

**MAR 29 2007**

**NOT FOR PUBLICATION**

**HAROLD S. MARENUS, CLERK  
U.S. BKCY. APP. PANEL  
OF THE NINTH CIRCUIT**

**UNITED STATES BANKRUPTCY APPELLATE PANEL  
OF THE NINTH CIRCUIT**

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28

In re:	)	BAP No.	AZ-06-1096-PaDS
	)		
GTI CAPITAL HOLDINGS, L.L.C.;	)	Bk. Nos.	03-07923
G.H. GOODMAN INVESTMENTS	)		03-07924
COMPANIES, L.L.C.,	)	(Jointly Administered)	
	)		
Debtors.	)		
	)		
COMERICA BANK-CALIFORNIA,	)		
	)		
Appellant,	)		
	)		
v.	)	<b><u>MEMORANDUM</u></b> <sup>1</sup>	
	)		
GTI CAPITAL HOLDINGS, L.L.C.;	)		
G.H. GOODMAN INVESTMENT	)		
COMPANIES, L.L.C.; EDWARD	)		
M. McDONOUGH, Examiner,	)		
	)		
Appellees.	)		

Argued and Submitted on January 18, 2007  
at Phoenix, Arizona

Filed - March 29, 2007

Appeal from the United States Bankruptcy Court  
for the District of Arizona

Honorable Sarah Sharer Curley, Bankruptcy Judge, Presiding

Before: PAPPAS, DUNN and SMITH, Bankruptcy Judges.

<sup>1</sup> 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.



1 Comerica alleges that GTI defaulted on the loans. On April  
2 3, 2003, Comerica commenced an action against GTI in the Arizona  
3 superior court for, among other relief, the appointment of a  
4 receiver.<sup>3</sup> At a May 6, 2003 hearing, the state court indicated  
5 that it would grant Comerica's request and appoint a receiver.  
6 GTI and GHG filed voluntary petitions for relief under chapter 11  
7 of the Bankruptcy Code on May 8, 2003. The bankruptcy court  
8 granted their motion for joint administration of the cases.

9 Before GTI filed its bankruptcy petition, Comerica had taken  
10 steps in anticipation of GTI's possible insolvency. On March 31,  
11 2003, Comerica placed the GTI loans on non-accrual status and,  
12 though the loans were secured by GTI's assets, it established a  
13 loss reserve for the loans of \$2,553,000 in compliance with  
14 applicable accounting standards (Financial Accounting Standards  
15 Board (FASB) 114). Shortly after GTI's bankruptcy filing,  
16 Comerica increased that loss reserve to \$4,600,000. According to  
17 a bank document dated July 31, 2003, Comerica had developed a plan  
18 of action to "attempt to liquidate all collateral" of GTI by  
19 selling GTI as a going concern by the end of 2003.

20 No trustee was appointed in the bankruptcy cases, nor was a  
21 committee of unsecured creditors organized or appointed. From the  
22 date of filing of the petitions through at least January 23, 2004,  
23 GTI operated its business as a debtor-in-possession.<sup>4</sup>

---

24  
25 <sup>3</sup> Internal Comerica documents indicate that the receivership  
26 action was taken in response to a lender liability lawsuit filed  
by Goodman against Comerica on March 27, 2003.

27 <sup>4</sup> On January 23, 2004, GTI filed a notice with the  
28 bankruptcy court that it would not pursue confirmation of a plan.  
In that notice, GTI advised the court and creditors that it had  
ceased operations, laid off almost all employees and would not

(continued...)

1 On June 18, 2003, GTI's § 341(a) meeting was held. Comerica  
2 alleges that, at the meeting, Goodman admitted: (1) that GTI was  
3 losing almost \$500,000 a month, (2) that GTI was not making  
4 monthly payments of \$432,000 to secured creditors, (3) that  
5 Goodman personally was drawing an exorbitant salary (\$25,000 per  
6 week), and (4) that Goodman was providing himself and his managers  
7 with luxury perks.

8 On June 19, 2003, Comerica filed a motion for the appointment  
9 of an examiner. See § 1104(c) (providing that, on request of a  
10 party in interest, the bankruptcy court may appoint an examiner to  
11 "conduct . . . an investigation of the debtor as is appropriate .  
12 . . ."). The bankruptcy court granted the motion at a July 2,  
13 2003 hearing. After the U.S. Trustee selected McDonough to serve  
14 as examiner, with Comerica's support, the bankruptcy court granted  
15 him the authority to perform the duties specified in § 1106(a) (3),  
16 (a) (4) and (b), and "the power and duty to handle and control all  
17 funds, bank accounts and disbursements" of GTI. To assist him in  
18 his efforts, again without objection from Comerica, Examiner  
19 retained several professionals, including a financial consulting  
20 firm, a law firm, and (later) an environmental consulting firm.

21 GTI was the lessee under a number of equipment and personal  
22 property leases. Some of this leased property was necessary for

---

23  
24 <sup>4</sup>(...continued)  
25 file a plan of reorganization. This information was e-mailed to  
26 counsel for Comerica the same day. Although GTI terminated all  
27 business operations on that date, no trustee subsequently  
28 displaced GTI, and so it continued in its status as a debtor-in-  
possession. See § 1101(a) (providing that "debtor in possession"  
means the debtor in a chapter 11 case unless a trustee is  
appointed). GTI therefore retained its authority to exercise the  
powers of a debtor-in-possession under the Bankruptcy Code that  
were not vested by the bankruptcy court in the examiner, including  
its power to pursue a surcharge under § 506(c).

1 GTI to remain operational. Comerica refused to consent to any  
2 payments by Examiner to these lessors from its cash collateral<sup>5</sup>  
3 until Examiner had carefully analyzed which leases were essential  
4 to GTI's operations. Examiner therefore undertook what was  
5 essentially a cash management analysis to determine what funds  
6 were available to pay the personal property leases that were  
7 determined to be essential to GTI operations.

8 Examiner filed a report with the bankruptcy court on July 22,  
9 2003, which focused on personal property leases. Supplemental  
10 reports were filed on August 28 and September 5 and 12, 2003.  
11 Examiner took steps to reduce GTI's operating costs substantially,  
12 resulting in savings of approximately \$455,000 from August 2003 to  
13 January 2004. While reviewing the leases, Examiner also focused  
14 on controlling cash and cash collateral. In addition, he provided  
15 Comerica with an extensive quantity of financial information  
16 regarding cash expenditures and other matters related to cash  
17 collateral.<sup>6</sup>

18 Examiner then submitted a comprehensive "Preliminary Report"  
19 to the bankruptcy court on August 6, 2003. The Preliminary Report  
20 contained a review of GTI's books and records and recounted  
21 discussions with key personnel. Among the Examiner's findings in

---

22  
23 <sup>5</sup> Comerica claimed a lien in all of GTI's cash.

