

MAR 26 2007

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U.S. BKCY. APP. PANEL
OF THE NINTH CIRCUIT

NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL
OF THE NINTH CIRCUIT

In re:) BAP No. CC-06-1032-KPaJ
)
 TEDDI OF CALIFORNIA,) Bk. No. LA 03-40849-ES
)
 Debtor.)
)
)
)
 STEPHEN MEADOW; WALFORD)
 INVESTMENTS, INC.,)
)
 Appellants,)
)
 v.) **MEMORANDUM***
)
)
 DAVID K. GOTTLIEB, Chapter 7)
 Trustee; SUNTRUST BANK,)
)
 Appellees.)
)

Argued and Submitted on January 17, 2007
at Pasadena, California

Filed - March 26, 2007

Appeal from the United States Bankruptcy Court
for the Central District of California

Honorable Erithe A. Smith, Bankruptcy Judge, Presiding

Before: KLEIN, PAPPAS and JAROSLOVSKY,** Bankruptcy Judges.

*This disposition is not appropriate for publication. Although it may be cited for whatever persuasive value it may have (see Fed. R. App. P. 32.1), it has no precedential value. See 9th Cir. BAP Rule 8013-1.

**Hon. Alan Jaroslovsky, U.S. Bankruptcy Judge for the Northern District of California, sitting by designation.

1 This is an appeal from a \$500,000 compromise of the
2 trustee's avoiding action against a secured creditor. Although
3 appellants, who are noncreditor insiders, withdrew their \$550,000
4 offer to trump the compromise by purchasing the trustee's
5 avoiding action, they contend that the \$500,000 compromise was
6 nevertheless inadequate. We AFFIRM the order approving the
7 compromise as fair and equitable.

8 FACTS

9 Appellee David K. Gottlieb is the chapter 7 trustee in this
10 involuntary case that was commenced in December 2003.

11 Appellant Walford Investments, Inc., ("Walford") is the 100
12 percent shareholder of the debtor corporation.

13 Appellant Stephen Meadow is the president of Walford and is
14 a trustor and trustee of the Stephen H. Meadow and Mary E. Meadow
15 1981 Trust, which owns 100 percent of the shares of Walford
16 (collectively, "Meadow-Walford").

17 Appellee SunTrust Bank ("SunTrust") was the debtor's primary
18 lender and is the defendant in the trustee's avoiding action that
19 is the subject of the presently contested compromise.

20 Three lawsuits pertain to this appeal, two of which are
21 bankruptcy court adversary proceedings (including the action
22 being compromised); the third is a district court civil action
23 presently on appeal to the court of appeals.

24 First, as a matter of background, the trustee sued Meadow-
25 Walford in adversary proceeding no. AD 04-02110-ES to avoid and
26 recover transfers alleged to exceed \$9,000,000. The court
27 approved the compromise of that action on the same day as the
28 compromise that Meadow-Walford is presently appealing.

1 Second, also as a matter of background, Meadow-Walford sued
2 SunTrust in the United States District Court for the Central
3 District of California, (Meadow v. SunTrust Bank, Case No. CV-
4 02439), asserting claims in the nature of lender liability to
5 which SunTrust counterclaimed for breach of contract. The
6 District Court granted summary judgment in favor of SunTrust on
7 the premise that Walford and Meadow lacked standing to assert a
8 cause of action that the district court deemed to be property of
9 the chapter 7 estate unless and until the chapter 7 trustee
10 abandons the cause of action. The termination of that civil
11 action is now before the Ninth Circuit as appeal no. 05-55631.

12 Third, the trustee sued SunTrust in adversary proceeding no.
13 AD 05-02129-ES seeking to avoid and recover allegedly fraudulent
14 and preferential transfers of \$1,745,000, as well as damages
15 based on allegations similar to those made by Meadow-Walford.
16 Before the action was filed, Meadow-Walford rebuffed the
17 trustee's attempt to amend the complaint in no. AD 04-02110-ES so
18 as to join SunTrust as a party to that action.

