly with Bernard L. Madoff Investment Securities LLC ("BLMIS"). When BLMIS turned out to be a massive Ponzi scheme, see *In re Bernard L. Madoff Inv. Sec. LLC, 654 F.3d 229, 231-33 (2d Cir. 2011)*, Optimal suffered losses it alleges totaled roughly $2.9 billion. SPV sued UBS AG and its affiliated entities (collectively, "UBS") and AIA LLC and its affiliated entities and individuals (collectively, "Access") in New York state court. In broad strokes, SPV alleges that UBS and Access aided and abetted BLMIS and Madoff by sponsoring, and providing support for, two European-based feeder funds. SPV alleges that the feeder funds channeled billions of dollars to Madoff and BLMIS, allowing them to further their fraud. SPV alleges UBS and Access chose to work with the feeder funds despite being aware of fraudulent activity on the part of Madoff and BLMIS. Absent assistance from UBS and Access, SPV allege, Madoff and BLMIS could not have continued to operate their Ponzi scheme. UBS removed the New York state action to the United States District Court for the Southern District of New York (Rakoff, J.) SPV moved to remand. The district court denied **[*2]** the motion, finding federal jurisdiction proper pursuant to *28 U.S.C. § 1334*, which provides federal courts with "original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11." *28 U.S.C. § 1334(b)*. See *SPV OSUS Ltd. v. UBS AG, 2015 U.S. Dist. LEXIS 89147, 2015 WL 4079079 (S.D.N.Y. July 1, 2015)*. The district court then granted UBS's motion to dismiss the complaint for lack of personal jurisdiction. See *SPV OSUS Ltd. v. UBS AG, 114 F. Supp. 3d 161 (S.D.N.Y. 2015)*. Finally, the district court granted a separate motion by the Access Defendants to dismiss the complaint against them, in relevant part, on the ground that SPV's complaint failed to adequately allege that actions by the Access Defendants proximately caused SPV's loss. See *SPV OSUS Ltd. v. UBS AG, 2016 U.S. Dist. LEXIS 69349, 2016 WL 3039192 (S.D.N.Y. May 26, 2016)* **[*1]** . On appeal, SPV primarily argues that (1) this litigation is not "related to" the Madoff/BLMIS bankruptcies, such that the federal courts lack jurisdiction; (2) the district court erred in finding it lacked personal jurisdiction over UBS; and (3) it adequately pled proximate cause. For the reasons detailed below, we affirm the district court in all respects. Judge Calabresi concurs in the judgment and opinion of the Court, except for Part II, and files a concurring opinion.

SPV OSUS Ltd. v. AIA LLC, 2016 U.S. Dist. LEXIS 69349 (S.D.N.Y., May 24, 2016)
SPV OSUS Ltd. v. UBS AG, 114 F. Supp. 3d 161, 2015 U.S. Dist. LEXIS 94386 (S.D.N.Y., July 20, 2015)
SPV OSUS Ltd. v. UBS AG, 2015 U.S. Dist. LEXIS 89147 (S.D.N.Y., July 1, 2015)

Disposition: Affirmed.

[1] The Clerk of the Court is directed to amend the caption as above.

Core Terms

personal jurisdiction, funds, contacts, aiding and abetting, district court, feeder, bankruptcy proceeding, alleges, merits, internal quotation marks, general jurisdiction, indemnification, invested, bankrupt estate, cases, entities, substantial assistance, bankruptcy court, proximate cause, federal court, forum state, subject-matter, investors, billion, principal place of business, breach of fiduciary duty, denial of motion, potential claim, proof of claim, conceivable

Case Summary

Overview
HOLDINGS: [1]-There was a high degree of interconnectedness between this action and the bankruptcies as appellant could only proceed on these claims if it established that the fraud occurred; [2]-Appellees lacked any presence in New York at all where each was incorporated, and had its principal place of business in, Luxembourg and none had any employees in the United States; [3]-The connections between appellees, appellant's claims, and its chosen New York forum were too tenuous to support the exercise of specific jurisdiction as none of appellees were resident in New York; [4]-The district court correctly determined that appellant's state law claims against appellees were deficient as a matter of law because appellant failed to adequately plead proximate cause where appellees did not owe appellant any fiduciary duty.

Outcome
Judgment affirmed.

LexisNexis® Headnotes

Bankruptcy Law > ... > Judicial Review > Standards of Review > Clear Error Review

Bankruptcy Law > ... > Judicial Review > Standards of Review > De Novo Standard of Review

Bankruptcy Law > Procedural Matters > Jurisdiction > Federal District Courts

HN1[ ] **Standards of Review, Clear Error Review**

On appeal from the denial of a motion to remand for lack of subject matter jurisdiction, an appellate court reviews the court's legal conclusions de novo and its factual findings for clear error. The bankruptcy removal statute grants federal courts original but not exclusive jurisdiction of all civil proceedings arising under Title 11, or arising in or related to cases under Title 11. *28 U.S.C.S. § 1334(b)*. Congress did not delineate the scope of "related to" jurisdiction, but its choice of words suggests a grant of some breadth.

Bankruptcy Law > Procedural Matters > Jurisdiction > Federal District Courts

HN2[ ] **Jurisdiction, Federal District Courts**

In the Eleventh Circuit, a civil proceeding is related to a Title 11 case if the action's outcome might have any conceivable effect on the bankrupt estate. If that question is answered affirmatively, the litigation falls within the "related to" jurisdiction of the bankruptcy court. Congress intended to grant comprehensive jurisdiction to the

bankruptcy courts so that they might deal efficiently and expeditiously with all matters connected with the bankruptcy estate. While "related to" jurisdiction is not limitless, it is fairly capacious, and includes suits between third parties which have an effect on the bankruptcy estate. An action is related to bankruptcy if the outcome could alter the debtor's rights, liabilities, options, or freedom of action (either positively or negatively) and which in any way impacts upon the handling and administration of the bankrupt estate.

Bankruptcy Law > Procedural Matters > Jurisdiction > Federal District Courts

HN3[] Jurisdiction, Federal District Courts

In determining whether potential claims by third party defendants against the debtor for either indemnification or contribution give rise to "related to" jurisdiction over litigation to which the debtor is not a party, courts in the Second Circuit have generally found jurisdiction where there is a "reasonable" legal basis for the claim. A claim need not be certain to provide a federal court with jurisdiction: contingent outcomes can satisfy the conceivable effects test, so long as there is the possibility of an effect on the estate.

Bankruptcy Law > ... > Bankruptcy > Claims > Allowance of Claims

Governments > Legislation > Statute of Limitations > Time Limitations

Torts > ... > Multiple Defendants > Contribution > Particular Actions

HN4[] Claims, Allowance of Claims

Bankruptcy courts are permitted to accept late proofs of claim. Unlike indemnification claims, contribution claims do not accrue until after liability is established. A party may not know of a potential contribution claim until sued, which may be years after bankruptcy proceedings have commenced.

Bankruptcy Law > ... > Bankruptcy > Claims > Allowance of Claims

Business & Corporate Compliance > ... > Contracts Law > Contract Conditions & Provisions > Indemnity Clauses

Governments > Legislation > Statute of Limitations > Time Limitations

HN5[] Claims, Allowance of Claims

An indemnification right arises at the time the indemnification agreement is executed, and it constitutes a claim under the Bankruptcy Code even if the act giving rise to indemnification has not yet occurred. Excusable neglect does not excuse the failure to file proof of claim for an indemnification liability by the bar date, such that the claim could not have any "conceivable effect" on the estate.

Bankruptcy Law > Case Administration > Examiners, Officers & Trustees > Duties & Functions

HN6[] Examiners, Officers & Trustees, Duties & Functions

Even unsuccessful claims require evaluation by the trustee, who recovers fees for such work from the estate. *11 U.S.C.S. § 704(a)(5)*; *15 U.S.C.S. § 78fff(e)*.

Bankruptcy Law > Procedural Matters > Jurisdiction > Federal District Courts

HN7[] **Jurisdiction, Federal District Courts**

Unless the underlying litigation automatically creates liability for the bankruptcy estate, the connection between the underlying litigation and the bankruptcy proceedings is too remote to support "related to" jurisdiction.

Bankruptcy Law > Procedural Matters > Jurisdiction > Federal District Courts

Torts > ... > Multiple Defendants > Contribution > Particular Actions

HN8[] **Jurisdiction, Federal District Courts**

A contingent contribution claim may serve as the basis for "related to" jurisdiction as it may have a "conceivable effect" on the bankruptcy estate.

Civil Procedure > Appeals > Standards of Review > De Novo Review

Civil Procedure > ... > Jurisdiction > In Rem & Personal Jurisdiction > In Personam Actions

HN9[] **Standards of Review, De Novo Review**

An appellate court reviews a district court's dismissal of an action for want of personal jurisdiction de novo, construing all pleadings and affidavits in the light most favorable to the plaintiff and resolving all doubts in the plaintiff's favor. In order to survive a motion to dismiss for lack of personal jurisdiction, a plaintiff must make a prima facie showing that jurisdiction exists. A plaintiff must include an averment of facts that, if credited by the ultimate trier of fact, would suffice to establish jurisdiction over the defendant.

Bankruptcy Law > Procedural Matters > Adversary Proceedings > Commencement of Adversary Proceedings

Civil Procedure > ... > In Rem & Personal Jurisdiction > In Personam Actions > Due Process

Civil Procedure > ... > In Rem & Personal Jurisdiction > In Personam Actions > Substantial Contacts

Civil Procedure > ... > In Rem & Personal Jurisdiction > In Personam Actions > Minimum Contacts

HN10[] **Adversary Proceedings, Commencement of Adversary Proceedings**

When a case is removed to federal court pursuant to *28 U.S.C.S. § 1452*, personal jurisdiction is allowed to the extent permitted by the Constitution of the United States. *Fed. R. Bankr. P. 7004(f)*. To establish personal jurisdiction over a defendant, due process requires a plaintiff to allege (1) that a defendant has certain minimum contacts with the relevant forum, and (2) that the exercise of jurisdiction is reasonable in the circumstances. For purposes of this initial inquiry, a distinction is made between "specific" jurisdiction and "general" jurisdiction. Specific jurisdiction exists when a State exercises personal jurisdiction over a defendant in a suit arising out of or related to the defendant's contacts with the forum; a court's general jurisdiction, on the other hand, is based on the defendant's general business contacts with the forum state and permits a court to exercise its power in a case where the subject matter of the suit is unrelated to those contacts.

Civil Procedure > ... > In Rem & Personal Jurisdiction > In Personam Actions > Substantial Contacts

HN11[] **In Personam Actions, Substantial Contacts**

Because general jurisdiction is not related to the events giving rise to the suit, courts impose a more stringent minimum contacts test, requiring the plaintiff to demonstrate the defendant's continuous and systematic general business contacts. For an individual, the paradigm forum for the exercise of general jurisdiction is the individual's domicile; for a corporation, it is an equivalent place, one in which the corporation is fairly regarded as at home. The inquiry is not whether a foreign corporation's in-forum contacts can be said to be in some sense continuous and systematic, but whether that corporation's affiliations with the State are so continuous and systematic as to render it essentially at home in the forum State.

Civil Procedure > ... > In Rem & Personal Jurisdiction > In Personam Actions > Substantial Contacts

HN12[] **In Personam Actions, Substantial Contacts**

Aside from the truly exceptional case, a corporation is at home and subject to general jurisdiction only in its place of incorporation or principal place of business.

Civil Procedure > ... > In Rem & Personal Jurisdiction > In Personam Actions > Minimum Contacts

Civil Procedure > ... > In Rem & Personal Jurisdiction > In Personam Actions > Purposeful Availment

HN13[] **In Personam Actions, Minimum Contacts**

The inquiry whether a forum State may assert specific jurisdiction over a nonresident defendant focuses on the relationship among the defendant, the forum, and the litigation. Specific jurisdiction is confined to adjudication of issues deriving from, or connected with, the very controversy that establishes jurisdiction. A court must look to whether there was some act by which the defendant purposefully availed itself of the privilege of conducting activities within the forum State, thus invoking the benefits and protections of its laws. The defendant's suit-related conduct must create a substantial connection with the forum State. A defendant's general connections with the forum are not enough to support the exercise of specific jurisdiction.

Civil Procedure > ... > In Rem & Personal Jurisdiction > In Personam Actions > Minimum Contacts

HN14[] **In Personam Actions, Minimum Contacts**

The U.S. Supreme Court has yet to address exactly how a defendant's activities must be tied to the forum for a court to properly exercise specific personal jurisdiction over a defendant. Some circuits require that the in-forum conduct to be the proximate cause of plaintiff's injuries, while others find the standard satisfied if the defendant's activities are the "but for" cause of those injuries. In the Second Circuit, the standard applied depends on the relationship among the defendant, the forum, and the litigation: Where the defendant has had only limited contacts with the state it may be appropriate to say that he will be subject to suit in that state only if the plaintiff's injury was proximately caused by those contacts. Where the defendant's contacts with the jurisdiction that relate to the cause of action are more substantial, however, it is not unreasonable to say that the defendant is subject to personal jurisdiction even though the acts within the state are not the proximate cause of the plaintiff's injury.

Torts > ... > Multiple Defendants > Concerted Action > Civil Aiding & Abetting

Torts > Intentional Torts > Breach of Fiduciary Duty > Elements

HN15[] Concerted Action, Civil Aiding & Abetting

A claim for aiding and abetting a breach of fiduciary duty under New York law: (1) a breach by a fiduciary of obligations to another, (2) that the defendant knowingly induced or participated in the breach, and (3) that plaintiff suffered damage as a result of the breach. With respect to the second requirement, although a plaintiff is not required to allege that the aider and abettor had an intent to harm, there must be an allegation that such defendant had actual knowledge of the breach of duty. And a person knowingly participates in a breach of fiduciary duty only when he or she provides substantial assistance to the primary violator. Under New York law, the elements of aiding and abetting a breach of fiduciary duty, aiding and abetting a conversion, and aiding and abetting a fraud are substantially similar.

Torts > ... > Multiple Defendants > Concerted Action > Civil Aiding & Abetting

HN16[] Concerted Action, Civil Aiding & Abetting

Substantial assistance occurs when a defendant affirmatively assists, helps conceal or fails to act when required to do so, thereby enabling the breach to occur. Substantial assistance requires the plaintiff to allege that the actions of the aider/abettor proximately caused the harm on which the primary liability is predicated. That is, the injury must be a direct or reasonably foreseeable result of the conduct.

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Judges: Before: CALABRESI and POOLER, Circuit Judges, and RAMOS, District Judge.[2]

Opinion by: POOLER

Opinion

POOLER, *Circuit Judge*:

This case presents yet another chapter in the Bernie Madoff saga. SPV Osus Ltd. is the putative assignee of Optimal Strategic U.S. Equity Ltd (collectively, "SPV"). Optimal invested money directly with Bernard L. Madoff Investment Securities LLC ("BLMIS"). When BLMIS turned out to be a massive Ponzi scheme, *see* In re Bernard L.

[2] Judge Edgardo Ramos, United States District Court for the Southern District ofNew York, sitting by designation.

Madoff Inv. Sec. LLC, 654 F.3d 229, 231-33 (2d Cir. 2011), Optimal suffered losses it alleges totaled roughly $2.9 billion.

Seeking a fresh path to recovery, SPV sued UBS AG and its affiliated entities (collectively, "UBS") and AIA LLC and its affiliated entities and individuals (collectively, "Access") **[*4]** in New York state court. The gravamen of SPV's complaint is that UBS and Access aided and abetted BLMIS and Madoff by sponsoring, and providing support for, two European-based feeder funds—Luxalpha SICAV and Groupement Financier Ltd. SPV alleges that the feeder funds in turn channeled billions of dollars to Madoff and BLMIS, allowing them to further their fraud. SPV alleges UBS and Access were involved with the feeder funds despite being aware of numerous signs of fraudulent activity on the part of Madoff and BLMIS. Absent such assistance from UBS and Access, SPV alleges, Madoff and BLMIS could not have continued to operate their Ponzi scheme.

UBS removed the state court action to the United States District Court for the Southern District of New York. SPV moved to remand. The district court denied the motion, finding federal jurisdiction proper pursuant to *28 U.S.C. § 1334*, which provides federal courts with "original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11." *28 U.S.C. § 1334(b)*. *See* *SPV OSUS Ltd. v. UBS AG, 2015 U.S. Dist. LEXIS 89147, 2015 WL 4079079 (S.D.N.Y. July 1, 2015)* ("*SPV I*"). The district court then granted UBS's motion to dismiss the complaint for lack of personal jurisdiction. *See* *SPV OSUS Ltd. v. UBS AG, 114 F. Supp. 3d 161 (S.D.N.Y. 2015)* ("*SPV II*"). Finally, the district **[*5]** court granted a separate motion by the Access Defendants to dismiss the complaint against them, in relevant part, on the ground that SPV's complaint failed to adequately allege that actions by the Access Defendants proximately caused SPV's loss. *See* *SPV OSUS Ltd. v. UBS AG, 2016 U.S. Dist. LEXIS 69349, 2016 WL 3039192 (S.D.N.Y. May 26, 2016)* ("*SPV III*").

On appeal, SPV primarily argues that the district court erred in (1) not granting SPV's motion to remand, as the instant litigation is not "related to" the Madoff/BLMIS bankruptcies and the federal courts lack jurisdiction; (2) finding it lacked personal jurisdiction over UBS; and (3) finding it failed to adequately plead proximate cause. For the reasons detailed below, we affirm the district court's decisions in all respects.

BACKGROUND

SPV is a Bahamian corporation that alleges is it the assignee of Optimal. Optimal invested directly with BLMIS, and its last statement from BLMIS in November 2008 reported roughly $2.9 billion in its accounts. Madoff was involuntarily forced into Chapter 7 in April 2009. In June 2009 the Madoff estate was consolidated with a separate bankruptcy proceeding against BLMIS that was filed under the *Securities Investor Protection Act ("SIPA")*. The order consolidating the bankruptcy proceedings states **[*6]** that the consolidated estate "shall be administered in accordance with *SIPA* and the Bankruptcy Code under the jurisdiction of" the bankruptcy court, but "the Chapter 7 Trustee shall remain Chapter 7 trustee of the Madoff estate and shall continue to have all powers, rights, claims and interests of a Chapter 7 trustee[,] . . . [and] all powers, rights, claims and interests of the Madoff estate are expressly preserved . . .".

In December 2014, SPV filed suit in New York state court against UBS and AIA. SPV's suit set forth claims for aiding and abetting fraud, breach of fiduciary duty, conversion, and knowing participation in a breach of trust. In essence, SPV alleges that the defendants facilitated BLMIS's fraud by moving billions of dollars from European investors to BLMIS by providing support to the Luxalpha and Groupement feeder funds. SPV alleges that by supporting the feeder funds, UBS and Access provided Madoff and BLMIS with a veneer of credibility that gave investors confidence in their decision to invest with Madoff and BLMIS, allowing the fraud to continue. SPV also alleges that UBS ignored certain "red flags" indicating Madoff and BLMIS were engaged in fraud, and continued **[*7]** to service the feeder funds so that it might pocket fees. All the while, SPV alleges, UBS protected itself and its clients by not marketing or recommending Madoff funds.

UBS AG is a Swiss entity with its principal place of business in Switzerland. The remaining UBS entities were, at all times relevant, Luxembourg entities with their principal places of business in Luxembourg. Luxalpha was organized and located in Luxembourg; Groupement was organized and located in the British Virgin Islands. SPV alleges that it

pleaded sufficient contacts to allow the exercise of personal jurisdiction by virtue of the UBS entities' contacts with New York related to their interactions with the Luxalpha and Groupement feeder funds. SPV also sued AIA LLC; Access International Advisors Ltd.; Access Partners (Suisse) S.A.; Access Management Luxembourg S.A.; Access Partners S.A. (Luxembourg); and Patrick Littaye (together, the "Access Defendants").

As described above, the district court denied SPV's motion to remand the matter to state court, then granted separate motions to dismiss the complaint. This appeal followed.

DISCUSSION

I. Appellate Jurisdiction.

SPV's notice of appeal designates its appeal as both **[*8]** from the judgment and from orders entered on July 21, 2015, July 24, 2015, May 26, 2016 and May 27, 2016. This list does not include the order and opinion denying the motion to remand. UBS argues that the failure to specify the remand order in the notice of appeal strips this Court of jurisdiction to consider an appeal from that order. We need not linger long over the issue, because even assuming arguendo that SPV waived its right to appeal, the denial of a motion to remand goes to this Court's subject matter jurisdiction, which may be raised at any time. *See* *In re Methyl Tertiary Butyl Ether ("MTBE") Prod. Liability Litig., 488 F.3d 112, 123 (2d Cir. 2007)*. "Indeed, we have often taken it upon ourselves to determine whether removal jurisdiction existed even where that issue was not itself appealed." *Id. at 121*. Satisfied that the appeal from the district court's denial of the motion to remand is properly before us, we turn to the merits.

II. "Related to" jurisdiction

HN1[] "On appeal from the denial of a motion to remand for lack of subject matter jurisdiction, we review the court's legal conclusions de novo and its factual findings for clear error." *Blockbuster, Inc. v. Galeno, 472 F.3d 53, 56 (2d Cir. 2006)*. UBS removed to federal court pursuant to the general removal statute, *28 U.S.C. § 1452(a)* and the bankruptcy removal statute, **[*9]** which grants federal courts "original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11." *28 U.S.C. § 1334(b)*. "Congress did not delineate the scope of 'related to' jurisdiction, but its choice of words suggests a grant of some breadth." *Celotex Corp. v. Edwards, 514 U.S. 300, 307-08, 115 S. Ct. 1493, 131 L. Ed. 2d 403 (1995)*.

HN2[] In this Circuit, "a civil proceeding is related to a title 11 case if the action's outcome might have any conceivable effect on the bankrupt estate." *Parmalat Capital Fin. Ltd. v. Bank of Am. Corp., 639 F.3d 572, 579 (2d Cir. 2011)* (internal quotation marks omitted). "If that question is answered affirmatively, the litigation falls within the 'related to' jurisdiction of the bankruptcy court." *In re Cuyahoga Equip. Corp., 980 F.2d 110, 114 (2d Cir. 1992)*. "Congress intended to grant comprehensive jurisdiction to the bankruptcy courts so that they might deal efficiently and expeditiously with all matters connected with the bankruptcy estate." *Celotex, 514 U.S. at 308*. While "related to" jurisdiction is not "limitless," *id.*, it is fairly capacious, and includes "suits between third parties which have an effect on the bankruptcy estate." *Id. at 307 n. 5*. "An action is related to bankruptcy if the outcome could alter the debtor's rights, liabilities, options, or freedom of action (either positively or negatively) and which in any way impacts upon the handling and administration **[*10]** of the bankrupt estate." *Id. at 308 n. 6*.

Here, the claims at issue arise in an action that does not directly involve the bankruptcy estates.***HN3***[] "In determining whether potential claims by third party defendants against the debtor for either indemnification or contribution give rise to "related to" jurisdiction over litigation to which the debtor is not a party, courts in this circuit . . . have generally found jurisdiction where there is a 'reasonable' legal basis for the claim." *In re Worldcom, Inc. Sec. Litig., 293 B.R. 308, 319 (S.D.N.Y. 2003)* (collecting cases). A claim need not be certain to provide a federal court with jurisdiction: "contingent outcomes can satisfy the 'conceivable effects' test, so long as there is the

possibility of an effect on the estate." *N.Y. Commercial Bank v. Pullo, No. 12-02052 (BRL), 2013 Bankr. LEXIS 520, 2013 WL 494050, at *3 (Bankr. S.D.N.Y. Feb. 7, 2013)*.

The gravamen of SPV's complaint is that defendants are joint tortfeasors with Madoff and BLMIS, which, if proven, would provide defendants with a putative contribution claim, to be asserted in the bankruptcy proceedings. SPV urges us to find that the district court erred in denying its motion to remand to state court because it erroneously found that UBS's potential contribution claims sufficiently "related to" the Madoff/BLMIS bankruptcy proceedings to support federal jurisdiction. SPV contends that UBS's **[*11]** potential claims are too remote from the bankruptcy proceedings to have any effect on the estates, making the exercise of federal jurisdiction improper. SPV argues that UBS's potential claim for contribution in the bankruptcy proceedings is illusory, primarily because (1) the bar date to assert claims against the Madoff and BLMIS estates expired, barring UBS from pursuing any claim in the bankruptcy proceeding; and (2) in any event, there is not enough money in either estate to pay out any such claims.

We agree with the district court that the failure to file claims prior to the bar date is not fatal to the potential claims at issue here. ***HN4***[] Bankruptcy courts are permitted to accept late proofs of claim. *See, e.g., In re PT-1 Commc'ns, Inc., 292 B.R. 482, 489 (Bankr. E.D.N.Y. 2003)* (allowing filing of late claim where claimant did not know claim existed until after the bar date lapsed). Unlike indemnification claims, contribution claims do not accrue until after liability is established. A party may not know of a potential contribution claim until sued, which may be years after bankruptcy proceedings have commenced. For example, here SPV sued UBS nearly five-and-half years after the *SIPA* bar date. This lack of notice forms, at a minimum, a credible **[*12]** basis for defendants to petition the bankruptcy court for leave to file a late proof of claim based on excusable neglect. *See Fed. R. Bankr. P. 9006(b)(1)* (bankruptcy court may allow late proof of claim "where the failure to act was the result of excusable neglect.").

Conversely, ***HN5***[] "[a]n indemnification right arises at the time the indemnification agreement is executed, and it constitutes a claim under the Bankruptcy Code even if the act giving rise to indemnification has not yet occurred." *Allstate Ins. Co. v. Credit Suisse Sec. (USA) LLC, 2011 U.S. Dist. LEXIS 120734, 2011 WL 4965150, at *5 (S.D.N.Y. Oct. 19, 2011)* (internal quotation marks omitted). Excusable neglect does not excuse the failure to file proof of claim for an indemnification liability by the bar date, such that the claim could not have any "conceivable effect" on the estate. *Id., see also Sealink Funding Ltd. v. Bear Stearns & Co. Inc., No. 12 Civ. 1397, 2012 U.S. Dist. LEXIS 145418, 2012 WL 4794450, at *3 (S.D.N.Y. Oct. 9, 2012)* (same).

Moreover, it is unclear whether the applicable bar date has passed. While a bar date was set and has passed in the *SIPA* action involving the BLMIS estate, no bar date was set in the Madoff estate. The consolidation order states only that the combined estate "shall be administered in accordance with *SIPA* and the Bankruptcy Code." If the *SIPA* bar date controls, as SPV argues, it cannot be waived. *See In re Lehman Bros., Inc., 493 B.R. 437, 443 (Bankr. S.D.N.Y. 2013)* (noting that unlike proceedings under bankruptcy chapters 7 and 11, a court lacks **[*13]** discretion to extend the bar date in *SIPA* cases, with several exceptions inapplicable here).

We need not resolve the issue of which bar date controls. Even if the bar date set in the *SIPA* estate controls, simply settling the issue of whether a late claim is allowable would likely have an effect on the estate. Any attempt to file a late claim would result in the estate incurring costs. As the district court noted, ***HN6***[] even unsuccessful claims require evaluation by the trustee, who recovers fees for such work from the estate. *See 11 U.S.C. § 704(a)(5)* (trustee charged with "examin[ing] proofs of claims and object[ing] to the allowance of any claim that is improper"); *15 U.S.C. § 78fff(e)* ("[a]ll costs and expenses of administration of the estate of the debtor . . . shall be borne by the general estate of the debtor."). Second, if SPV were successful in its claims against UBS, it would reduce the amount it is owed as a creditor of the BLMIS/Madoff estate. *See, e.g., In re Adelphia Commc'ns Corp. Sec. & Deriv. Litig., No. 03 MDL 1529, 2005 U.S. Dist. LEXIS 11683, 2005 WL 1404798, at *2 (S.D.N.Y. June 14, 2005)* ("To the extent that plaintiffs are successful against the defendants, plaintiffs' recoveries will in all probability (and certainly conceivably) reduce the total of Adelphia's liabilities"); *see also WorldCom, 293 B.R. at 323* ("The potential **[*14]** alteration of the liabilities of the estate and change in the amount available for distribution to other creditors is sufficient to find that litigation among non-debtors is 'related to' the bankruptcy proceeding.").

The need for litigation to settle the issue of whether a late claim would be permitted does not militate against finding this litigation "related to" the bankruptcy proceeding. SPV relies on *Pacor, Inc. v. Higgins* for the proposition that*HN7*[] unless the underlying litigation "automatic[ally] creat[es] liability" for the bankruptcy estate, the connection between the underlying litigation and the bankruptcy proceedings is too remote to support "related to" jurisdiction. *743 F.2d 984, 995 (3d Cir. 1984)*. Like the other circuits to reject this branch of the *Pacor* analysis, we think a more flexible approach appropriate. *See In re El Paso Refinery, LP, 302 F.3d 343, 348-49 (5th Cir. 2002)* (holding a "chain of indemnification provisions" that could be used to assert a claim against the debtor allowed for "related to" jurisdiction); *In re Dow Corning Corp., 86 F.3d 482, 489-94 (6th Cir. 1996)* (holding that suits against manufacturers and suppliers of silicone gel breast implants were "related to" the bankruptcy of the Dow Corning Corporation because of potential claims for contribution and indemnification against Dow); *In re Wolverine Radio Co., 930 F.2d 1132, 1143 (6th Cir. 1991)* ("related to" jurisdiction **[*15]** found based on contractual indemnification provision even though the debtor "would not be affected until and unless [the third party] invoked the indemnification" clause); *A.H. Robins v. Piccinin, 788 F.2d 994, 1001 (4th Cir. 1986)* (litigation "related to" bankruptcy proceedings when brought against officers of debtor who may be entitled to indemnification under debtor's insurance policy); *see also Arnold v. Garlock, Inc., 278 F.3d 426, 440 (5th Cir. 2001)* (noting that "related to" jurisdiction possible based on contribution claims). As discussed above, ***HN8***[] a contingent contribution claim may serve as the basis for "related to" jurisdiction as it may have a "conceivable effect" on the bankruptcy estate.

SPV also challenges the district court's conclusion that it is "within the realm of possibility" for defendants to receive a distribution from the estate. *SPV I, 2015 U.S. Dist. LEXIS 89147, 2015 WL 4079079, at *4*. SPV notes that the amount of loss claim greatly exceeds the assets recovered by the estates. Thus, it argues, there will be no funds available to pay UBS, assuming SPV prevails in the underlying litigation and UBS asserts a contribution claim against the bankruptcy estate. The district court found recovery possible because "the estate continues to recover substantial assets, including almost $1 billion in 2014 alone," and that "the Trustee is aggressively **[*16]** pursuing numerous other recoveries." *Id.* While a payout by the estate to defendants may be improbable, it is not impossible. In addition, any claim by defendants potentially alters that distribution of assets among the estates' creditors, further supporting a finding that this litigation is "related to" the bankruptcy proceedings.

Finally, there is a high degree of interconnectedness between this action and the Madoff bankruptcies: SPV can only proceed on these claims if it establishes that the Madoff fraud occurred. SPV's assignor invested directly with BLMIS. But for the automatic stay, it is difficult to imagine a scenario wherein SPV would not also sue Madoff and BLMIS, given that SPV alleges that UBS aided and abetted in their fraud. "The existence of strong interconnections between the third party action and the bankruptcy has been cited frequently by courts in concluding that the third party litigation is related to the bankruptcy proceeding." *See WorldCom, 293 B.R. at 321* ("but for WorldCom's bankruptcy, [defendants] would have been named as a defendant in [this] action, and despite its absence as a party, its conduct will remain at the heart of [this] litigation.").

II. Personal jurisdiction

HN9[] "We review **[*17]** a district court's dismissal of an action for want of personal jurisdiction de novo, construing all pleadings and affidavits in the light most favorable to the plaintiff and resolving all doubts in the plaintiff's favor." *Penguin Grp. (USA) Inc. v. Am. Buddha, 609 F.3d 30, 34 (2d Cir. 2010)*. "In order to survive a motion to dismiss for lack of personal jurisdiction, a plaintiff must make a prima facie showing that jurisdiction exists." *Id. at 34-35* (internal quotation marks omitted). A plaintiff "must include an averment of facts that, if credited by the ultimate trier of fact, would suffice to establish jurisdiction over the defendant." *Chloe v. Queen Bee of Beverly Hills, LLC, 616 F.3d 158, 163 (2d Cir. 2010)* (internal quotation marks and brackets omitted).