24 <sup>6</sup> The bankruptcy court would later note in its memorandum  
25 decision that:

26 What is unusual is that the Examiner undertook  
27 the tasks of an independent thorough review  
28 that the Court would normally expect to be  
undertaken by Comerica's business people or by  
professionals retained by the Bank.

28 Memorandum Decision Regarding Surcharge Trial (November 22,  
2005) (the "Memorandum Decision") at 11.

1 the Preliminary Report were the following:

- 2 • Debtor had made significant pre- and post-petition payments  
3 to insiders. There was a lack of timely and reliable  
4 accounting data. There were significant problems with the  
5 cash collateral budget. There was no supporting  
6 documentation for over \$2 million of post-petition  
7 expenditures. There were questionable dealings with post-  
8 petition related third parties.
- 9 • Although the business operations had stabilized and the core  
10 business was intact, GTI did not have the working capital  
11 necessary to increase revenue, GTI could not meet required  
12 debt service, and it would require significant infusion of  
13 cash to reorganize.
- 14 • "The Examiner believes that (based on his investigation to  
15 date) the business affairs of the Debtors under the direction  
16 and control of Mr. Goodman have been mismanaged both pre- and  
17 post-bankruptcy."

18 On August 19, 2003, Comerica requested that the bankruptcy  
19 court expand the Examiner's powers to include the authority to  
20 sell GTI's assets. After notice and a hearing, on October 30,  
21 2003, the court issued its order expanding the Examiner's powers:

22 The powers of the Examiner shall be, and  
23 hereby are, expanded to include all powers  
24 necessary and appropriate to facilitate and  
25 accomplish a sale of substantially all of the  
26 assets (together with any of the Debtors'  
27 executory contracts and unexpired leases) on a  
28 going concern basis pursuant to Bankruptcy  
Code [§ ]363 . . . .

29 The court's order provided further that, if a private going  
30 concern sale of GTI's assets was not arranged by December 31,  
31 2003, Examiner was authorized to sell the assets under § 363 and  
32 assume or reject executory contracts and unexpired leases under  
33 § 365 in an orderly liquidation process, after notice and a  
34 hearing.

35 Following the bankruptcy court's approval of his expanded  
36 powers, Examiner commenced his efforts to market GTI's assets.

1 After soliciting offers, Arizona Materials, LLC ("Arizona  
2 Materials") emerged as the leading prospective buyer of the five  
3 bids submitted.

4 Examiner alleges that he kept Comerica closely apprised of,  
5 and involved in, the asset marketing and sale process. Indeed,  
6 Comerica's counsel provided the lead by which Examiner contacted  
7 the successful bidder, Arizona Materials. Counsel for Comerica  
8 also previewed the bids and received drafts of the purchase  
9 agreement as it was negotiated between Examiner and Arizona  
10 Materials.

11 On December 31, 2003, Arizona Materials executed an Asset  
12 Purchase Agreement in which it agreed to purchase substantially  
13 all of GTI's assets as a going concern for an all-cash price of  
14 \$7.8 million. Examiner filed a motion to approve the sale. While  
15 Comerica supported the sale, after a hearing, the bankruptcy court  
16 declined to approve the sale and sent the parties back to the  
17 negotiating table. Ultimately, Examiner and Arizona Materials  
18 agreed to an all-cash purchase price of \$8 million. On January  
19 23, 2004, Examiner filed an amended motion to approve the sale.<sup>7</sup>

20 On February 19, 2004, the bankruptcy court held a final  
21 hearing concerning the proposed sale transaction. Comerica again  
22 endorsed the sale. There were no bids submitted in excess of  
23 Arizona Materials' bid, and the court approved the sale. The sale  
24 transaction closed on February 20, 2004. As noted, it generated  
25 \$8 million in cash proceeds.

26

27

---

28 <sup>7</sup> This was also the date GTI ceased business operations.  
Supra note 4, at 3-4.

1           On March 16, 2004, Comerica submitted a Motion for  
2 Disbursement of Proceeds of Asset Sale. The primary relief  
3 requested in this motion was an order directing Examiner to pay  
4 Comerica \$7,050,000 plus interest from the date of sale from  
5 proceeds of the sale. Comerica allowed in this motion that the  
6 disbursement would be without prejudice to any claims asserted  
7 against Comerica in any avoidance actions by GTI or Examiner.<sup>8</sup>

8           At a hearing on February 24, 2004, the bankruptcy court had  
9 directed the Examiner to prepare and file a summary of all  
10 administrative expense claims. The Examiner's report, docketed on  
11 April 12, 2004, included recommendations regarding a process for  
12 resolving outstanding claims and other key issues remaining in the  
13 bankruptcy cases, and in particular a suggestion that Examiner "be  
14 authorized to meet and confer with all administrative claimants  
15 and secured creditors in an effort to negotiate a final resolution  
16 of the asserted claims and payment thereon." Before a status  
17 hearing on April 15, 2004, Examiner shared this report on  
18 administrative expenses with Comerica's counsel. Comerica also  
19 filed a Reply in Support of [Comerica's] Motion for Disbursement  
20 of Proceeds of Asset Sale on April 15, 2004, in which it objected  
21 to disbursement of sale proceeds (other than to Comerica) until a  
22 proper allocation of proceeds had been determined. Comerica  
23 suggested modifications of Examiner's protocol, but generally  
24 supported the concept of expanding the Examiner's authority to  
25 engage in "shuttle diplomacy" with the other creditors "to attempt

---

26  
27           <sup>8</sup> Examiner had asserted that Comerica's security interest in  
28 some of GTI's vehicles was avoidable (the "Rolling Stock Avoidance  
Action"), and that Comerica may have received avoidable transfers  
or payments.



1 to negotiate settlements with administrative and secured  
2 claimants.”

3 GTI, Examiner and Comerica appeared with counsel at an  
4 April 15, 2004 hearing. The parties agreed on the record to adopt  
5 a protocol to resolve the remaining major issues in the bankruptcy  
6 case based on the Examiner’s report as modified by suggestions  
7 from Comerica. The protocol was a “joint recommendation of  
8 Comerica and the Examiner.” It established reserves for payment  
9 of administrative and other secured claims, pending their  
10 resolution by settlement or court order, and provided an interim  
11 distribution to Comerica of \$1,698,300 from the sale proceeds. As  
12 presented to the bankruptcy court at the hearing, the protocol  
13 also endorsed the suggestion in Examiner’s report that Examiner’s  
14 power be expanded to include the authority to negotiate  
15 settlements with administrative and secured claimants. In  
16 addressing the bankruptcy court, Comerica’s counsel strongly  
17 endorsed this expansion of the Examiner’s powers:

18 I do encourage you to empower the examiner to  
19 do whatever arm twisting that he can do  
20 between now and the next time we’re here to  
21 see if he can squeeze down those claims a  
22 little bit more through a little bit of  
23 cajoling, and thereby save all of us the time  
24 and energy, and you importantly the time and  
25 energy of having to do the claim objection and  
26 estimation process.