19 The trustee agreed to compromise with SunTrust under terms
20 providing that SunTrust would pay the trustee \$500,000 in
21 exchange for a mutual release of claims, SunTrust's filed proof
22 of claim for \$1,256,641.72 would be allowed subject to
23 reconciliation for payments received, and SunTrust would withdraw
24 its objection to the employment of the trustee's litigation
25 counsel.¹

26
27 ¹Such an objection by a defendant can be of dubious merit.
28 A defendant ordinarily is not a "person aggrieved" and, hence,
lacks standing to object to the trustee's employment of counsel

(continued...)

1 Consistent with the rule that compromises affecting the
2 estate be reviewed on notice to the entire creditor body with a
3 view to whether they are "fair and equitable," the trustee then
4 filed a motion in the parent bankruptcy case to approve the
5 compromise. In the motion, consistent with decisional law
6 requiring a simultaneous opportunity for a competitive sale when
7 a cause of action capable of being transferred is being
8 compromised, the trustee included a proposed bidding procedure so
9 that parties in interest could purchase the estate's claims
10 against SunTrust. The bidding procedures required a prospective
11 bidder to:

- 12 (a) deposit with the trustee \$75,000 at least five days
prior to the hearing;
- 13 (b) put forth an initial minimum bid of no less than
\$550,000;
- 14 (c) subsequent overbids to be in increments of \$25,000;
- 15 (d) "hold the trustee and estate harmless and indemnify the
trustee and estate for any and all losses, liabilities and
16 expenses arising from the prosecution of the litigation
against SunTrust, as well as any and all losses, liabilities
17 and expenses arising out of any claim made by SunTrust
against the trustee which would have otherwise been released
if SunTrust was the highest bidder" ("Indemnity Provision");
- 18 (e) acknowledge that the trustee has no obligation to
19 participate in continuing litigation arising out of the
purchase of the claims in the complaint.

20 Motion For Order Approving Compromise of Controversy Between
21 David K. Gottlieb, Chapter 7 Trustee and Sun Trust Bank Which is
22 Subject to Overbid, page 3.

23 Appellants filed an opposition to the compromise motion,
24 deposited \$75,000 with the trustee and indicated their desire to
25 submit an overbid.

26
27 ¹(...continued)
28 to prosecute that defendant. Fondiller v. Robertson (In re
Fondiller), 707 F.2d 441, 442 (9th Cir. 1983). To be sure,
SunTrust is simultaneously a defendant and a creditor.

1 At the hearing held on December 6, 2005, Meadow-Walford
2 submitted an overbid of \$550,000, subject to two conditions: (1)
3 that the trustee be required to negotiate a mutually acceptable
4 agreement regarding the assignment of the estate's claims against
5 SunTrust (specifically, the Indemnity Provision), and (2) that
6 their bid be made subject to their right to appeal the court's
7 ruling on the compromise motion.

8 The trustee declined to accept the appellants' bid with the
9 two conditions. The court clarified that any sale would be a
10 sale of the causes of action (rather than the compromise
11 agreement), that its order would be the definitive document
12 transferring the causes of action, and that there would be no
13 separate assignment agreement.

14 The appellants then elected to withdraw their \$550,000
15 overbid and not to participate further in the bidding.

16 As there were no overbids, the court proceeded to consider
17 the \$500,000 compromise under the long-settled "fair and
18 equitable" standards applicable to review of compromises.

19 Meadow-Walford continued to oppose the compromise,
20 contending that it was not fair and equitable. Taking aim at the
21 hold harmless provision, they argued that "the proposed bidding
22 procedures are vague, ambiguous, and designed to chill, rather
23 than encourage, competitive bidding."

24 The court announced its ruling and thereafter rendered
25 written findings of fact and conclusions of law and entered its
26 order approving the compromise. This timely appeal ensued.

1 JURISDICTION

2 The bankruptcy court had jurisdiction via 28 U.S.C. § 1334.
3 We have jurisdiction under 28 U.S.C. § 158(a)(1).
4

5 ISSUES

6 (1) Whether the appellants have standing.