HN10[] When a case is removed to federal court pursuant to *28 U.S.C. § 1452*, personal jurisdiction is allowed to the extent permitted by the Constitution of the United States. *Fed. R. Bankr. P. 7004(f)*. "To establish personal jurisdiction over a defendant, due process requires a plaintiff to allege (1) that a defendant has certain minimum contacts with the relevant forum, and (2) that the exercise of jurisdiction is reasonable in the circumstances." *In re Terrorist Attacks on September 11, 2001, 714 F.3d 659, 674 (2d Cir. 2013)* (internal quotation marks omitted). "For

purposes of this initial inquiry, a distinction is made between 'specific' jurisdiction and **[*18]** 'general' jurisdiction." *Met. Life Ins. Co. v. Robertson-Ceco Corp., 84 F.3d 560, 567 (2d Cir. 1996)*. "Specific jurisdiction exists when a State exercises personal jurisdiction over a defendant in a suit arising out of or related to the defendant's contacts with the forum; a court's general jurisdiction, on the other hand, is based on the defendant's general business contacts with the forum state and permits a court to exercise its power in a case where the subject matter of the suit is unrelated to those contacts." *Id.* (internal quotation marks omitted).

HN11[] "Because general jurisdiction is not related to the events giving rise to the suit, courts impose a more stringent minimum contacts test, requiring the plaintiff to demonstrate the defendant's continuous and systematic general business contacts." *Id.* (internal quotation marks omitted). "For an individual, the paradigm forum for the exercise of general jurisdiction is the individual's domicile; for a corporation, it is an equivalent place, one in which the corporation is fairly regarded as at home." *Goodyear Dunlop Tires Operations, S.A. v. Brown, 564 U.S. 915, 923, 131 S. Ct. 2846, 180 L. Ed. 2d 796 (2011)*. "The inquiry under *Goodyear* is not whether a foreign corporation's in-forum contacts can be said to be in some sense continuous and systematic," but "whether that corporation's affiliations with the State are **[*19]** so continuous and systematic as to render it essentially at home in the forum State." *Daimler AG v. Bauman, 134 S. Ct. 746, 752, 187 L. Ed. 2d 624 (2014)* (internal quotation marks and brackets omitted).

Our Court, in interpreting *Daimler*, noted that the case "expressly cast doubt on previous Supreme Court and New York Court of Appeals cases that permitted general jurisdiction on the basis that a foreign corporation was doing business through a local branch office in the forum." *Gucci Am., Inc. v. Weixing Li, 768 F.3d 122, 135 (2d Cir. 2014)*. In *Gucci*, we held that a court could not properly exercise general jurisdiction over the Bank of China, which had branch offices in New York but was "incorporated and headquartered elsewhere" and conducted only a small portion of its worldwide business within the forum. *Id. at 135*.

Here, UBS SA, UBS FSL and UBS TPM lack any presence in New York at all: each is incorporated, and has its principal place of business in, Luxembourg. None have any employees in the United States. UBS AG's place of incorporation and principal place of business is in Switzerland. As the district court correctly adduced, *Daimler* bars the court's exercise general jurisdiction over the UBS defendants.***HN12***[] "[A]side from the truly exceptional case, a corporation is at home and subject to general jurisdiction only in **[*20]** its place of incorporation or principal place of business." *Brown v. Lockheed Martin Corp., 814 F.3d 619, 629 (2d Cir. 2016)*. SPV points to nothing that would render this an exceptional case. In *Brown*, we found defendant Lockheed Martin's contacts with Connecticut insufficient to maintain general jurisdiction even though Lockheed continuously maintained a physical presence in Connecticut for over 30 years, ran operations out of as many as four leased locations in the State, employed up to 70 workers there, and derived about $160 million in revenue from its Connecticut-based work during the relevant timeframe. *Brown, 814 F.3d at 627-29*. But Lockheed was neither headquartered nor incorporated in Connecticut, and facts fatal to the attempt to subject Lockheed to general jurisdiction in Connecticut. *Id. at 628-31*. Similarly, here the UBS defendants simply lack sufficient contacts with the United States to allow the exercise of general jurisdiction.

Turning to the exercise of specific jurisdiction,***HN13***[] "[t]he inquiry whether a forum State may assert specific jurisdiction over a nonresident defendant focuses on the relationship among the defendant, the forum, and the litigation." *Walden v. Fiore, 134 S. Ct. 1115, 1121, 188 L. Ed. 2d 12 (2014)* (internal quotation marks omitted). "[S]pecific jurisdiction is confined to adjudication of issues deriving from, **[*21]** or connected with, the very controversy that establishes jurisdiction." *Goodyear, 564 U.S. at 919*. A court must look to "whether there was some act by which the defendant purposefully availed itself of the privilege of conducting activities within the forum State, thus invoking the benefits and protections of its laws." *Id. at 924* (internal quotation marks and brackets omitted). "[T]he defendant's suit-related conduct must create a substantial connection with the forum State." *Walden, 134 S. Ct. at 1121*; *see also* *Goodyear, 137 S. Ct. at 919* (exercise of specific jurisdiction requires an "affiliation between the forum and the underlying controversy, principally, [an] activity or an occurrence that takes place in the forum State"). "[A] defendant's general connections with the forum are not enough" to support the exercise of specific jurisdiction. *Bristol-Myers Squibb Co. v. Superior Court of Calif., San Francisco Cty., 137 S.Ct. 1773, 1781, 198 L. Ed. 2d 395 (2017)*.

HN14[] The Supreme Court has yet to address exactly how a defendant's activities must be tied to the forum for a court to properly exercise specific personal jurisdiction over a defendant. Some circuits require that the in-forum conduct to be the proximate cause of plaintiff's injuries, while others find the standard satisfied if the defendant's activities are the "but for" cause of those injuries. *See* *Chew v. Dietrich, 143 F.3d 24, 29 (2d Cir. 1998)* (collecting and comparing cases). **[*22]** In this Circuit, the standard applied depends on "the relationship among the defendant, the forum, and the litigation:"

> Where the defendant has had only limited contacts with the state it may be appropriate to say that he will be subject to suit in that state only if the plaintiff's injury was proximately caused by those contacts. Where the defendant's contacts with the jurisdiction that relate to the cause of action are more substantial, however, it is not unreasonable to say that the defendant is subject to personal jurisdiction even though the acts within the state are not the proximate cause of the plaintiff's injury.

Id.

Here, the connections between the UBS Defendants, SPV's claims, and its chosen New York forum are too tenuous to support the exercise of specific jurisdiction. None of the UBS Defendants are resident in New York. SPV's complaint alleges the injuries suffered by OSUS were caused by Madoff and BLMIS. Missing from the complaint is any allegation that OSUS relied on UBS's contacts with the feeder funds when OSUS decided to invest directly with BLMIS. Nor are there any allegations that OSUS based its decision to invest with BLMIS on the fact that the UBS defendants helped **[*23]** create and service the feeder funds. Indeed, OSUS began investing in BLMIS in 1997, and the feeder funds were not created until 2003 (Groupement) and 2004 (Luxalpha). At bottom, the contacts alleged by SPV between the UBS Defendants, the forum and the litigation amount to a handful of communications and transfers of funds. These limited contacts are insufficient to allow the exercise of specific personal jurisdiction over the UBS Defendants. *See, e.g.,* *Hau Yin To v. HSBC Holdings PLC, 2017 U.S. Dist. LEXIS 28931, 2017 WL 816136 (S.D.N.Y. 2017)* ("communications with and payments to New York merely to ensure compliance with contract terms negotiated and executed outside of New York do not 'project' a defendant into the state sufficiently to confer" specific jurisdiction over foreign defendants) (citation omitted)).

III. Proximate cause

As to the Access Defendants, SPV alleges that they aided and abetted Madoff and BLMIS by luring investors into the feeder funds, which in turn invested funds in BLMIS, and those funds allowed BLMIS to continue to perpetuate its fraud. SPV asserted state law claims for aiding and abetting fraud, aiding and abetting breach of fiduciary duty, aiding and abetting conversion, and knowing participation in a breach of trust (which is essentially an aiding **[*24]** and abetting claim). As set forth in *Lerner v. Fleet Bank, N.A.*, ***HN15***[] a claim for aiding and abetting a breach of fiduciary duty under New York law:

> (1) a breach by a fiduciary of obligations to another, (2) that the defendant knowingly induced or participated in the breach, and (3) that plaintiff suffered damage as a result of the breach. With respect to the second requirement, although a plaintiff is not required to allege that the aider and abettor had an intent to harm, there must be an allegation that such defendant had actual knowledge of the breach of duty. And a person knowingly participates in a breach of fiduciary duty only when he or she provides substantial assistance to the primary violator.

459 F.3d 273, 294 (2d Cir. 2006) (internal citation and brackets omitted). Under New York law, "the elements of aiding and abetting a breach of fiduciary duty, aiding and abetting a conversion, and aiding and abetting a fraud are substantially similar." *Kirschner v. Bennett, 648 F. Supp. 2d 525, 533 (S.D.N.Y. 2009)*; *see also* *Fed. Ins. Co. v. Am. Home Assurance Co., 639 F.3d 557, 566 (2d Cir. 2011)* ("[W]here the parties agree that New York law controls, this is sufficient to establish choice of law.").

The district court dismissed SPV's state law claims against the Access Defendants after finding that SPV failed to adequately plead the "substantial assistance" **[*25]** element of its claims. *SPV III, 2016 U.S. Dist. LEXIS 69349, 2016 WL 3039192 at *6-8*.***HN16***[] "Substantial assistance occurs when a defendant affirmatively assists, helps

conceal or fails to act when required to do so, thereby enabling the breach to occur." *Lerner, 459 F.3d at 295* (citation omitted). "Substantial assistance requires the plaintiff to allege that the actions of the aider/abettor proximately caused the harm on which the primary liability is predicated." *Cromer Fin. Ltd. v. Berger, 137 F. Supp. 2d 452, 470 (S.D.N.Y. 2001)*. That is, the injury must "be a direct or reasonably foreseeable result of the conduct." *Id.* The district court correctly determined that SPV's state law claims against the Access Defendants are deficient as a matter of law because SPV failed to adequately plead proximate cause. At most, SPV pleads but-for causation. If the Access Defendants did not provide support and assistance to the feeder funds, the feeder funds would not have collected money from investors. If the money stopped flowing into BLMIS, such that the fraudulent scheme would have collapsed much sooner, staunching OSUS's losses. The link between the Access Defendants' actions (or inactions) and the harm suffered by OSUS is simply too attenuated to constitute proximate cause. As the district court pointed out, "if any entity that injected massive **[*26]** sums into BLMIS could be said to have aided and abetted Madoff's Ponzi scheme, OSUS, which plaintiff claims invested $1.6 billion in BLMIS, would presumably be subject to liability on the same theory." *SPV III, 2016 U.S. Dist. LEXIS 69349, 2016 WL 3039192, at *6*; *see also* *Cromer Fin. Ltd., 137 F. Supp. 2d at 472* (granting motion to dismiss aiding and abetting claims on substantial assistance grounds because "[w]hile the Ponzi scheme may only have been possible because of Bear Stearns' actions, or inaction, Bear Stearns' conduct was not a proximate cause of the Ponzi scheme").

SPV offers two different theories of proximate cause that it proposes to incorporate into an amended complaint. Neither theory can salvage SPV's claims. The first alternate theory is that the Access Defendants, through misleading marketing materials, aided and abetted the BLMIS fraud by providing BLMIS an "air of legitimacy." Appellant's Br. at 64. SPV points to nothing showing OSUS relied on the marketing materials provided by the Access Defendants, was aware of the Access Defendants or even knew of the feeder funds at issue. As noted above, OSUS invested with BLMIS directly, and its investments began before the feeder funds were created. SPV's second alternate theory is that the Access Defendants are liable **[*27]** because they failed to notify "the world at large and international investors in particular" of BLMIS's fraud. Appellant's Br. at 59. This theory of causation is unavailing because the Access Defendants owed neither OSUS nor SPV any fiduciary duty. *See* *Lerner, 459 F.3d at 295* ("The mere inaction of an alleged aider and abettor constitutes substantial assistance only if the defendant owes a fiduciary duty directly to the plaintiff.") (citation omitted)).

CONCLUSION

For the reasons given above, the judgment of the district court is AFFIRMED.

Concur by: Calabresi

Concur

Calabresi, *Circuit Judge*, concurring:

I join in the opinion except for its analysis of personal jurisdiction. It is not that I necessarily disagree with that analysis. But I believe the better course, in circumstances like those before us, is to assume personal jurisdiction arguendo and direct a dismissal with prejudice for failure to state a claim. Our prior case law allows us to do so.

Before *Steel Co. v. Citizens for a Better Environment, 523 U.S. 83, 118 S. Ct. 1003, 140 L. Ed. 2d 210 (1998)*, we, and other circuits, regularly assumed jurisdiction when "the merits question [wa]s more readily resolved . . . ." *Id. at 93-94*. But, in *Steel Co.*, the Supreme Court held that this practice, dubbed the "doctrine of hypothetical jurisdiction," "offend[ed] fundamental principles of separation **[*28]** of powers" and, thus, was impermissible. *Id. at 94, 101*.

Steel Co. does not, however, undermine the appropriateness of our deciding the merits in the current case. *Steel Co.* was concerned with the judiciary's powers under Article III. *See* *id. at 95-98*. Personal jurisdiction, on the other

hand, is concerned with individual rights under the *Due Process Clause*. *Burger King v. Rudzewicz, 471 U.S. 462, 471-72, 105 S. Ct. 2174, 85 L. Ed. 2d 528 (1985)*.

The relevant differences between personal and subject-matter jurisdiction are legion. Parties cannot stipulate to subject-matter jurisdiction, *Great Southern Fire Proof Hotel Co. v. Jones, 177 U.S. 449, 453, 20 S. Ct. 690, 44 L. Ed. 842 (1900)*, but can to personal jurisdiction, *see Burger King, 471 U.S. at 472 n. 14*. Courts have an independent duty to assess subject-matter jurisdiction, *Great Southern, 177 U.S. at 453*, but not personal jurisdiction, *Sinoying Logistics Pte Ltd. v. Yi Da Xin Trading Corp., 619 F.3d 207, 213 (2d Cir. 2010)*. And while subject-matter jurisdiction is an absolute limit on the court's power to adjudicate a claim, *Mansfield, C. & L. M. R. Co. v. Swan, 111 U.S. 379, 382, 4 S. Ct. 510, 28 L. Ed. 462 (1884)*, personal jurisdiction is not, *cf. In re DES Litigation, 7 F.3d 20, 23-24 (2d Cir. 1993)* (explaining that an interlocutory order finding personal jurisdiction cannot be appealed by a prevailing party because a finding of personal jurisdiction is not a "necessary step" for a district court's dismissal of a complaint and entry of judgment). I believe that *Steel Co.* is not controlling in cases of personal jurisdiction. *But see Rationis Enter. Inc. of Panama v. AEP/Borden Indus., 261 F.3d 264, 267-68 (2d Cir. 2001)* (suggesting there is no difference between personal and subject-matter jurisdiction in this regard).

Even if there **[*29]** is no difference in how personal jurisdiction and subject-matter jurisdiction are to be treated, the prior cases would allow us to assume jurisdiction in the circumstances before us. *See Chevron Corp. v. Naranjo, 667 F.3d 232, 246 n. 17 (2d Cir. 2012)* (reaching the merits and declining to "address the personal jurisdictional claims made by some defendants" where the court had personal jurisdiction over other defendants). In *Norton v. Mathews, 427 U.S. 524, 528-31, 96 S. Ct. 2771, 49 L. Ed. 2d 672 (1976)*, the Supreme Court avoided a jurisdictional question, and instead dismissed on the merits. The Court did so because it had already decided the merits question in a companion case. We applied *Norton in Center for Reproductive Law and Policy v. Bush, 304 F.3d 183 (2d Cir. 2002)* ("*Center*"). In *Center*, we directed a dismissal on the merits without reaching an open standing question because the appellants pressed a merits argument that had been squarely rejected in an earlier case. *Id. at 193*. We read *Norton* to allow courts to assume jurisdiction "in those peculiar circumstances where the outcome on the merits has been foreordained" and the court is not "us[ing] the pretermission of the jurisdictional question as a device for reaching a question of law that otherwise would have gone unaddressed." *Center, 304 F.3d at 194* (internal quotation marks omitted).

The *Norton* rule applies here as well. "[T]he outcome on the merits" against the UBS defendants **[*30]** "has been foreordained." We already reached the merits in resolving the claims against the Access defendants, who are, except for the personal jurisdiction issue, identically placed to the UBS defendants. Thus, if we assume jurisdiction we would not be doing so "as a device for reaching a question of law that otherwise would have gone unaddressed," but instead as a means of preventing waste of judicial resources.

We note that the *Norton* rule survived *Steel Co. Steel Co.* specifically distinguished *Norton. Steel Co., 523 U.S. at 98*. And this Court in *Center* affirmed that *Norton* was still good law after *Steel Co. Center*, *304 F.3d at 194*.

For these reasons, I conclude that we can and should assume personal jurisdiction and reach the merits in this case. Moreover, I believe an additional practical consideration favors our doing so here. A dismissal for lack of personal jurisdiction, which must be without prejudice, invites Appellant to seek another jurisdiction in which to bring claims we have already deemed meritless. This result would be doubly wasteful of judicial resources.

Accordingly, while I fully join the rest of the court's opinion, I do not join the discussion of personal jurisdiction as to the UBS defendants. Instead, I would hold in favor of **[*31]** Appellees on the merits, and dismiss the entire suit with prejudice.

Neutral
As of: March 14, 2018 6:01 PM Z

Janvey v. Romero

United States Court of Appeals for the Fourth Circuit

December 6, 2017, Argued; February 21, 2018, Decided

No. 17-1197

Reporter
2018 U.S. App. LEXIS 4108 *; 2018 WL 987801

RALPH JANVEY, Creditor - Appellant, v. PETER ROMERO, Debtor - Appellee.

Prior History: [*1] Appeal from the United States District Court for the District of Maryland, at Baltimore. (1:16-cv-03355-JFM). J. Frederick Motz, Senior District Judge.

Janvey v. Romero, 2017 U.S. Dist. LEXIS 12068 (D. Md., Jan. 30, 2017)

Disposition: AFFIRMED.

Core Terms

bankruptcy court, bad faith, exempt, factors, repay, bad-faith, settle, bankruptcy petition, motivation, settlement, expenses, parties, courts, motion to dismiss, settlement offer, fresh start, disability, reasons, underlying litigation, denial of motion, district court, misconduct, lifestyle, policies, boat

Case Summary

Overview
ISSUE: Whether a bankruptcy court and district court erred in declining to dismiss a debtor's petition under *11 U.S.C.S. § 707(a)*. HOLDINGS: [1]-Although a creditor's judgment, which accounted for 90 percent of debtor's total debt, served as the catalyst for his bankruptcy petition, this single factor was not a per se test for bad faith under *§ 707(a)*, as this would blind a court to the totality of debtor's circumstances, which included his wife's medical condition that entailed substantial expenses for her care; [2]-Nor were debtor's two attempts to settle the underlying judgment evidence of a bad faith motivation for filing a Chapter 7 petition; [3]-Debtor's ability to repay debts did not alone amount to cause for dismissal; [4]-Forcing debtor to repay his debts using exempt assets before resorting to bankruptcy would undercut the entire exemption scheme.

Outcome
The court affirmed the order denying a motion to dismiss debtor's bankruptcy petition.

LexisNexis® Headnotes

Bankruptcy Law > ... > Judicial Review > Standards of Review > Abuse of Discretion

Bankruptcy Law > ... > Bankruptcy > Conversion & Dismissal > Liquidations

Bankruptcy Law > ... > Judicial Review > Standards of Review > Clear Error Review

Bankruptcy Law > ... > Judicial Review > Standards of Review > De Novo Standard of Review

HN1[] Standards of Review, Abuse of Discretion

A court of appeals, like a district court, reviews a bankruptcy court's denial of a motion to dismiss under *11 U.S.C.S. § 707(a)* for abuse of discretion, its factual findings for clear error, and its legal conclusions de novo.

Bankruptcy Law > Exemptions > Claims & Objections

Bankruptcy Law > ... > Business & Corporate Compliance > Bankruptcy > Discharge & Dischargeability

Bankruptcy Law > ... > Business & Corporate Compliance > Bankruptcy > Debtor Benefits & Duties

HN2[] Exemptions, Claims & Objections

The Bankruptcy Code balances the interests of both creditors and debtors in the distribution of an insolvent party's assets. The purpose of the Code is therefore twofold: to convert the estate of the bankrupt into cash and distribute it among creditors and then to give the bankrupt a fresh start. The Code serves the interests of creditors by consolidating the debtor's assets into a broadly defined estate from which, in an equitable and orderly process, the debtor's unsatisfied obligations to creditors are paid to the extent possible. At the same time, the Code aims to grant a fresh start to the honest but unfortunate debtor. This fresh start allows the debtor to restructure his financial obligations, discharge his pre-existing debt, and emerge from bankruptcy with a new capital structure that better reflects financial reality. To ensure that a debtor is able to receive this fresh start, the Code prevents creditors from making claims on certain assets. *11 U.S.C.S. § 522*. These so-called exemptions ensure that individuals are able to actually rehabilitate themselves after the bankruptcy process has concluded.

Bankruptcy Law > ... > Bankruptcy > Discharge & Dischargeability > Individuals With Regular Income

Bankruptcy Law > ... > Bankruptcy > Discharge & Dischargeability > Liquidations

Bankruptcy Law > ... > Bankruptcy > Discharge & Dischargeability > Reorganizations

HN3[] Discharge & Dischargeability, Individuals With Regular Income

Although the interests of creditors and debtors are at odds during insolvency -- the creditor would like to be paid in full and the debtor would like to pay as little as possible -- as a general matter, the Bankruptcy Code's balance benefits creditors and debtors alike. If debtors had to pay their creditors no matter what, or if they were forced to give up all their assets before they could discharge their debts, individuals and businesses would be less likely to borrow money. In protecting certain assets from creditor claims, the Code incentivizes individuals to incur debt and thereby support both creditors and our capital markets. Similarly, by ensuring that creditors receive a fair and predictable distribution of assets, the Code reduces the risks creditors face and allows creditors to account for the risk that a borrower will fail to repay. The benefit of these decreased risks is then passed on to debtors in the form of lower interest rates. The fresh start policy is therefore of public as well as private interest. In furtherance of this dual mandate, the Code supplies various avenues of relief to debtors seeking to discharge their debts.

Bankruptcy Law > ... > Bankruptcy > Discharge & Dischargeability > Liquidations

Bankruptcy Law > ... > Bankruptcy > Conversion & Dismissal > Liquidations

HN4[] Discharge & Dischargeability, Liquidations

Chapter 7 allows debtors to discharge their outstanding debts in exchange for liquidating their nonexempt assets and distributing them to their creditors. Chapter 7 also supplies various tools for bankruptcy courts to use in policing the Bankruptcy Code's enduring tension between debtors and creditors. *11 U.S.C.S. § 707(a)* sets forth the grounds on which a Chapter 7 bankruptcy petition may be dismissed. It states that a court may dismiss a case under this chapter only after notice and a hearing and only for cause, including -- (1) unreasonable delay by the debtor that is prejudicial to creditors; (2) nonpayment of any fees or charges required under Chapter 123 of Title 28; and (3) failure of the debtor in a voluntary case to file, within 15 days or such additional time as the court may allow after the filing of the petition commencing such case, the information required by *11 U.S.C.S. § 521(a)(1)*, but only on a motion by the United States trustee.

Bankruptcy Law > ... > Bankruptcy > Conversion & Dismissal > Liquidations

Governments > Legislation > Interpretation

HN5[] Conversion & Dismissal, Liquidations

"Cause" is an open-ended term. It is not defined in *11 U.S.C.S. § 707(a)*, and the examples provided are illustrative rather than exhaustive. *11 U.S.C.S. § 102(3)* (noting that for purposes of the Bankruptcy Code, "includes" and "including" are not limiting. Bankruptcy courts are therefore left to determine case by case what constitutes valid cause for dismissal of a Chapter 7 bankruptcy petition.

Bankruptcy Law > Conversion & Dismissal > Lack of Good Faith

Bankruptcy Law > ... > Bankruptcy > Conversion & Dismissal > Liquidations

HN6[] Conversion & Dismissal, Lack of Good Faith

For the most part, courts have recognized that a debtor's bad faith in filing may constitute cause for dismissal under *11 U.S.C.S. § 707(a)*. The United States Court of Appeals for the Fourth Circuit thinks the majority view is the sounder one, because it is the most helpful in preventing serious abuses of the bankruptcy process. But acknowledging that bad faith may constitute "cause" under *§ 707(a)* also requires that the remedy of dismissal be reserved for cases of real misconduct. Those courts that have found that bad faith in filing for bankruptcy can constitute cause for dismissal have counseled caution in dispensing the remedy of dismissal for bad faith because of the need to maintain the balance of remedies in bankruptcy. They have accordingly emphasized that the bar for finding bad faith is a high one. In short, bad faith exists only where the petitioner has abused the provisions, purpose, or spirit of bankruptcy law.

Bankruptcy Law > Conversion & Dismissal > Lack of Good Faith

Bankruptcy Law > ... > Bankruptcy > Conversion & Dismissal > Liquidations

HN7[] Conversion & Dismissal, Lack of Good Faith

For purposes of cause for dismissal under *11 U.S.C.S. § 707(a)*, the concept of bad faith does not lend itself to a strict formula. Courts must consider the totality of the circumstances underlying each case to determine whether a

debtor has acted in bad faith. To aid in this effort, bankruptcy courts have developed a number of multifactor tests. These tests are meant to be guides only. A bankruptcy court need not mechanically tick off each factor and tally up its tick-marks at the end. It may be the case that many factors are relevant, or it may be the case that relatively few of them are. It all depends. Evaluating these factors and their comparative relevance is a discretionary exercise that is best left to bankruptcy judges. After all, many of the potentially pertinent factors involve credibility determinations or exercises in fact-finding.

Bankruptcy Law > Conversion & Dismissal > Lack of Good Faith

Bankruptcy Law > ... > Bankruptcy > Conversion & Dismissal > Liquidations

HN8[] Conversion & Dismissal, Lack of Good Faith

The 11 factor bad-faith test set forth by the United States Bankruptcy Court for the Eastern District of Virginia in McDow represent a distillation of the various totality of the circumstances tests courts have applied in determining whether a debtor's actions amounted to bad-faith cause for dismissal under *11 U.S.C.S. § 707(a)*. They are meant to represent the factors that are typically considered in that analysis. Theses factors are: the debtor's lack of candor and completeness in his statements and schedules; the debtor has sufficient resources to repay his debts, and leads a lavish lifestyle; the debtor's motivation in filing is to avoid a large single debt incurred through conduct akin to fraud, misconduct, or gross negligence; and the debtor's lack of attempt to repay creditors; the debtor's concealment or misrepresentation of assets and/or sources of income; the debtor's petition is part of a deliberate and persistent pattern of evading a single creditor; the debtor is overutilizing the protection of the Bankruptcy Code to the detriment to his creditors; the debtor reduced his creditors to a single creditor prior to filing the petition; the debtor's payment of debts to insider creditors; the debtor's procedural gymnastics that have the effect of frustrating creditors; and the unfairness of the debtor's use of the bankruptcy process.

Bankruptcy Law > Conversion & Dismissal > Lack of Good Faith

Bankruptcy Law > ... > Bankruptcy > Conversion & Dismissal > Liquidations

HN9[] Conversion & Dismissal, Lack of Good Faith

The fact that a bankruptcy petition was filed in response to a single debt need not alone constitute bad-faith cause for dismissal under *11 U.S.C.S. § 707(a)*. Almost every bankruptcy case is filed because a creditor is pursuing a debtor. The purpose of bankruptcy law, after all, is to provide a procedure by which certain insolvent debtors can reorder their affairs, make peace with their creditors, and enjoy a new opportunity in life. A person becomes insolvent when he is no longer able to meet his financial obligations as they become due. *11 U.S.C.S. § 101(32)(A)*. This may happen over time, or it may happen very suddenly. But in every case, the debtor reaches a tipping point. That may well happen because of a single additional debt. Equating a decision to file for bankruptcy in response to a sizeable debt with cause for dismissal would fault debtors for using the Bankruptcy Code in precisely the way Congress intended. Without additional evidence of fraud or misconduct, the fact that a debtor filed for bankruptcy in response to a single large debt is not sufficient for a finding of bad faith. None of this is to say that courts may not consider the nature of a debtor's motivation to file for bankruptcy. The fact that a bankruptcy petition was filed to skirt the collection efforts of a single creditor may well prove relevant in the overall bad-faith analysis.

Bankruptcy Law > ... > Business & Corporate Compliance > Bankruptcy > Claims

Civil Procedure > Settlements > Settlement Agreements

HN10[] **Bankruptcy Law, Claims**

The law encourages voluntary settlement of disputes. Settlement yields both private and public benefits. It spares the parties substantial costs in terms of time and money, and it lightens the docket of a resource-strapped judicial system. In line with these principles, debtors and creditors remain free to settle their debts among themselves outside the courtroom and before resorting to bankruptcy. The tools at their disposal are varied. A creditor, for instance, may choose to forbear from immediately collecting a debt and thereby offer the debtor a momentary reprieve. Or he may allow the debtor to refinance or modify his loan in order to provide a more permanent solution. Settlement is simply a way creditors and debtors can avoid protracted litigation and resolve their disputes in a mutually satisfactory manner. But the fact that parties often settle does not mean that the failure to settle should deprive debtors of the backstop provided by bankruptcy law. Far from amounting to "blackmail," the backstop of bankruptcy encourages parties to come to the table to reach an agreement when debts cannot be paid in full. It is altogether right that the parties can rest assured that, should settlement fail, bankruptcy will provide a way for them to resolve their case.

Bankruptcy Law > ... > Business & Corporate Compliance > Bankruptcy > Claims

Bankruptcy Law > ... > Avoidance > Prepetition Transfers > Preferential Transfers

HN11[] **Bankruptcy Law, Claims**

There are limitations on settlement in bankruptcy, among them the prohibition on preferred treatment of certain creditors in the immediate prepetition period. *11 U.S.C.S. § 547*. But the Bankruptcy Code's voidable preference provisions are designed to prevent parties from privileging some creditors at the expense of others; they are not designed to hinder the efforts of parties to settle to avoid bankruptcy in the first place.

Bankruptcy Law > ... > Bankruptcy > Conversion & Dismissal > Liquidations

HN12[] **Conversion & Dismissal, Liquidations**

A debtor's ability to repay debts does not alone amount to cause for dismissal under *11 U.S.C.S. § 707(a)*. Such a conclusion also follows logically from the Bankruptcy Code's fresh-start philosophy. A penniless start is not a fresh start. Were absolute depletion of one's assets a prerequisite for bankruptcy relief, debtors and their families would be left destitute and without the means to become productive members of society. This would increase the strain on our social safety net by increasing the number of people who might potentially qualify for government benefits.

Bankruptcy Law > Exemptions > Claims & Objections

HN13[] **Exemptions, Claims & Objections**

Forcing a debtor to repay his debts using exempt assets before resorting to bankruptcy would undercut the entire exemption scheme that Congress designed. The historical purpose of bankruptcy exemptions has been to protect a debtor from his creditors, to provide him with the basic necessities of life so that even if his creditors levy on all of his nonexempt property, the debtor will not be left destitute and a public charge. Bankruptcy exemptions are meant to afford the debtor some economic and social stability, which is important to the fresh start guaranteed by bankruptcy. They represent a careful balance of the difficult choices that exemption limits impose on debtors with the economic harm that exemptions visit on creditors.

Bankruptcy Law > ... > Judicial Review > Standards of Review > Abuse of Discretion

Bankruptcy Law > ... > Bankruptcy > Conversion & Dismissal > Liquidations

Bankruptcy Law > ... > Discharge & Dischargeability > Liquidations > Denial of Discharge

HN14[] **Standards of Review, Abuse of Discretion**

It remains for bankruptcy judges to detect in the first instance those cases of fraud upon the court and creditors that constitute cause for dismissal under *11 U.S.C.S. § 707(a)* or reason for a denial of discharge under the scenarios set forth in *11 U.S.C.S. § 727(a)*. The standard of review -- one of abuse of discretion -- is of paramount importance.

Counsel: ARGUED: Kevin Marshall Sadler, BAKER BOTTS L.L.P., Palo Alto, California, for Appellant.

Kevin Gerald Hroblak, WHITEFORD TAYLOR & PRESTON, L.L.P., Baltimore, Maryland, for Appellee.

ON BRIEF: Scott D. Powers, Stephanie F. Cagniart, BAKER BOTTS L.L.P., Austin, Texas, for Appellant.

Judges: Before GREGORY, Chief Judge, and WILKINSON and HARRIS, Circuit Judges. Judge Wilkinson wrote the opinion, in which Chief Judge Gregory and Judge Harris joined.