27 Tr. Hr’g 17:14-20 (April 15, 2004).

28 At this April 15 hearing, the issue of surcharging Comerica’s  
collateral was raised by its counsel:

We can also file - well, I don’t know if we’ve  
gotten to the point on surcharge. I mean  
frankly nobody has raised that issue. And if  
that’s something you [the bankruptcy court]  
think we need to preview with you by then [the

1 next hearing], we're happy to do that and it  
2 makes sense.

3 Tr. Hr'g 18:2-6 (April 15, 2004). In response to Comerica's  
4 introduction of the surcharge issue, Examiner proposed to file a  
5 statement of his position on surcharge. This discussion ensued:

6 MILLER [Examiner's counsel]: I do think that  
7 the surcharge issue obviously is the elephant  
8 in the room. I think we should just take it  
9 head on . . . .

10 THE COURT: [W]e need to get that [Examiner's  
11 position on asset allocation, claims  
12 estimation and surcharge] out there as quickly  
13 as possible. . . .

14 MILLER: We can do that, judge, and circulate  
15 it for everybody, and say what we think a fair  
16 surcharge would be.

17 THE COURT: Okay.

18 MILLER: Yes, by Monday, end of business  
19 Monday.

20 THE COURT: Understood. . . .

21 ROTH [counsel for GTI]: I'm assuming that if  
22 three days from now, the examiner has a  
23 position on surcharge, if somebody has a  
24 different position on surcharge, they could  
25 file within this objection deadline as well  
26 their position on surcharges?

27 THE COURT: Right. What we're doing is we're  
28 basically having the examiner lead off on  
surcharge, allocation, all of these issues by  
Monday. . . . It looks like we've got a game  
plan. . . .

Tr. Hr'g 19:8 - 20:9, 30:17-23 (April 15, 2004).

From mid-April through June 2004, Examiner negotiated with  
the administrative expense claimants and arranged several claim  
settlements. Examiner filed notice of these settlements with  
accompanying memoranda to the bankruptcy court for its  
consideration at a status hearing to be held on June 25, 2004. At

1 the hearing, Examiner and Comerica informed the court that most of  
2 the administrative claims had been resolved, and that the  
3 framework of an agreement among Examiner, Comerica and the  
4 settling claimants was close to being finalized. The court  
5 continued the hearing to July 7, 2004.

6 On June 9, 2004, the bankruptcy court signed another order,  
7 with the consent of Comerica, Examiner and GTI, further expanding  
8 the Examiner's powers to collect accounts receivable. In the  
9 following two months, Examiner collected \$261,000 in cash for the  
10 bankruptcy estate.

11 On July 1, 2004, Examiner and Comerica executed a Term Sheet  
12 intended by them to establish the framework for an agreement  
13 between Examiner and Comerica regarding the various administrative  
14 claim settlements and how they would be paid. Examiner filed a  
15 motion to approve the Term Sheet.

16 The Term Sheet is composed of a two-page outline of eleven  
17 issues, with two appendices. The following is a synopsis of its  
18 major provisions:

- 19 • As of May 18, 2003, GTI owed Comerica at least \$18.3 million.
- 20 • Comerica holds a first priority valid lien on substantially  
21 all assets of GTI, except for the Orix lien that is resolved  
22 in the Term Sheet. The Orix claim up to \$505,520 will be  
23 paid out of Comerica collateral. After deducting for  
24 settlement payments (Exhibit A), reserve for disputed claims  
25 (Exhibit B), and the windup reserve (\$200,000), all remaining  
26 asset sale proceeds and cash collateral will be turned over  
27 immediately to Comerica.
- 28 • Examiner and Comerica will seek approval of the compromised  
administrative claims listed on Exhibit A. Any party  
objecting to compromised amount will be transferred to  
Exhibit B as a disputed claim. Examiner and Comerica will  
seek disallowance of all disputed claims (Exhibit B).  
Examiner will set aside a reserve in full amount of the  
disputed claims and will turn over to Comerica any funds in  
reserve not ordered paid by the court to the holders of  
disputed claims.

- 1 • Conditions precedent to Comerica's willingness to agree to  
2 these terms were: (a) settlement of Rolling Stock Avoidance  
3 Action against Comerica; and (b) court approval of the Term  
4 Sheet's recommendation of settlement of other claims against  
5 Comerica.
- 4 • Exhibit A lists 17 claims totaling \$5,540,266.14, to be  
5 settled for a total of \$2,420,205.54. Exhibit B lists five  
6 disputed claims for \$1,317,293.12.

6 On July 7, 2004, the bankruptcy court conducted its initial  
7 hearing on Examiner's motion to approve the Term Sheet. GTI  
8 expressed concern about approving a Term Sheet as opposed to a  
9 definitive settlement agreement. The court denied approval of the  
10 Term Sheet and instructed the parties to prepare and submit a  
11 definitive settlement agreement. Comerica agreed at the July 7,  
12 2004 hearing to work with Examiner to develop a formal settlement  
13 agreement.<sup>9</sup>

14 Unfortunately, Examiner and Comerica could not negotiate a  
15 final settlement agreement. The parties dispute the reasons for  
16 the breakdown in the settlement process. However, the three  
17 issues most frequently mentioned by the parties concern Examiner's  
18 addition of two lessors to the settled claims list (Exhibit A)  
19 requiring an approximate \$500,000 additional expenditure from  
20 Comerica's cash collateral; Comerica's demand that the

---

22 <sup>9</sup> Ironically, Comerica's counsel warned at the hearing that,  
23 if the bankruptcy court later failed to approve a settlement  
24 agreement based on the Term Sheet, the resulting disputes could  
25 last into 2005. Comerica's counsel stated:

25 And the only last thing I would say is the  
26 whole framework of this proposed settlement is  
27 designed so that there will be a pot of money  
28 for creditors to get . . . including Comerica.  
But without that settlement, then we'd be  
fighting probably into 2005.