7 (2) Whether the bankruptcy court abused its discretion when
8 it found that the compromise between the trustee and SunTrust was
9 "fair and equitable" and that the bidding procedures contained in
10 the compromise motion were appropriate.
11

12 STANDARD OF REVIEW

13 The bankruptcy court's decision to approve a compromise is
14 reviewed for an abuse of discretion. Martin v. Kane (In re A&C
15 Props.), 784 F.2d 1377, 1380 (9th Cir. 1986); Goodwin v. Mickey
16 Thompson Entm't Grp., Inc. (In re Mickey Thompson Entm't Grp.,
17 Inc.), 292 B.R. 415, 420 (9th Cir. BAP 2003). It is an abuse of
18 discretion to apply an incorrect legal rule. Simantob v. Claims
19 Prosecutor, LLC (In re Lahijani), 325 B.R. 282, 287 (9th Cir. BAP
20 2005). Otherwise, we do not reverse unless we have a definite
21 and firm conviction that the court's findings are a result of a
22 clear error of judgment. Mickey Thompson, 292 B.R. at 420.
23

24 DISCUSSION

25 Before addressing the merits, we note that there is a
26 question regarding standing.
27
28

1
2 The appellees argue that the appellants lack standing to
3 appeal the compromise order because they are not creditors of the
4 debtor. Rather, Walford is an equity holder of the debtor, and
5 Meadow is in control of Walford. The appellees contend that
6 equity holders have no expectation of a distribution because the
7 claims of creditors exceed the probable availability of funds of
8 the estate; in other words, it is not a "surplus" estate. The
9 appellants contend that they nevertheless have standing because
10 they are challenging the inherent fairness of the "failed
11 auction," separate and apart from Walford's equity holder status.

12 The factual scenario implicates both a sale and a
13 compromise, which are separate concepts that require separate
14 analysis. The appellants, as equity holders in a case in which
15 there will be no surplus, ordinarily lack standing to appeal a
16 compromise of a dispute affecting the estate. Since there is no
17 likely return for equity holders, they are not "injured in fact"
18 and, accordingly, normally lack standing. E.g., Duckor Spradling
19 & Metzger v. Baum Trust (In re P.R.T.C., Inc.), 177 F.3d 774,
20 777-79 (9th Cir. 1999); Fondiller, 707 F.2d at 442; Cheng v. K&S
21 Diversified Invs., Inc. (In re Cheng), 308 B.R. 448, 454 (9th
22 Cir. BAP 2004), aff'd mem., 160 F. App'x 644 (9th Cir. 2005).

23 While we have recognized the appellate standing of
24 unsuccessful bidders at auction sales in the contexts presented
25 by Mickey Thompson and Lahijani, this appeal presents a different
26 situation. In those cases, the court either rejected or declined
27 to entertain a bid. Here, in contrast, the appellants elected to
28 withdraw their bid, which makes their case for standing weaker.

1 The appellants, however, explain the withdrawal of their bid
2 as a response to the unsatisfactory "intrinsic structure" of the
3 bidding procedures associated with the sale. They contend that
4 the trustee's proposed bidding procedures were vague, ambiguous
5 and designed to chill competitive bidding.

6 While the case for standing is thin, the critique of the
7 "intrinsic structure of the sale" brings the appellants
8 sufficiently "within the zone of interests" to be protected by
9 the Bankruptcy Code that we will treat them as if they have
10 standing to bring this appeal. In view of the overlap between
11 concepts of compromise and sale, we will address both.

12 II

13 The standard for assessing a compromise is whether the
14 compromise is "fair and equitable," taking into account
15 probability of success in the litigation, and any difficulties in
16 collection, and the expense, inconvenience, and delay of
17 litigation, as well as the view of creditors. A&C Props., 874
18 F.2d at 1381.