Opinion by: WILKINSON

Opinion

WILKINSON, Circuit Judge:

Appellee Peter Romero filed a Chapter 7 bankruptcy petition after he was found liable for $1.275 million to the victims of a multibillion-dollar Ponzi scheme. Appellant Ralph Janvey, the receiver in the Ponzi scheme litigation, moved to dismiss Romero's bankruptcy petition for cause under *11 U.S.C. § 707(a)*. The bankruptcy court denied the motion, and the district court affirmed the bankruptcy court's order. We focus only on the matter before us—that is, whether Romero's decision to file for bankruptcy rises to the level of bad faith and therefore constitutes cause for dismissal under **[*2]** *§ 707(a)*. Because the bankruptcy court did not abuse its discretion in denying Janvey's motion to dismiss, we affirm.

I.

A.

We begin with the facts of the underlying litigation, which hover above and around the present action but do not strictly pertain to the question before us. They are, to borrow a term from film, the McGuffin in this case.[1]

Peter Romero had a storied career in the Foreign Service. He served for twenty-four years with the State Department, most prominently as an Ambassador and as Assistant Secretary of State for Western Hemisphere Affairs. Upon retiring from the Foreign Service, Romero founded a private consulting company to advise companies that do business overseas. One of his clients was the Stanford Financial Group (Stanford). Romero consulted for Stanford for approximately seven years. He earned a total of $700,000 in fees plus reimbursements for travel expenses and returns on his own Stanford investments. While Romero was working for Stanford, the company was

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[1] *See* 3 *Oxford English Dictionary Additions Series* 285 (John Simpson & Michael Proffitt eds., 1997) (defining "McGuffin" as "a particular event, object, factor, etc., which assumes great significance to the characters and acts as the impetus for the sequence of events depicted, although often proving tangential to the plot as it develops").

being used to carry out a multibillion-dollar Ponzi scheme. The scheme was unearthed in 2009, at which point Romero cut ties with Stanford.

The Securities and Exchange Commission **[*3]** sued Stanford, its affiliated entities, and its leadership in the Northern District of Texas. That court appointed Ralph Janvey to be the receiver in the litigation. Pursuant to his duties as receiver, Janvey sued Romero to recover for victims of the scheme the payments Romero had received while consulting for Stanford. Romero participated in mediation and offered to settle with Janvey. But mediation proved unsuccessful, and Janvey rejected the settlement offer without proposing a counteroffer. Romero ultimately lost at trial, and Janvey was awarded approximately $1.275 million in damages, interest, and fees. Romero appealed the judgment to the Fifth Circuit with no success. *See Janvey v. Romero, 817 F.3d 184 (5th Cir. 2016)*. While the appeal was pending, he again offered to settle with Janvey, who again rejected the offer without a counteroffer. Janvey instead moved for leave to register the judgment in California under *28 U.S.C. § 1963* on the belief that Romero had property there. The district court granted the motion.

B.

And so we arrive at the present bankruptcy action. Romero voluntarily filed a Chapter 7 bankruptcy petition in the District of Maryland the day after the judgment against him was certified in California. At the time, Romero's **[*4]** financial situation was as follows:

Assets: Romero's assets totaled more than $5.348 million. The majority of these assets, however, were statutorily exempt. Nobody challenged these claimed exemptions. Among Romero's exempt assets were three real properties he owned with his wife as tenants by the entirety, one of which was their home and the others of which were rental properties. Romero also claimed as exempt pension, retirement, and benefit plans. Romero's nonexempt assets included one car and two boats, which he turned over to the Chapter 7 trustee for administration. The trustee sold both the car and one of the boats, and Romero agreed to pay the docking and insurance fees for the other boat until it was sold.[2]

Unsecured Debts: Janvey's judgment accounted for roughly 90% of Romero's unsecured debt when he filed for bankruptcy. The remainder was composed of debts with two law firms for unpaid legal fees totaling approximately $150,000.[3]

Expenses: Most prominent among Romero's expenses were his wife's medical costs, which averaged $12,000 per month. Romero's wife had contracted a bacterial brain infection in 2013 that left her incapacitated and in need of extensive care. Until recently, **[*5]** the majority of Romero's wife's medical expenses were covered by her three disability policies and Romero employed a live-in caretaker. After Romero filed for bankruptcy, however, two of his wife's three disability policies were terminated; meanwhile, her condition slightly improved and Romero was able to scale back to daily care. Romero also listed entertainment expenses of $1,000 per month, most of which went to the docking and other costs for the boat he had turned over to the trustee.

Income: Romero reported monthly income approximately $350 less than his monthly expenses. Romero and his wife were both unemployed—she because of her illness and he because he had been unable to find work after the Stanford scheme was discovered. Their combined monthly income came entirely from Romero's State Department pension plan, their two rental properties, social security, and long-term disability.

More than six months after Romero filed for bankruptcy, Janvey moved to dismiss his petition under *11 U.S.C. § 707(a)* on the ground that Romero had abused the bankruptcy process to avoid Janvey's judgment. The bankruptcy court denied the motion. *See In re Romero, 557 B.R. 875 (Bankr. D. Md. 2016)*. It acknowledged that bad faith can constitute cause for dismissal **[*6]** under *§ 707(a)*, but it found that Romero had not acted in bad faith. In doing so, it applied the eleven bad-faith factors set forth in *McDow v. Smith, 295 B.R. 69 (Bankr. E.D. Va. 2003)*. The

[2] The remaining boat sold after Janvey moved to dismiss Romero's petition.

[3] Romero initially listed three unpaid credit card debts among his unsecured debts. Those cards, however, were primarily in his wife's name, and Romero later amended his petition to reflect that all three debts had been paid.

bankruptcy court acknowledged that Romero's "primary motivation in filing the petition was to address [Janvey]'s judgment" but that he also "faced the inability to earn a living, his wife's illness and care needs, the pending termination of two disability policies, and aggressive and costly litigation tactics by [Janvey]." *Romero, 557 B.R. at 883-84*. The court also noted that Romero had twice tried and failed to settle the matter in the course of the underlying litigation. *Id. at 884*. It observed that most of Romero's assets were statutorily exempt and that he "lives a comfortable, but not exorbitant, lifestyle. Perhaps his primary discretionary expense is eating out at restaurants. He belongs to no country clubs or social clubs." *Id. at 883*. The court accordingly denied Janvey's motion to dismiss and ultimately granted Romero a discharge under *11 U.S.C. § 727*.

Janvey appealed the denial of his motion to dismiss and—by inference, at least—the eventual discharge of Romero's debt to the district court, which affirmed the order of the bankruptcy court. He now appeals to this court. ***HN1***[] We, like the district court, review **[*7]** the bankruptcy court's denial of a motion to dismiss for abuse of discretion, its factual findings for clear error, and its legal conclusions de novo. *See In re Jenkins, 784 F.3d 230, 234 (4th Cir. 2015)*; *In re Piazza, 719 F.3d 1253, 1271 (11th Cir. 2013)*. Janvey's claims boil down to an accusation that Romero has abused the bankruptcy process and should therefore be ineligible for its protections. For the reasons that follow, we do not agree.

II.

A bit of background may be helpful in understanding the operation of the relevant statutes. ***HN2***[] The Bankruptcy Code balances the interests of both creditors and debtors in the distribution of an insolvent party's assets. The purpose of the Code is therefore twofold: "to convert the estate of the bankrupt into cash and distribute it among creditors and then to give the bankrupt a fresh start." *Kokoszka v. Belford, 417 U.S. 642, 645-46, 94 S. Ct. 2431, 41 L. Ed. 2d 374 (1974)* (quoting *Burlingham v. Crouse, 228 U.S. 459, 473, 33 S. Ct. 564, 57 L. Ed. 920 (1913))*. The Code serves the interests of creditors by "consolidat[ing] the debtor's assets into a broadly defined estate from which, in an equitable and orderly process, the debtor's unsatisfied obligations to creditors are paid to the extent possible." *In re Andrews, 80 F.3d 906, 909-10 (4th Cir. 1996)* (footnote omitted).

At the same time, the Code aims to "grant a 'fresh start' to the 'honest but unfortunate debtor.'" *Marrama v. Citizens Bank of Mass., 549 U.S. 365, 367, 127 S. Ct. 1105, 166 L. Ed. 2d 956 (2007)* (quoting *Grogan v. Garner, 498 U.S. 279, 286, 287, 111 S. Ct. 654, 112 L. Ed. 2d 755 (1991))*. This fresh start allows the debtor to "restructure [his] financial **[*8]** obligations, discharge [his] pre-existing debt, and emerge from bankruptcy with a new capital structure that better reflects financial reality." *Bosiger v. U.S. Airways, 510 F.3d 442, 448 (4th Cir. 2007)*. To ensure that a debtor is able to receive this fresh start, the Code prevents creditors from making claims on certain assets. *See 11 U.S.C. § 522*. These so-called exemptions ensure that individuals are able to actually rehabilitate themselves after the bankruptcy process has concluded.

HN3[] Although the interests of creditors and debtors are at odds during insolvency—the creditor would like to be paid in full and the debtor would like to pay as little as possible—as a general matter, the Code's balance benefits creditors and debtors alike. *See generally* Douglas C. Baird, *Bankruptcy's Uncontested Axioms*, *108 Yale L.J. 573, 583-86 (1998)*; Thomas H. Jackson, *The Fresh-Start Policy in Bankruptcy Law*, *98 Harv. L. Rev. 1393, 1424-47 (1985)*. If debtors had to pay their creditors no matter what, or if they were forced to give up all their assets before they could discharge their debts, individuals and businesses would be less likely to borrow money. In protecting certain assets from creditor claims, the Code incentivizes individuals to incur debt and thereby support both creditors and our capital markets. Similarly, by ensuring that **[*9]** creditors receive a fair and predictable distribution of assets, the Code reduces the risks creditors face and allows creditors to account for the risk that a borrower will fail to repay. The benefit of these decreased risks is then passed on to debtors in the form of lower interest rates. The fresh start policy is therefore "of public as well as private interest." *Local Loan Co. v. Hunt, 292 U.S. 234, 244, 54 S. Ct. 695, 78 L. Ed. 1230 (1934)*.

In furtherance of this dual mandate, the Code supplies various avenues of relief to debtors seeking to discharge their debts. Relevant here is ***HN4***[] Chapter 7, which allows debtors to discharge their outstanding debts in exchange for liquidating their nonexempt assets and distributing them to their creditors. Chapter 7 also supplies various tools for bankruptcy courts to use in policing the Code's enduring tension between debtors and creditors.

This case involves *§ 707(a)*, which sets forth the grounds on which a Chapter 7 bankruptcy petition may be dismissed:

> The court may dismiss a case under this chapter only after notice and a hearing and only for cause, including—
>
> (1) unreasonable delay by the debtor that is prejudicial to creditors;
>
> (2) nonpayment of any fees or charges required under chapter 123 of title 28; and
>
> (3) failure of the **[*10]** debtor in a voluntary case to file, within fifteen days or such additional time as the court may allow after the filing of the petition commencing such case, the information required by *paragraph (1) of section 521(a)*, but only on a motion by the United States trustee.

11 U.S.C. § 707(a).

HN5[] "Cause" is an open-ended term. It is not defined in *§ 707(a)*, and the examples provided are illustrative rather than exhaustive. *See id. § 102(3)* (noting that for purposes of the Code, "'includes' and 'including' are not limiting"); *Fed. Land Bank of St. Paul v. Bismarck Lumber Co., 314 U.S. 95, 100, 62 S. Ct. 1, 86 L. Ed. 65 (1941)* ("[T]he term 'including' is not one of all-embracing definition, but connotes simply an illustrative application of the general principle."). Bankruptcy courts are therefore left to determine case by case what constitutes valid cause for dismissal of a Chapter 7 bankruptcy petition.

III.

A.

HN6[] For the most part, courts have recognized that a debtor's bad faith in filing may constitute cause for dismissal under *§ 707(a)*. *See In re Krueger, 812 F.3d 365, 370 (5th Cir. 2016)* ("[A] debtor's bad faith in the bankruptcy process can serve as the basis of a dismissal 'for cause' . . . ."); *In re Schwartz, 799 F.3d 760, 764 (7th Cir. 2015)* ("[A]n unjustified refusal to pay one's debts is a valid ground under *11 U.S.C. § 707(a)* to deny a discharge of a bankrupt's debts."); *Piazza, 719 F.3d at 1260-61* ("[T]he power to dismiss 'for cause' in *§ 707(a)* includes the power to involuntarily dismiss a Chapter **[*11]** 7 case based on prepetition bad faith."); *In re Tamecki, 229 F.3d 205, 207 (3d Cir. 2000)* ("*Section 707(a)* allows a bankruptcy court to dismiss a petition for cause if the petitioner fails to demonstrate his good faith in filing."); *In re Zick, 931 F.2d 1124, 1127 (6th Cir. 1991)* ("[L]ack of good faith is a valid basis of decision in a 'for cause' dismissal by a bankruptcy court."). *But see In re Padilla, 222 F.3d 1184, 1191 (9th Cir. 2000)* ("[B]ad faith as a general proposition does not provide 'cause' to dismiss a Chapter 7 petition under *§ 707(a)*."); *In re Huckfeldt, 39 F.3d 829, 832 (8th Cir. 1994)* (adopting a "narrow, cautious" approach that requires "extreme misconduct falling outside the purview of more specific Code provisions").

We think the majority view is the sounder one, because it is the most helpful in preventing serious abuses of the bankruptcy process. But acknowledging that bad faith may constitute "cause" under *§ 707(a)* also requires that the remedy of dismissal be reserved for cases of real misconduct. Those courts that have found that bad faith in filing for bankruptcy can constitute cause for dismissal have counseled "[c]aution in dispensing the remedy of dismissal for bad faith" because of "the need . . . to maintain the balance of remedies in bankruptcy." *In re Khan, 172 B.R. 613, 626 (Bankr. D. Minn. 1994)*. They have accordingly emphasized that the bar for finding bad faith is a high one. *See, e.g., Zick, 931 F.2d at 1129* (explaining that bad faith **[*12]** exists "only in those egregious cases that entail concealed or misrepresented assets and/or sources of income, and excessive and continued expenditures, lavish life-style, and intention to avoid a large single debt based on conduct akin to fraud, misconduct, or gross negligence"). In short, bad faith exists only where "the petitioner has abused the provisions, purpose, or spirit of bankruptcy law." *Tamecki, 229 F.3d at 207*.

B.

HN7[] The concept of bad faith "does not lend itself to a strict formula." *Piazza, 719 F.3d at 1271*. Courts must consider the totality of the circumstances underlying each case to determine whether a debtor has acted in bad faith. To aid in this effort, bankruptcy courts have developed a number of multifactor tests. *See, e.g., McDow, 295 B.R. at 79 n.22* (proposing eleven factors); *In re Griffieth, 209 B.R. 823, 827 (Bankr. N.D.N.Y. 1996)* (proposing six factors); *In re Spagnolia, 199 B.R. 362, 365 (Bankr. W.D. Ky. 1995)* (proposing fourteen factors). These tests are meant to be guides only. A bankruptcy court need not mechanically tick off each factor and tally up its tick-marks at

the end. It may be the case that many factors are relevant, or it may be the case that relatively few of them are. It all depends. Evaluating these factors and their comparative relevance is a discretionary exercise that is best left to bankruptcy judges. After all, many of the **[*13]** potentially pertinent factors involve credibility determinations or exercises in fact-finding. *See, e.g., Griffieth, 209 B.R. at 827* ("debtor's failure to make significant lifestyle changes"); *Spagnolia, 199 B.R. at 365* ("an intent to avoid a large single debt"); *id.* ("debtor is paying debts to insiders").

The bankruptcy court in this case employed the eleven-factor bad-faith test set forth in *McDow, 295 B.R. at 79 n.22*. ***HN8***[] Those eleven factors represent a distillation of the various "totality of the circumstances test[s]" courts have applied in determining whether a debtor's actions amounted to bad-faith cause for dismissal. *Id. at 79*. They are meant to represent the "factors [that] are typically considered" in that analysis. *Id. at 79 n.22*. Among them are "[t]he debtor's lack of candor and completeness in his statements and schedules"; "[t]he debtor has sufficient resources to repay his debts, and leads a lavish lifestyle"; "[t]he debtor's motivation in filing is to avoid a large single debt incurred through conduct akin to fraud, misconduct, or gross negligence"; and "[t]he debtor's lack of attempt to repay creditors." *See id.*[4]

Careful consideration of the *McDow* factors here—aided by lengthy briefing from the parties, dozens of exhibits, and a three-hour evidentiary hearing—led the bankruptcy **[*14]** court to conclude that Romero had not acted in bad faith. While Janvey's judgment may have been Romero's "primary motivation in filing," the bankruptcy court found that it was not the only reason he filed. *Romero, 557 B.R. at 883*. Romero's wife was suffering from a brain infection that required extensive care and left her "100% incapacitated for work." *Id. at 879*. The bankruptcy court found that this infection had impaired her motor skills, balance, and eyesight to such an extent that she and Romero had to remodel their home so that she could live on the first floor. *Id.* It also found that Romero's wife's condition had at one point necessitated employment of a live-in caretaker and that it still required "a daily home caregiver, except for Sundays and part of Saturdays when [Romero] manages his wife's care on his own." *Id.* Moreover, the court noted that two of Romero's wife's disability policies—which together comprised the majority of her disability payments—were about to end when he filed for bankruptcy. *Id. at 879, 883-84*. It predicted that the subsequent termination of these policies would result in an increase in the couple's out-of-pocket medical expenses, which were already steep at $55,000 in the year before Romero filed. *Id. at 884* **[*15]** .

The bankruptcy court also found that, as a result of his affiliation with Stanford, Romero had "found it impossible to obtain work." *Id. at 883*. And he still owed approximately $150,000 in legal fees from the underlying litigation, in which Janvey had employed "aggressive and costly litigation tactics." *Id. at 884*. The bankruptcy court commended Romero for being candid, forthcoming, timely, and cooperative throughout both the instant and the underlying litigation. It explained that he had surrendered his nonexempt assets and twice attempted to settle with Janvey. The bankruptcy court also found that Romero's lifestyle was "comfortable, but not exorbitant." *Id. at 883*. And it found nothing duplicitous about Romero's desire to preserve exempt assets he and his wife would "be required to live off" in the future. *Id. at 885*. In light of these circumstances, the bankruptcy court concluded that no "cause" for dismissal existed in this case.

IV.

Janvey raises three primary objections to the bankruptcy court's denial of his motion to dismiss. First, he argues that Romero should not be allowed to benefit from the Code's protections because he filed for bankruptcy solely to avoid Janvey's judgment. Second, he suggests that Romero's **[*16]** efforts to settle the underlying litigation betrayed his bad-faith motive. And finally, Janvey maintains that Romero's petition ought to be dismissed on the basis of his substantial assets and attendant ability to pay the judgment.

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[4] The other seven factors are: "[t]he debtor's concealment or misrepresentation of assets and/or sources of income"; "[t]he debtor's petition is part of a 'deliberate and persistent pattern' of evading a single creditor"; "[t]he debtor is 'overutilizing the protection of the Code' to the detriment to his creditors"; "[t]he debtor reduced his creditors to a single creditor prior to filing the petition"; "[t]he debtor's payment of debts to insider creditors"; "[t]he debtor's 'procedural gymnastics' that have the effect of frustrating creditors"; and "[t]he unfairness of the debtor's use of the bankruptcy process." *McDow, 295 B.R. at 79 n.22*.

Each of these objections is rooted in a factor that may well prove relevant to the bad-faith analysis. *See McDow, 295 B.R. at 79 n.22* (listing as potentially relevant factors "[t]he debtor's motivation in filing is to avoid a large single debt incurred through" improper conduct; "[t]he debtor's lack of attempt to repay creditors"; and the debtor's "sufficient resources to repay his debts"). But there is a risk in elevating any single factor above all others as the sine qua non of bad faith. And yet this is precisely what Janvey's objections would have us do.

A.

Janvey first objects that bankruptcy should be unavailable to Romero because he seeks to avoid a single large debt—namely, Janvey's judgment against him. This objection is flawed for two reasons.

As a factual matter, it is simply not the case that Romero filed for bankruptcy solely to avoid the judgment. The bankruptcy court found that Romero filed for many reasons. *Romero, 557 B.R. at 883-84*. Chief among his motivations was his wife's medical condition, **[*17]** which left her totally incapacitated and entailed substantial expenses for her care. Additionally, Romero had multiple debts. Aside from to the $1.275 million he owed Janvey, he also owed debts to two separate law firms totaling approximately $150,000. The fact that Janvey's judgment accounted for roughly 90% of Romero's total debt does not negate those other claims. In fact, courts have declined to dismiss Chapter 7 petitions filed in response to debts that constitute similarly large fractions of the debtor's total debt. *See In re Bage, No. 13-33367, 2014 Bankr. LEXIS 4069, 2014 WL 4749072, at *2, *5 (Bankr. N.D. Ohio Sept. 24, 2014)* (denying a motion to dismiss where litigation-related debt accounted for more than 90% of the total unsecured debt); *In re Ajunwa, No. 11-11363 (ALG), 2012 Bankr. LEXIS 4096, 2012 WL 3820638, at *1, *9 (Bankr. S.D.N.Y. Sept. 4, 2012)* (denying a motion to dismiss where one judgment "accounted for over 90% of the total claims listed").

As a legal matter, ***HN9***[] the fact that a bankruptcy petition was filed in response to a single debt need not alone constitute bad-faith cause for dismissal. "Almost every bankruptcy case is filed because a creditor is pursuing a debtor." *In re Bushyhead, 525 B.R. 136, 149 (Bankr. N.D. Okla. 2015)*. The purpose of bankruptcy law, after all, "is to provide a procedure by which certain insolvent debtors can reorder their affairs, make peace with their creditors, and enjoy 'a new opportunity in life.'" *Grogan, 498 U.S. at 286* (quoting **[*18]** *Local Loan Co., 292 U.S. at 244*). A person becomes insolvent when he is no longer able to meet his financial obligations as they become due. *See 11 U.S.C. § 101(32)(A)*. This may happen over time, or it may happen very suddenly. But in every case, the debtor reaches a tipping point. That may well happen because of a single additional debt. And that debt may be either large or small. It may be the result of litigation, or it may be the product of a large hospital bill or a decline in the housing market. Regardless, equating a decision to file for bankruptcy in response to a sizeable debt with cause for dismissal would fault debtors for using the Code in precisely the way Congress intended. As one bankruptcy court has observed, "if filing bankruptcy to avoid the payment of a debt was cause for dismissal, no debtor would ever be able to file a bankruptcy case." *In re Uche, 555 B.R. 57, 62 (Bankr. M.D. Fla. 2016)*.

For these reasons, courts have frequently held that without additional evidence of fraud or misconduct, the fact that a debtor filed for bankruptcy in response to a single large debt is not sufficient for a finding of bad faith. *See, e.g., In re Chovev, 559 B.R. 339, 347 (Bankr. E.D.N.Y. 2016)*; *In re McVicker, 546 B.R. 46, 51 (N.D. Ohio 2016)*; *In re Gutierrez, 528 B.R. 1, 15 (Bankr. D. Vt. 2014)*; *In re Grullon, No. 13-11716 (ALG), 2014 Bankr. LEXIS 2238, 2014 WL 2109924, at *3 (Bankr. S.D.N.Y. May 20, 2014)*; *In re Mazzella, No. 09-78449-478, 2010 Bankr. LEXIS 4459, 2010 WL 5058395, at *6 (Bankr. E.D.N.Y. Dec. 6, 2010)*; *In re Glunk, 342 B.R. 717, 736 (Bankr. E.D. Pa. 2006)*.

None of this is to say that courts may not consider the nature of a debtor's motivation to file for bankruptcy. The fact that a bankruptcy **[*19]** petition was filed to skirt the collection efforts of a single creditor may well prove relevant in the overall bad-faith analysis. *See McDow, 295 B.R. at 79 n.22* (listing this factor among others); *Griffieth, 209 B.R. at 827* (same); *Spagnolia, 199 B.R. at 365* (same). Indeed, both the district and bankruptcy courts below took note of the fact that Janvey's judgment served as the catalyst for Romero's bankruptcy petition. But Janvey now attempts to transform this single factor into a per se test for bad faith. Because such an attempt would blind us to the totality of Romero's circumstances, we reject it.

B.

Janvey's second objection attributes bad-faith motivation to Romero's two attempts to settle the underlying judgment. He suggests that Romero was trying to pressure him into accepting a mere fraction of his judgment by casting bankruptcy as the alternative to settlement.

Janvey was, of course, well within his rights to reject Romero's settlement offers. But we find groundless the notion that Romero's attempts to settle with a judgment creditor constitute cause to dismiss his case. ***HN10***[] The law encourages voluntary settlement of disputes. *See* *United States v. Cannons Eng'g Corp., 899 F.2d 79, 84 (1st Cir. 1990)* ("[I]t is the policy of the law to encourage settlements."); *Bank of Am. Nat. Tr. & Sav. Ass'n v. Hotel Rittenhouse Assocs., 800 F.2d 339, 344 (3d Cir. 1986)* (describing "the strong public interest in encouraging settlement **[*20]** of private litigation"). Settlement yields both private and public benefits. It spares the parties substantial costs in terms of time and money, and it lightens the docket of a resource-strapped judicial system.

In line with these principles, debtors and creditors remain free to settle their debts among themselves outside the courtroom and before resorting to bankruptcy. The tools at their disposal are varied. A creditor, for instance, may choose to forbear from immediately collecting a debt and thereby offer the debtor a momentary reprieve. Or he may allow the debtor to refinance or modify his loan in order to provide a more permanent solution. Settlement is simply a way creditors and debtors can avoid protracted litigation and resolve their disputes in a mutually satisfactory manner.

But the fact that parties often settle does not mean that the failure to settle should deprive debtors of the backstop provided by bankruptcy law. Far from amounting to "blackmail," Appellant's Br. at 38, the backstop of bankruptcy encourages parties to come to the table to reach an agreement when debts cannot be paid in full. It is altogether right that the parties can rest assured that, should settlement **[*21]** fail, bankruptcy will provide a way for them to resolve their case.

HN11[] There are, to be sure, limitations on settlement in bankruptcy, among them the prohibition on preferred treatment of certain creditors in the immediate prepetition period. *See 11 U.S.C. § 547*. But the Code's voidable preference provisions are designed to prevent parties from privileging some creditors at the expense of others; they are not designed to hinder the efforts of parties to settle to avoid bankruptcy in the first place. Nobody has claimed that questions of preference are at issue here. Rather, Janvey claims that Romero's two settlement offers were unacceptably low. But the bankruptcy court determined that this was not the entire story. *Romero, 557 B.R. at 884*. As Janvey himself explained in rejecting Romero's second settlement offer, "[p]ursuing the Ambassador ha[d] strategic importance beyond the amount of money involved." *Id. at 878*. Janvey sought to make an example of Romero to ease his collection efforts elsewhere. He aimed to show through his relentless pursuit of the judgment that those found liable in the Ponzi scheme litigation would be required to compensate the victims in full. But just as Janvey was within his rights to reject Romero's settlement **[*22]** offers, Romero, too, had every right to take advantage of the mechanism by which insolvent individuals can discharge their debts.

C.

Janvey's final objection boils down to a belief that Romero should not be allowed to discharge his debts in bankruptcy because he has too much money. Janvey suggests that Romero should use his substantial assets—which were almost all exempt—to pay the judgment against him. This argument falters not only on its assumption that a debtor's ability to repay his debts alone constitutes cause for dismissal but also on its reliance on Romero's exempt assets. We address these flaws in turn.

HN12[] A debtor's ability to repay debts does not alone amount to cause for dismissal. *See* *Bushyhead, 525 B.R. at 148* (noting a "consensus among the courts" on this issue). As the House Report noted, "[t]he section *[§ 707(a)]* does not contemplate . . . that the ability of the debtor to repay his debts in whole or in part constitutes adequate cause for dismissal."[5] H.R. Rep. No. 95-595, at 380 (1977). Such a conclusion also follows logically from the

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[5] The language of what is today ***§ 707(a)*** was enacted as ***§ 707***. *See* Bankruptcy Reform Act of 1978, *Pub. L. No. 95-598, 92 Stat. 2549, 2606* (codified as amended at ***11 U.S.C. § 707(a)***). It was later renumbered as ***§ 707(a)*** when ***§707(b)*** was added to

Code's fresh-start philosophy. A penniless start is not a fresh start. Were absolute depletion of one's assets a prerequisite for bankruptcy relief, debtors and their families **[*23]** would be left destitute and without the means to become productive members of society. This would increase the strain on our social safety net by increasing the number of people who might potentially qualify for government benefits.

HN13[] Forcing a debtor to repay his debts using exempt assets before resorting to bankruptcy would also undercut the entire exemption scheme that Congress designed. The "historical purpose" of bankruptcy exemptions "has been to protect a debtor from his creditors, to provide him with the basic necessities of life so that even if his creditors levy on all of his nonexempt property, the debtor will not be left destitute and a public charge." H.R. Rep. No. 95-595, at 126. Bankruptcy exemptions are meant to "afford the debtor some economic and social stability, which is important to the fresh start guaranteed by bankruptcy." *In re Morehead, 283 F.3d 199, 203 (4th Cir. 2002)*. They represent a careful balance of "the difficult choices that exemption limits impose on debtors with the economic harm that exemptions visit on creditors." *Schwab v. Reilly, 560 U.S. 770, 791, 130 S. Ct. 2652, 177 L. Ed. 2d 234 (2010)*. Janvey's suggestion that Romero should use his exempt assets to pay the judgment turns this carefully crafted scheme on its head. We reiterate that the ability to repay debts may **[*24]** be a relevant factor in the holistic bad-faith analysis. *See* *McDow, 295 B.R. at 79 n.22*. But for the reasons stated above, we reject Janvey's attempt to transform it into a per se bar to bankruptcy relief.

V.

In ruling that the bankruptcy and district courts did not err in declining to dismiss Romero's petition, we remain aware that the bankruptcy process is subject to real abuse. *See* *Robinson v. Worley, 849 F.3d 577, 583 (4th Cir. 2017)* (denying debtor a discharge for "knowingly and fraudulently" making "a false oath or account" under *11 U.S.C. § 727(a)(4)* (quoting *11 U.S.C. § 727(a)(4)(A)*)). Any process that is established for legitimate reasons will occasionally be hijacked for illegitimate ends. ***HN14***[] It remains for bankruptcy judges to detect in the first instance those cases of fraud upon the court and creditors that constitute cause for dismissal under *§ 707(a)* or reason for a denial of discharge under the scenarios set forth in *11 U.S.C. § 727(a)*. The standard of review—one of abuse of discretion—is of paramount importance here. We do not ask whether we necessarily would have reached the same result as the bankruptcy court, but we do note its greater familiarity with Romero's case and the fact that the court gave good and sound reasons for ruling as it did. Its decision is hereby

AFFIRMED.

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the provision in 1984. *See* *Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 333, 355* (codified as amended at ***11 U.S.C. § 707(a)***).

2018 WL 1076760
United States Court of Appeals, Ninth Circuit.

Allan B. DIAMOND, Chapter 7 Trustee of the Estate of Howrey LLP, Plaintiff-Appellant,
v.
HOGAN LOVELLS US LLP, Defendant-Appellee.
Allan B. Diamond, Chapter 7 Trustee of the Estate of Howrey LLP, Plaintiff-Appellant,
v.
Pillsbury Winthrop Shaw Pittman LLP, Defendant-Appellee.
Allan B. Diamond, Chapter 7 Trustee of the Estate of Howrey LLP, Plaintiff-Appellant,
v.
Seyfarth Shaw LLP, Defendant-Appellee.
Allan B. Diamond, Chapter 7 Trustee of the Estate of Howrey LLP, Plaintiff-Appellant,
v.
Perkins Coie LLP, Defendant-Appellee.
Allan B. Diamond, Chapter 7 Trustee of the Estate of Howrey LLP, Plaintiff-Appellant,
v.
Neal, Gerber & Eisenberg LLP, Defendant-Appellee.
Allan B. Diamond, Chapter 7 Trustee of the Estate of Howrey LLP, Plaintiff-Appellant,
v.
Kasowitz Benson Torres LLP, Defendant-Appellee.
Allan B. Diamond, Chapter 7 Trustee of the Estate of Howrey LLP, Plaintiff-Appellant,
v.
Sheppard Mullin Richter & Hampton LLP, Defendant-Appellee.
Allan B. Diamond, Chapter 7 Trustee of the Estate of Howrey LLP, Plaintiff-Appellant,
v.
Jones Day, Defendant-Appellee.