28 Tr. Hr'g 13:20 - 14:1 (July 7, 2004).

1 administrative expense claimants receive only 90 percent of the  
2 amount of the settlements previously negotiated by Examiner listed  
3 in Exhibit A; and Comerica's assertion that Examiner had  
4 "overspent."<sup>10</sup>

5 On August 11, 2004, GTI and Examiner jointly filed a motion  
6 to surcharge Comerica's collateral for the fees and expenses of  
7 Examiner and his various professionals. On August 25, 2004, the  
8 bankruptcy court conducted a scheduling hearing concerning this  
9 motion. At the hearing, a lessor, Bombardier Capital, Inc.,  
10 argued that it also may assert a surcharge claim and that it would  
11 be appropriate to get all surcharge claims "on the table"  
12 including the claims of the equipment lessors. Tr. Hr'g 6:14  
13 (August 25, 2004). Neither Examiner nor Comerica opposed that  
14 approach. Indeed, Comerica endorsed it and indicated that  
15 Comerica would prefer "surcharge litigation once and not  
16 piecemeal." Tr. Hr'g 7:23 - 8:1 (August 25, 2004). The  
17 bankruptcy court decided that it would allow a supplemental  
18 surcharge motion to be filed, on condition that any party wishing  
19 to join in the proposed surcharge litigation did not unduly delay  
20 the litigation.

---

21  
22 <sup>10</sup> Comerica moved to convert the bankruptcy cases to chapter  
23 7 on July 26, 2004. The motion was opposed by GTI, the Examiner  
24 and four creditors. The motion to convert was denied by the court  
25 in a minute order on August 25, 2004, no appeal was taken by  
26 Comerica, and so the cases continue as chapter 11 cases. On July  
27 28, 2004, Comerica also filed an objection to all the claims  
28 proposed to be paid by Examiner listed on both Exhibits A and B of  
the Term Sheet. Comerica ultimately consented to entry of an  
order on August 25, 2004, approving all the settled administrative  
claims as priority claims under § 507(a)(1) in the amounts  
Comerica and Examiner had listed in Exhibit A. The bankruptcy  
court entered this allowance order shortly after the hearing in  
which it had praised the "Herculean effort" of Examiner in  
resolving these administrative claims.

1 On September 1, 2004, GTI and Examiner filed a joint  
2 supplemental surcharge motion. This supplemental surcharge motion  
3 added July 2004 professional fees and expenses to the earlier  
4 motion. It also sought to surcharge Comerica's collateral for the  
5 amounts required to pay claims under nine personal property leases  
6 for post-petition rent and taxes under the leases in the  
7 approximate amount of \$1,500,000.

8 The bankruptcy court conducted extensive evidentiary hearings  
9 concerning the surcharge motions spanning seven days from December  
10 2004 to June 2005. Testimony was provided by Examiner; Diane  
11 McDonald, a Comerica officer; and Goodman. Over one hundred  
12 documents were admitted into evidence.

13 The bankruptcy court filed its Memorandum Decision regarding  
14 the surcharge on November 22, 2005. In response to Comerica's  
15 motion to amend the decision, the court issued a two-page order on  
16 March 2, 2006.

17 The court's decision is an impressive 96-page narrative which  
18 contains extensive findings of fact and conclusions of law, and  
19 analysis. Summarizing only the most critical points of the  
20 bankruptcy court's ruling, it decided that:

- 21 • GTI had standing to pursue the surcharge motion. Examiner  
22 was also a proper movant given the facts of this case.
- 23 • Comerica caused the bankruptcy court to appoint an examiner  
24 with pervasively broad powers. Because Comerica asked the  
25 court to empower Examiner to perform these duties, Comerica  
26 consented to or caused Examiner and his professionals to  
27 perform these duties.
- 28 • Comerica refused to consent to any payments to personal  
property lessors from funds in its cash collateral until the  
Examiner had analyzed which leases were essential to Debtors'  
operations. Examiner provided Comerica with extensive  
financial information regarding cash expenditures and other  
matters related to Comerica's cash collateral. This was

1 unusual in that the court would ordinarily expect Comerica to  
2 undertake this thorough review.

3 • Examiner's Preliminary Report was lengthy, detailed and a  
4 significant undertaking in light of time constraints. The  
5 Preliminary Report directly and substantially benefitted  
6 Comerica and the bankruptcy estate.

7 • Following the Preliminary Report, Comerica moved to expand  
8 Examiner's powers even further to sell GTI's assets.  
9 Comerica's internal documents establish that Comerica aspired  
10 to have its collateral sold by the end of 2003.

11 • "The Examiner became convinced, in September to October 2003,  
12 that he would be lucky to sell the debtors' assets above the  
13 amount that would be due and owing to Comerica. At trial,  
14 [Examiner] testified that he was of the view in October 2003  
15 that he would have been ecstatic if these assets had sold in  
16 the \$12,000,000 to \$14,000,000 range. Since the approximate  
17 amount of Comerica's debt was at least \$17,000,000 at the  
18 time, the Court conclude[d] that Comerica was undersecured as  
19 early as October 2003." Comerica had called Examiner as a  
20 witness, and it did not object to, nor controvert, this  
21 testimony.

22 • Comerica wanted all of GTI's assets to be sold as one package  
23 as a going concern because liquidation of those assets would  
24 yield less for the bank.

25 • Comerica used the bankruptcy process to accomplish its  
26 business goals. Comerica decided early in the proceedings  
27 that its best course of action was to seek the appointment of  
28 an examiner to force sale of its collateral through the  
court. Comerica filed, but then failed to follow through on,  
a stay relief motion, preferring, instead, to grant Examiner  
the power of sale through the bankruptcy court.

• Comerica repeatedly sought the expansion of Examiner's powers  
with knowledge that the bankruptcy estates did not have the  
resources to pay the accrued and accruing professional fees  
and equipment lease payments.

• Comerica knew of the likely administrative insolvency of the  
bankruptcy estates when it consented on the record at the  
April 14, 2004 hearing that Examiner and his professionals  
should proceed with at least an initial surcharge analysis.  
In doing so, Comerica consented to having at least initial  
costs of Examiner and his law firm surcharged against its  
collateral.

• The court was unable to conclude that all costs on the  
surcharge issue should be the sole responsibility of  
Comerica. As a result, the court analyzed the different  
expenses, deducted certain costs of the professionals, and  
indicated that they must be addressed at another hearing.