19 The appellants raise only one question: whether the release
20 of the trustee by SunTrust was appropriate.

21 The compromise provided for a payment of \$500,000 with
22 SunTrust's proof of claim being allowed, plus a Release of the
23 Trustee by SunTrust:

24 Except for: (a) a breach of this Agreement, and claims
25 arising by reason of such breach; (b) enforcement of
26 rights, obligations and duties arising under this
27 Agreement; and (c) satisfaction of the executory
28 provisions of this Agreement (collectively, the
"Preserved Claims"), and (d) SunTrust's Proof of Claim
filed in the bankruptcy case on February 2, 2005 (the

1 "SunTrust Proof of Claim") in consideration of the
2 provisions of this Agreement, and provided that
3 SunTrust is the successful bidder at the hearing on the
4 Approval Motion, SunTrust does hereby fully and finally
5 compromise and settle with, and forever releases,
6 remises, relieves, waives, relinquishes and discharges
7 the Trustee and the Debtor's bankruptcy estate from any
8 and all claims, complaints, rights, manner of action or
9 actions, cause or causes of action, suits, debts, dues,
10 demands, obligations, charges, costs, expenses
11 (including but not limited to attorney's fees) sums of
12 money, controversies, damages, accounts, agreements,
covenants, contracts, judgments, reckonings, liens and
liabilities of every kind and nature whatsoever,
whether at law or in equity, whether based upon
statute, common law or otherwise, whether matured,
contingent or non-contingent, whether direct or
indirect, whether known or unknown, whether suspected
or unsuspected, whether or not hidden and without
regard to the subsequent discovery or existence of
different or additional facts, which SunTrust ever had,
now have, or may claim to have against the Trustee, or
the bankruptcy estate (the "SunTrust Claims.")

13 Motion for Order Approving Compromise of Controversy Between
14 David K. Gottlieb, Chapter 7 Trustee and Sun Trust Bank Which is
15 Subject to Overbid, exhibit 1.

16 SunTrust and the trustee also agreed to waive the
17 application of California Civil Code § 1542,² which operates to
18 limit the terms of a general release. Essentially, the release
19 acted to absolve the trustee from all future liability.

20 While the trustee was adamant about requiring this
21 provision, the trustee also contended that he knew of nothing
22 that might lead to liability to SunTrust and hence that the
23 "value" of the compromise was impossible to evaluate. From his
24

25 ²California Civil Code § 1542 provides,

26 A general release does not extend to claims which
27 the creditor does not know or suspect to exist in his
28 or her favor at the time of executing the release,
which if known by him or her must have materially
affected his or her settlement with the debtor.

1 standpoint, the value of the release (upon which the trustee
2 nevertheless insisted) was nil.

3 The appellants attempt to make much of this and, in
4 particular, emphasize that the trustee ought not to be able to
5 obtain protection from his own misconduct. While that position
6 would have theoretical appeal in a situation in which the
7 trustee's conduct was questionable, it turns out to be much ado
8 about nothing in this instance because nobody has articulated any
9 actual claims that might be encompassed by the release. In other
10 words, the trustee's seemingly paradoxical insistence on
11 something he contended lacked value was merely the usual
12 reciprocal release upon which prudent parties insist as a
13 precaution even when there is no trouble on the horizon - this is
14 not, in context, overreaching.

15 Moreover, the release would have dropped out of the picture
16 if the appellants had outbid SunTrust. The above-quoted terms of
17 the compromise provided that there would be no release if
18 SunTrust was not the successful bidder at the sale facet of the
19 hearing on the motion to approve the compromise.

20 An acid test of a compromise of a cause of action that is
21 capable of being sold is whether there is anyone who is willing
22 to pay the trustee more than the compromise amount in order to
23 acquire and prosecute the cause of action. The appellants
24 elected not to outbid SunTrust when they chose to withdraw their
25 \$550,000 bid. Hence, one must view their predicament as largely
26 self-inflicted: by withdrawing their bid, they caused the
27 \$500,000 SunTrust bid to pass the acid test.

28

1 In short, the appellants have not carried their appellate
2 burden to demonstrate that the court's assessment of the
3 compromise as fair and equitable was error.