No. 15-16326, No. 15-16327, No. 15-16328, No. 15-16329, No. 15-16330, No. 15-16331, No. 15-16332, No. 15-16333
|
Filed February 27, 2018

Synopsis
Background: Trustee for estate of bankrupt law firm brought action against law firms, seeking to recover profits earned from hourly-billed client matters started at bankrupt law firm, but completed at other firms that hired former partners of bankrupt firm. The United States Bankruptcy Court for the Northern District of California, Dennis Montali, United States Bankruptcy Judge, 2014 WL 507511, denied motion to dismiss. Law firms appealed. The United States District Court for the Northern District of California, James Donato, J., 531 B.R. 814, reversed. Trustee appealed.

Holdings: The Court of Appeals held that:

[1] it would certify question of whether a dissociated partner owes duty to his or her former law firm to account for profits earned post-departure on ongoing legal matters;

[2] it would certify question of whether, if a dissociated partner owes a duty to account for profits in such circumstances, a partner's former law firm is allowed to recover those profits; and

[3] it would certify question of what interest, if any, a dissolved law firm has in profits earned on matters in progress at time of dissolution.

Ordered accordingly.

West Headnotes (5)

[1] **Federal Courts**
Particular questions

Court would certify to District of Columbia Court of Appeals question of whether, under District of Columbia law, a dissociated partner owes a duty to his or her former law firm to account for profits earned post-departure on legal matters that were in progress but not completed at the time of the partner's departure, where the partner's former law firm had been hired to handle

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those matters on an hourly basis and where those matters were completed at another firm that hired the partner.

Cases that cite this headnote

[2] **Federal Courts**
Particular questions
Court would certify to District of Columbia Court of Appeals question of whether, under District of Columbia law, if a dissociated partner does owe a duty to his or her former law firm to account for profits earned post-departure on legal matters that were in progress but not completed at time of the partner's departure, a partner's former law firm is allowed to recover those profits from the partner's new law firm under an unjust enrichment theory.

Cases that cite this headnote

[3] **Federal Courts**
Particular questions
Court would certify to District of Columbia Court of Appeals question of what interest, if any, a dissolved law firm has in profits earned on legal matters that were in progress but not completed at the time the law firm was dissolved, where the dissolved law firm had been retained to handle the matters on an hourly basis, and where those matters were completed at different pre-existing firms that hired partners of the dissolved firm post-dissolution.

Cases that cite this headnote

[4] **Partnership**
Division and distribution of profits
The "unfinished business rule" requires that upon dissolution and winding up of a partnership's business, any profits derived from completion of such unfinished business inure to the partnership's benefit, even if received after dissolution.

Cases that cite this headnote

[5] **Bankruptcy**
Property or rights transferred
For purposes of bankruptcy law, debtors have an interest in any property that would have been part of the bankruptcy estate if not for the transfer of an interest of the debtor. 11 U.S.C.A. § 548.

Cases that cite this headnote

D.C. Nos. 3:14-cv-04882-JD, 3:14-cv-04883-JD, 3:14-cv-04884-JD, 3:14-cv-04885-JD, 3:14-cv-04886-JD, 3:14-cv-04887-JD, 3:14-cv-04888-JD, 3:14-cv-04889-JD

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Before: Ronald M. Gould and Mary H. Murguia, Circuit Judges, and Nancy Freudenthal, [*] Chief District Judge.

Opinion

ORDER

Alan B. Diamond, Trustee for Howrey LLP's bankruptcy estate, seeks to recover profits earned from hourly-billed client matters started at Howrey, but completed at other firms that hired the former Howrey partners. He raises both a fraudulent transfer and an unjust enrichment theory of recovery. The viability of both theories turns on the answers to unresolved questions of D.C. partnership law concerning the scope of the interest, if any, that a partnership has in client matters started at the partnership but completed at another firm.

Certified Questions

[1] [2] [3] Pursuant to D.C. Code § 11-723 we respectfully ask the District of Columbia Court of Appeals to resolve three questions of District of Columbia law that "may be determinative" of this bankruptcy appeal. D.C. Code § 11-723(a):

(1) Under District of Columbia law does a dissociated partner owe a duty to his or her former law firm to account for profits earned post-departure on legal matters that were in progress but not completed at the time of the partner's departure, where the partner's former law firm had been hired to handle those matters on an hourly basis and where those matters were completed at another firm that hired the partner?

(2) If the answer to question (1) is "yes," then does District of Columbia law allow a partner's former law firm to recover those profits from the partner's new law firm under an unjust enrichment theory?

***2** (3) Under District of Columbia law what interest, if any, does a dissolved law firm have in profits earned on legal matters that were in progress but not completed at the time the law firm was dissolved, where the dissolved law firm had been retained to handle the matters on an hourly basis, and where those matters were completed at different pre-existing firms that hired partners of the dissolved firm post-dissolution?

Our phrasing of the questions should not restrict the Court's consideration of the issues. The Court may rephrase a question as it sees fit in order to best address the contentions of the parties or the specifics of D.C. law. [1] If the District of Columbia Court of Appeals resolves these questions we will resolve the issue in our case in accordance with its answers.

Background

We offer the following statement of the "facts relevant to the questions certified and the nature of the controversy in which the questions arose." D.C. Code § 11-723(c).

Howrey LLP, a law firm organized under D.C. law, faced significant financial difficulties after the economic crisis of 2008. By early 2010 the firm was insolvent, and in March 2011 Citibank prohibited Howrey from using any cash collateral without permission. Howrey's partners voted to dissolve the firm effective March 15, 2011. As part of its dissolution, Howrey's partners amended their partnership agreement to include a "*Jewell* waiver" which would free any departing partner from any obligation to account for profits related to the winding up of unfinished business. [2] In April of 2011, Howrey's creditors filed an involuntary petition for bankruptcy against the firm.

***3** Partners left Howrey both before and after dissolution of the firm and started to work for other law firms. In many instances, these former Howrey partners continued to work on client matters that were formerly Howrey business.

In 2013, the bankruptcy estate's Trustee brought adversary proceedings against firms that had hired Howrey partners and had profited from work done on client matters that had been started at Howrey ("defendant firms"), attempting to recover portions of payments made by former Howrey clients for work done on those ongoing matters. [3] The Trustee presented two different legal theories of recovery depending on whether a partner left before or after Howrey's dissolution.

To summarize briefly, the Trustee argues that partners who dissociated pre-dissolution had a duty to account for profits earned on ongoing client matters, and that Howrey can recover those profits from the defendant firms under an unjust enrichment theory. The Trustee argues that partners who left after the March 15, 2011 dissolution had a duty to account to Howrey for any profits earned on ongoing client matters, that the *Jewel* waiver constituted a fraudulent transfer of that interest from Howrey to the partners under 11 U.S.C. § 548, and that the Trustee can recover from the defendant firms as subsequent transferees under 11 U.S.C. § 550.

The law firms moved to dismiss the adversary proceedings. The bankruptcy court denied the motion to dismiss the post-dissolution claims on grounds that the unfinished business rule as articulated in *Beckman v. Farmer*, 579 A.2d 618 (D.C. 1990), and *Young v. Delaney*, 647 A.2d 784 (D.C. 1994)—cases involving contingency fee matters—applied with equal force to client matters billed on an hourly basis, and that therefore the Trustee could seek to recover profits from partners who left *after* the *Jewel* waiver passed under a fraudulent transfer theory. The bankruptcy court also held that the Trustee had stated a valid claim for unjust enrichment.

The law firms appealed, and the district court reversed. The district court held that profits generated from ongoing legal matters were not subject to the duty to account where the client had entered into a new retainer agreement with a different firm. For that reason, it rejected both the pre-dissolution unjust enrichment claim and the post-dissolution fraudulent transfer claim.

Reasons for Certification

Section 404(b)(1) of the Revised Uniform Partnership Act ("RUPA") (D.C. Code § 29-604.07(b)(1)) imposes a duty on a partner "to account to the partnership and hold as trustee for it any property, profit, or benefit derived by the partner in the conduct and winding up of the partnership business." Section 603(b) of the RUPA (D.C. Code § 29-606.03(b)) governs the duties of dissociating partners. It holds that "[t]he [dissociating] partner's duty of loyalty under Section 404(b)(1) and (2) and duty of care under Section 404(c) continue only with regard to matters arising and events occurring before a partner's dissociation, unless the partner participates in winding up of the partnership's business." [4]

***4** The Trustee argues that ongoing hourly-billed client matters were "matters arising" before the partner's dissociation, and, hence, the partner had a duty to account for profits earned from those matters.

The defendant firms, in contrast, contend that "matters arising" should be interpreted narrowly to include only work actually performed prior to dissociation. On this interpretation, the duty to account would apply only to payments made after dissociation for work performed before dissociation. Our review of District of Columbia case law has found no case resolving this dispute.

If a dissociating partner owes a duty to Howrey to account for profits earned from ongoing client matters that raises an additional question: whether District of Columbia unjust enrichment law allows Howrey to recover those profits from the defendant firms. The District of Columbia Court of Appeals has provided different statements of the requirements for an unjust enrichment claim. Sometimes the Court presents an unjust enrichment claim in terms of specific elements—"(1) the plaintiff conferred a benefit on the defendant; (2) the defendant retains the benefit; and (3) under the circumstances, the defendant's retention of the benefit is unjust." *Falconi-Sachs v. LPF Senate Square, LLC*, 142 A.3d 550, 556 (D.C. 2016) (quoting *News World Commc'ns, Inc. v. Thompsen*, 878 A.2d 1218, 1222 (D.C. 2005)). Other District of Columbia decisions describe unjust enrichment differently. For example, in *4934, Inc.*

the court stated that "[u]njust enrichment occurs when a person retains a benefit (usually money) which in justice and equity belongs to another." *4934, Inc. v. D.C. Dep't of Emp't Servs.*, 605 A.2d 50, 55 (D.C. 1992); *see also* *Jordan Keys & Jessamy, LLP v. St. Paul Fire & Marine Ins. Co.*, 870 A.2d 58, 63 (D.C. 2005).

The defendant firms argue that under the initially described test, the first element is not satisfied in a case like this, because the benefit—the profits earned on ongoing client matters—was not directly conferred by Howrey on the defendant firms. Rather, the client conferred the benefit. However, as stated, the first element does not explicitly rule out transfers where the benefit flows from the plaintiff to the defendant in an indirect manner through a third party. And we have found no decisions from the District of Columbia courts that speak to this issue—that is, where an unjust enrichment claim was rejected because the benefit was not directly conferred, or where an unjust enrichment claim was allowed to proceed despite an indirect transfer of the benefit.

Under the test for unjust enrichment as described in the *4934 Inc.* decision, there is no requirement that there be a direct transfer of the benefit from the plaintiff to the defendant. And we note that this is the view adopted in Section 48 of the Restatement (Third) of Restitution and Unjust Enrichment (2011), which states that "[i]f a third person makes a payment to the defendant to which (as between claimant and defendant) the claimant has a better legal or equitable right, the claimant is entitled to restitution from the defendant as necessary to prevent unjust enrichment."

[4] There is also an unanswered question under D.C. law about the applicability of the unfinished business rule, as articulated in *Beckman*, 579 A.2d at 636 and *Young*, 647 A.2d at 789, to the facts of this case. The unfinished business rule as described in *Beckman* requires that upon dissolution and winding up of a partnership's business, "any profits derived from completion of such unfinished business inure to the partnership's benefit, even if received after dissolution." 579 A.2d at 636.

***5** In *Beckman* the District of Columbia Court of Appeals held that the unfinished business rule required former partners of a law firm to account for profits earned on matters that were pending at the time of dissolution. *Id.* *Beckman* involved a three person firm that went into dissolution. *Id.* at 624–25. One of the partners sued the other two partners to recover money earned on a contingency fee matter that was ongoing at the time of dissolution. *Id.* at 625. Prior to the resolution of the contingency fee matter, the other two partners had started a separate firm. *Id.* Citing a number of cases in other jurisdictions, the *Beckman* court reasoned that "pending cases are uncompleted transactions requiring winding up after dissolution, and are therefore assets of the partnership subject to post-dissolution distribution." *Id.* at 636.

A second District of Columbia Court of Appeals case reached a similar conclusion in *Young v. Delany*. The *Young* court held that "[p]rofits derived from the completion of legal cases or uncompleted transactions after dissolution of a law partnership are assets of the partnership, subject to distribution after dissolution." 647 A.2d at 789. The *Young* court went on to hold that during "dissolution and completion of the wind-up, the partners have a fiduciary obligation to hold such assets for the benefit of the other partners. Absent an agreement to the contrary, fees must be shared regardless of which partner provides post-dissolution services." *Id.* at 792 (internal citation omitted).

Beckman and *Young*, however, differ from this case in at least three ways that might bear on the applicability of the unfinished business rule here. First, *Beckman* and *Young* were decided under the UPA, not the RUPA. The RUPA differs from the UPA in that it entitles a partner of a dissolving firm to "reasonable compensation for services rendered in winding up the business of the partnership." RUPA § 401; (D.C. Code § 29-604.01(k)).

Second, *Beckman* and *Young* both dealt with ongoing contingency fee arrangements and not, as here, hourly fee arrangements. There are different interests at stake under hourly as opposed to contingency fee arrangements. For example, under a contingency fee arrangement if there was no duty to account, then work performed by the former firm would go unpaid. Under hourly arrangements, at least some payment would have been made to the firm for work done on the client's matter, even if other overhead costs associated with recruiting the client or administrative handling of the matter may go uncompensated. No District of Columbia Court of Appeals decision has addressed whether the unfinished

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business rule would allow recovery of some of the fees paid to a third-party firm under an hourly fee arrangement.

Third, both *Beckman* and *Young* involved partners who took client matters to firms composed entirely of former partners of the dissolving firm and not, as here, pre-existing firms. The equities in *Beckman* and *Young*, therefore, may relevantly differ from the situation here, where an existing large firm takes on a client matter by hiring a partner of a dissolved firm. In resolving such client matters the departing partner will use the resources of the new firm, including its associates and staff. And in such a case it is plausible to say that the client is hiring a new firm rather than remaining with a particular attorney. These three differences give us pause and uncertainty in applying the unfinished business rule, as articulated in *Beckman* and *Young*, to the facts of this case without further guidance from the D.C. courts.

[5] The District of Columbia Court of Appeals' answer to the question of whether a dissolving firm has a property interest in profits earned from hourly ongoing client matters relates to bankruptcy law in the following way. Under 11 U.S.C. § 548, a bankruptcy trustee has the power to avoid any fraudulent transfer of an interest of the debtor in property within a specified period before the bankruptcy. A transfer will be fraudulent if it was done with intent to "hinder, delay, or defraud" creditors, § 548(a)(1)(A), or if it meets certain criteria for a constructive fraudulent transfer, § 548(a)(1)(B). For purposes of bankruptcy law, debtors have an interest in any property that would have been part of the bankruptcy estate if not for the transfer. *See Begier v. IRS*, 496 U.S. 53, 58, 110 S.Ct. 2258, 110 L.Ed.2d 46 (1990). Certain subsequent transferees of the debtor's property can also be liable under 11 U.S.C. § 550.

***6** If the District of Columbia Court of Appeals holds that a dissolved firm has a property interest in the profits earned from ongoing client matters billed on an hourly basis, we will remand to the district court for an assessment, in the first instance, of whether the defendant firms are liable as subsequent transferees under the fraudulent transfer provisions of the bankruptcy code, 11 U.S.C. §§ 548 and 550.

We believe that the answers to the questions we present are important for D.C. attorneys and their clients. Because these issues are substantive, and affect the outcome of the litigation, they should be resolved in accord with the substantive law of the District of Columbia. *See Erie R. Co. v. Tompkins*, 304 U.S. 64, 78, 58 S.Ct. 817, 82 L.Ed. 1188 (1938) (holding that federal courts sitting in diversity shall apply state substantive law); *Guaranty Trust Co. v. York*, 326 U.S. 99 111–12, 65 S.Ct. 1464, 89 L.Ed. 2079 (1945) (holding that federal courts sitting in diversity should apply state law that determines the outcome of the case). The answers provided will help clarify the duties partners owe to their firms. And in the bankruptcy context, the District of Columbia Court of Appeals' answer to these questions will have important implications for both the suppliers operating in the District of Columbia and the law firms practicing law there. On the one hand, if a firm goes into bankruptcy all of its suppliers become creditors and will be impacted by the scope of a partner's duty to account for profits. Those suppliers might believe that a law firm's receivables from its current client base and its ongoing relationships with those clients are significant assets of the firm that stand behind its credit. And as the Trustee has argued, the rule endorsed by the defendant firms and the district court "ignores the plight of hundreds of creditors left holding the bag when partners flee with the most valuable assets." On the other hand, if the scope of a partner's duty to account for profits is described too broadly, this will have real-world impacts on the lawyers who practice in Washington D.C. If, when a firm is failing, a lawyer cannot complete any pending client work for the benefit of his or her new firm, that will make it harder for lawyers to find a new home if their firm fails. That in turn may discourage lawyers from entering the D.C. bar and practicing there. And as the district court noted, lateralling between firms is increasingly common in modern legal practice, and the scope of a partner's duty to account for profits from ongoing matters will likely have a substantial impact on this commonplace practice. We believe, however, that these questions are best answered by a court sitting in the applicable jurisdiction that will have greater familiarity with the local concerns of lawyers practicing in the District of Columbia and suppliers to those firms in a supporting marketplace.

Conclusion

We respectfully request that the District of Columbia Court of Appeals exercise its discretionary authority to accept and decide these questions of law. The Clerk of

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this Court is hereby ordered to transmit forthwith to the District of Columbia Court of Appeals, under official seal of the United States Court of Appeals for the Ninth Circuit, a copy of this order and request for certification and all relevant briefs and excerpts of record pursuant to D.C. Code § 11-723.

Further proceedings in our court on the certified questions are stayed pending the District of Columbia Court of Appeals' decision as to whether it will accept review, and if so, our receipt of its answer to the certified questions. The case is withdrawn from submission until further order from this Court. The panel will resume control and jurisdiction on the certified questions upon receiving an answer to one or both of the questions or upon the District of Columbia Court of Appeals' decision to decline to answer the questions. The Clerk is directed to administratively close this docket, pending further order. The parties shall file a joint report notifying this court of the District of Columbia Court of Appeals' decision regarding whether to accept the certified questions. If the District of Columbia Court of Appeals accepts one or more of the certified questions, the parties shall file a joint status report every six months after the date of acceptance, or more frequently if the circumstances warrant.

***7 IT IS SO ORDERED.**

All Citations

--- F.3d ----, 2018 WL 1076760, 18 Cal. Daily Op. Serv. 1884

Footnotes

* The Honorable Nancy Freudenthal, Chief United States District Judge for the District of Wyoming, sitting by designation.

1 The parties framed the issues differently. Appellant, Diamond, would certify the following questions:

(1) Under District of Columbia law, does a dissolved law firm have a property interest in legal matters that are in progress but not completed at the time the law firm is dissolved, when the dissolved law firm had been retained to handle the matters on an hourly basis?

(2) Would the District of Columbia Court of Appeals adopt section 48 of the Restatement (Third) of Restitution and Unjust Enrichment (2011) and hold that unjust enrichment is available where "a third person makes payment to the defendant to which (as between the claimant and defendant) the claimant has a better legal or equitable right"?

If so, under the District of Columbia law as codified in the Revised Uniform Partnership Action ("RUPA"), D.C. Code § 33-101.01 *et seq.*, does a departing partner of a law partnership owe a duty to her former partnership to account for the profits on matters that are in progress but not completed at the time the departing partner brings those matters to a new partnership?

The law firm appellees would certify a single question:

Under D.C. law, does a law firm that dissolves and liquidates in bankruptcy have a property right to profits earned by third-party law firms on hourly-rate matters that clients chose those other firms to handle (either before or after dissolution of the defunct firm)?

2 Specifically, the waiver was intended to "expressly waive, opt out of and be in lieu of any rights any Partner or Partnership may have to 'unfinished business' of the Partnership, as that term is defined in *Jewel v. Boxer*, 156 Cal. App. 3d 171, 203 Cal.Rptr. 13 (1984), or as otherwise might be provided in the absence of this provision through interpretation or application of the LLP Act."

3 The defendant firms include Jones Day; Perkins Coie; Pillsbury, Winthrop, Shaw and Pittman; Sheppard, Mullin, Richter, & Hampton; Neal, Gerber & Eisenberg; Seyfarth Shaw; Hogan Lovells; and Kasowitz, Benson, Torres & Friedman.

4 We note that D.C. partnership law has been recodified, and there appears to be an internal inconsistency in the cross-references. § 29–606.03 cross-references § 29-604.04(b)(1), but the duty of loyalty appears to have been moved to § 29-604.07(b)(1). Since the D.C. Code, in its essential terms, adopts the RUPA, we assume that this is a scrivener's error. Because the district court and bankruptcy court decisions refer to a yet different codification of the D.C. Code, we adopt the convention of referring to the RUPA codification for sake of clarity. The parties are in agreement that this is the relevant language under dispute.

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2018 WL 1135497
Only the Westlaw citation is currently available.
United States Bankruptcy Court, D. New Mexico.

IN RE: Manuela Q. FRANCO,
Manuela Q. Franco, Debtor.
Clarke C. Coll, Chapter 7 trustee,
Plaintiff and Counterdefendant,
v.
Carla Franco, individually and as personal
representative of Hipolito Q. Franco, and
Drennan, Langdon, & Fidel, LLP, Defendants,
Counterplaintiffs, and Third Party Plaintiffs,
v.
Manuela Q. Franco, HV Franco Minerals,
Celia F. Hougland, and Robert D.
Hougland, Third Party Defendants.

Case No. 03–13492 tr7, Case No. 13–12941 tr7
|
Adv. No. 17–1001 t
|
Signed February 28, 2018

Attorneys and Law Firms

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Drennan & Langdon, LLP, pro se.

Elizabeth Leigh Hightower, Sanders, Bruin, Coll, & Worley, P.A., Roswell, NM, for Third Party Defendants.

Opinion

OPINION

David T. Thuma, United States Bankruptcy Judge

***1** Before the Court is the chapter 7 trustee's motion to dismiss the counterclaims of Carla Franco and Drennan, Langdon, and Fidel, LLP, under, inter alia, the *Barton* doctrine and quasi-judicial immunity. The motion has been fully briefed. After reviewing the relevant law, the Court concludes that Counts Two, Three, and Four of the counterclaims should be dismissed.

I. ALLEGATIONS

For the limited purpose of ruling on the trustee's motion to dismiss, the Court accepts the following allegations as true: [1]

By warranty deeds recorded in Book 251, Pg. 295 (1982), and Book 264, Pg. 222 (1996), Epolito V. Franco ("E. Franco") and Manuela Q. Franco ("Debtor") conveyed 123.48 acres of real property in Eddy County, New Mexico to Hipolito Franco ("H. Franco") and Carla Franco ("C. Franco"). The deeds did not reserve any mineral rights in, on, or under the property (the "Mineral Rights").

Debtor signed and recorded a third warranty deed in Book 326, Pg. 278 (1998), [2] that purported to correct the legal description of the prior deeds by describing the property conveyed as "the surface estate only." The deed was neither signed nor ratified by H. Franco or C. Franco.

Debtor also recorded in Book 825, Pg. 570 (2010) a document styled "CLARIFICATION Letter of Warranty Deed's & Mineral Rights." The letter asserts that E. Franco and Debtor never transferred any mineral rights, notwithstanding the numerous recorded deeds reflecting otherwise. The document concludes: "Upon my husband's passing in November of 1997, I, Manuela Q. Franco, became soul [sic] holder of one-half of the mineral right originally received from O.J. McCarty & Mary McCarty." This document clouds C. Franco's title to the Mineral Rights.

Debtor also recorded an affidavit in Book 858, Pg. 713 (2011) ("Debtor Affidavit"). The affidavit lists and summarizes several documents attached as exhibits, a number of which are fabricated and fraudulent. These include:

- A "Deed Transter," [sic] which purports to convey mineral rights from E. Franco to Debtor (the "Deed Transter");

• An affidavit, allegedly signed by Sharon Hill on April 1, 2011 (the "Hill Affidavit");

• A "Reservation," purportedly dated April 17, 1969, reserving all mineral rights and asserting Debtor's ownership of the Mineral Rights ("Reservation"); and

• A "Mineral Deed" recorded in Book 858, Pg. 747 (2011), purporting to convey the Mineral Rights to HV Franco Minerals.

Debtor filed Chapter 7 bankruptcy cases in 2003 and 2013. Clarke Coll was appointed the case trustee in both cases (the "Trustee"). Debtor did not disclose any of the Mineral Rights she now claims are estate property. Debtor received "no-asset" discharges in both cases.

***2** Debtor's claim to the Mineral Rights is made in bad faith because in both bankruptcy petitions she represented that she had no interest in the Mineral Rights.

Debtor did not attempt to reopen her bankruptcy cases to disclose her purported interest in the Mineral Rights until C. Franco obtained a state court judgment against her and others.

After entry of the judgment, the Trustee asserted an interest in the Mineral Rights.

The Trustee's assertions regarding the estate's alleged interest in the Mineral Right constitute disparaging statements to third parties concerning C. Franco's title to the Mineral Rights. If and to the extent the Trustee has filed documents in public records making such assertions, such documents also constitute disparaging and unfounded statements to third parties concerning ownership of the Mineral Rights.

The publication of the disparaging statements and the filing of the disparaging documents by the Trustee was done without right or privilege. The Trustee acted with malice in disparaging C. Franco's title to the Mineral Rights.

One or both of the Houglands fabricated the Debtor Affidavit, the Sharon Hill Affidavit, the Deed Transter, the Reservation, and an attachment to a crop share lease. The Houglands attempted to offer these documents as evidence in legal proceedings. The Houglands filed the documents in the Eddy County Records. These acts violated state and federal law, and were designed to defraud C. Franco and others.

C. Hougland tampered with purported receipts or work orders from a title company by hand-writing comments that purport to evidence that the deeds originally prepared by the title company included scrivener's errors. C. Hougland used these documents to induce a title company employee to sign affidavits of scrivener's error that falsely assert numerous deeds prepared by the title company mistakenly omitted mineral reservations, including deeds involving the Mineral Rights.

In 2006, Debtor leased the Mineral Rights to OGX Resources LLC (the "OGX Lease"), even though she knew C. Franco owned the Mineral Rights. Debtor kept all the money paid under the OGX Lease even though she knew she had no right to the money.

C. Hougland knowingly gave false testimony in a deposition about ownership of the Mineral Rights. For example, she swore that certain documents were legitimate when she knew that she and her husband had fabricated them. Debtor also gave false testimony in a deposition about ownership of the Mineral Rights, e.g., she swore she signed the "Reservation" in 1969, although that was impossible.

The Trustee asserts that Debtor's estate owns part of the Mineral Rights, even though he knows or should know that the estate has no good faith claim to the Mineral Rights.

The documents discussed above, which were published or filed by the Trustee, disparage C. Franco's ownership of the Mineral Rights.

It was foreseeable to the Trustee that the publication and/or filing of the documents would impair the marketability and value of C. Franco's interest in the Mineral Rights, particularly her the ability to lease them.

It was foreseeable to the Trustee that the publication and/or filing of the documents would require C. Franco to spend money to remove the clouds on title.

***3** C. Franco's damages caused by the Trustee's actions include, without limitation, (i) at least $61,740.00, paid

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to Debtor under the OGX Lease; and (ii) $115,000.00 in costs, including attorney's fees, incurred removing the clouds on C. Franco's title. C. Franco is also entitled to an award of punitive damages against the third party defendants.

The Houglands had a plan and an agreement with Debtor to, inter alia, fabricate documents, forge signatures, give false testimony, and tamper with the public records in the furtherance of a scheme to disparage C. Franco's title to the Mineral Rights, their objective being to appropriate the Mineral Rights and the benefits flowing therefrom.

The Houglands and Debtor are jointly and severally liable for damages arising from their conspiracy to disparage C. Franco's title.

Debtor received money under the OGX Lease she had no right to receive. Debtor would be unjustly enriched if she were allowed to retain the money. It is appropriate for the Court to impose a constructive trust upon the money, and C. Franco asks the Court to do so.

Counterplaintiffs did not seek or obtain approval from the Court before bringing their claims against the Trustee. Counterplaintiffs do not allege that the Trustee breached his fiduciary duties.

II. DISCUSSION

A. Rule [3] 12(b)(1) Standards.

The Trustee seeks dismissal of the counterclaims under Rule 12(b)(1) (lack of subject matter jurisdiction). Rule 12(b)(1) applies to *Barton* doctrine issues. *See, e.g., Satterfield v. Mallory,* 700 F.3d 1231, 1234 (10th Cir. 2012) ("[t]he *Barton* doctrine is jurisdictional in nature").

Rule 12(b)(1) allows a party to argue, by motion, that a court lacks jurisdiction over the subject matter of a claim. Such motions "generally take one of two forms: (1) a facial attack on the sufficiency of the complaint's allegations as to subject-matter jurisdiction; or (2) a challenge to the actual facts upon which subject matter jurisdiction is based." *Ruiz v. McDonnell,* 299 F.3d 1173, 1180 (10th Cir. 2002). In the case of a facial attack (such as the Trustee's motion to dismiss), the Court presumes that all of the allegations in the counterclaims are true. *Id.*; *Williamson v. Tucker,* 645 F.2d 404, 412 (5th Cir. 1981). Based on this presumption, the Court then determines whether, as a matter of law, it has jurisdiction over the claims.

B. Rule 12(b)(6) Standards.

Rule 12(b)(6) allows the Court to dismiss a complaint for "failure to state a claim upon which relief can be granted." "The nature of a Rule 12(b)(6) motion tests the sufficiency of the allegations within the four corners of the complaint after taking those allegations as true." *Mobley v. McCormick,* 40 F.3d 337, 340 (10th Cir. 1994). The sufficiency of a complaint is a question of law, and when considering and addressing a Rule 12(b)(6) motion, the Court must accept as true all well-pleaded factual allegations in the complaint, view those allegations in the light most favorable to the non-moving party, and draw all reasonable inferences in the plaintiff's favor. *Genesee County Employees' Retirement System v. Thornburg Mortgage Securities Trust 2006–3,* 825 F. Supp. 2d 1082, 1120–21 (D.N.M. 2011), citing *Tellabs, Inc. v. Makor Issues & Rights, Ltd.,* 551 U.S. 308, 322 (2007). Legal conclusions cast in the form of factual allegations need not be taken as true for Rule 12(b)(6) purposes. *See Ashcroft v. Iqbal,* 556 U.S. 662 ("the tenet that a court must accept as true all of the allegations contained in a complaint is inapplicable to legal conclusions").

***4** When entertaining a motion to dismiss, the Court is permitted "to take judicial notice of its own files and records, as well as facts which are a matter of public record." *Van Woudenberg v. Gibson,* 211 F.3d 560, 568 (10th Cir. 2000), *abrogated on other grounds* by *McGregor v. Gibson,* 248 F.3d 946, 955 (10th Cir. 2001). A court may also consider any documents to which the complaint refers, provided the documents are central to the plaintiff's claim and the parties do not dispute their authenticity. *See Jacobsen v. Deseret Book Co.,* 287 F.3d 936, 941–942 (10th Cir. 2002).

Motions to dismiss based on quasi-judicial immunity are typically evaluated under Rule 12(b)(6). *See Moss v. Kopp,* 559 F.3d 1155, 1170 (10th Cir. 2009); *Gregory v. U.S./U.S. Bankruptcy Court for the Dist. of Colorado,* 942 F.2d 1498, 1500 (10th Cir. 1991) (*sua sponte* invocation of Rule 12(b)(6) was appropriate because it "appear[ed] beyond doubt" that based on the allegations in the complaint, the trustee was entitled to quasi-judicial immunity).

C. The *Barton* Doctrine.

The Trustee seeks dismissal of the counterclaim under the "*Barton* doctrine."[4] The *Barton* doctrine "precludes suit against a bankruptcy trustee for claims based on alleged misconduct in the discharge of a trustee's official duties absent approval from the appointing bankruptcy court." *Lankford v. Wagner,* 853 F.3d 1119, 1122 (10th Cir. 2017), quoting *Satterfield v. Malloy,* 700 F.3d 1231, 1234–35 (10th Cir. 2012). "This is true even if the trustee allegedly acted 'with improper motives.' " 853 F.3d at 1122. The doctrine is intended to prevent a plaintiff from obtaining "some advantage over the other claimants upon the assets in the receiver's hands.' " *Satterfield v. Malloy*, 700 F.3d at 1234, quoting *Barton,* 104 U.S. at 128. Here, the counterplaintiffs seek compensatory and other damages from the Trustee for actions he took, and continues to take, in his capacity as the chapter 7 trustee.

D. The Trustee's Quasi–Judicial Immunity.
The Trustee also asserts that the counterclaims are barred under the doctrine of quasi-judicial immunity.