- 1 • At the time of preparation of the Term Sheet, Comerica and  
2 Examiner knew that there were limited funds available to pay  
3 the remaining claimants. The Term Sheet was structured such  
4 that Comerica waived claims to a portion of its alleged  
5 collateral to create funding to pay the administrative  
6 claimants. "Comerica was consenting to its collateral being  
7 surcharged to resolve all remaining issues in the case."  
8  
9 • "The evidence at trial establishes, and the Court so finds,  
10 that Comerica breached the letter and spirit of the Term  
11 Sheet when the Bank demanded that all administrative expense  
12 creditors take less than prompt payment in full on their  
13 settled claims and absorb the economic risk associated with  
14 the outcome of the Registry Funds dispute. Comerica's  
15 actions in this regard were taken in bad faith and resulted  
16 in the failure of the Examiner and Comerica to enter into a  
17 definitive settlement agreement."  
18  
19 • Comerica received a direct, substantial and quantifiable  
20 benefit from all of the work of the Examiner and his counsel  
21 in connection with: preparation of the Preliminary Report and  
22 stabilization of GTI's business; Examiner's efforts in  
23 controlling cash, eliminating the possibility of insider  
24 defalcations, negotiating and documenting cash collateral  
25 budgets, and paring down personal property leases; and in  
26 Examiner's quick sale of Comerica's collateral as a going  
27 concern when Comerica knew that it would receive less in a  
28 liquidation.
- Comerica benefitted from Examiner's sale of GTI's assets  
through the bankruptcy court, thereby avoiding the costs of  
stay relief litigation, foreclosure of its real estate  
collateral, and general expenses associated with personal  
property sales.
- The efforts of Examiner and his legal counsel resulted in  
recovery of approximately \$1 million in accounts receivable  
which were Comerica collateral.
- An internal document, Comerica's "Dispute Litigation  
Settlement Authorization," dated June 30, 2004, establishes  
that its senior executives approved the Term Sheet because in  
return for resolving all the issues involved in the  
administration of the GTI cases, Comerica could also thereby  
settle the three pending adversary proceedings for the cost  
of what it already expected to lose in the Rolling Stock  
Avoidance Action.<sup>11</sup>

---

<sup>11</sup> Comerica did eventually lose \$1,010,581 in the Rolling  
Stock Avoidance Action (approximately \$89,000 less than the \$1.1  
million it would have given up in the Term Sheet). Obviously,  
however, it was required to pay the costs of litigating that  
action. See this Panel's unpublished decision in Comerica v.  
McDonough, et al. (BAP no. AZ-05-1045, September 7, 2006).



1 • "The court concludes, based on this record, that Comerica  
2 consented to have its collateral surcharged to pay a majority  
3 of the fees incurred by the Examiner and his professionals in  
4 this case."

5 Based upon these extensive findings and conclusions, on March  
6 1, 2006, the bankruptcy court eventually entered an amended order  
7 approving a surcharge against Comerica's collateral in the total  
8 amount of \$1,399,458.47. Comerica filed a timely appeal on March  
9 9, 2006.<sup>12</sup>

10 **JURISDICTION**

11 The bankruptcy court had jurisdiction under 28 U.S.C. §§ 1334  
12 and 157(b) (2). We have jurisdiction under 28 U.S.C. § 158(b).

13 **ISSUES**

- 14 1. Whether the bankruptcy court erred in determining that  
15 Examiner had standing to assert a surcharge claim.  
16 2. Whether the bankruptcy court erred in allowing lessors'  
17 claims to be included in the surcharge litigation.  
18 3. Whether the bankruptcy court applied the proper legal  
19 standard and burden of proof in ordering a surcharge of  
20 Comerica's collateral.

---

21 <sup>12</sup> In October 2006, Examiner filed a Motion to Strike  
22 Improper Record References from Appellant's Opening Brief.  
23 Comerica filed a response to Examiner's motion and Examiner  
24 replied to Comerica's response. We do not find merit in  
25 Examiner's motion. Examiner's objections to tabs 146, 211, 212,  
26 215, 114, 131, 145, 153, 163, 110 and 207 concern various de  
27 minimis defects in the text or requests that they be replaced with  
28 the Examiner's copies. None of these objections are material.  
Examiner's objections to tabs 148, 151, 166, 279, 180, 186, 188  
and 189 on the grounds that they were not admitted in the  
surcharge trial or only conditionally admitted are overruled on  
the grounds that they are in the docket of the bankruptcy case or  
adversary proceeding and this Panel may consult the docket of the  
underlying bankruptcy proceedings. Examiner's objection to tabs  
137, 108 and 208 are not material because the Panel did not find  
it necessary to examine those documents. For these reasons,  
Examiner's motion to strike is DENIED.

1 4. Whether the bankruptcy court abused its discretion when it  
2 excluded from evidence the report and testimony of Comerica's  
3 expert.

#### 4 **STANDARDS OF REVIEW**

5 Standing is a jurisdictional issue that is subject to de novo  
6 review. McClellan Fed. Credit Union v. Parker (In re Parker), 193  
7 B.R. 525, 527 (9th Cir. BAP 1996).

8 The bankruptcy court's interpretation and application of  
9 § 506(c) of the Bankruptcy Code is reviewed de novo. Debbie  
10 Reynolds Hotel & Casino, Inc. v. Calstar Corp. (In re Debbie  
11 Reynolds Hotel & Casino, Inc.), 255 F.3d 1061, 1065 (9th Cir.  
12 2001). However, "[t]he issue of whether expenses were reasonable,  
13 necessary, and benefitted the secured creditor is a question of  
14 fact which we review for clear error." Golden v. Chicago Title  
15 Ins. Co. (In re Choo), 273 B.R. 608, 611 (9th Cir. BAP 2002)  
16 citing Bank of Honolulu v. Anderson (In re Anderson), 66 B.R. 97,  
17 99 (9th Cir. BAP 1986).

18 A court's decision to exclude expert testimony is reviewed  
19 for abuse of discretion. United States v. Rahm, 993 F.2d 1405,  
20 1410 (9th Cir. 1993).

#### 21 **DISCUSSION**

22 1. GTI had standing to pursue a surcharge claim against  
23 Comerica, and Examiner could properly join in that motion.

24 A.

25 Section 506(c) authorizes a trustee to surcharge the  
26 collateral of a secured claimant under certain conditions:

27 The trustee may recover from property securing  
28 an allowed secured claim the reasonable,  
necessary costs and expenses of preserving, or

1 disposing of, such property to the extent of  
2 any benefit to the holder of such claim.

3 The bankruptcy court granted the joint motions of Examiner  
4 and GTI to surcharge the cash collateral of Comerica for a portion  
5 of the costs and expenses of Examiner and his professionals, and  
6 for certain payments made by Examiner to equipment lessors during  
7 the bankruptcy case. Comerica objected to this request, in part  
8 because it contends Examiner lacks standing<sup>13</sup> under the Bankruptcy  
9 Code to request a surcharge. Comerica's objection lacks merit.