4
5 III

6 The focus now shifts to the sale aspect of the compromise
7 proceeding. First, for the sake of clarity, the basics. What
8 was being compromised was a cause of action (i.e., a "chose in
9 action") by the trustee against SunTrust. Such actions are
10 transferrable by a bankruptcy trustee in this circuit. P.R.T.C.,
11 177 F.3d at 781. SunTrust was willing to pay \$500,000 to acquire
12 and extinguish the chose in action. The sale aspect of the
13 situation was whether there was anyone willing to pay more than
14 \$500,000 to acquire the chose in action.

15 The nub of the issue on appeal is whether the bidding
16 procedures were appropriate under the circumstances.

17 The appellants' challenge to the bidding procedures boils
18 down to two main points of contention: (1) the unknown value of
19 the release given to SunTrust, and (2) the putative overbreadth
20 of the indemnity provision.

21 The appellants argue that the trustee's refusal to disclose
22 to potential bidders and to the court the nature or value of any
23 claims that SunTrust may have against the trustee or the estate
24 made it impossible for the court to determine if the compromise
25 with SunTrust was "fair and equitable."

26 Part of the deal with SunTrust was a mutual release of
27 claims between the trustee and SunTrust, together with an
28 indemnification provision. The appellants argue that because of

1 the lack of disclosure, the indemnification provision was too
2 broad. Not only does it cover claims that SunTrust may bring
3 against the estate, but it also encompasses any claims relating
4 to the trustee's own misconduct.

5 The trustee asserts that he did not value the release and
6 accompanying indemnification provision in the SunTrust compromise
7 because "placing a value on claims that are unknown would be an
8 arbitrary and fruitless exercise." The trustee argues that the
9 inability to value the prospective counterclaims was not due to a
10 lack of due diligence, but rather because "any claims would be
11 specious."

12 Although the appellants argue that absent such valuation of
13 the release, the court was in no position to determine whether
14 their bid of \$550,000 without the release was superior to
15 SunTrust's offer of \$500,000 with the release, we are not
16 persuaded. In the absence of any hint in the record that the
17 trustee has done something to expose the estate to liability to
18 SunTrust (which did not assert a counterclaim addressed to the
19 trustee's conduct), the release and indemnification provisions
20 appear to be routine provisions that are, in context, more form
21 than substance.

22 In any event, the scope of the Indemnity Provision was no
23 broader than the scope of the release agreed to by SunTrust.
24 Both had the same value. If the release had no value because
25 SunTrust had no valid claims against the trustee and the estate,
26 then the appellants would be giving no value in agreeing to the
27 Indemnity Provision. Similarly, if the release had value because
28 counterclaims did arise, then the appellants would be giving an

1 equivalent value by having given the indemnity against the same
2 claims as to which the release would apply. Thus, the value of
3 the indemnity equaled the value of the release.

4 The appellants rely on our decisions in Mickey Thompson and
5 Lahijani to support their contention that the trustee did not
6 meet his burden to demonstrate that the court-approved compromise
7 was fair and equitable.

8 In Mickey Thompson, 292 B.R. 415, there was a settlement
9 that included mutual releases between the estate and a third
10 party purchaser that the trustee did not value. The record was
11 such that, given the nature of that complex litigation, there was
12 a substantial possibility that something of value was involved.
13 Due to the lack of evidence in the record regarding the value of
14 the release, we reversed the court-approved settlement. The
15 distinction here is that the trustee in the present appeal has
16 consistently contended there is nothing of value (other than the
17 trustee's lawsuit) pertinent to the release and there is nothing
18 of record to suggest otherwise.

19 The appellants also argue that our decision in Lahijani, 325
20 B.R. at 282, requires the court to consider an offer to share in
21 the proceeds of any prospective recovery. In that instance, the
22 bidder unambiguously offered a combination of cash and a
23 percentage of the net recovery and then was outbid because the
24 court declined to give any value to the proposed share of the
25 potential recovery. In contrast, in this instance, the withdrawn
26 bid was all cash, and the record does not establish that the
27 appellants unambiguously made an offer to share a recovery with
28 the estate as a component of their bid. The vague,

1 unsubstantiated assertion that appellants informed the trustee
2 that they would be willing to include a judgment sharing
3 provision as part of their offer does not equate with the
4 Lahijani situation.