1. Judicial Immunity. A trustee's immunity has roots in the immunity granted to judges. *Forrester v. White,* 484 U.S. 219, 225 (1987); *Stump v. Sparkman,* 435 U.S. 349 (1978). Judges are given a "sweeping form of immunity." *Forrester,* 484 U.S. at 225 (1987). "This absolute immunity insulates judges from charges of erroneous acts or irregular action, even when it is alleged that such action was driven by malicious or corrupt motives." *In re Castillo*, 297 F.3d 940, 947 (9th Cir. 2002) (quoting *Forrester,* 484 U.S. at 227–28). *See also Whitesel v. Sengenberger*, 222 F.3d 861, 867 (10th Cir. 2000) ("Judges are absolutely immune from civil liability for judicial acts, unless committed in the clear absence of all jurisdiction."). Judicial immunity is a creature of the common law, and can trace its roots back hundreds of years to English law precedents. *See* Block, *Stump v. Sparkman* and the History of Judicial Immunity, 1980 Duke L.J. 879; *Forrester,* 484 U.S. at 225 ("judicial immunity is a well settled doctrine of the English courts for many centuries, and has never been denied, that we are aware of, in the courts of this country").

2. Quasi–Judicial Immunity. Judicial immunity "has been extended to non-judicial officers where their duties had an integral relationship with the judicial process." *Whitesel,* 222 F.3d at 867 (quotations omitted). This extension is referred to as "quasi-judicial immunity." Quasi-judicial immunity can apply to law clerks, military and naval officers, prosecutors, administrative law judges, agency officials, jurors, mediators, advocates, and witnesses. *Castillo*, 297 F.3d at 948. *See also Martinez v. Roth,* 53 F.3d 342 (10th Cir. 1995) (quasi-judicial immunity has been extended to a court-appointed psychologist, law clerks, probation officers, and mediators).

***5** 3. Quasi–Judicial Immunity for Bankruptcy Trustees. Application of the quasi-judicial immunity doctrine to suits against bankruptcy trustees varies a great deal. In the Tenth Circuit, for all claims except those alleging breach of fiduciary duty, trustees have absolute quasi-judicial immunity from personal liability if they acted within the scope of their authority. *See, e.g., Castillo,* 297 F.3d at 951 (citing *Antoine v. Byers & Anderson, Inc.,* 508 U.S. 429, 433–34 (1993)); *Gregory v. U.S./U.S. Bankruptcy Court for the Dist. of Colorado,* 942 F.2d 1498, 1500 (10th Cir. 1991); *Whitesel,* 222 F.3d at 867; *Castillo,* 297 F.3d at 951–952. A trustee has absolute quasi-judicial immunity for any mistakes made while discharging the judicial function, just as a judge would have absolute immunity for any mistakes in applying the law. *Id.*

Using essentially the same reasoning, other courts have extended quasi-judicial immunity to trustees' actions taken within the "scope of their authority." *See In re J & S Properties, LLC,* 545 B.R. 91, 103 (Bankr. W.D. Pa. 2015) (collecting cases); *Carrillo v. Wieland,* 527 Fed. Appx. 754, 757 (10th Cir. 2013); *Barbee v. Price Waterhouse, LLP (In re Solar Fin. Servs.),* 255 B.R. 801, 803 (Bankr. S.D. Fla. 2000); *Grant v. Florida Power Corp. (In re Markos Gurnee P'ship),* 186 B.R. 526 (Bankr. M.D. Fla. 1995). "Scope" cases generally involve third parties, but the Tenth Circuit has applied the analysis to claims asserted by estate beneficiaries. *See, e.g., Carrillo,* 526 Fed. Appx. at 757; *Gregory*, 942 F.2d at 1499. Thus, except for breach of duty claims, so long as trustees act pursuant to their court-appointed function and authority, they are immune from personal liability.

E. The Counterclaims.
Count One: Quiet Title. The Court construes this claim as being brought against Debtor's estate only, not against the Trustee personally. Under this construction, the Court will not dismiss the quiet title claim. The claim seems duplicative of the Trustee's Count I, but it does not run afoul of the *Barton* doctrine or quasi-judicial immunity.

Count Two: Disparagement of Title.[5] In this count, the counterplaintiffs seek money damages from the Trustee personally for disparagement/slander of title. Counterplaintiffs are unhappy the Trustee asserts that the estate has an interest in the Mineral Rights. Counterplaintiffs did not seek the Court's approval before bringing the claim. The Trustee may (or may not) prevail, but the Court has already ruled that there is a bona fide dispute about ownership of the Mineral Rights. The Trustee is therefore acting well within the scope of his official duties. Count Two violates the *Barton* doctrine, so the Court lacks subject matter jurisdiction over the claim. *See Lankford v. Wagner*, 853 F.3d at 1122 (affirming dismissal of claim against a bankruptcy trustee for failure to comply with the *Barton* doctrine). Further, the Trustee is protected against the claim by quasi-judicial immunity. Clearly, it is not a breach of duty for the Trustee to assert that his bankruptcy estate owns a valuable asset. Count Two must be dismissed.

Count Three: Civil Conspiracy to Disparage Title. This claim does not appear to be brought against the Trustee. To the extent it is, it will be dismissed for the same reasons as Count Two.

***6** Count Four: Constructive Trust. The Trustee is correct that imposing a constructive trust is a remedy, not an independent cause of action. *See, e.g., U.S. Dept. of Energy v. Seneca Oil Co. (In re Seneca Oil Co.)*, 906 F.2d 1445, 1450 (10th Cir. 1990) ("a constructive trust is an equitable remedy that is imposed for the recovery of wrongfully-held property."). As such, Count Four is not properly pled (it should have been a claim to recover the lease payments under a conversion or similar theory), and should be dismissed. Further, the claim does not appear to be directed against the Trustee. Third, to the extent the claim is asserted against the Trustee personally, it must be dismissed for the same reasons as Count Two.

III. CONCLUSION

The Trustee's motion to dismiss is well taken as it relates to Counts Two, Three, and Four. Count One shall remain, subject to the understanding that the defendant is the estate, not the Trustee personally. The Court will enter a separate order.

All Citations

Slip Copy, 2018 WL 1135497

Footnotes

1 In construing the complaint, the Court presents the allegations in the manner most favorable to Plaintiffs. *See Davis v. McCollum,* 798 F.3d 1317, 1319 n. 2 (10th Cir. 2015). Further, to better understand and construe the allegations, the Court took judicial notice of the relevant docket entries. *See* St. Louis Baptist Temple, Inc. v. Fed. Deposit Ins. Corp., 605 F.2d 1169, 1172 (10th Cir. 1979) (a court may *sua sponte* take judicial notice of its docket).

2 H. Franco died in 1997.

3 A "Rule" refers to the Federal Rules of Civil Procedure.

4 The name of the doctrine is taken from the Supreme Court's decision in *Barton v. Barbour*, 104 U.S. 126, 131 (1881).

5 As the Trustee points out, there is no cause of action in New Mexico for "disparagement of title." The Court construes the count as seeking relief for an alleged slander of title. *See Den–Gar Enterprises v. Romero*, 94 N.M. 425, 430 (Ct. App. 1980).

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This case was not selected for
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See Fed. Rule of Appellate Procedure 32.1
generally governing citation of judicial
decisions issued on or after Jan. 1, 2007.
See also U.S. Ct. of App. 11th Cir. Rule 36-2.
United States Court of Appeals,
Eleventh Circuit.

IN RE: Nicolas MEUS, Debtor.
Nicolas Meus, Plaintiff-Appellant,
v.
Laurie K. Weatherford, Chapter
13 Trustee, Defendant-Appellee.
In Re: Nicolas Meus, Debtor.
Nicolas Meus, Plaintiff-Appellant,
v.
US Bank National Association, Defendant-Appellee.

No. 16-16036
|
Non-Argument Calendar
|
(February 14, 2018)

Appeal from the United States District Court for the Middle District of Florida, D.C. Docket Nos. 6:15-cv-01380-PGB, 6:14-bkc-10332-CCJ, 6:15-cv-01732-PGB

Attorneys and Law Firms

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Laura Marie Carbo, H. Michael Muniz, Kahane & Associates, PA, Plantation, FL, for Defendant-Appellee US Bank National Association

Before MARCUS, JULIE CARNES, and FAY, Circuit Judges.

Opinion

PER CURIAM:

***1** Nicolas Meus, the debtor in these Chapter 13 bankruptcy proceedings, appeals the district court's order affirming (1) the bankruptcy court's order granting U.S. Bank National Association ("U.S. Bank") relief from the automatic stay; and (2) the bankruptcy court's dismissal of the case. After careful review, we conclude that we have no jurisdiction to consider Meus's appeal of the district court's affirmance of the bankruptcy court's order granting U.S. Bank relief from the automatic stay, and thus dismiss Meus's appeal of that stay-relief order. We affirm the district court's affirmance of the order dismissing the case.

I. BACKGROUND

A. Factual History

In 2007, U.S. Bank's predecessor in interest, Aurora Loan Services LLC ("Aurora"), sought to foreclose on a mortgage secured by real property owned by Meus and his fiancée, Ms. Altanie Andre. Aurora obtained a final judgment of foreclosure on October 29, 2007.

The state court eventually scheduled a foreclosure sale for June 25, 2009. On June 25, 2009, Ms. Andre filed for bankruptcy and the sale was cancelled. The bankruptcy case was dismissed less than a month later for failure to file required information.

The sale was rescheduled for February 9, 2010. On February 9, 2010, Ms. Andre again filed for bankruptcy and the sale was cancelled. That bankruptcy case was dismissed less than a month later for failure to file required information.

The sale was then rescheduled for July 8, 2010. On July 7, 2010, Ms. Andre filed for bankruptcy and the sale was cancelled. That bankruptcy case was dismissed less than a month later for failure to file required information.

The sale was then rescheduled for Monday, April 11, 2011. On Friday, April 8, 2011, Ms. Andre filed for bankruptcy. The sale was cancelled. That bankruptcy case was dismissed less than a month later for failure to file required information. In its dismissal order, the bankruptcy court enjoined Ms. Andre from filing another bankruptcy petition for 180 days.

The sale was then rescheduled for Monday, October 10, 2011—within the 180-day injunction period. On Friday,

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October 7, 2011, Ms. Andre filed for bankruptcy. Later that same day, Meus filed his own bankruptcy petition. The bankruptcy court dismissed Ms. Andre's petition because it violated the 180-day injunction entered in her prior case. [1]

The October 10, 2011, sale was cancelled due to Meus's bankruptcy filing. Meus's bankruptcy case remained open for several months until the bankruptcy court dismissed it for failure to maintain timely plan payments.

The foreclosure sale was then rescheduled for August 7, 2012. On August 6, 2012, Meus again filed for bankruptcy. The sale was cancelled. The bankruptcy court dismissed Meus's case several months later because Meus failed to attend the meeting of creditors, as required under 11 U.S.C. § 341(d) and Rule 2003(b)(1) of the Federal Rules of Bankruptcy Procedure.

***2** The sale was then rescheduled for November 27, 2013. On November 27, 2013, Ms. Andre filed for bankruptcy. The sale was not cancelled, but was subsequently set aside. [2] Ten days after the sale was set aside, Ms. Andre's bankruptcy case was dismissed for failure to maintain timely plan payments.

The sale was then rescheduled for September 11, 2014. On September 11, 2014, Meus initiated the instant bankruptcy proceedings. This time, the sale was not cancelled, and the state court issued a certificate of sale on September 12, 2014. On September 24, 2014, the state court returned the check presented at the foreclosure sale and declined to issue a certificate of title. On December 10, 2014, the state court reversed course and issued a certificate of title.

B. Procedural History

In October 2014—a month after Meus filed the instant Chapter 13 petition—U.S. Bank moved the bankruptcy court for both prospective and retroactive relief from the automatic stay. U.S. Bank sought relief that would prevent any bankruptcy filing by either Meus or Ms. Andre from triggering the automatic stay until after (1) the foreclosure sale was completed, (2) the state court issued a certificate of title and writ of possession, and (3) any current occupants were evicted from the property. It asked that such relief be declared effective *nunc pro tunc* to September 11, 2014.

The bankruptcy court held an evidentiary hearing at which Meus testified that he did not complete his previous bankruptcies because his mortgage company told him that it would work with him on a modification of his mortgage. Meus also testified that he filed the instant petition in good faith and that he intended to make payments and complete his Chapter 13 plan in this case. He further asserted that he was not aware of any of Ms. Andre's bankruptcy filings.

On July 31, 2015, the bankruptcy court ruled in favor of U.S. Bank. It granted U.S. Bank relief from the automatic stay *nunc pro tunc* to September 11, 2014—specifically to encompass the September 11, 2014, foreclosure sale and related proceedings. It also granted U.S. Bank prospective relief for a period of 180 days. In ruling for U.S. Bank, the bankruptcy court found that the serial bankruptcy filings by Meus and Ms. Andre—each within days of a scheduled foreclosure sale—were calculated to hinder, delay, or defraud U.S. Bank.

Meus appealed the bankruptcy court's July 31, 2015, order to the district court. He also moved for a stay of that order pending appeal. The bankruptcy court declined to issue a stay pending the duration of the appeal, but granted a temporary stay so Meus could seek a stay pending appeal from the district court.

In August 2015, the bankruptcy court dismissed Meus's case for failure to maintain timely plan payments. [3] Meus filed a motion for reconsideration, which the bankruptcy court denied. Meus appealed the dismissal, and the district court consolidated his appeals.

Meus moved the district court for a stay of the bankruptcy court's July 31, 2015, stay-relief order pending the resolution of his appeals. On December 2, 2015, the district court denied the motion and declined to issue a stay pending appeal. The district court subsequently affirmed both the July 31, 2015, stay-relief order and the dismissal of Meus's case. Meus now appeals to this Court.

II. DISCUSSION

A. Standard of Review

***3** As the second court of review, we review the bankruptcy court's orders independently of the district court. *Westgate Vacation Villas, Ltd. v. Tabas (In re Int'l Pharmacy & Disc. II, Inc.)*, 443 F.3d 767, 770 (11th Cir. 2005). We review determinations of law made by

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either court *de novo*. *Id.* We review the bankruptcy court's findings of fact for clear error. *Id.*

B. The Order Granting U.S. Bank Relief from the Automatic Stay

Under 11 U.S.C. § 362(d)(4), a bankruptcy court "shall grant relief" from the automatic stay to a creditor whose claim is secured by an interest in real property if, after notice and a hearing, the court finds that the filing of the bankruptcy petition was "part of a scheme to delay, hinder, or defraud creditors that involved ... multiple bankruptcy filings affecting such real property." 11 U.S.C. § 362(d)(4)(B). Here, the bankruptcy court concluded that the series of eight bankruptcy cases filed by Meus and Ms. Andre between 2009 and 2014—each within days of a scheduled foreclosure sale—demonstrated that Meus and Ms. Andre engaged in a "coordinated effort to keep U.S. Bank from collecting." In other words, the "filings were calculated to hinder, delay, or defraud U.S. Bank." Meus challenges that conclusion on appeal.

Before we can reach Meus's arguments, however, we must determine whether we have jurisdiction to entertain his appeal of the bankruptcy court's July 31, 2015, order granting relief from the automatic stay. *See Sinochem Int'l Co. v. Malaysia Int'l Shipping Corp.*, 549 U.S. 422, 430–31, 127 S.Ct. 1184, 167 L.Ed.2d 15 (2007). We "may not assume jurisdiction for the purpose of deciding the merits of the case." *Id.* at 431, 127 S.Ct. 1184. Indeed, we are obligated to review both our jurisdiction and the district court's jurisdiction before addressing the merits of the appeal. *See Mallory & Evans Contractors & Eng'rs, LLC v. Tuskegee Univ.*, 663 F.3d 1304, 1304 (11th Cir. 2011); *Thomas v. Blue Cross & Blue Shield Ass'n*, 594 F.3d 814, 818 (11th Cir. 2010). One jurisdictional issue that we are obligated to consider is mootness. *See Nat'l Advert. Co. v. City of Miami*, 402 F.3d 1329, 1331–32 (11th Cir. 2005) ("[B]ecause the question of mootness is jurisdictional in nature, it may be raised by the court *sua sponte*, regardless of whether the district court considered it or if the parties briefed the issue."). "[A]n issue is moot when it no longer presents a live controversy with respect to which the court can give meaningful relief." *Christian Coal. of Fla., Inc. v. United States*, 662 F.3d 1182, 1189 (11th Cir. 2011) (quoting *Friends of the Everglades v. S. Fla. Water Mgmt. Dist.*, 570 F.3d 1210, 1216 (11th Cir. 2009)).

When a debtor fails to obtain a stay pending appeal of an order granting a creditor relief from the automatic stay and allowing that creditor to foreclose on the debtor's property, a completed foreclosure and sale of the property will render any appeal moot, as this Court is powerless to rescind the completed sale on appeal.[4] *See, e.g.*, *Sewanee Land, Coal & Cattle, Inc. v. Lamb (In re Sewanee Land, Coal & Cattle, Inc.)*, 735 F.2d 1294, 1295–96 (11th Cir. 1984); *see also Hope v. Gen. Fin. Corp. of Ga. (In re Kahihikolo)*, 807 F.2d 1540, 1542–43 (11th Cir. 1987). This principle applies even when the purchaser of the property is a party to the appeal. *See In re Sewanee Land, Coal & Cattle, Inc.*, 735 F.2d at 1296.

***4** Here, the state court held a foreclosure sale on September 11, 2014, and issued a certificate of sale the following day. The state court subsequently issued a certificate of title to the purchaser of the property on December 10, 2014. On July 31, 2015, the bankruptcy court retroactively lifted the automatic stay specifically to encompass the September 11, 2014, sale and related proceedings. Meus moved both the bankruptcy court and the district court for a stay of the bankruptcy court's July 31, 2015, stay-relief order, but both courts denied his request. Therefore, Meus's appeal of the bankruptcy court's July 31, 2015, stay-relief order became moot, at the latest, on December 2, 2015, when the district court declined to issue a stay of that decision.[5] *See In re Sewanee Land, Coal & Cattle, Inc.*, 735 F.2d at 1295–96.

Accordingly, we lack jurisdiction to consider the merits of Meus's challenge to the bankruptcy court's order granting relief from the automatic stay. *See id.*; *see also In re Kahihikolo*, 807 F.2d at 1542–43.

C. The Dismissal of the Case

Meus has offered no argument challenging the bankruptcy court's dismissal of his case based on Meus's failure to maintain timely plan payments. Meus has therefore abandoned any challenge to that decision. *See, e.g.*, *Timson v. Sampson*, 518 F.3d 870, 874 (11th Cir. 2008) ("While we read briefs filed by *pro se* litigants liberally, issues not briefed on appeal by a *pro se* litigant are deemed abandoned." (citations omitted)). It follows that the district court's affirmance of the bankruptcy court's dismissal order is due to be affirmed. *See id.*; *see also Sapuppo v. Allstate Floridian Ins. Co.*, 739 F.3d 678, 681–83 (11th Cir. 2014).

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III. CONCLUSION

For the reasons set out above, we **DISMISS** Meus's appeal of the July 31, 2015, order as moot and **AFFIRM** the district court's affirmance of the bankruptcy court's dismissal of the case.

All Citations

--- Fed.Appx. ----, 2018 WL 846551

Footnotes

1 In its dismissal order, the bankruptcy court enjoined Ms. Andre from filing another bankruptcy petition until April 4, 2012.

2 The state court issued a certificate of sale on December 3, 2013, but did not issue a certificate of title. On March 3, 2014, the state court vacated the certificate of sale and set aside the sale in its entirety.

3 In its dismissal order, the bankruptcy court enjoined Meus from filing another bankruptcy petition for 180 days.

4 Indeed, once a state-court foreclosure sale is complete, even the bankruptcy court is unable to retroactively void the sale by re-imposing the automatic stay so the debtor can pursue an appeal of a previous order lifting the automatic stay. *Lashley v. First Nat'l Bank of Live Oak (In re Lashley)*, 825 F.2d 362, 364 (11th Cir. 1987).

5 The bankruptcy court took judicial notice of the docket in the state-court foreclosure proceeding, and copies of that docket were filed in the bankruptcy court by both U.S. Bank and Meus. The copy filed in the bankruptcy court by Meus indicates that the state court issued a certificate of title on December 10, 2014. We take judicial notice of the state-court record solely for the purpose of confirming the validity and finality of the foreclosure sale as reflected in the record below. *See* Fed. R. Evid. 201; *Keith v. DeKalb Cty.*, 749 F.3d 1034, 1041 & n.18 (11th Cir. 2014) (taking judicial notice of a state court's online judicial system). A review of the state-court docket and the filings in that case confirms that the foreclosure sale remains valid and final.

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See Fed. Rule of Appellate Procedure 32.1
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decisions issued on or after Jan. 1, 2007.
See also U.S. Ct. of App. 11th Cir. Rule 36-2.
United States Court of Appeals,
Eleventh Circuit.

David BEEM, Plaintiff-Appellee,
v.
Gary Allan FERGUSON, Defendant-Appellant.

No. 16-11842
|
(February 6, 2018)

Synopsis
Background: Individual Chapter 11 debtor's former business partner brought adversary proceeding to except debt from discharge, and debtor moved to dismiss complaint as untimely. The United States Bankruptcy Court for the Southern District of Florida, No. 1:12-bkc-02010-LMI, denied motion, and granted former business partner's motion for summary judgment on dischargeability issue based on preclusive effect of prior state court judgment, and debtor appealed. The District Court, No. 1:15-cv-20550-RNS, affirmed. Debtor appealed.

Holdings: The Court of Appeals held that:

[1] motion to dismiss debtor's individual Chapter 11 case or, in alternative, for determination that debtor's debt to movant was nondischargeable was the functional equivalent of complaint, which was filed prior to expiration of bar date on such complaints, and to which movant's subsequent nondischargeability complaint could relate back, and

[2] Florida state court judgment previously entered against debtor for abuse of process, upon finding that he willfully and intentionally misused process for some wrongful and unlawful object or collateral purpose as required by governing Florida law, was entitled to issue preclusive effect and barred debtor from contesting nondischargeability of state court judgment debt as one for his "willful and malicious injury."

Affirmed.

Appeal from the United States District Court for the Southern District of Florida, D.C. Docket No. 1:15-cv-20550-RNS; 1:12-bkc-02010-LMI

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Before JORDAN and JILL PRYOR, Circuit Judges, and REEVES, [*] District Judge.

Opinion

PER CURIAM:

***1** On August 24, 1992, Hurricane Andrew made landfall near Homestead, Florida, destroying at least 63,000 homes and 82,000 businesses, and leaving at least 175,000 people homeless. The extreme damage (about $25 billion) left an extensive amount of construction material debris across Homestead, and some entrepreneurs found new business opportunities among the wreckage. One of those men was Gary Ferguson, who in 1994 joined with David Beem to form Floors to Doors, Inc., which sold discount home improvement and building supplies. But like far too many homes in Hurricane Andrew's path, the business partnership between Mr. Ferguson and Mr. Beem collapsed. And, when that happened, the two did what disgruntled business partners often do—litigate.

This appeal marks the latest episode in a decade-long legal battle fought by Messrs. Ferguson and Beem in state and federal courts. Nine years ago, Mr. Beem won summary judgment in state court against Mr. Ferguson on his claim for "defamation; abuse of process." A jury awarded him

damages on that claim in 2011 and the court entered judgment accordingly.

In 2012, Mr. Ferguson filed for bankruptcy and Mr. Beem sought to have the debt for that judgment declared non-dischargeable. Mr. Beem's lawyer, however, made a mistake. We must now decide whether Mr. Beem's untimely complaint in the adversary proceeding may relate back to the filing of a timely, but procedurally improper, motion in the bankruptcy case. We also must decide whether the bankruptcy court appropriately granted Mr. Beem's motion for summary judgment, declaring Mr. Ferguson's debt non-dischargeable. After careful review of the full record and the parties' briefs, and with the benefit of oral argument, we answer both questions yes, and affirm.

I

Mr. Ferguson and Mr. Beem incorporated Floors to Doors, Inc. on December 15, 1994. From that date until 2007, FTD served as a retailer of surplus building and construction supplies. The parties admit that the business never thrived and, over time, the business relationship deteriorated. The reasons for that deterioration have been hotly contested. In October of 2007, Mr. Ferguson filed a complaint in state court, alleging that Mr. Beem had been embezzling funds from FTD. Mr. Ferguson's complaint also alleged that Mr. Beem breached his fiduciary duties, and sought a judicial dissolution of FTD. Mr. Beem responded with seven counterclaims (brought both derivatively on behalf of FTD and by Mr. Beem individually). One of those seven counterclaims against Mr. Ferguson alleged "defamation; abuse of process," and was brought by Mr. Beem individually. In it, Mr. Beem alleged that Mr. Ferguson engaged a "campaign of harassment and defamation" against him and had filed numerous baseless complaints with government agencies to harm his reputation and "for the improper purpose of extorting [him] into selling FTD."

In January of 2009, Mr. Beem obtained summary judgment on four of his claims, including Count Three. The court's order stated that the ruling on that count was:

> ***2** based upon the Court's finding that [Mr. Ferguson], despite having had more than a year to submit evidence in support of his allegation that Mr. Beem stole over $1 million from Floors to Doors, and despite [Mrs.] Ferguson's sworn testimony that she possessed this evidence before this lawsuit was filed, has failed to establish or submit any competent evidence of any such theft.

AP Doc. 106-1 at 72.[1] The state court held a trial on damages in March of 2011. The jury awarded Mr. Beem a total of $318,025, of which $118,025 was for attorney's fees "incurred ... resulting from the necessity to defend against" Mr. Ferguson's complaint, and the remaining $200,000 was for "emotional damages which were the direct and proximate result of [Mr. Beem's] defending against" Mr. Ferguson's complaint. AP Doc. 106-1 at 75. The judgment was affirmed on appeal.

Mr. Ferguson filed a Chapter 11 bankruptcy petition on May 21, 2012. On August 9, 2012, Mr. Beem sought an unopposed extension to file a complaint objecting to the discharge of Mr. Ferguson's debt for the state court judgment under 11 U.S.C. § 523. The bankruptcy court granted the motion and set October 12, 2012, as the deadline to file the complaint and commence an adversary proceeding under § 523. But instead of filing a "complaint" and initiating an adversary proceeding, Mr. Beem's attorney filed an original and an amended "Motion to Dismiss or for Determination of Non-Dischargeability of His Debt" on October 5 and 9, respectively. Then, apparently realizing his procedural mistake, Mr. Beem's attorney filed an adversary complaint regarding dischargeability on October 17, 2012.

Mr. Ferguson moved to dismiss the adversary complaint as untimely. The bankruptcy court ruled that the complaint was timely for two reasons: it could retroactively extend the deadline to file the complaint because there was excusable neglect and the complaint related back to the timely, but improperly filed, motion.

In September of 2014, Mr. Beem moved for summary judgment, arguing that the debt arising out of the state court judgment for abuse of process was non-dischargeable. The bankruptcy court granted Mr. Beem's motion on December 8, 2014, ruling that, as a matter of law, the state court abuse of process judgment constituted

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a non-dischargeable debt for a willful and malicious injury under § 523(a)(6).

Mr. Ferguson appealed the bankruptcy court's orders denying his motion to dismiss and granting Mr. Beem's motion for summary judgment to the district court, which affirmed, ruling that Mr. Beem's untimely adversary complaint related back to the timely motion and that summary judgment was appropriate. This is Mr. Ferguson's appeal.

II

In bankruptcy cases, we sit as a "second court of review" and "examine [ ] independently the factual and legal determinations of the bankruptcy court and employ[ ] the same standard of review as the district court." *In re Optical Techs., Inc.*, 425 F.3d 1294, 1299–1300 (11th Cir. 2005) (citation omitted). Factual findings of the bankruptcy court are reviewed for clear error, and legal conclusions by either the bankruptcy court or the district court are reviewed *de novo*. *Id.* at 1300. *See also In re Fin. Federated Title & Tr., Inc.*, 309 F.3d 1325, 1328–29 (11th Cir. 2002).

III

***3** The "central purpose" of the Bankruptcy Code "is to provide a procedure by which certain insolvent debtors can reorder their affairs, make peace with their creditors, and enjoy a new opportunity in life with a clear field for future effort." *In re St. Laurent*, 991 F.2d 672, 680 (11th Cir. 1993) (quotation omitted). "[T]his 'fresh start' policy is only available to the 'honest but unfortunate debtor,' " *In re Fretz*, 244 F.3d 1323, 1326 (11th Cir. 2001) (quoting *Grogan v. Garner*, 498 U.S. 279, 286–87, 111 S.Ct. 654, 112 L.Ed.2d 755 (1991)), and under 11 U.S.C. § 523, certain types of debts are not dischargeable. A debt incurred "for willful and malicious injury by the debtor to another entity or to the property of another entity" is one such non-dischargeable debt. 11 U.S.C. § 523(a)(6). For creditors asserting that a debt is non-dischargeable, the Federal Rules of Bankruptcy Procedure provide that the proper means to achieve a non-dischargeability determination is through an adversary proceeding. *See* Fed. R. Bankr. P. 7001(6). An adversary proceeding is commenced by the filing of a complaint, which usually must be done with the same court that is handling the bankruptcy petition. *See* Fed. R. Bankr. P. 5005(a)(1); 7003.

"[A] complaint to determine the non-dischargeability of a debt under [11 U.S.C.] § 523(c) shall be filed no later than 60 days after the first date set for the meeting of creditors." Fed. R. Bankr. P. 4007(c). Although the bankruptcy court may extend this deadline for cause upon the motion of a party in interest, the motion must be filed before the deadline expires. *See id.* We have explained that Rule 4007(c) removes a bankruptcy court's discretion to grant a *late filed* motion to extend time to file a dischargeability complaint. *See In re Alton*, 837 F.2d 457, 459 (11th Cir. 1988).

In this case, the bankruptcy court purported to extend the deadline for Mr. Beem to file his complaint after the deadline had expired. The district court, however, ruled that the bankruptcy court lacked the authority to retroactively extend this deadline. Mr. Beem has not challenged this ruling on appeal. Therefore, the only basis upon which Mr. Beem's non-dischargeability complaint could be timely is if it relates back, pursuant to Federal Rule of Bankruptcy Procedure 7015, to his motion to determine dischargeability that was filed in the main bankruptcy action before the deadline.

A

Bankruptcy Rule 7015 incorporates Federal Rule of Civil Procedure 15. Rule 15(c) provides, in relevant part:

> (c) Relation Back of Amendments
>
> (1) When an Amendment Relates Back. An amendment to a pleading relates back to the date of the original pleading when: ...
>
> (B) the amendment asserts a claim or defense that arose out of the conduct, transaction, or occurrence set out—or attempted to be set out—in the original pleading.

We must first determine whether Mr. Beem's timely filed motion in the bankruptcy case functioned as an "original pleading" to which the untimely adversary complaint related back. If it does, we must then address the merits and consider whether the complaint's non-dischargeability allegations "arose out of the conduct,

transaction, or occurrence set out—or attempted to be set out—in the original pleading."

[1] We first address whether Mr. Beem's improperly filed and mislabeled motion qualifies as an "original pleading" to which relation back applies. Mr. Ferguson presents a textual argument against the application of the relation back doctrine. First, Rule 15(c), incorporated into adversary proceedings by Bankruptcy Rule 7015, applies only to "pleadings." *See* Fed. R. Civ. P. 15(c). Next, a motion is not a "pleading" permitted by Bankruptcy Rule 7007 (which incorporates Federal Rule of Civil Procedure 7). *See* Fed. R. Civ. P. 7; Fed R. Bankr. P. 7007. Mr. Ferguson notes that Bankruptcy Rule 7001(6) requires a non-dischargeability claim to be pursued as an adversary proceeding. *See* Fed. R. Bankr. P. 7001(6). And, under Bankruptcy Rule 7003, an adversary proceeding must be commenced by the filing of a complaint. *See* Fed. R. Bankr. P. 7003.

***4** If these were the only applicable rules, we might agree with Mr. Ferguson. But absent from Mr. Ferguson's analysis is Bankruptcy Rule 7008. And when we add Bankruptcy Rule 7008 to the deck, Mr. Ferguson's argument falls.