10 Had Examiner independently filed the surcharge motions,  
11 Comerica's objection might warrant serious consideration. The  
12 Supreme Court has ruled that § 506(c) unambiguously provides that  
13 only a trustee has standing to bring surcharge actions. Hartford  
14 Underwriters Ins. Co. v. Union Planters Bank, 530 U.S. 1, 6 (2000)  
15 ("We conclude that 11 U.S.C. § 506(c) does not provide an  
16 administrative claimant an independent right to use the section to  
17 seek payment of its claim.").

18 However, in this case, Examiner did not file the surcharge  
19 motions "independently." Both surcharge motions were filed  
20 jointly by Examiner and by GTI as debtor-in-possession. The  
21 Supreme Court in Hartford Underwriters acknowledged that "Debtors-  
22 in-possession may also use [§ 506(c)], because they are expressly  
23 given the rights and powers of a trustee by 11 U.S.C. § 1107."  
24

---

25 <sup>13</sup> As a preliminary matter, we note that the bankruptcy court  
26 never ruled that Examiner had independent standing to initiate the  
27 surcharge motions. Instead, the court described its analysis of  
28 this question in terms of "the Examiner's right to be heard in  
connection with the Surcharge Motions." As the bankruptcy court  
correctly noted, it is Comerica that has attempted to characterize  
this issue as one of standing.

1 530 U.S. at 3 n.3. Regardless of any question as to the standing  
2 of Examiner to assert a right to a surcharge independently, the  
3 surcharge requests in this case were properly initiated by the  
4 entity authorized in the Bankruptcy Code to do so, GTI, the  
5 debtor-in-possession.

6 Moreover, there is nothing in Hartford Underwriters to  
7 suggest that an examiner in a chapter 11 case, especially one with  
8 the enhanced powers given Examiner here, may not join in a  
9 surcharge motion, as opposed to acting independently of the  
10 debtor-in-possession. As the bankruptcy court observed, there is  
11 no requirement that the court examine the standing of a co-movant  
12 once it has established that one of the parties initiating an  
13 action has standing to do so. "The general rule applicable to  
14 federal court suits with multiple plaintiffs is that once the  
15 court determines that one of the plaintiffs has standing, it need  
16 not decide the standing of the others." Leonard v. Clark, 12 F.3d  
17 885, 888 (9th Cir. 1994) (citing Carey v. Population Servs. Int'l,  
18 431 U.S. 678, 682 (1977)). Since the bankruptcy court correctly  
19 decided that one of the parties pursuing the surcharge claim had  
20 standing, as explained in Leonard, that "end[s] the inquiry." 12  
21 F.3d at 888.<sup>14</sup>

22 We agree with the bankruptcy court in its Memorandum Decision  
23 that "because the debtors are proper movants on the surcharge

---

24  
25 <sup>14</sup> Comerica reminds us that in Leonard, the court ultimately  
26 held that the co-plaintiffs did not have standing. The principal  
27 plaintiff in Leonard was a union and the co-plaintiffs were  
28 members of the union. The court determined that the union had  
waived its right to pursue the action and, therefore, the co-  
plaintiffs, who derived standing from their membership rights in  
the union, lost that standing. Here GTI did not waive its right  
to seek a surcharge, and consequently, the co-movant, Examiner,  
need not assert independent standing.

1 motions, the Examiner's technical standing under § 506(c) is  
2 largely irrelevant." Memorandum Decision at 64.<sup>15</sup>

3 B.

4 We also agree with the bankruptcy court that, under the facts  
5 of this case, it was proper that Examiner "take the lead" in  
6 prosecuting the surcharge litigation in this case. Indeed, GTI  
7 would be greatly hampered in its ability to pursue the surcharge  
8 motions without the benefit of Examiner's insight and familiarity  
9 with the facts and circumstances of these cases. Clearly,  
10 Examiner is the party most familiar with the financial aspects of  
11 these cases, having been placed in control of GTI's cash  
12 resources, at Comerica's request, from early on.<sup>16</sup>

13 Even if Examiner lacked standing independent of GTI to pursue  
14 surcharge, Examiner had the right to be heard on the surcharge  
15 issue in order to perform those duties authorized by the  
16 bankruptcy court. Comerica disputes Examiner's status based upon

---

17  
18 <sup>15</sup> Even on appeal, GTI continues to act in concert with  
19 Examiner concerning the surcharge claims. GTI filed a joinder in  
20 the appellate brief of Examiner, in which it "join[s] in and fully  
21 support[s] the Answering Brief of Appellee Edward M. McDonough."  
22 GTI Joinder Brief at 2.

23 <sup>16</sup> We are perplexed by Comerica's suggestion that, had GTI  
24 solely pursued the surcharge motions, the relief requested would  
25 be substantially different and would not include any payments for  
26 compensation and expenses for Examiner and his professionals.  
27 This notion is apparently premised on a series of letters from  
28 Goodman to GTI's attorneys instructing them not to support  
payments to Examiner or his professionals. But GTI's counsel  
never implemented these instructions. Instead, GTI joined with  
Examiner in the original and supplemental surcharge motions filed  
in the bankruptcy court, both of which provide for recovery of  
amounts for compensation for Examiner and his professionals.  
Through counsel, GTI continues its support for the surcharges even  
now before this Panel. On this record, Comerica's suggestion that  
GTI's position on the surcharge issue would be, without Examiner's  
joint status, "different" is at best, speculation.

1 a narrow reading of § 1109(b), which provides that:

2 A party in interest, including the debtor, the trustee,  
3 a creditors' committee, an equity security holders'  
4 committee, a creditor, an equity security holder, or any  
indenture trustee, may raise and may appear and be heard  
on any issue in a case under this chapter.

5 But the Code's listing of the parties entitled to be heard in a  
6 chapter 11 case is not meant to be exclusive. See § 102(3)  
7 (prescribing that the term "including" is not limiting); 7 COLLIER  
8 ON BANKRUPTCY ¶ 1109.03 (15th ed. rev. 2001). Courts have extended  
9 party in interest status to examiners under a variety of expanded  
10 powers. Williamson v. Roppollo, 114 B.R. 127, 129 (W.D. La. 1990)  
11 (examiner given power to recover preferences is party in  
12 interest); In re Torrez, 132 B.R. 924, 934 (Bankr. E.D. Cal.  
13 1991); Weld v. Sweeney Agcy., Inc. (In re Patton's Busy Bee  
14 Disposal Serv., Inc.), 182 B.R. 681, 686 (Bankr. W.D.N.Y. 1995)  
15 ("Where the examiner has assumed certain duties of a trustee, that  
16 examiner is a party in interest as to the obligations that are so  
17 assumed."); In re Great Barrington Fair & Amusement, Inc., 53 B.R.  
18 241 (Bankr. D.Mass. 1985) (examiner is a party in interest); In re  
19 Carnegie Int'l Corp., 51 B.R. 252 (Bankr. S.D.Ind. 1984).