5 As noted, the disposition of intangible estate property,
6 such as a chose in action, may be sold by the trustee. P.R.T.C.,
7 177 F.3d at 781; Lahijani, 325 B.R. at 288. Disposition of that
8 chose in action by way of compromise is the equivalent of a sale
9 of that property that simultaneously invokes the sale provisions
10 of 11 U.S.C. § 363, and the compromise procedure of Federal Rule
11 of Bankruptcy Procedure 9019(a). Mickey Thompson, 292 B.R. at
12 421.

13 When confronted with a motion to approve a settlement
14 under Rule 9019(a), a bankruptcy court is obliged to
15 consider, as part of the 'fair and equitable' analysis,
16 whether any property of the estate that would be
17 disposed of in connection with the settlement might
18 draw a higher price through a competitive process and
19 be the proper subject of a section 363 sale. Whether
20 to impose formal sale procedures is ultimately a matter
21 of discretion that depends upon the dynamics of the
22 particular situation.

23 Id. at 421-22 (footnote omitted).

24 When viewed as a sale, the issue is whether the terms of the
25 sale to SunTrust created a greater benefit to the estate than the
26 offer with the two conditions given by the appellants. See
27 Lahijani, 325 B.R. at 288. Thus, if the appellants had not
28 withdrawn their bid, the court would have been required to
compare the competing bids. When the appellants withdrew the
bid, they prevented the court from making the necessary
comparison and now are not in a position to complain.

1 factors being urged upon us now on appeal. The bankruptcy court
2 had only one legitimate concern, which was the best interests of
3 the bankruptcy estate. Goodwin v. Mickey Thompson Entm't Grp.,
4 Inc. (In re Mickey Thompson Entm't Grp., Inc.), 292 B.R. 415, 420
5 (9th Cir. BAP 2003).¹ Appellants have made it clear, both in
6 their brief and at oral argument, that they care nothing about
7 the bankruptcy estate. They just want to get their hands on
8 estate property.²

9 Just because technical standing has been established does
10 not mean that either the bankruptcy court was or we are compelled
11 to consider every argument raised by a frustrated buyer.
12 Standing does not confer upon a frustrated buyer the right to
13 assert that it has been harmed. It only confers the right to
14 assert that the bankruptcy estate has been harmed.

15 In egregious cases, the argument of a frustrated buyer that
16 it has been harmed may also establish that the estate has been
17 harmed. For instance, corruption or fraud in the marketing of
18 estate property necessarily harms an estate and a frustrated
19 buyer may be allowed to demonstrate such facts. However, the
20 focus must remain the best interests of the estate, not the
21 would-be buyer.

22
23 ¹The court must of course find that a compromise is fair and
24 reasonable. However, this means fair and reasonable *to the*
25 *creditors*, whose interests are paramount, not frustrated buyers.
26 See Simantob v. Claims Prosecutor, LLC (In re Lahijani), 325 B.R.
27 282, 290 (9th Cir. BAP 2005); Mickey Thompson, 292 B.R. at 420.

28 ²When asked at oral argument how his clients were harmed by
the bankruptcy court's decision, counsel for appellants responded
that "We were precluded from having a fair opportunity to bid . .
. . We spent time, energy and effort . . . wanting to acquire
this interest."

1 In this case, there is no indication of any wrongdoing. All
2 we have is a trustee trying diligently to liquidate an estate and
3 a bankruptcy court properly trying to ensure that the trustee's
4 actions are in the best interests of the estate. Appellants
5 simply have no standing to argue that the bankruptcy court should
6 be reversed because under a different scenario they end up being
7 successful purchasers. Lahijani, 325 B.R. at 290 n.13.

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