Bankruptcy Rule 7008 provides that Federal Rule of Civil Procedure 8, which sets forth the pleading standard for a complaint, applies in adversary proceedings. Rule 8 provides that to state a claim for relief, a pleading must contain the following: (1) "a short and plain statement of the grounds for the court's jurisdiction[;]" (2) "a short and plain statement of the claim showing the pleader is entitled to relief;" and (3) "a demand for the relief sought." Fed. R. Civ. P. 8(a). The short and plain statement of the claim "need only 'give the defendant fair notice of what the claim is and the grounds upon which it rests.' " *Erickson v. Pardus*, 551 U.S. 89, 93–94, 127 S.Ct. 2197, 167 L.Ed.2d 1081 (2007) (quoting *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 555, 127 S.Ct. 1955, 167 L.Ed.2d 929 (2007)) (alteration omitted). Rule 8 also makes clear that "[p]leadings must be construed so as to do justice." Fed. R. Civ. P. 8(e). *See also Swierkiewicz v. Sorema N.A.*, 534 U.S. 506, 513–14, 122 S.Ct. 992, 152 L.Ed.2d 1 (2002) (explaining that "[t]he liberal notice pleading of Rule 8(a) is the starting point of a simplified pleading system, which was adopted to focus litigation on the merits of the claim").

Moreover, the "Federal Rules reject the approach that pleading is a game of skill in which one misstep by counsel may be decisive to the outcome and accept the principle that the purpose of pleading is to facilitate a proper decision on the merits." *Conley v. Gibson*, 355 U.S. 41, 48, 78 S.Ct. 99, 2 L.Ed.2d 80 (1957), *abrogated in part by Twombly*, 550 U.S. at 563, 127 S.Ct. 1955;[2] *Harris v. Garner*, 216 F.3d 970, 996 (11th Cir. 2000) (same). *See also* 6-107 Collier Bankruptcy Practice Guide P. 107.03 ("[Rule] 8(e) provides that 'pleadings must be construed so as to do justice.' This rule is at the very heart of the rules regarding pleadings. 'Pleadings are intended to serve as a means of arriving at fair and just settlements of controversies between litigants. They should not raise barriers which prevent the achievement of that end.' ") (quoting *Maty v. Grasselli Chem. Co.*, 303 U.S. 197, 200, 58 S.Ct. 507, 82 L.Ed. 745 (1938)); *De Loach v. Crowley's Inc.*, 128 F.2d 378, 380 (5th Cir. 1942) ("Just what [Rule 8(e)] means is not clear, but it excludes requiring technical exactness, or the making of refined inferences against the pleader, and requires an effort fairly to understand what he attempts to set forth.").[3]

***5** We have previously held that certain documents and filings were sufficient to constitute a "complaint" under Rule 8, even though they were not labeled as such. *See, e.g., Robinson v. City of Fairfield*, 750 F.2d 1507, 1511 (11th Cir. 1985) (a plaintiff's application for the appointment of counsel which stated "legal nature and factual basis of his claim"); *Judkins v. Beech Aircraft Corp.*, 745 F.2d 1330, 1332 (11th Cir. 1984) (a plaintiff's right-to-sue letter and "charge of discrimination"); *Commodity Futures Trading Comm'n v. Am. Commodity Grp. Corp.*, 753 F.2d 862, 865 (11th Cir. 1984) (an application for an order to show cause was "the functional equivalent of a complaint"). Our sister circuits have done the same. *See, e.g, Page v. Ark. Dep't of Corr.*, 222 F.3d 453, 454–55 (8th Cir. 2000) (a plaintiff's letter and attachments sent to the district court sufficient to constitute a complaint under Title VII). And, in the criminal context, we have determined that a government motion for a final order of forfeiture was "the functional equivalent of a complaint" and therefore was treated as a civil case. *See United States v. De La Mata*, 535 F.3d 1267, 1278 (11th Cir. 2008).

We apply the same Rule 8 analysis here in determining whether Mr. Beem's motion should be treated as the functional equivalent of a complaint. In doing so, we

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join the Ninth Circuit and several bankruptcy courts across the country that have applied the same analysis. *See, e.g.*, *In re Dominguez*, 51 F.3d 1502, 1509 (9th Cir. 1995) (holding that a creditor's "discharge memorandum" was a sufficient "complaint" under Bankruptcy Rule 7008 to commence non-dischargeability proceeding); *In re Thompson*, 572 B.R. 638, 656 (Bankr. S.D. Tex. 2017); *In re Rand*, 144 B.R. 253, 255–56 (Bankr. S.D.N.Y. 1992); *In re Levine*, 132 B.R. 464, 467 (Bankr. M.D. Fla. 1991).

In our view, Mr. Beem's timely filed "Motion to Dismiss or for Determination of Non-Dischargeability of His Debt" satisfied the Rule 8 pleading requirements for a complaint. The motion prominently requested the bankruptcy court to "enter an order holding Beem's debt is non-dischargeable," cited to § 523(a)(6) and the applicable legal standards, and included seven pages of facts detailing the basis for why Mr. Beem maintained that Mr. Ferguson's "gross and voluminous abuse of process" in the state case justified "non-dischargeability of debt." Through these facts, the motion alleged that Mr. Ferguson filed a baseless lawsuit accusing Mr. Beem of stealing $1 million from FTD, that there was no proof for such accusations, that Mr. Ferguson made an unfounded complaint to the Small Business Administration alleging Mr. Beem committed fraud, and that Mr. Beem prevailed on a judgment for abuse of process in the state court. These allegations, although contained in a "motion," clearly gave Mr. Ferguson "fair notice of what [Mr. Beem's] claim [was] and the grounds upon which it rest[ed]." *Twombly*, 550 U.S. at 555, 127 S.Ct. 1955.

Mr. Beem's motion differs starkly from the motions and filings that other courts have found inadequate to constitute a complaint regarding non-dischargeability. *See In re Markus*, 313 F.3d 1146, 1150 (9th Cir. 2002) (motion stating "object debtors discharge," without setting forth legal criteria for non-dischargeability or "any facts having to do with the nature of the conduct that caused the debt, or a claim for relief based on non-dischargeability," held insufficient); *In re Bozeman*, 226 B.R. 627, 632 (8th Cir. BAP 1998) (cover sheet describing "Nature of Suit" as "To determine the dischargeability of a debt" and motions to extend time to file complaint held insufficient because "they are insufficient to satisfy the notice requirements of the Federal Rules"); *In re Hunter*, 552 B.R. 864, 870 (Bankr. D. Kan. 2016) (initial filings insufficient because they were "so bare that, even if construed as an original pleading [they] did not sufficiently describe[ ] the 'conduct, transaction, or occurrence' ").

***6** We recognize that Mr. Beem's filing was denominated a "motion" and not a "complaint." It also does not contain a caption indicating that Mr. Beem is the plaintiff in an adversary proceeding against the defendant, Mr. Ferguson. Rather, it contains the caption of the main bankruptcy case. But these technical deficiencies are not determinative, for we have refused to treat the caption of a complaint as determinative of the nature of the action. *See Lundgren v. McDaniel*, 814 F.2d 600, 604 n.2 (11th Cir. 1987) (citing, in part, 5 C. Wright & A. Miller, Federal Practice & Procedure § 1321, pp. 458–59 (1969)). And bankruptcy courts have done the same. *See In re Morysville Body Works, Inc.*, 89 B.R. 440, 441–42 (Bankr. E.D. Pa. 1988) ("As a general proposition, this court is willing to overlook an error in presenting a complaint by motion, or vice versa. Our authority to do this flows from Rule 8[(e)].... Our ability to overlook such structural deficiencies has become so accepted that it is often done as a matter of course, without further discussion.") (citations omitted); Bankr. Proc. Manual § 7007:2 (2017 ed.) ("A failure to properly denominate a pleading is not fatal.... Thus, pleadings should be given the effect required by their content without regard to the name given them by the pleader"). In everyday terms: if it walks like a complaint and talks like a complaint, it's a complaint—even though it calls itself a motion.

For these reasons, we agree with the bankruptcy court and the district court that Mr. Beem's motion, "although a deficient pleading, [was] sufficient to place the debtor on notice of the claim against him and substantially complie[d] with the notice pleading requirements of Rule 7008." *In re Dominguez*, 51 F.3d at 1509.

B

[2] Mr. Ferguson makes three additional arguments in support of reversal. We do not find them persuasive.

First, he argues that Mr. Beem failed to commence an adversary proceeding by the deadline prescribed in Bankruptcy Rule 4007 because he filed a motion (not a complaint) in the main bankruptcy action and not as a separate adversary proceeding. As noted, however, we have determined that Mr. Beem's motion was the

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functional equivalent of a complaint under Rule 8 and Bankruptcy Rule 7008. Because Mr. Beem's motion was the functional equivalent of a complaint, his adversary proceeding should be deemed commenced on the date which he filed the motion in the main bankruptcy action. Other bankruptcy courts have similarly found an adversary proceeding commenced even though the filing was made in the main bankruptcy case, and not as a separate adversary proceeding. *See In re Weeks Landing, LLC*, 439 B.R. 897, 908–09 (M.D. Fla. 2010) ("Although filed in the underlying bankruptcy case and not as a separate adversary proceeding, this still constitutes being 'filed' because an adversary proceeding 'is commenced by filing a complaint with the court.' ") (quoting Fed. R. Bankr. P. 7003); *In re Rand*, 144 B.R. at 256 (concluding that a letter creditor sent to the bankruptcy judge timely commenced an adversary proceeding). We therefore disagree with Mr. Ferguson that Mr. Beem's complaint was untimely because it was filed in the main bankruptcy action.

Second, Mr. Ferguson argues that relation back is impermissible because the adversary proceeding is not the same proceeding as the bankruptcy case in which Mr. Beem timely filed his motion. Mr. Ferguson's argument makes sense in an ordinary civil case—Rule 15 does not permit an amendment in one case to relate back to the filing of an earlier complaint in a separate action. *See Dade Cnty. v. Rohr Indus., Inc.*, 826 F.2d 983, 989 (11th Cir. 1987). *See also Velez-Diaz v. United States*, 507 F.3d 717, 719 (1st Cir. 2007) ("Rule 15(c), by its terms, applies to amended pleadings in the *same* action as an original, timely pleading; the pleading sought to be amended may not be a pleading filed in a different case."). But the argument does not account for the unique meaning of "case" in the bankruptcy context. "[T]he word 'case,' as used in the bankruptcy context, 'is a term of art' with a specialized meaning. It 'refers to litigation commenced by the filing with the bankruptcy court of a petition under the appropriate chapter of Title 11.' The term 'proceeding,' on the other hand, refers to a 'particular dispute or matter arising within a pending case—as opposed to the case as a whole.' " *In re Fin. Oversight & Mgmt. Bd. for Puerto Rico*, 872 F.3d 57, 62–63 (1st Cir. 2017) (quoting *In re Caldor Corp.*, 303 F.3d 161, 168 n.3 (2d Cir. 2002)). *See also In re Thompson*, 965 F.2d 1136, 1140 (1st Cir. 1992) ("An adversary proceeding is a subsidiary lawsuit within the larger framework of a bankruptcy case."); 7 Collier on Bankruptcy 1109.04(1)(a)(i) (16th ed. 2016) ("Collectively, the term 'case' encompasses all of the discrete proceedings that follow the filing of a petition for bankruptcy relief, including adversary proceedings."). Accordingly, the adversary proceeding between Mr. Beem and Mr. Ferguson was part of the same "case" as Mr. Ferguson's larger bankruptcy case. This raises no barrier to relation back.

***7** Third, Mr. Ferguson asserts that the outcome here is guided by our decision in *In re Mendenhall*, 572 Fed.Appx. 858 (11th Cir. 2014). We disagree. *In re Mendenhall*, which is not binding because it is unpublished, considered only the late filing of a non-dischargeability complaint under Bankruptcy Rule 4007(c). *See id.* at 862–63. There was no timely filing of any document which could serve as an "original pleading" in that case. *See id.* Likewise, *In re Mendenhall*'s approval of "strict time limitations imposed by Rule 4007(c)" does not dictate the result here, where the creditor has made the facts supporting his objection to dischargeability known in a filing before the deadline. *Id.* at 863. The Ninth Circuit has recognized the same distinction—holding (like *In re Mendenhall*) that a bankruptcy court has no discretion to retroactively extend the Bankruptcy Rule 4007(c) deadline, *see Anwar v. Johnson*, 720 F.3d 1183, 1185–87 (9th Cir. 2013), while also (like us here) permitting relation back when the requirements of Rule 15 are satisfied. *See In re Dominguez*, 51 F.3d at 1509.

C

[3] Because Mr. Beem's motion functioned as an original adversary complaint, we must next determine whether the allegations described in his later-filed complaint "arose out of the conduct, transaction, or occurrence set out—or attempted to be set out—in the original pleading." Fed. R. Civ. P. 15(c)(1)(B). "The critical issue in Rule 15(c) determinations is whether the original complaint gave notice to the defendant of the claim now being asserted." *Makro Cap. of Am., Inc. v. UBS AG*, 543 F.3d 1254, 1260 (11th Cir. 2008) (alteration and quotation omitted). Mr. Beem's later-filed complaint contains nearly-identical factual allegations regarding non-dischargeability as those in his timely motion. As noted, those allegations were sufficient notice to Mr. Ferguson that Mr. Beem objected to the dischargeability of the debt related to the abuse of process judgement. Thus, the same issue was clearly raised in the original pleading and the complaint may

relate back to Mr. Beem's timely filing. *See Gibson v. Resolution Tr. Corp.*, 51 F.3d 1016, 1027 (11th Cir. 1995) ("[A]mendments to complaints relate back to the original filing date when the issue was raised in the original complaint.").

In sum, we agree with the bankruptcy court and district court that Mr. Beem's complaint for non-dischargeability under 11 U.S.C. § 523(a)(6) was timely under the relation back doctrine provided by Bankruptcy Rule 7015. The bankruptcy court thus properly denied Mr. Ferguson's motion to dismiss.

IV

[4] We next must determine whether the grant of summary judgment in favor of Mr. Beem was appropriate. Both the bankruptcy court and the district court ruled that Mr. Ferguson's debt (in the form of Mr. Beem's state court judgment for "defamation; abuse of process") was a non-dischargeable debt under 11 U.S.C. § 523(a)(6). Applying our well-settled collateral estoppel precedent, we affirm the grant of summary judgment.

Collateral estoppel, which bars the relitigation of issues that have been adjudicated in a prior action, applies to an adversary proceeding challenging the dischargeability of a debt. *See In re Bush*, 62 F.3d 1319, 1322 (11th Cir. 1995). "If the prior judgment was rendered by a state court, then the collateral estoppel law of that state must be applied to determine the judgment's preclusive effect." *In re St. Laurent*, 991 F.2d at 675–76. Because Mr. Beem's judgment against Mr. Ferguson was rendered by a Florida state court, we look to Florida law.

Under Florida law, for collateral estoppel to apply, among other things, the issue at stake in this litigation must be identical to the one involved in the prior litigation. *See Aronowitz v. Home Diagnostics, Inc.*, 174 So.3d 1062, 1066 (Fla. 4th DCA 2015). Issues are "sufficiently identical" when their elements and requirements "closely mirror" each other. *See In re St. Laurent*, 991 F.2d at 676 (quotation omitted).

***8** Mr. Ferguson asserts that the issue at stake in the state court litigation regarding whether he acted willfully is not sufficiently identical to the requirement that there be a willful and malicious injury for a debt to be non-dischargeable under § 523(a)(6). Thus, we must consider what Mr. Beem was required to prove for each claim.

Under Florida law, a claim for abuse of process has three elements: "(1) the defendant made an illegal, improper, or perverted use of process; (2) the defendant had an ulterior motive or purpose in exercising the illegal, improper, or perverted process; and (3) the plaintiff was injured as a result of defendant's action." *Hardick v. Homol*, 795 So.2d 1107, 1111 n.2 (Fla. 5th DCA 2001). Florida courts have further explained that an action for abuse of process consists of a "*willful* and *intentional* misuse of process for some wrongful and unlawful object or collateral purpose." *Gause v. First Bank of Marianna*, 457 So.2d 582, 584 (Fla. 1st DCA 1984) (emphasis added) (citing *Peckins v. Kaye*, 443 So.2d 1025, 1026 (Fla. 2d DCA 1983)).

In relevant part, § 523(a)(6) provides that any debt "for willful and malicious injury by the debtor to another entity or to the property of another entity" is non-dischargeable. "Willful" in this provision means "a deliberate or intentional *injury*, not merely a deliberate or intentional *act* that leads to injury." *Kawaauhau v. Geiger*, 523 U.S. 57, 61, 118 S.Ct. 974, 140 L.Ed.2d 90 (1998) (emphasis in original). "Malicious" means "wrongful and without just cause or excessive even in the absence of personal hatred, spite or ill will." *In re Jennings*, 670 F.3d 1329, 1334 (11th Cir. 2012) (quotation omitted). To establish malice "a showing of specific intent to harm another is not necessary." *Id.* (quotation omitted).

We agree with the bankruptcy court and the district court that the state court judgment for abuse of process and the requirements of non-dischargeability for knowing and willful injury under § 523(a)(6) are sufficiently identical for collateral estoppel purposes. Abuse of process contains an express requirement of willfulness or intent, just like § 523(a)(6). *Compare Gause*, 457 So.2d at 584, *with Kawaauhau*, 523 U.S. at 61, 118 S.Ct. 974. It also requires an ulterior motive or purpose, *Hardick*, 795 So.2d at 1111 n.2, which closely mirrors the lack of just cause requirement for malice. *See In re Jennings*, 670 F.3d at 1334 (transfer of property without just cause and effected only to prevent creditor from satisfying personal injury judgment was malicious under § 523(a)(6)). It is thus unsurprising that our sister circuits have held that similar abuse of process judgements are non-dischargeable. *See In re Scarborough*, 171 F.3d 638, 642–44 (8th Cir. 1999); *In re Abbo*, 168 F.3d 930, 932 (6th Cir. 1999). [4]

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***9** Mr. Ferguson seeks to relitigate the state court judgment, raising facts to dispute whether his conduct was actually willful and malicious. But, he had a "full and fair opportunity to litigate that issue in the earlier case," and therefore collateral estoppel bars relitigation of that issue. *See Allen v. McCurry*, 449 U.S. 90, 94–95, 101 S.Ct. 411, 66 L.Ed.2d 308 (1980). In sum, Mr. Ferguson wants an impermissible "second bite at the apple" despite having fully participated in the prior action that resulted in an adverse judgment for abuse of process. *See In re Bush*, 62 F.3d at 1324. The bankruptcy court and the district court correctly determined that collateral estoppel prevented this relitigation and that Mr. Ferguson caused willful and malicious injury to Mr. Beem. Therefore, we affirm the grant of summary judgment.

V

For the foregoing reasons, we find that the bankruptcy court and the district court properly determined that Mr. Beem's complaint related back to his previous filing (the motion), and affirm the grant of summary judgment in favor of Mr. Beem.

AFFIRMED.

All Citations

--- Fed.Appx. ----, 2018 WL 718609

Footnotes

* The Honorable Danny C. Reeves, United States District Judge for the Eastern District of Kentucky, sitting by designation.

1 AP Doc. refers to the docket in the Adversary Proceeding, *Beem v. Ferguson*, Adv. Proc. No. 12-02010-LMI (Bankr. S.D. Fla. 2012).

2 We recognize that *Conley* has been abrogated in part. In *Conley*, the Supreme Court stated that "a complaint could not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." 355 U.S. at 45–46, 78 S.Ct. 99. In *Twombly*, the Supreme Court "retire[d]" *Conley's* "no set of facts" pleading standard. 550 U.S. at 563, 127 S.Ct. 1955. But the Court did not completely abrogate *Conley* as it relied on *Conley's* statement that Rule 8's pleading standard required only that a complaint "give the defendant fair notice of" the plaintiff's claim and the grounds upon which it rests. *Id.* at 555, 127 S.Ct. 1955 (quoting *Conley*, 355 U.S. at 47, 78 S.Ct. 99). The Court thus did not abrogate the portion of *Conley* on which we rely.

3 In *Bonner v. City of Pritchard*, we adopted as binding precedent all decisions of the former Fifth Circuit handed down prior to October 1, 1981. 661 F.2d 1206, 1209 (11th Cir. 1981) (en banc).

4 Our conclusion is not altered by the captioning of Count Three as one for "defamation; abuse of process." Count Three explicitly included the requisite elements of abuse of process. For example, Mr. Beem alleged that Mr. Ferguson filed false complaints with government agencies "for the improper purpose of extorting" him. *See* AP Doc. 106-1 at 63. Extortion is often associated with abuse of process. *See Bothmann v. Harrington*, 458 So.2d 1163, 1169 (Fla. 3d DCA 1984). In granting summary judgment on Count Three, the state court noted that Mr. Ferguson failed to support his allegations with any evidence, despite prosecuting the action for more than a year. Moreover, the jury damage award specifically found that Mr. Beem suffered "emotional damages which were the direct and proximate cause of his defending against Gary Ferguson's Complaint," which is consistent with damages for abuse of process. And, further reinforcing this conclusion, the arguments on appeal to the Florida appellate court focused on abuse of process.

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138 S.Ct. 883
Supreme Court of the United States

MERIT MANAGEMENT GROUP, LP, Petitioner
v.
FTI CONSULTING, INC.

No. 16–784.
|
Argued Nov. 6, 2017.
|
Decided Feb. 27, 2018.

Synopsis
Background: Trustee of litigation trust created pursuant to confirmed Chapter 11 plan of debtor, an entity that sought to develop a "racino" in Pennsylvania, brought adversary proceeding, seeking to avoid debtor's allegedly fraudulent transfers of $16,503,850 to transferee, the partial owner of debtor's competitor, as part of debtor's purchase of competitor's stock. The United States District Court for the Northern District of Illinois, Joan B. Gottschall, J., 541 B.R. 850, granted motion for judgment on the pleadings in transferee's favor. Trustee appealed. The Seventh Circuit Court of Appeals, Wood, Chief Judge, 830 F.3d 690, reversed. Certiorari was granted.

Holdings: The Supreme Court, Justice Sotomayor, held that:

[1] the only relevant transfer for purposes of the Bankruptcy Code's "securities safe harbor" provision is the transfer that the trustee seeks to avoid under a substantive avoiding power, abrogating *In re Quebecor World (USA) Inc.*, 719 F.3d 94, *In re QSI Holdings, Inc.*, 571 F.3d 545, *Contemporary Indus. Corp. v. Frost*, 564 F.3d 981, *In re Resorts Int'l, Inc.*, 181 F.3d 505, and *In re Kaiser Steel Corp.*, 952 F.2d 1230, and

[2] in the present case, the transfer between debtor and transferee was not "made by or to (or for the benefit of)" a financial institution and so fell outside the safe harbor.

Affirmed and remanded.

***885** *Syllabus* [*]

The Bankruptcy Code allows trustees to set aside and recover certain transfers for the benefit of the bankruptcy estate, including, as relevant here, certain fraudulent transfers "of an interest of the debtor in property." 11 U.S.C. § 548(a). It also sets out a number of limits on the exercise of these avoiding powers. Central here is the securities safe harbor, which, *inter alia,* provides that "the trustee may not avoid a transfer that is a ... settlement payment ... made by or to (or for the benefit of) a ... financial institution ... or that is a transfer made by or to (or for the benefit of) a ... financial institution ... in connection with a securities contract." § 546(e).

Valley View Downs, LP, and Bedford Downs Management Corp. entered into an agreement under which Valley View, if it got the last harness-racing license in Pennsylvania, would purchase all of Bedford Downs' stock for $55 million. Valley View was granted the license and arranged for the Cayman Islands branch of Credit Suisse to wire $55 million to third-party escrow agent Citizens Bank of Pennsylvania. The Bedford Downs shareholders, including petitioner Merit Management Group, LP, deposited their stock certificates into escrow. Citizens Bank disbursed the $55 million over two installments according to the agreement, of which petitioner Merit received $16.5 million.

Although Valley View secured the harness-racing license, it was unable to achieve its goal of opening a racetrack casino. Valley View and its parent company, Centaur, LLC, filed for Chapter 11 bankruptcy. Respondent FTI Consulting, Inc., was appointed to serve as trustee of the Centaur litigation trust. FTI then sought to avoid the transfer from Valley View to Merit for the sale of Bedford Downs' stock, arguing that it was constructively fraudulent under § 548(a)(1)(B). Merit contended that the § 546(e) safe harbor barred FTI from avoiding the transfer because it was a "settlement payment ... made by or to (or for the benefit of)" two "financial institutions," Credit Suisse and Citizens Bank. The District Court agreed with Merit, but the Seventh ***886** Circuit reversed, holding that § 546(e) did not protect transfers in which financial institutions served as mere conduits.

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Held : The only relevant transfer for purposes of the § 546(e) safe harbor is the transfer that the trustee seeks to avoid. Pp. 891 – 897.

(a) Before a court can determine whether a transfer was "made by or to (or for the benefit of)" a covered entity, it must first identify the relevant transfer to test in that inquiry. Merit posits that the relevant transfer should include not only the Valley–View–to–Merit end-to-end transfer, but also all of its component parts, *i.e.,* the Credit–Suisse–to–Citizens–Bank and the Citizens–Bank–to–Merit transfers. FTI maintains that the only relevant transfer is the transfer that it sought to avoid, specifically, the overarching transfer between Valley View and Merit. Pp. 891 – 895.

(1) The language of § 546(e) and the specific context in which that language is used support the conclusion that the relevant transfer for purposes of the safe-harbor inquiry is the transfer the trustee seeks to avoid. The first clause of the provision—"Notwithstanding sections 544, 545, 547, 548(a)(1)(B), and 548(b) of this title"—indicates that § 546(e) operates as an exception to trustees' avoiding powers granted elsewhere in the Code. The text makes clear that the starting point for the § 546(e) inquiry is the expressly listed avoiding powers and, consequently, the transfer that the trustee seeks to avoid in exercising those powers. The last clause—"except under section 548(a)(1)(A) of this title"—also focuses on the transfer that the trustee seeks to avoid. Creating an exception to the exception for § 548(a)(1)(A) transfers, the text refers back to a specific type of transfer that falls within the avoiding powers, signaling that the exception applies to the overarching transfer that the trustee seeks to avoid, not any component part of that transfer. This reading is reinforced by the § 546 section heading, "Limitations on avoiding powers," and is confirmed by the rest of the statutory text: The provision provides that "the trustee may not avoid" certain transfers, which naturally invites scrutiny of the transfers that "the trustee ... may avoid," the parallel language used in the avoiding powers provisions. The text further provides that the transfer that is saved from avoidance is one "that *is* " (not one that involves) a securities transaction covered under § 546(e). In other words, to qualify for protection under the securities safe harbor, § 546(e) provides that the otherwise avoidable transfer itself be a transfer that meets the safe-harbor criteria. Pp. 893 – 894.

(2) The statutory structure also supports this reading of § 546(e). The Code establishes a system for avoiding transfers as well as a safe harbor from avoidance. It is thus only logical to view the pertinent transfer under § 546(e) as the same transfer that the trustee seeks to avoid pursuant to one of its avoiding powers. In an avoidance action, the trustee must establish that the transfer it seeks to set aside meets the carefully set out criteria under the substantive avoidance provisions of the Code. The defendant in that avoidance action is free to argue that the trustee failed to properly identify an avoidable transfer under the Code, including any available arguments concerning the role of component parts of the transfer. If a trustee properly identifies an avoidable transfer, however, the court has no reason to examine the relevance of component parts when considering a limit to the avoiding power, where that limit is defined by reference to an otherwise avoidable transfer, as is the case with § 546(e). Pp. 894 – 895.

***887** (b) The primary argument Merit advances that is moored in the statutory text—concerning Congress' 2006 addition of the parenthetical "(or for the benefit of)" to § 546(e)—is unavailing. Merit contends that Congress meant to abrogate the Eleventh Circuit decision in *In re Munford, Inc.,* 98 F.3d 604, which held that § 546(e) was inapplicable to transfers in which a financial institution acted only as an intermediary. However, Merit points to nothing in the text or legislative history to corroborate its argument. A simpler explanation rooted in the text of the statute and consistent with the interpretation of § 546(e) adopted here is that Congress added the "or for the benefit of" language that is common in other substantive avoidance provisions to the § 546(e) safe harbor to ensure that the scope of the safe harbor and scope of the avoiding powers matched.

That reading would not, contrary to what Merit contends, render other provisions ineffectual or superfluous. Rather, it gives full effect to the text of § 546(e). If the transfer the trustee seeks to avoid was made "by" or "to" a covered entity, then § 546(e) will bar avoidance without regard to whether the entity acted only as an intermediary. It will also bar avoidance if the transfer was made "for the benefit of" that entity, even if it was not made "by" or "to" that entity.

Finally, Merit argues that reading the safe harbor so that its application depends on the identity of the investor and the manner in which its investment is held rather than

on the general nature of the transaction is incongruous with Congress' purportedly "prophylactic" approach to § 546(e). But this argument is nothing more than an attack on the text of the statute, which protects only certain transactions "made by or to (or for the benefit of)" certain covered entities. Pp. 894 – 896.

(c) Applying this reading of the § 546(e) safe harbor to this case yields a straightforward result. FTI sought to avoid the Valley–View–to–Merit transfer. When determining whether the § 546(e) safe harbor saves that transfer from avoidance liability, the Court must look to that overarching transfer to evaluate whether it meets the safe-harbor criteria. Because the parties do not contend that either Valley View or Merit is a covered entity, the transfer falls outside of the § 546(e) safe harbor. Pp. 896 – 897.

830 F.3d 690, affirmed and remanded.

SOTOMAYOR, J., delivered the opinion for a unanimous Court.

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Opinion

Justice SOTOMAYOR delivered the opinion of the Court.

[1] To maximize the funds available for, and ensure equity in, the distribution to creditors in a bankruptcy proceeding, the Bankruptcy Code gives a trustee the power to invalidate a limited category of ***888** transfers by the debtor or transfers of an interest of the debtor in property. Those powers, referred to as "avoiding powers," are not without limits, however, as the Code sets out a number of exceptions. The operation of one such exception, the securities safe harbor, 11 U.S.C. § 546(e), is at issue in this case. Specifically, this Court is asked to determine how the safe harbor operates in the context of a transfer that was executed via one or more transactions, *e.g.,* a transfer from A → D that was executed via B and C as intermediaries, such that the component parts of the transfer include A → B → C → D. If a trustee seeks to avoid the A → D transfer, and the § 546(e) safe harbor is invoked as a defense, the question becomes: When determining whether the § 546(e) securities safe harbor saves the transfer from avoidance, should courts look to the transfer that the trustee seeks to avoid (*i.e.,* A → D) to determine whether that transfer meets the safe-harbor criteria, or should courts look also to any component parts of the overarching transfer (*i.e.,* A → B → C → D)? The Court concludes that the plain meaning of § 546(e) dictates that the only relevant transfer for purposes of the safe harbor is the transfer that the trustee seeks to avoid.

I

A

[2] **[3]** Because the § 546(e) safe harbor operates as a limit to the general avoiding powers of a bankruptcy trustee, [1] we begin with a review of those powers. Chapter 5 of the Bankruptcy Code affords bankruptcy trustees the authority to "se[t] aside certain types of transfers ... and ... recaptur[e] the value of those avoided transfers for the benefit of the estate." Tabb § 6.2, p. 474. These avoiding powers "help implement the core principles of bankruptcy." *Id.,* § 6.1, at 468. For example, some "deter the race of diligence of creditors to dismember the debtor before bankruptcy" and promote "equality of distribution." *Union Bank v. Wolas,* 502 U.S. 151, 162, 112 S.Ct. 527, 116 L.Ed.2d 514 (1991) (internal quotation marks omitted); see also Tabb § 6.2. Others set aside transfers that "unfairly or improperly deplete ... assets or ... dilute the claims against those assets." 5 Collier on Bankruptcy ¶ 548.01, p. 548–10 (16th ed. 2017); see also Tabb § 6.2, at 475 (noting that some avoiding powers are designed "to ensure that the debtor deals fairly with its creditors").

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Sections 544 through 553 of the Code outline the circumstances under which a trustee may pursue avoidance. See, *e.g.,* 11 U.S.C. § 544(a) (setting out circumstances under which a trustee can avoid unrecorded liens and conveyances); § 544(b) (detailing power to avoid based on rights that unsecured creditors have under nonbankruptcy law); § 545 (setting out criteria that allow a trustee to avoid a statutory lien); § 547 (detailing criteria for avoidance of so-called "preferential transfers"). The particular avoidance provision at issue here is § 548(a), which provides that a "trustee may avoid" certain fraudulent transfers "of an interest of the debtor in property." § 548(a)(1). Section 548(a)(1)(A) addresses so-called "actually" fraudulent transfers, which are "made ... with actual intent to hinder, delay, or defraud ***889** any entity to which the debtor was or became ... indebted." Section 548(a)(1)(B) addresses "constructively" fraudulent transfers. See *BFP v. Resolution Trust Corporation,* 511 U.S. 531, 535, 114 S.Ct. 1757, 128 L.Ed.2d 556 (1994). As relevant to this case, the statute defines constructive fraud in part as when a debtor:

> "(B)(i) received less than a reasonably equivalent value in exchange for such transfer or obligation; and
>
> "(ii)(I) was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation. 11 U.S.C. § 548(a)(1).