20 In this case, primarily at Comerica's request, the bankruptcy  
21 court bestowed broad powers on Examiner to take control of GTI's  
22 cash, to liquidate GTI's assets, and to propose the distribution  
23 of the proceeds generated in that process. In particular, during  
24 that process, at the hearing on April 15, 2004, the bankruptcy  
25 court expressly directed Examiner to take the lead on the  
26 surcharge question. Comerica participated at that hearing and did  
27 not object to the court's suggestion, nor did it oppose Examiner's  
28 right to proceed (and be heard) on the surcharge issue. It is

1 clear from the record that, in the unique context of these chapter  
2 11 cases, Examiner was a party in interest with the right to be  
3 heard by the bankruptcy court concerning whether Comerica's  
4 collateral should be surcharged.

5 Comerica argues that, because of the provisions of § 1106(b)  
6 addressing the statutory duties of an examiner, GTI and Examiner  
7 cannot act in concert here. It argues that, under the Code, an  
8 examiner may perform only those duties that the bankruptcy court  
9 has forbidden the debtor to perform:

10 Under the plain meaning of 11 U.S.C.  
11 § 1106(b), besides investigating and reporting  
12 on various issues, an examiner is only  
13 permitted to do those things "that the Court  
14 orders the debtor-in-possession not to  
15 perform."

16 Comerica's Opening Brief at 10 (which is repeated verbatim in  
17 Comerica's Reply Brief at 5). According to Comerica, then, the  
18 Code prohibits Examiner from pursuing a surcharge because the  
19 bankruptcy court did not prohibit GTI from doing so. We disagree.

20 The provisions of § 1106(b) include an important exception to  
21 the general rule suggested by Comerica. The statute provides:

22 An examiner appointed under section 1104(d) of  
23 this title shall perform the duties specified  
24 in paragraphs (3) and (4) of subsection (a) of  
25 this section, and, except to the extent that  
26 the court orders otherwise, any other duties  
27 of the trustee that the court orders the  
28 debtor-in-possession not to perform.

29 § 1106(b) (emphasis added). Subsections (3) and (4) of § 1106(a)  
30 require an examiner in a chapter 11 case to investigate the  
31 debtor's affairs and file a report. The statute also provides  
32 that an examiner shall perform other duties that the debtor-in-  
33 possession is ordered not to perform. But the statute also allows

1 the court to "order otherwise." In other words, even without  
2 prohibiting the debtor-in-possession from, for example, pursuing a  
3 surcharge, the bankruptcy court may "order otherwise" that the  
4 examiner do so. Contrary to Comerica's assertion, the "plain  
5 meaning" of this statute is that the bankruptcy court may (and  
6 frequently in practice does) assign tasks and powers to a chapter  
7 11 examiner, in addition to investigating and reporting, without  
8 first prohibiting the debtor-in-possession from so acting.

9 The bankruptcy court did not err in determining that Examiner  
10 could join in, and be heard in connection with, the surcharge  
11 motions, and that GTI would be seriously hampered in its  
12 prosecution of the surcharge without the joinder of Examiner.  
13 Nothing in the Bankruptcy Code prevents the bankruptcy court from  
14 authorizing an examiner to perform such a role.

15 2. Based on the record presented by Comerica, the Panel is  
16 unable to determine if the bankruptcy court erred in allowing  
17 lessors to "opt-in" to the surcharge litigation.

18 Comerica argues that the bankruptcy court erred when it  
19 allowed certain personal property lessors to include their  
20 administrative claims in the supplemental surcharge motion. We  
21 are unable to examine this issue because of the state of the  
22 record on appeal provided by Comerica.

23 Comerica has taken a cavalier approach to helping us review  
24 the record. In an attempt to comply with BAP Rule 8009(b)-1(B),<sup>17</sup>

---

25  
26 <sup>17</sup> BAP Rule 8009(b)-1(b) Organization of the Appendix.

27 (1) Documents in the appendix shall be divided by tabs.  
28 (2) The pages of the excerpts shall be continuously  
paginated.

(continued...)



1 it has supplied information in excerpts divided by "tabs" with  
2 pages continuously paginated. But in its Opening Brief, Comerica  
3 frequently cites to the tabs, rather than to the page numbers of  
4 the excerpts. Some of the tabs to which we are referred by  
5 Comerica contain over 200 pages of material. When Comerica  
6 occasionally does refer in its Opening Brief<sup>18</sup> to a specific page  
7 of a document in the record, it cites the internal page number of  
8 that document within the tab, not the consecutive numbered pages  
9 of the excerpts. This departure from proper procedure is  
10 aggravated by the fact that 110 of the 220 tabs in Comerica's  
11 excerpts are identified in the table of contents solely by their  
12 trial exhibit numbers from the bankruptcy court proceedings,<sup>19</sup> and  
13 no conversion table is provided that would allow us to identify  
14 the documents to which Comerica refers.

15 In examining the other issues raised by Comerica, we have  
16 made our best efforts to understand its problematic citations to  
17 the record, in spite of the notion that opposing parties and the  
18 court are not obligated to search the entire record unaided for  
19

---

20  
21 <sup>17</sup>(...continued)

22 (3) The appendix shall contain a complete table of  
23 contents listing the documents and identifying both  
24 the tab and page number where each document is  
located. If the appendix has more than one volume,  
the table of contents shall also identify the  
volume in which each document is located.

25 <sup>18</sup> Comerica's Reply Brief in some places cites to the  
26 numbered pages in the excerpts and in other places repeats the  
27 errors of the Opening Brief by referring to tab locations, but  
that is of little assistance in finding the materials cited in the  
Opening Brief.

28 <sup>19</sup> For example, Tab 219 is identified in the table of  
contents only as "Examiner's Surcharge Trial Exhibit 102."

1 error. See Dela Rosa v. Scottsdale Mem'l Health Sys., Inc., 136  
2 F.3d 1241 (9th Cir. 1998). But we are unwilling to do so as to  
3 this particular "opt-in" issue, since Comerica argues that neither  
4 Examiner nor GTI did any analysis to determine whether the  
5 equipment lessors or other administrative creditors provided any  
6 direct or measurable benefit associated with Comerica's collateral  
7 as required by § 506(c). In support of that statement, Comerica  
8 generally cites to four of the Examiner's reply documents,  
9 including responses to interrogatories, spanning 88 pages of  
10 responses. However, Comerica fails to provide the Panel with the  
11 text of the interrogatories to which Examiner is responding!