If a transfer is avoided, § 550 identifies the parties from whom the trustee may recover either the transferred property or the value of that property to return to the bankruptcy estate. Section 550(a) provides, in relevant part, that "to the extent that a transfer is avoided ... the trustee may recover ... the property transferred, or, if the court so orders, the value of such property" from "the initial transferee of such transfer or the entity for whose benefit such transfer was made," or from "any immediate or mediate transferee of such initial transferee." § 550(a).

B

The Code sets out a number of limits on the exercise of these avoiding powers. See, *e.g.,* § 546(a) (setting statute of limitations for avoidance actions); §§ 546(c)-(d) (setting certain policy-based exceptions to avoiding powers); § 548(a)(2) (setting limit to avoidance of "a charitable contribution to a qualified religious or charitable entity or organization"). Central to this case is the securities safe harbor set forth in § 546(e), which provides (as presently codified and in full):

> "Notwithstanding sections 544, 545, 547, 548(a)(1)(B), and 548(b) of this title, the trustee may not avoid a transfer that is a margin payment, as defined in section 101, 741, or 761 of this title, or settlement payment, as defined in section 101 or 741 of this title, made by or to (or for the benefit of) a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency, or that is a transfer made by or to (or for the benefit of) a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency, in connection with a securities contract, as defined in section 741(7), commodity contract, as defined in section 761(4), or forward contract, that is made before the commencement of the case, except under section 548(a)(1)(A) of this title."

The predecessor to this securities safe harbor, formerly codified at 11 U.S.C. § 764(c), was enacted in 1978 against the backdrop of a district court decision in a case called *Seligson v. New York Produce Exchange,* 394 F.Supp. 125 (S.D.N.Y.1975), which involved a transfer by a bankrupt commodity broker. See S. Rep. No. 95–989, pp. 8, 106 (1978); see also Brubaker, Understanding the Scope of the § 546(e) Securities Safe Harbor Through the Concept of the "Transfer" Sought To Be Avoided, 37 Bkrtcy. L. Letter 11–12 (July 2017). The bankruptcy trustee in *Seligson* filed suit seeking to avoid over $12 million in margin payments made by the commodity broker debtor to a clearing association on the basis that the transfer was constructively fraudulent. The clearing association attempted to defend on the theory that it was a mere "conduit" for the transmission of the margin payments. 394 F.Supp., at 135. The District Court found, however,

triable issues of fact on that question and denied summary judgment, ***890** leaving the clearing association exposed to the risk of significant liability. See *id.,* at 135–136. Following that decision, Congress enacted the § 764(c) safe harbor, providing that "the trustee may not avoid a transfer that is a margin payment to or deposit with a commodity broker or forward contract merchant or is a settlement payment made by a clearing organization." 92 Stat. 2619, codified at 11 U.S.C. § 764(c) (repealed 1982).

Congress amended the securities safe harbor exception over the years, each time expanding the categories of covered transfers or entities. In 1982, Congress expanded the safe harbor to protect margin and settlement payments "made by or to a commodity broker, forward contract merchant, stockbroker, or securities clearing agency." § 4, 96 Stat. 236, codified at 11 U.S.C. § 546(d). Two years later Congress added "financial institution" to the list of protected entities. See § 461(d), 98 Stat. 377, codified at 11 U.S.C. § 546(e).[2] In 2005, Congress again expanded the list of protected entities to include a "financial participant" (defined as an entity conducting certain high-value transactions). See § 907(b), 119 Stat. 181–182; 11 U.S.C. § 101(22A). And, in 2006, Congress amended the provision to cover transfers made in connection with securities contracts, commodity contracts, and forward contracts. § 5(b)(1), 120 Stat. 2697–2698. The 2006 amendment also modified the statute to its current form by adding the new parenthetical phrase "(or for the benefit of)" after "by or to," so that the safe harbor now covers transfers made "by or to (or for the benefit of)" one of the covered entities. *Id.,* at 2697.

C

[4] With this background, we now turn to the facts of this case, which comes to this Court from the world of competitive harness racing (a form of horse racing). Harness racing is a closely regulated industry in Pennsylvania, and the Commonwealth requires a license to operate a racetrack. See *Bedford Downs Management Corp. v. State Harness Racing Comm'n,* 592 Pa. 475, 485–487, 926 A.2d 908, 914–915 (2007) (*per curiam*). The number of available licenses is limited, and in 2003 two companies, Valley View Downs, LP, and Bedford Downs Management Corporation, were in competition for the last harness-racing license in Pennsylvania.

Valley View and Bedford Downs needed the harness-racing license to open a " 'racino,' " which is a clever moniker for racetrack casino, "a racing facility with slot machines." Brief for Petitioner 8. Both companies were stopped before the finish ***891** line, because in 2005 the Pennsylvania State Harness Racing Commission denied both applications. The Pennsylvania Supreme Court upheld those denials in 2007, but allowed the companies to reapply for the license. See *Bedford Downs,* 592 Pa., at 478–479, 926 A.2d, at 910.

Instead of continuing to compete for the last available harness-racing license, Valley View and Bedford Downs entered into an agreement to resolve their ongoing feud. Under that agreement, Bedford Downs withdrew as a competitor for the harness-racing license, and Valley View was to purchase all of Bedford Downs' stock for $55 million after Valley View obtained the license.[3]

With Bedford Downs out of the race, the Pennsylvania Harness Racing Commission awarded Valley View the last harness-racing license. Valley View proceeded with the corporate acquisition required by the parties' agreement and arranged for the Cayman Islands branch of Credit Suisse to finance the $55 million purchase price as part of a larger $850 million transaction. Credit Suisse wired the $55 million to Citizens Bank of Pennsylvania, which had agreed to serve as the third-party escrow agent for the transaction. The Bedford Downs shareholders, including petitioner Merit Management Group, LP, deposited their stock certificates into escrow as well. At closing, Valley View received the Bedford Downs stock certificates, and in October 2007 Citizens Bank disbursed $47.5 million to the Bedford Downs shareholders, with $7.5 million remaining in escrow at Citizens Bank under the multiyear indemnification holdback period provided for in the parties' agreement. Citizens Bank disbursed that $7.5 million installment to the Bedford Downs shareholders in October 2010, after the holdback period ended. All told, Merit received approximately $16.5 million from the sale of its Bedford Downs stock to Valley View. Notably, the closing statement for the transaction reflected Valley View as the "Buyer," the Bedford Downs shareholders as the "Sellers," and $55 million as the "Purchase Price." App. 30.

In the end, Valley View never got to open its racino. Although it had secured the last harness-racing license, it was unable to secure a separate gaming license for the

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operation of the slot machines in the time set out in its financing package. Valley View and its parent company, Centaur, LLC, thereafter filed for Chapter 11 bankruptcy. The Bankruptcy Court confirmed a reorganization plan and appointed respondent FTI Consulting, Inc., to serve as trustee of the Centaur litigation trust.

FTI filed suit against Merit in the Northern District of Illinois, seeking to avoid the $16.5 million transfer from Valley View to Merit for the sale of Bedford Downs' stock. The complaint alleged that the transfer was constructively fraudulent under § 548(a)(1)(B) of the Code because Valley View was insolvent when it purchased Bedford Downs and "significantly overpaid" for the Bedford Downs stock. [4] Merit moved for judgment on the pleadings under Federal Rule of Civil Procedure 12(c), contending that the § 546(e) safe harbor barred FTI from avoiding the Valley View–to–Merit transfer. According to Merit, the safe harbor applied because the transfer was a "settlement payment ***892** ... made by or to (or for the benefit of)" a covered "financial institution"—here, Credit Suisse and Citizens Bank.

The District Court granted the Rule 12(c) motion, reasoning that the § 546(e) safe harbor applied because the financial institutions transferred or received funds in connection with a "settlement payment" or "securities contract." See 541 B.R. 850, 858 (N.D.Ill.2015). [5] The Court of Appeals for the Seventh Circuit reversed, holding that the § 546(e) safe harbor did not protect transfers in which financial institutions served as mere conduits. See 830 F.3d 690, 691 (2016). This Court granted certiorari to resolve a conflict among the circuit courts as to the proper application of the § 546(e) safe harbor. [6] 581 U.S. ——, 137 S.Ct. 2092, 197 L.Ed.2d 894 (2017).

II

[5] The question before this Court is whether the transfer between Valley View and Merit implicates the safe harbor exception because the transfer was "made by or to (or for the benefit of) a ... financial institution." § 546(e). The parties and the lower courts dedicate much of their attention to the definition of the words "by or to (or for the benefit of)" as used in § 546(e), and to the question whether there is a requirement that the "financial institution" or other covered entity have a beneficial interest in or dominion and control over the transferred property in order to qualify for safe harbor protection. In our view, those inquiries put the proverbial cart before the horse. Before a court can determine whether a transfer was made by or to or for the benefit of a covered entity, the court must first identify the relevant transfer to test in that inquiry. At bottom, that is the issue the parties dispute in this case.

On one side, Merit posits that the Court should look not only to the Valley View–to–Merit end-to-end transfer, but also to all its component parts. Here, those component parts include one transaction by Credit Suisse to Citizens Bank (*i.e.,* the transmission of the $16.5 million from Credit Suisse to escrow at Citizens Bank), and two transactions by Citizens Bank to Merit (*i.e.,* the transmission of $16.5 million over two installments by Citizens Bank as escrow agent to Merit). Because those component parts include transactions by and to financial institutions, Merit contends that § 546(e) bars avoidance.

FTI, by contrast, maintains that the only relevant transfer for purposes of the § 546(e) safe-harbor inquiry is the overarching transfer between Valley View and Merit of $16.5 million for purchase of the stock, which is the transfer that the trustee seeks to avoid under § 548(a)(1)(B). Because that transfer was not made by, to, or for the benefit of a financial institution, FTI contends that the safe harbor has no application.

The Court agrees with FTI. The language of § 546(e), the specific context in ***893** which that language is used, and the broader statutory structure all support the conclusion that the relevant transfer for purposes of the § 546(e) safe-harbor inquiry is the overarching transfer that the trustee seeks to avoid under one of the substantive avoidance provisions.

A

[6] **[7]** Our analysis begins with the text of § 546(e), and we look to both "the language itself [and] the specific context in which that language is used...." *Robinson v. Shell Oil Co.,* 519 U.S. 337, 341, 117 S.Ct. 843, 136 L.Ed.2d 808 (1997). The pertinent language provides:

> "Notwithstanding sections 544, 545, 547, 548(a)(1)(B), and 548(b) of this

> title, the trustee may not avoid a transfer that is a ... settlement payment ... made by or to (or for the benefit of) a ... financial institution ... or that is a transfer made by or to (or for the benefit of) a ... financial institution ... in connection with a securities contract ..., except under section 548(a)(1)(A) of this title."

The very first clause—"Notwithstanding sections 544, 545, 547, 548(a)(1)(B), and 548(b) of this title"—already begins to answer the question. It indicates that § 546(e) operates as an exception to the avoiding powers afforded to the trustee under the substantive avoidance provisions. See A. Scalia & B. Garner, Reading Law: The Interpretation of Legal Texts 126 (2012) ("A dependent phrase that begins with *notwithstanding* indicates that the main clause that it introduces or follows derogates from the provision to which it refers"). That is, when faced with a transfer that is otherwise avoidable, § 546(e) provides a safe harbor notwithstanding that avoiding power. From the outset, therefore, the text makes clear that the starting point for the § 546(e) inquiry is the substantive avoiding power under the provisions expressly listed in the "notwithstanding" clause and, consequently, the transfer that the trustee seeks to avoid as an exercise of those powers.

Then again in the very last clause—"except under section 548(a)(1)(A) of this title"—the text reminds us that the focus of the inquiry is the transfer that the trustee seeks to avoid. It does so by creating an exception to the exception, providing that "the trustee may not avoid a transfer" that meets the covered transaction and entity criteria of the safe harbor, "except" for an actually fraudulent transfer under § 548(a)(1)(A). 11 U.S.C. § 546(e). By referring back to a specific type of transfer that falls within the avoiding power, Congress signaled that the exception applies to the overarching transfer that the trustee seeks to avoid, not any component part of that transfer.

[8] Reinforcing that reading of the safe-harbor provision, the section heading for § 546—within which the securities safe harbor is found—is: "Limitations on avoiding powers." Although section headings cannot limit the plain meaning of a statutory text, see *Florida Dept. of Revenue v. Piccadilly Cafeterias, Inc.,* 554 U.S. 33, 47, 128 S.Ct. 2326, 171 L.Ed.2d 203 (2008), "they supply cues" as to what Congress intended, see *Yates v. United States,* 574 U.S. ——, ——, 135 S.Ct. 1074, 1083, 191 L.Ed.2d 64 (2015). In this case, the relevant section heading demonstrates the close connection between the transfer that the trustee seeks to avoid and the transfer that is exempted from that avoiding power pursuant to the safe harbor.

The rest of the statutory text confirms what the "notwithstanding" and "except" clauses and the section heading begin to suggest. The safe harbor provides that "the trustee may not avoid" certain transfers. § 546(e). Naturally, that text invites ***894** scrutiny of the transfers that "the trustee may avoid," the parallel language used in the substantive avoiding powers provisions. See § 544(a) (providing that "the trustee ... may avoid" transfers falling under that provision); § 545 (providing that "[t]he trustee may avoid" certain statutory liens); § 547(b) (providing that "the trustee may avoid" certain preferential transfers); § 548(a)(1) (providing that "[t]he trustee may avoid" certain fraudulent transfers). And if any doubt remained, the language that follows dispels that doubt: The transfer that the "the trustee may not avoid" is specified to be "a transfer that *is* " either a "settlement payment" or made "in connection with a securities contract." § 546(e) (emphasis added). Not a transfer that involves. Not a transfer that comprises. But a transfer that is a securities transaction covered under § 546(e). The provision explicitly equates the transfer that the trustee may otherwise avoid with the transfer that, under the safe harbor, the trustee may not avoid. In other words, to qualify for protection under the securities safe harbor, § 546(e) provides that the otherwise avoidable transfer itself be a transfer that meets the safe-harbor criteria.

Thus, the statutory language and the context in which it is used all point to the transfer that the trustee seeks to avoid as the relevant transfer for consideration of the § 546(e) safe-harbor criteria.

B

The statutory structure also reinforces our reading of § 546(e). See *Hall v. United States,* 566 U.S. 506, 516, 132 S.Ct. 1882, 182 L.Ed.2d 840 (2012) (looking to statutory structure in interpreting the Bankruptcy Code). As the Seventh Circuit aptly put it, the Code "creates both a system for avoiding transfers and a safe harbor from

avoidance—logically these are two sides of the same coin." 830 F.3d, at 694; see also *Fidelity Financial Services, Inc. v. Fink,* 522 U.S. 211, 217, 118 S.Ct. 651, 139 L.Ed.2d 571 (1998) ("Section 546 of the Code puts certain limits on the avoidance powers set forth elsewhere"). Given that structure, it is only logical to view the pertinent transfer under § 546(e) as the same transfer that the trustee seeks to avoid pursuant to one of its avoiding powers.

[9] As noted in Part I–A, *supra,* the substantive avoidance provisions in Chapter 5 of the Code set out in detail the criteria that must be met for a transfer to fall within the ambit of the avoiding powers. These provisions, as Merit admits, "focus mostly on the characteristics of the transfer that may be avoided." Brief for Petitioner 28. The trustee, charged with exercising those avoiding powers, must establish to the satisfaction of a court that the transfer it seeks to set aside meets the characteristics set out under the substantive avoidance provisions. Thus, the trustee is not free to define the transfer that it seeks to avoid in any way it chooses. Instead, that transfer is necessarily defined by the carefully set out criteria in the Code. As FTI itself recognizes, its power as trustee to define the transfer is not absolute because "the transfer identified must satisfy the terms of the avoidance provision the trustee invokes." Brief for Respondent 23.

Accordingly, after a trustee files an avoidance action identifying the transfer it seeks to set aside, a defendant in that action is free to argue that the trustee failed to properly identify an avoidable transfer under the Code, including any available arguments concerning the role of component parts of the transfer. If a trustee properly identifies an avoidable transfer, however, the court has no reason to examine the relevance of component ***895** parts when considering a limit to the avoiding power, where that limit is defined by reference to an otherwise avoidable transfer, as is the case with § 546(e), see Part II–A, *supra*.

In the instant case, FTI identified the purchase of Bedford Downs' stock by Valley View from Merit as the transfer that it sought to avoid. Merit does not contend that FTI improperly identified the Valley View–to–Merit transfer as the transfer to be avoided, focusing instead on whether FTI can "ignore" the component parts at the safe-harbor inquiry. Absent that argument, however, the Credit Suisse and Citizens Bank component parts are simply irrelevant to the analysis under § 546(e). The focus must remain on the transfer the trustee sought to avoid.

III

A

The primary argument Merit advances that is moored in the statutory text concerns the 2006 addition of the parenthetical "(or for the benefit of)" to § 546(e). Merit contends that in adding the phrase "or for the benefit of" to the requirement that a transfer be "made by or to" a protected entity, Congress meant to abrogate the 1998 decision of the Court of Appeals for the Eleventh Circuit in *In re Munford, Inc.,* 98 F.3d 604, 610 (1996) (*per curiam*), which held that the § 546(e) safe harbor was inapplicable to transfers in which a financial institution acted only as an intermediary. Congress abrogated *Munford,* Merit reasons, by use of the disjunctive "or," so that even if a beneficial interest, *i.e.,* a transfer "for the benefit of" a financial institution or other covered entity, is sufficient to trigger safe harbor protection, it is not necessary for the financial institution to have a beneficial interest in the transfer for the safe harbor to apply. Merit thus argues that a transaction "by or to" a financial institution such as Credit Suisse or Citizens Bank would meet the requirements of § 546(e), even if the financial institution is acting as an intermediary without a beneficial interest in the transfer.

Merit points to nothing in the text or legislative history that corroborates the proposition that Congress sought to overrule *Munford* in its 2006 amendment. There is a simpler explanation for Congress' addition of this language that is rooted in the text of the statute as a whole and consistent with the interpretation of § 546(e) the Court adopts. A number of the substantive avoidance provisions include that language, thus giving a trustee the power to avoid a transfer that was made to "or for the benefit of" certain actors. See § 547(b)(1) (avoiding power with respect to preferential transfers "to or for the benefit of a creditor"); § 548(a)(1) (avoiding power with respect to certain fraudulent transfers "including any transfer to or for the benefit of an insider ..."). By adding the same language to the § 546(e) safe harbor, Congress ensured that the scope of the safe harbor matched the scope of the avoiding powers. For example, a trustee seeking to avoid a preferential transfer under § 547 that was made "for the benefit of a creditor," where that creditor is a covered entity under § 546(e), cannot now escape application of

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the § 546(e) safe harbor just because the transfer was not "made by or to" that entity.

Nothing in the amendment therefore changed the focus of the § 546(e) safe-harbor inquiry on the transfer that is otherwise avoidable under the substantive avoiding powers. If anything, by tracking language already included in the substantive avoidance provisions, the amendment reinforces the connection between the inquiry under § 546(e) and the otherwise ***896** avoidable transfer that the trustee seeks to set aside.

Merit next attempts to bolster its reading of the safe harbor by reference to the inclusion of securities clearing agencies as covered entities under § 546(e). Because a securities clearing agency is defined as, *inter alia,* an intermediary in payments or deliveries made in connection with securities transactions, see 15 U.S.C. § 78c(23)(A) and 11 U.S.C. § 101(48) (defining "securities clearing agency" by reference to the Securities Exchange Act of 1934), Merit argues that the § 546(e) safe harbor must be read to protect intermediaries without reference to any beneficial interest in the transfer. The contrary interpretation, Merit contends, "would run afoul of the canon disfavoring an interpretation of a statute that renders a provision ineffectual or superfluous." Brief for Petitioner 25.

[10] Putting aside the question whether a securities clearing agency always acts as an intermediary without a beneficial interest in a challenged transfer—a question that the District Court in *Seligson* found presented triable issues of fact in that case—the reading of the statute the Court adopts here does not yield any superfluity. Reading § 546(e) to provide that the relevant transfer for purposes of the safe harbor is the transfer that the trustee seeks to avoid under a substantive avoiding power, the question then becomes whether that transfer was "made by or to (or for the benefit of)" a covered entity, including a securities clearing agency. If the transfer that the trustee seeks to avoid was made "by" or "to" a securities clearing agency (as it was in *Seligson*), then § 546(e) will bar avoidance, and it will do so without regard to whether the entity acted only as an intermediary. The safe harbor will, in addition, bar avoidance if the transfer was made "for the benefit of" that securities clearing agency, even if it was not made "by" or "to" that entity. This reading gives full effect to the text of § 546(e).

B

In a final attempt to support its proposed interpretation of § 546(e), Merit turns to what it perceives was Congress' purpose in enacting the safe harbor. Specifically, Merit contends that the broad language of § 546(e) shows that Congress took a "comprehensive approach to securities and commodities transactions" that "was prophylactic, not surgical," and meant to "advanc[e] the interests of parties in the finality of transactions." Brief for Petitioner 41–43. Given that purported broad purpose, it would be incongruous, according to Merit, to read the safe harbor such that its application "would depend on the identity of the investor and the manner in which it held its investment" rather than "the nature of the transaction generally." *Id.,* at 33. Moreover, Merit posits that Congress' concern was plainly broader than the risk that is posed by the imposition of avoidance liability on a securities industry entity because Congress provided a safe harbor not only for transactions "to" those entities (thus protecting the entities from direct financial liability), but also "by" these entities to non-covered entities. See Reply Brief 10–14. And, according to Merit, "[t]here is no reason to believe that Congress was troubled by the possibility that transfers *by* an industry hub could be unwound but yet was unconcerned about trustees' pursuit of transfers made *through* industry hubs." *Id.,* at 12–13 (emphasis in original).

Even if this were the type of case in which the Court would consider statutory purpose, see, *e.g., Watson v. Philip Morris Cos.,* 551 U.S. 142, 150–152, 127 S.Ct. 2301, 168 L.Ed.2d 42 (2007), here Merit fails to ***897** support its purposivist arguments. In fact, its perceived purpose is actually contradicted by the plain language of the safe harbor. Because, of course, here we do have a good reason to believe that Congress was concerned about transfers "*by* an industry hub" specifically: The safe harbor saves from avoidance certain securities transactions "made by or to (or for the benefit of)" covered entities. See § 546(e). Transfers "through" a covered entity, conversely, appear nowhere in the statute. And although Merit complains that, absent its reading of the safe harbor, protection will turn "on the identity of the investor and the manner in which it held its investment," that is nothing more than an attack on the text of the statute, which protects only certain transactions "made by or to (or for the benefit of)" certain covered entities.

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For these reasons, we need not deviate from the plain meaning of the language used in § 546(e).

IV

[11] For the reasons stated, we conclude that the relevant transfer for purposes of the § 546(e) safe harbor is the same transfer that the trustee seeks to avoid pursuant to its substantive avoiding powers. Applying that understanding of the safe-harbor provision to this case yields a straightforward result. FTI, the trustee, sought to avoid the $16.5 million Valley View–to–Merit transfer. FTI did not seek to avoid the component transactions by which that overarching transfer was executed. As such, when determining whether the § 546(e) safe harbor saves the transfer from avoidance liability, *i.e.,* whether it was "made by or to (or for the benefit of) a ... financial institution," the Court must look to the overarching transfer from Valley View to Merit to evaluate whether it meets the safe-harbor criteria. Because the parties do not contend that either Valley View or Merit is a "financial institution" or other covered entity, the transfer falls outside of the § 546(e) safe harbor. The judgment of the Seventh Circuit is therefore affirmed, and the case is remanded for further proceedings consistent with this opinion.

It is so ordered.

All Citations

138 S.Ct. 883, 86 USLW 4088, 65 Bankr.Ct.Dec. 92, 18 Cal. Daily Op. Serv. 1861

Footnotes

* The syllabus constitutes no part of the opinion of the Court but has been prepared by the Reporter of Decisions for the convenience of the reader. See *United States v. Detroit Timber & Lumber Co.,* 200 U.S. 321, 337, 26 S.Ct. 282, 50 L.Ed. 499.

1 Avoiding powers may be exercised by debtors, trustees, or creditors' committees, depending on the circumstances of the case. See generally C. Tabb, Law of Bankruptcy § 6.1 (4th ed. 2016) (Tabb). Because this case concerns an avoidance action brought by a trustee, we refer throughout to the trustee in discussing the avoiding power and avoidance action. The resolution of this case is not dependent on the identity of the actor exercising the avoiding power.

2 The term "financial institution" is defined as:
"(A) a Federal reserve bank, or an entity that is a commercial or savings bank, industrial savings bank, savings and loan association, trust company, federally-insured credit union, or receiver, liquidating agent, or conservator for such entity and, when any such Federal reserve bank, receiver, liquidating agent, conservator or entity is acting as agent or custodian for a customer (whether or not a 'customer', as defined in section 741) in connection with a securities contract (as defined in section 741) such customer; or
"(B) in connection with a securities contract (as defined in section 741) an investment company registered under the Investment Company Act of 1940." 11 U.S.C. § 101(22).
The parties here do not contend that either the debtor or petitioner in this case qualified as a "financial institution" by virtue of its status as a "customer" under § 101(22)(A). Petitioner Merit Management Group, LP, discussed this definition only in footnotes and did not argue that it somehow dictates the outcome in this case. See Brief for Petitioner 45, n. 14; Reply Brief 14, n. 6. We therefore do not address what impact, if any, § 101(22)(A) would have in the application of the § 546(e) safe harbor.

3 A separate provision of the agreement providing that Bedford Downs would sell land to Valley View for $20 million is not at issue in this case.

4 In its complaint, FTI also sought to avoid the transfer under § 544(b). See App. 20–21. The District Court did not address the claim, see 541 B.R. 850, 852–853, n. 1 (N.D.Ill.2015), and neither did the Court of Appeals for the Seventh Circuit.

5 The parties do not ask this Court to determine whether the transaction at issue in this case qualifies as a transfer that is a "settlement payment" or made in connection with a "securities contract" as those terms are used in § 546(e), nor is that determination necessary for resolution of the question presented.

6 Compare *In re Quebecor World (USA) Inc.,* 719 F.3d 94, 99 (C.A.2 2013) (finding the safe harbor applicable where covered entity was intermediary); *In re QSI Holdings, Inc.,* 571 F.3d 545, 551 (C.A.6 2009) (same); *Contemporary Indus. Corp. v. Frost,* 564 F.3d 981, 987 (C.A.8 2009) (same); *In re Resorts Int'l, Inc.,* 181 F.3d 505, 516 (C.A.3 1999) (same);

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In re Kaiser Steel Corp., 952 F.2d 1230, 1240 (C.A.10 1991) (same), with *In re* *Munford, Inc.,* 98 F.3d 604, 610 (C.A.11 1996) (*per curiam*) (rejecting applicability of safe harbor where covered entity was intermediary).

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Supreme Court of the United States

U.S. BANK NATIONAL ASSOCIATION, Trustee, by and through CWCAPITAL ASSET MANAGEMENT LLC, Petitioner
v.
The VILLAGE AT LAKERIDGE, LLC.

No. 15–1509.
|
Argued Oct. 31, 2017.
|
Decided March 5, 2018.

Synopsis
Background: In a Chapter 11 bankruptcy proceeding, the trustee moved to designate creditor's claim and disallow creditor's vote to confirm reorganization plan. The United States Bankruptcy Court for the District of Nevada, Bruce T. Beesley, J., granted the motion in part, and denied the motion in part. Parties cross-appealed. The Bankruptcy Appellate Panel (BAP), Kirscher, Pappas, and Taylor, JJ., 2013 WL 1397447, affirmed in part, reversed in part, and vacated in part. Trustee appealed. The United States Court of Appeals for the Ninth Circuit, N.R. Smith, Circuit Judge, 814 F.3d 993, affirmed, and certiorari was granted.

[Holding:] The Supreme Court, Justice Kagan, held that Bankruptcy Court's determination that creditor did not qualify as a non-statutory insider resolved a mixed question of law and fact subject to review for clear error.

Affirmed.

Justice Kennedy filed a concurring opinion.

Justice Sotomayor filed a concurring opinion in which Justices Kennedy, Thomas, and Gorsuch joined.

Syllabus [*]

***1** Respondent Lakeridge is a corporate entity with a single owner, MBP Equity Partners. When Lakeridge filed for Chapter 11 bankruptcy, it had a pair of substantial debts: It owed petitioner U.S. Bank over $10 million and MBP another $2.76 million. Lakeridge submitted a reorganization plan, proposing to impair the interests of both U.S. Bank and MBP. U.S. Bank refused the offer, thus blocking Lakeridge's option for reorganization through a fully consensual plan. See 11 U.S.C. § 1129(a)(8). Lakeridge then turned to the so-called "cramdown" plan option for imposing a plan impairing the interests of a non-consenting class of creditors. See § 1129(b). Among the prerequisites for judicial approval of such a plan is that another impaired class of creditors has consented to it. See § 1129(a)(10). But crucially here, the consent of a creditor who is also an "insider" of the debtor does not count for that purpose. *Ibid.* The Bankruptcy Code's definition of an insider "includes" any director, officer, or "person in control" of the entity. § 101(31)(B)(i)-(iii). Courts have devised tests for identifying other, so-called "non-statutory" insiders, focusing, in whole or in part, on whether a person's transactions with the debtor were at arm's length.

Here, MBP (an insider of Lakeridge) could not provide the partial agreement needed for a cramdown plan, and Lakeridge's reorganization was thus impeded. MBP sought to transfer its claim against Lakeridge to a non-insider who could agree to the cramdown plan. Kathleen Bartlett, an MBP board member and Lakeridge officer, offered MBP's claim to Robert Rabkin, a retired surgeon, for $5,000. Rabkin purchased the claim and consented to Lakeridge's proposed reorganization. U.S. Bank objected, arguing that Rabkin was a non-statutory insider because he had a "romantic" relationship with Bartlett and the purchase was not an arm's-length transaction. The Bankruptcy Court rejected U.S. Bank's argument. The Ninth Circuit affirmed. Viewing the Bankruptcy Court's decision as one based on a finding that the relevant transaction was conducted at arm's length, the Ninth Circuit held that that finding was entitled to clear-error review, and could not be reversed under that deferential standard.

Held : The Ninth Circuit was right to review the Bankruptcy Court's determination for clear error (rather than *de novo*). At the heart of this case is a so-called "mixed question" of law and fact—whether the Bankruptcy Court's findings of fact satisfy the legal test

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chosen for conferring non-statutory insider status. U.S. Bank contends that the Bankruptcy Court's resolution of this mixed question must be reviewed *de novo,* while Lakeridge (joined by the Federal Government) argues for a clear-error standard.

For all their differences, both parties rightly point to the same query: What is the nature of the mixed question here and which kind of court (bankruptcy or appellate) is better suited to resolve it? Mixed questions are not all alike. Some require courts to expound on the law, and should typically be reviewed *de novo*. Others immerse courts in case-specific factual issues, and should usually be reviewed with deference. In short, the standard of review for a mixed question depends on whether answering it entails primarily legal or factual work.

Here, the Bankruptcy Court confronted the question whether the basic facts it had discovered (concerning Rabkin's relationships, motivations, etc.) were sufficient to make Rabkin a non-statutory insider. Using the transactional prong of the Ninth Circuit's legal test for identifying such insiders (whether the transaction was conducted at arm's length, *i.e.,* as though the two parties were strangers) the mixed question became: Given all the basic facts found, was Rabkin's purchase of MBP's claim conducted as if the two were strangers to each other? That is about as factual sounding as any mixed question gets. Such an inquiry primarily belongs in the court that has presided over the presentation of evidence, that has heard all the witnesses, and that has both the closest and deepest understanding of the record—*i.e.,* the bankruptcy court. One can arrive at the same point by asking how much legal work applying the arm's-length test requires. It is precious little—as shown by judicial opinions applying the familiar legal term without further elaboration. Appellate review of the arm's-length issue—even if conducted *de novo*—will not much clarify legal principles or provide guidance to other courts resolving other disputes. The issue is therefore one that primarily rests with a bankruptcy court, subject only to review for clear error. Pp. —— – ——.

***2** 814 F.3d 993, affirmed.

KAGAN, J., delivered the opinion for a unanimous Court. KENNEDY, J., filed a concurring opinion. SOTOMAYOR, J., filed a concurring opinion, in which KENNEDY, THOMAS, and GORSUCH, JJ., joined.

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Opinion

JUSTICE KAGAN delivered the opinion of the Court.

[1] The Bankruptcy Code places various restrictions on anyone who qualifies as an "insider" of a debtor. The statutory definition of that term lists a set of persons related to the debtor in particular ways. See 11 U.S.C. § 101(31). Courts have additionally recognized as insiders some persons not on that list—commonly known as "non-statutory insiders." The conferral of that status often turns on whether the person's transactions with the debtor (or another of its insiders) were at arm's length. In this case, we address how an appellate court should review that kind of determination: *de novo* or for clear error? We hold that a clear-error standard should apply.

I

Chapter 11 of the Bankruptcy Code enables a debtor company to reorganize its business under a court-approved plan governing the distribution of assets to creditors. See 11 U.S.C. § 1101 *et seq.* The plan divides claims against the debtor into discrete "classes" and specifies the "treatment" each class will receive. § 1123; see § 1122. Usually, a bankruptcy court may approve such a plan only if every affected class of creditors agrees to its terms. See § 1129(a)(8). But in certain circumstances, the court may confirm what is known as a "cramdown" plan—that is, a plan impairing the interests of some non-consenting class. See § 1129(b). Among the prerequisites for judicial approval of a cramdown plan is that another impaired class of creditors has consented to it. See § 1129(a)(10). But crucially for this case, the consent of a creditor who is also an "insider" of the debtor does not count for that purpose. See *ibid.* (requiring "at least one" impaired class to have "accepted the plan, determined

with-out including any acceptance of the plan by any insider”).

The Code enumerates certain insiders, but courts have added to that number. According to the Code's definitional section, an insider of a corporate debtor “includes” any director, officer, or “person in control” of the entity. §§ 101(31)(B)(i)-(iii). Because of the word “includes” in that section, courts have long viewed its list of insiders as non-exhaustive. See § 102(3) (stating as one of the Code's “[r]ules of construction” that “ ‘includes' and ‘including’ are not limiting”); 2 A. Resnick & H. Sommer, Collier on Bankruptcy ¶ 101.31, p. 101–142 (16th ed. 2016) (discussing cases). Accordingly, courts have devised tests for identifying other, so-called “non-statutory” insiders. The decisions are not entirely uniform, but many focus, in whole or in part, on whether a person's “transaction of business with the debtor is not at arm's length.” *Ibid.* (quoting *In re U.S. Medical, Inc.,* 531 F.3d 1272, 1280 (C.A.10 2008)).

***3** This case came about because the Code's list of insiders placed an obstacle in the way of respondent Lakeridge's attempt to reorganize under Chapter 11. Lakeridge is a corporate entity which, at all relevant times, had a single owner, MBP Equity Partners, and a pair of substantial debts. The company owed petitioner U.S. Bank over $10 million for the balance due on a loan. And it owed MBP another $2.76 million. In 2011, Lakeridge filed for Chapter 11 bankruptcy. The reorganization plan it submitted placed its two creditors in separate classes and proposed to impair both of their interests. U.S. Bank refused that offer, thus taking a fully consensual plan off the table. But likewise, a cramdown plan based only on MBP's consent could not go forward. Recall that an insider cannot provide the partial agreement needed for a cramdown plan. See *supra,* at ——; § 1129(a)(10). And MBP was the consummate insider: It owned Lakeridge and so was—according to the Code's definition —“in control” of the debtor. § 101(31)(B)(iii). The path to a successful reorganization was thus impeded, and Lakeridge was faced with liquidation. Unless ...

Unless MBP could transfer its claim against Lakeridge to a non-insider who would then agree to the reorganization plan. So that was what MBP attempted. Kathleen Bartlett, a member of MBP's board and an officer of Lakeridge, approached Robert Rabkin, a retired surgeon, and offered to sell him MBP's $2.76 million claim for $5,000. Rabkin took the deal. And as the new holder of MBP's old loan, he consented to Lakeridge's proposed reorganization. As long as he was not himself an insider, Rabkin's agreement would satisfy one of the prerequisites for a cramdown plan. See § 1129(a)(10); *supra,* at ——. That would bring Lakeridge a large step closer to reorganizing its business over U.S. Bank's objection.

Hence commenced this litigation about whether Rabkin, too, was an insider. U.S. Bank argued that he qualified as a non-statutory insider because he had a “romantic” relationship with Bartlett and his purchase of MBP's loan “was not an arm's-length transaction.” Motion to Designate Claim of Robert Rabkin as an Insider Claim in No. 11–51994 (Bkrtcy. Ct. Nev.), Doc. 194, p. 11 (Motion).[1] At an evidentiary hearing, both Rabkin and Bartlett testified that their relationship was indeed “romantic.” App. 128, 142–143.[2] But the Bankruptcy Court still rejected U.S. Bank's view that Rabkin was a non-statutory insider. See App. to Pet. for Cert. 66a. The court found that Rabkin purchased the MBP claim as a “speculative investment” for which he did adequate due diligence. *Id.,* at 67a. And it noted that Rabkin and Bartlett, for all their dating, lived in separate homes and managed their finances independently. See *id.,* at 66a.

The Court of Appeals for the Ninth Circuit affirmed by a divided vote. According to the court, a creditor qualifies as a non-statutory insider if two conditions are met: “(1) the closeness of its relationship with the debtor is comparable to that of the enumerated insider classifications in [the Code], and (2) the relevant transaction is negotiated at less than arm's length.” *In re Village at Lakeridge, LLC,* 814 F.3d 993, 1001 (2016). The majority viewed the Bankruptcy Court's decision as based on a finding that the relevant transaction here (Rabkin's purchase of MBP's claim) “was conducted at arm's length.” *Id.,* at 1003, n. 15. That finding, the majority held, was entitled to clear-error review, and could not be reversed under that deferential standard. See *id.,* at 1001–1003. Rabkin's consent could therefore support the cramdown plan. See *id.,* at 1003. Judge Clifton dissented. He would have applied *de novo* review, but in any event thought the Bankruptcy Court committed clear error in declining to classify Rabkin as an insider. See *id.,* at 1006.

***4** This Court granted certiorari to decide a single question: Whether the Ninth Circuit was right to review for clear error (rather than *de novo*) the Bankruptcy

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Court's determination that Rabkin does not qualify as a non-statutory insider because he purchased MBP's claim in an arm's-length transaction. 580 U.S. ——, 137 S.Ct. 1372, 197 L.Ed.2d 553 (2017).

II

To decide whether a particular creditor is a non-statutory insider, a bankruptcy judge must tackle three kinds of issues—the first purely legal, the next purely factual, the last a combination of the other two. And to assess the judge's decision, an appellate court must consider all its component parts, each under the appropriate standard of review. In this case, only the standard for the final, mixed question is contested. But to resolve that dispute, we begin by describing the unalloyed legal and factual questions that both kinds of courts have to address along the way, as well as the answers that the courts below provided.

[2] Initially, a bankruptcy court must settle on a legal test to determine whether someone is a non-statutory insider (again, a person who should be treated as an insider even though he is not listed in the Bankruptcy Code). But that choice of standard really resides with the next court: As all parties agree, an appellate panel reviews such a legal conclusion without the slightest deference. See *Highmark, Inc. v. Allcare Health Management System, Inc.,* 572 U.S. ——, ——, 134 S.Ct. 1744, 1748, 188 L.Ed.2d 829 (2014) ("Traditionally, decisions on questions of law are reviewable *de novo* " (internal quotation marks omitted)); Tr. of Oral Arg. 29–30, 33. The Ninth Circuit here, as noted earlier, endorsed a two-part test for non-statutory insider status, asking whether the person's relationship with the debtor was similar to those of listed insiders and whether the relevant prior transaction was at "less than arm's length." 814 F.3d, at 1001; see *supra,* at —— – ——. And the Ninth Circuit held that the Bankruptcy Court had used just that standard—more specifically, that it had denied insider status under the test's second, transactional prong. See 814 F.3d, at 1002–1003, and n. 15; *supra,* at —— – ——. We do not address the correctness of the Ninth Circuit's legal test; indeed, we specifically rejected U.S. Bank's request to include that question in our grant of certiorari. See 580 U.S. ——, 137 S.Ct. 1372, 197 L.Ed.2d 553; Pet. for Cert. i. We simply take that test as a given in deciding the standard-of-review issue we chose to resolve.

[3] Along with adopting a legal standard, a bankruptcy court evaluating insider status must make findings of what we have called "basic" or "historical" fact—addressing questions of who did what, when or where, how or why. *Thompson v. Keohane,* 516 U.S. 99, 111, 116 S.Ct. 457, 464, 133 L.Ed.2d 383 (1995). The set of relevant historical facts will of course depend on the legal test used: So under the Ninth Circuit's test, the facts found may relate to the attributes of a particular relationship or the circumstances and terms of a prior transaction. By well-settled rule, such factual findings are reviewable only for clear error—in other words, with a serious thumb on the scale for the bankruptcy court. See Fed. Rule Civ. Proc. 52(a)(6) (clear-error standard); Fed. Rules Bkrtcy. Proc. 7052 and 9014(c) (applying Rule 52 to various bankruptcy proceedings). Accordingly, as all parties again agree, the Ninth Circuit was right to review deferentially the Bankruptcy Court's findings about Rabkin's relationship with Bartlett (*e.g.,* that they did not "cohabitate" or pay each other's "bills or living expenses") and his motives for purchasing MBP's claim (*e.g.,* to make a "speculative investment"). App. to Pet. for Cert. 66a–67a; see Tr. of Oral Arg. 8, 39.

***5** What remains for a bankruptcy court, after all that, is to determine whether the historical facts found satisfy the legal test chosen for conferring non-statutory insider status. We here arrive at the so-called "mixed question" of law and fact at the heart of this case. *Pullman–Standard v. Swint,* 456 U.S. 273, 289, n. 19, 102 S.Ct. 1781, 1790, n. 19, 72 L.Ed.2d 66 (1982) (A mixed question asks whether "the historical facts ... satisfy the statutory standard, or to put it another way, whether the rule of law as applied to the established facts is or is not violated"). As already described, the Bankruptcy Court below had found a set of basic facts about Rabkin; and it had adopted a legal test for non-statutory insider status that requires (as one of its two prongs) a less-than-arm's-length transaction. See *supra,* at ——, ——. As its last move, the court compared the one to the other—and determined that the facts found did not show the kind of preferential transaction necessary to turn a creditor into a non-statutory insider. For that decisive determination, what standard of review should apply?

The parties, after traveling so far together, part ways at this crucial point. U.S. Bank contends that the Bankruptcy Court's resolution of the mixed question must be reviewed *de novo*. That is because, U.S. Bank claims, application of the Ninth Circuit's "very general"

standard to a set of basic facts requires the further elaboration of legal principles—a task primarily for appellate courts. Brief for Petitioner 35; see *id.,* at 53 (The "open-ended nature of the Ninth Circuit's standard" compels courts to "develop the norms and criteria they deem most appropriate" and so should be viewed as "quasi-legal"). By contrast, Lakeridge (joined by the Federal Government as *amicus curiae*) thinks a clear-error standard should apply. In Lakeridge's view, the ultimate law-application question is all "bound up with the case-specific details of the highly factual circumstances below"—and thus falls naturally within the domain of bankruptcy courts. Brief for Respondent 17; see Brief for United States 21 (similarly describing the mixed question as "fact-intensive").

[4] [5] [6] [7] For all their differences, both parties rightly point us to the same query: What is the nature of the mixed question here and which kind of court (bankruptcy or appellate) is better suited to resolve it? See *Miller v. Fenton,* 474 U.S. 104, 114, 106 S.Ct. 445, 451, 88 L.Ed.2d 405 (1985) (When an "issue falls somewhere between a pristine legal standard and a simple historical fact," the standard of review often reflects which "judicial actor is better positioned" to make the decision).[3] Mixed questions are not all alike. As U.S. Bank suggests, some require courts to expound on the law, particularly by amplifying or elaborating on a broad legal standard. When that is so—when applying the law involves developing auxiliary legal principles of use in other cases—appellate courts should typically review a decision *de novo*. See *Salve Regina College v. Russell,* 499 U.S. 225, 231–233, 111 S.Ct. 1217, 1220–1222, 113 L.Ed.2d 190 (1991) (discussing appellate courts' "institutional advantages" in giving legal guidance). But as Lakeridge replies, other mixed questions immerse courts in case-specific factual issues—compelling them to marshal and weigh evidence, make credibility judgments, and otherwise address what we have (emphatically if a tad redundantly) called "multifarious, fleeting, special, narrow facts that utterly resist generalization." *Pierce v. Underwood,* 487 U.S. 552, 561–562, 108 S.Ct. 2541, 2548, 101 L.Ed.2d 490 (1988) (internal quotation marks omitted). And when that is so, appellate courts should usually review a decision with deference. See *Anderson v. Bessemer City,* 470 U.S. 564, 574–576, 105 S.Ct. 1504, 1511–1512, 84 L.Ed.2d 518 (1985) (discussing trial courts' "superiority" in resolving such issues).[4] In short, the standard of review for a mixed question all depends—on whether answering it entails primarily legal or factual work.

***6 [8]** Now again, recall the mixed question the Bankruptcy Court confronted in this case. See *supra,* at ––––. At a high level of generality, the court needed to determine whether the basic facts it had discovered (concerning Rabkin's relationships, motivations, and so on) were sufficient to make Rabkin a non-statutory insider. But the court's use of the Ninth Circuit's legal test for identifying such insiders reduced that question to a more particular one: whether the facts found showed an arm's-length transaction between Rabkin and MBP. See *ibid.*[5] And still, we can further delineate that issue just by plugging in the widely (universally?) understood definition of an arm's-length transaction: a transaction conducted as though the two parties were strangers. See, *e.g.,* Black's Law Dictionary 1726 (10th ed. 2014). Thus the mixed question becomes: Given all the basic facts found, was Rabkin's purchase of MBP's claim conducted as if the two were strangers to each other?

That is about as factual sounding as any mixed question gets. Indeed, application of the Ninth Circuit's arm's-length legal standard really requires what we have previously described as a "factual inference[ ] from undisputed basic facts." *Commissioner v. Duberstein,* 363 U.S. 278, 291, 80 S.Ct. 1190, 1200, 4 L.Ed.2d 1218 (1960) (holding that clear-error review applied to a decision that a particular transfer was a statutory "gift"). The court takes a raft of case-specific historical facts,[6] considers them as a whole, balances them one against another—all to make a determination that when two particular persons entered into a particular transaction, they were (or were not) acting like strangers. Just to describe that inquiry is to indicate where it (primarily) belongs: in the court that has presided over the presentation of evidence, that has heard all the witnesses, and that has both the closest and the deepest understanding of the record—*i.e.,* the bankruptcy court.

***7** And we can arrive at the same point from the opposite direction—by asking how much legal work applying the arm's-length test requires. Precious little, in our view—as shown by judicial opinions addressing that concept. Our own decisions, arising in a range of contexts, have never tried to elaborate on the established idea of a transaction conducted as between strangers; nor, to our knowledge, have lower courts. See, *e.g., Jones v. Harris Associates L.*

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P., 559 U.S. 335, 346, 130 S.Ct. 1418, 1426, 176 L.Ed.2d 265 (2010); *Commissioner v. Wemyss,* 324 U.S. 303, 307, 65 S.Ct. 652, 654, 89 L.Ed. 958 (1945); *Pepper v. Litton,* 308 U.S. 295, 306–307, 60 S.Ct. 238, 245, 84 L.Ed. 281 (1939). The stock judicial method is merely to state the requirement of such a transaction and then to do the fact-intensive job of exploring whether, in a particular case, it occurred. See, *e.g., Wemyss,* 324 U.S., at 307, 65 S.Ct. 652. Contrary to U.S. Bank's view, there is no apparent need to further develop "norms and criteria," or to devise a supplemental multi-part test, in order to apply the familiar term. Brief for Petitioner 53; see Tr. of Oral Arg. 18; *supra,* at ——. So appellate review of the arm's-length issue—even if conducted *de novo*—will not much clarify legal principles or provide guidance to other courts resolving other disputes. And that means the issue is not of the kind that appellate courts should take over. [7]

The Court of Appeals therefore applied the appropriate standard in reviewing the Bankruptcy Court's determination that Rabkin did not qualify as an insider because his transaction with MBP was conducted at arm's length. A conclusion of that kind primarily rests with a bankruptcy court, subject only to review for clear error. We accordingly affirm the judgment below.

It is so ordered.

Justice KENNEDY, concurring.

I join the opinion for the Court and the concurring opinion by Justice SOTOMAYOR. In doing so, it seems appropriate to add these further comments.

***8** As the Court's opinion makes clear, courts of appeals may continue to elaborate in more detail the legal standards that will govern whether a person or entity is a non-statutory insider under the Bankruptcy Code. *Ante,* at ——, ——, n. 7. At this stage of the doctrine's evolution, this ongoing elaboration of the principles that underlie non-statutory insider status seems necessary to ensure uniform and accurate adjudications in this area.

In particular, courts should consider the relevance and meaning of the phrase "arms-length transaction" in this bankruptcy context. See *ibid.* As courts of appeals address these issues and make more specific rulings based on the facts and circumstances of individual cases, it may be that instructive, more specifically defined rules will develop.

This leads to an additional point. Under the test that the Court of Appeals applied here, there is some room for doubt that the Bankruptcy Judge was correct in concluding that Rabkin was not an insider, especially without further inquiry into whether the offer Bartlett made to Rabkin could and should have been made to other parties who might have paid a higher price. See *In re Village at Lakeridge, LLC,* 814 F.3d 993, 1006 (C.A.9 2016) (Clifton, J., concurring in part and dissenting in part) ("[E]ven if the clear error standard applies, the finding that Rabkin was not a non-statutory insider cannot survive scrutiny"). MBP's failure to offer its claim more widely could be a strong indication that the transaction was not conducted at arm's length. As the Court is careful and correct to note, however, certiorari was not granted on this question. See *ante,* at ——, n. 7. As a result, whether the test for non-statutory insider status as formulated and used by courts in the Ninth Circuit is sufficient is not before us; and whether on these facts it was clear error to find that Rabkin was not an insider is also not before us.

The Court's holding should not be read as indicating that the non-statutory insider test as formulated by the Court of Appeals is the proper or complete standard to use in determining insider status. Today's opinion for the Court properly limits its decision to the question whether the Court of Appeals applied the correct standard of review, and its opinion should not be read as indicating that a transaction is arm's length if the transaction was negotiated simply with a close friend, without broader solicitation of other possible buyers.

Justice SOTOMAYOR, with whom Justice KENNEDY, Justice THOMAS, and Justice GORSUCH join, concurring.

The Court granted certiorari to decide "[w]hether the appropriate standard of review for determining non-statutory insider status" under the Bankruptcy Code is *de novo* or clear error. Pet. for Cert. i. To answer that question, the Court "take[s] ... as a given" the two-prong test that the Court of Appeals for the Ninth Circuit has adopted for determining whether a person or entity is an insider. *Ante,* at ——. I join the Court's opinion in full because, within that context, I agree with the Court's analysis that a determination whether a particular transaction was conducted at arm's length is a mixed

question of law and fact that should be reviewed for clear error. See *ante,* at –––– – ––––.

I write separately, however, because I am concerned that our holding eludes the more fundamental question whether the Ninth Circuit's underlying test is correct. If that test is not the right one, our holding regarding the standard of review may be for naught. That is because the appropriate standard of review is deeply intertwined with the test being applied. As the Court puts it, "the standard of review for a mixed question all depends—on whether answering it entails primarily legal or factual work." *Ante,* at ––––.

***9** Here, the Court identifies the Ninth Circuit as having affirmed on the basis of the second prong of its test, pursuant to which the Ninth Circuit concluded that the relevant transaction between Robert Rabkin and MBP Equity Partners was conducted at arm's length. *Ante,* at ––––. Because that analysis is primarily factual in nature, the Court rightly concludes that appellate review of the Bankruptcy Court's decision is for clear error. *Ante,* at –––– – ––––. However, if the proper inquiry did not turn solely on an arm's-length analysis but rather involved a different balance of legal and factual work, the Court may have come to a different conclusion on the standard of review.

The Court's discussion of the standard of review thus begs the question of what the appropriate test for determining non-statutory insider status is. I do not seek to answer that question, as the Court expressly declined to grant certiorari on it. I have some concerns with the Ninth Circuit's test, however, that would benefit from additional consideration by the lower courts.

As the Ninth Circuit interpreted the Code, "[a] creditor is not a non-statutory insider unless: (1) the closeness of its relationship with the debtor is comparable to that of the enumerated insider classifications in [11 U.S.C.] § 101(31), *and* (2) the relevant transaction is negotiated at less than arm's length." *In re Village at Lakeridge, LLC,* 814 F.3d 993, 1001 (2016) (emphasis added). Under this test, because prongs one and two are conjunctive, a court's conclusion that the relevant transaction was conducted at arm's length necessarily defeats a finding of non-statutory insider status, regardless of how close a person's relationship with the debtor is or whether he is otherwise comparable to a statutorily enumerated insider. [1]

It is not clear to me, however, that the Ninth Circuit has explained how this two-prong test is consistent with the plain meaning of the term "insider" as it appears in the Code. The concept of "insider" generally rests on the presumption that a person or entity alleged to be an insider is so connected with the debtor that any business conducted between them necessarily cannot be conducted at arm's length. See Black's Law Dictionary 915 (10th ed. 2014) (defining "insider" as "[a]n entity or person who is so closely related to a debtor that any deal between them will not be considered an arm's-length transaction and will be subject to close scrutiny"). Title 11 U.S.C. § 101(31) defines "insider" by identifying certain individuals or entities who are considered insiders merely on the basis of their status, without regard to whether any relevant transaction is conducted at arm's length. Such an individual is not under any circumstance able to vote for a reorganization plan. See § 1129(a)(10).

In contrast, under prong two of the Ninth Circuit's test, an individual who is similar to, but does not fall precisely within, one of the categories of insiders listed in § 101(31) will not be considered an insider and will be able to vote under § 1129(a)(10) so long as the transaction relevant to the bankruptcy proceeding is determined to have been conducted at arm's length. This would include, for example, a romantic partner of an insider, even one who in all or most respects acts like a spouse.

***10** Given that courts have interpreted "non-statutory insiders" as deriving from the same statutory definition as the enumerated insiders in § 101(31), the basis for the disparate treatment of two similar individuals is not immediately apparent. Lower courts have concluded that the Code's use of the term "includes" in the definition of "insider" in § 101(31) signals that Congress contemplated that certain other persons or entities in addition to those listed would qualify as insiders. See *ante,* at ––––. Notably, this Court has never addressed that issue directly, although the Court has held in other contexts that "the term 'including' is not one of all-embracing definition, but connotes simply an illustrative application of the general principle." *Federal Land Bank of St. Paul v. Bismarck Lumber Co.,* 314 U.S. 95, 100, 62 S.Ct. 1, 4, 86 L.Ed. 65 (1941).

Assuming § 101(31) encompasses such "non-statutory insiders," the only clue we have as to which persons or entities fall within that category is the list of enumerated insiders and the presumption of lack of arm's length that follows from that label. Because each of those persons or entities are considered insiders regardless of whether a particular transaction appears to have been conducted at arm's length, it is not clear why the same should not be true of non-statutory insiders. That is, an enumerated "insider" does not cease being an insider just because a court finds that a relevant transaction was conducted at arm's length. Then why should a finding that a transaction was conducted at arm's length, without more, conclusively foreclose a finding that a person or entity is a "non-statutory insider"?

Of course, courts must develop some principled method of determining what other individuals or entities fall within the term "insider" other than those expressly provided. I can conceive of at least two possible legal standards that are consistent with the understanding that insider status inherently presumes that transactions are not conducted at arm's length. First, it could be that the inquiry should focus solely on a comparison between the characteristics of the alleged non-statutory insider and the enumerated insiders, and if they share sufficient commonalities, the alleged person or entity should be deemed an insider regardless of the apparent arm's-length nature of any transaction. Cf. *In re Longview Aluminum, LLC,* 657 F.3d 507, 510–511 (C.A.7 2011) (considering only whether a manager of a debtor corporation was comparable to the enumerated insiders, regardless of whether any transaction was conducted at less-than-arm's length).

Second, it could be that the test should focus on a broader comparison that includes consideration of the circumstances surrounding any relevant transaction. If a transaction is determined to have been conducted at less-than-arm's length, it may provide strong evidence in the context of the relationship as a whole that the alleged non-statutory insider should indeed be considered an insider. Relatedly, if the transaction does appear to have been undertaken at arm's length, that may be evidence, considered together with other aspects of the parties' relationship, that the alleged non-statutory insider should not, in fact, be deemed an insider.

***11** Neither of these conceptions reflects the Ninth Circuit's test. Rather, the Ninth Circuit considered separately whether Rabkin was comparable to an enumerated insider and whether the transaction between Rabkin and MBP was conducted at arm's length. See 814 F.3d, at 1002–1003. Because the Ninth Circuit concluded that the transaction was undertaken at arm's length, that finding was dispositive of non-statutory insider status under their test, leading this Court, in turn, to consider the standard of review only with respect to that prong.

It is conceivable, however, that if the appropriate test were different from the one articulated by the Ninth Circuit, such as the two examples I outlined above, the applicable standard of review would be different as well. See *ante,* at ——, ——, n. 5. To make more concrete how this may play out in practice, I briefly walk through how I might apply my two proposed tests to the facts of this case.

If a comparative analysis were the right test, and assuming, *arguendo,* that it involves more legal than factual work thus resulting in *de novo* review, certain aspects of Rabkin's relationship with Kathleen Bartlett, an undisputed insider of the debtor, strike me as suggesting that Rabkin should have been designated as a non-statutory insider. Rabkin purchased the claim from MBP, but Bartlett, a member of MBP's board, facilitated the transaction. Even though Rabkin and Bartlett kept separate finances and lived separately, they shared a "romantic" relationship, see *ante,* at ——; Rabkin knew that the debtor was in bankruptcy, 814 F.3d, at 1003; and Bartlett approached only Rabkin with the offer to sell MBP's claim, *id.,* at 1002. In a strict comparative analysis, Rabkin's interactions with Bartlett and MBP suggest that he may have been acting comparable to an enumerated insider, for example, like a relative of an officer of an insider. See § 101(31)(B)(vi).

Even if the comparative analysis included a broader consideration of features of the transaction that suggest it was conducted at arm's length, and assuming, *arguendo,* that *de novo* review would apply, it is not obvious that those features would outweigh the aspects of the relationship that are concerning. Even though Rabkin purportedly lacked knowledge of the cramdown plan prior to his purchase and considered the purchase a "small investment" not warranting due diligence, 814 F.3d, at 1003, there was no evidence of negotiation over the price, *id.,* at 1004 (Clifton, J., dissenting), or any concrete evidence that MBP obtained real value in the deal aside from the prospect of Rabkin's vote in the cramdown. [2]

Even if the proper test for insider status called for clear error review, it is possible that the facts of this case when considered through the lens of that test, as opposed to one focused solely on arm's length, may have warranted a finding that Rabkin was a non-statutory insider.

***12** This is all to say that I hope that courts will continue to grapple with the role that an arm's-length inquiry should play in a determination of insider status. In the event that the appropriate test for determining non-statutory insider status is different from the one that the Ninth Circuit applied, and involves a different balance of legal and factual work than the Court addresses here, it is possible I would view the applicable standard of review differently. Because I do not read the Court's opinion as foreclosing that result, I join it in full.

All Citations

--- S.Ct. ----, 2018 WL 1143822, 65 Bankr.Ct.Dec. 91

Footnotes

* The syllabus constitutes no part of the opinion of the Court but has been prepared by the Reporter of Decisions for the convenience of the reader. See *United States v. Detroit Timber & Lumber Co.,* 200 U.S. 321, 337, 26 S.Ct. 282, 287, 50 L.Ed. 499 (1906).

1 U.S. Bank also contended that Rabkin automatically inherited MBP's statutory insider status when he purchased its loan. See Motion, p. 10 ("[A]n entity which acquires a claim steps into the shoes of that claimant" (internal quotation marks omitted)). We did not grant review of that question and therefore do not address it in this opinion.

2 Perhaps Bartlett expressed some ambivalence on that score. The transcript of her direct examination reads:
"Q. Okay. And I think the term has been a romantic relationship—you have a romantic relationship?
A. I guess.
Q. Why do you say I guess?
A. Well, no—yes." App. 142–143.
One hopes Rabkin was not listening.

3 In selecting standards of review, our decisions have also asked whether a "long history of appellate practice" supplies the answer. *Pierce v. Underwood,* 487 U.S. 552, 558, 108 S.Ct. 2541, 2543, 101 L.Ed.2d 490 (1988). But we cannot find anything resembling a "historical tradition" to provide a standard for reviewing the mixed question here. *Ibid.*

4 Usually but not always: In the constitutional realm, for example, the calculus changes. There, we have often held that the role of appellate courts "in marking out the limits of [a] standard through the process of case-by-case adjudication" favors *de novo* review even when answering a mixed question primarily involves plunging into a factual record. *Bose Corp. v. Consumers Union of United States, Inc.,* 466 U.S. 485, 503, 104 S.Ct. 1949, 1961, 80 L.Ed.2d 502 (1984); see *Ornelas v. United States,* 517 U.S. 690, 697, 116 S.Ct. 1657, 1662, 134 L.Ed.2d 911 (1996) (reasonable suspicion and probable cause under the Fourth Amendment); *Hurley v. Irish–American Gay, Lesbian and Bisexual Group of Boston, Inc.,* 515 U.S. 557, 567, 115 S.Ct. 2338, 2344, 132 L.Ed.2d 487 (1995) (expression under the First Amendment); *Miller v. Fenton,* 474 U.S. 104, 115–116, 106 S.Ct. 445, 452, 88 L.Ed.2d 405 (1985) (voluntariness of confession under the Fourteenth Amendment's Due Process Clause).

5 A bankruptcy court applying the Ninth Circuit's test might, in another case, reach its separate, non-transactional prong: whether "the closeness of [a person's] relationship with the debtor is comparable to that of the enumerated insider classifications" in the Code. *In re Village at Lakeridge, LLC,* 814 F.3d 993, 1001 (2016); see *supra,* at ——. We express no opinion on how an appellate court should review a bankruptcy court's application of that differently framed standard to a set of established facts.

6 Or, to use the more abundant description we quoted above, "multifarious, fleeting, special, narrow facts that utterly resist generalization." *Pierce,* 487 U.S., at 561–562, 108 S.Ct. 2541 (internal quotation marks omitted); see *supra,* at ——.

7 That conclusion still leaves some role for appellate courts in this area. They of course must decide whether a bankruptcy court committed clear error in finding that a transaction was arm's length (or not). (We express no view of that aspect of the Ninth Circuit's decision because we did not grant certiorari on the question. See *supra,* at ——.) In addition, an appellate court must correct any legal error infecting a bankruptcy court's decision. So if the bankruptcy court somehow misunderstood the nature of the arm's-length query—or if it devised some novel multi-factor test for addressing that issue—an appellate court should apply *de novo* review. And finally, if an appellate court someday finds that further refinement of the arm's-length standard is necessary to maintain uniformity among bankruptcy courts, it may step in to perform that

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legal function. By contrast, what it may *not* do is review independently a garden-variety decision, as here, that the various facts found amount to an arm's-length (or a non-arm's-length) transaction and so do not (or do) confer insider status.

1 Other Circuits have developed analogous rules. See, *e.g., Matter of Holloway,* 955 F.2d 1008, 1011 (C.A.5 1992); *In re U.S. Medical, Inc.,* 531 F.3d 1272, 1277–1278 (C.A.10 2008); *In re Winstar Communications, Inc.,* 554 F.3d 382, 396–397 (C.A.3 2009). But see *In re Longview Aluminum, LLC,* 657 F.3d 507, 510 (C.A.7 2011).

2 Outside the context of a determination of insider status, it is possible that the nature of a transaction is relevant to assessing the integrity of bankruptcy proceedings in other ways; for example, in assessing whether a vote in a reorganization plan was “not in good faith, or was not solicited or procured in good faith.” § 1126(e). It troubles me here that neither the Bankruptcy Court nor the Ninth Circuit considered whether Rabkin's purchase of MBP's claim for $5,000 was for value. See App. to Pet. for Cert. 67a (bankruptcy order); *In re Village at Lakeridge, LLC,* 634 Fed.Appx. 619, 621 (2016). Cf. *In re DBSD North Am., Inc.,* 634 F.3d 79, 104 (C.A.2 2011) (stating that a transferee's overpayment for claims was relevant to a good-faith determination under § 1126(e)); § 548(c) (providing that a transfer will not be considered constructively fraudulent, and will not be voidable under § 548(a), where “a transferee ... takes for value and in good faith”). Indeed, we have no concrete information about what benefit MBP received from the transaction aside from the prospect of Rabkin's vote in the cramdown. Of course, the Ninth Circuit's decision with respect to § 1126(e) is not before this Court, but it again prompts a concern with how the courts below considered the nature of the transaction.

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