12       Apparently, Examiner was equally confused by Comerica's brief  
13 on this issue. In Examiner's Reply Brief, he charges that the  
14 opt-in issue was never raised in the bankruptcy court. In  
15 Comerica's Reply Brief, Comerica states that the issue was raised  
16 and cites to the record, but at a location that contains no  
17 reference to Comerica's position on the opt-in issue.<sup>20</sup>

18       Appellant bears the burden of providing an adequate record on  
19 appeal. In re Burkhart, 84 B.R. 658, 660 (9th Cir. BAP 1988).

---

20  
21       <sup>20</sup> This inadequate reference in Comerica's Reply Brief  
22 exemplifies the problems the Panel faced in considering Comerica's  
23 opt-in issue. Like many of its "block" references, Comerica  
24 simply refers to seven pages of the court's Memorandum Decision to  
25 show that it raised the opt-in issue at the bankruptcy court. We  
26 have examined those pages and find no evidence there that Comerica  
27 raised the opt-in issue. In fairness to Comerica, we note that  
28 the court referred in those seven pages to portions of an earlier  
hearing on August 25, 2004. We have examined the three pages  
cited by the bankruptcy court from the earlier hearing and they  
also do not include Comerica's position on the opt-in issue.  
Finally, we read the entire transcript of that hearing (52 pages)  
and discovered that Comerica may have raised the opt-in issue on  
pages 21-22, locations that were not cited by either Comerica in  
its briefs or the bankruptcy court in its Memorandum Decision.

1 Where the inadequacy of the record on appeal is egregious, the  
2 Panel may summarily affirm the findings of fact of the bankruptcy  
3 court. Massoud v. Ernie Goldberger & Co. (In re Massoud), 248 B.R.  
4 160, 163 (9th Cir. BAP 2000). In this instance, based upon  
5 Comerica's flawed approach to citing the record, we are unable to  
6 determine what findings of fact are challenged by Comerica. For  
7 that reason, the Panel will not examine the issue raised by  
8 Comerica, and we will not disturb the ruling of the bankruptcy  
9 court.

10 Although we are unable to do an effective review concerning  
11 Comerica's argument, and therefore decline to modify the  
12 bankruptcy court's decision on this point, from what we can  
13 discern from the record, it appears Comerica acquiesced to adding  
14 the lessors' claims to the surcharge litigation. At the August  
15 25, 2004 scheduling hearing, Comerica did not object to Bombardier  
16 Capital's attorney's suggestion that all surcharge claims be put  
17 "on the table" via a supplemental motion. Tr. Hr'g 6:14 (August  
18 25, 2004). Instead, Comerica endorsed the approach, and indicated  
19 its desire that the bankruptcy court consider all surcharge claims  
20 at "once, not piecemeal." Id. at 7:23 - 8:1. Comerica cannot now  
21 argue that because GTI and Examiner complied by adding lessor  
22 claims in the supplemental motion, the bankruptcy court erred in  
23 considering those claims.<sup>21</sup>

---

24  
25 <sup>21</sup> There is also evidence in the record that, the day before  
26 the August 25, 2004 hearing, Comerica had strongly advocated  
27 adding the lessor claims to the surcharge motion. As part of its  
28 aborted effort to convert the case to chapter 7 and appoint a  
trustee, Comerica submitted its "Statement of Position With  
Respect to: (A) the Debtors' Surcharge Motion; and (B) Surcharge  
(continued...)

1 3. The bankruptcy court applied the proper legal standard and  
2 burden of proof in ordering a surcharge of Comerica's  
3 collateral.

4 A.

5 The bankruptcy court employed a two-pronged legal standard to  
6 decide whether it should order a surcharge in this case.  
7 Historically, these two approaches have been referred to as the  
8 subjective and objective tests. Under these tests, a party  
9 seeking to surcharge a secured creditor's collateral must show  
10 either: (1) under the subjective test, that the secured creditor

11

12 <sup>21</sup> (...continued)  
13 Matters, Generally." On page 4 of that statement, Comerica  
14 argues:

15 Comerica should not be subjected to multiple  
16 surcharge motions filed by different parties,  
17 seeking piecemeal determinations from the  
18 Court on how much (if any) of Comerica's  
19 collateral should be invaded to pay  
20 administrative expenses in these cases that  
21 continue to grow at alarming rates. . . .  
22 [P]iecemeal litigation filed by parties  
23 (including parties without standing) is not  
24 fair to Comerica, and is not an efficient way  
25 to handle an issue (surcharge) that quickly is  
26 becoming the central issue in the cases.  
27 Accordingly, Comerica requests that the Court  
28 direct the Debtors (or preferably, an  
independent Chapter 7 trustee) to prepare and  
file a single, comprehensive surcharge motion,  
and thereafter provide Comerica a fair  
opportunity for discovery and an evidentiary  
hearing before ruling on any surcharge motion.  
Comerica believes that a single surcharge  
proceeding will conserve judicial resources,  
and reduce litigation costs by bringing  
related issues with related arguments and  
controlling case law before the court in one  
coordinated proceeding.

27 (Emphasis added.) The Panel observes that, except for the  
28 appointment of a trustee, Comerica received everything that it  
requested in this passage.

1 "caused or consented to" the expenses to be surcharged; or (2)  
2 under the objective test, and consistent with the criteria  
3 explicitly stated in § 506(c), that the expenses sought to be  
4 surcharged were reasonable, necessary and beneficial to the  
5 secured creditor. In re Compton Impressions, Ltd., 217 F.3d 1256,  
6 1260 (9th Cir. 2000).

7 The subjective test is rooted in pre-1978 Bankruptcy Code  
8 practice. It is inherently an equitable standard.

9 Section 506(c) had its origins in the  
10 equitable principle that where a court has  
11 custody of property, administration and  
12 preservation expenses are a dominant charge  
13 against the property. Hartford Underwriters  
14 Ins. Co. v. Union Planters Bank, N.A., 530  
15 U.S. 1, 9, 120 S.Ct. 1942, 147 L.Ed.2d 1  
16 (2000).

17 In re Los Gatos Lodge, Inc., 278 F.3d 890, 893 (9th Cir. 2002).

18 When a reorganization is unsuccessful and the debtor's estate  
19 is administratively insolvent, the Ninth Circuit has long  
20 recognized that the bankruptcy judge has the authority to decide  
21 the extent to which a secured lender's collateral can be  
22 surcharged for administrative costs and expenses. Silver State  
23 Sav. & Loan Ass'n v. Young, 252 F.2d 236, 238-39 (9th Cir. 1958)  
24 ("Where the free assets involved in an unsuccessful reorganization  
25 proceeding are insufficient to cover allowances, the extent to  
26 which mortgaged property should be charged therewith rests with  
27 the sound discretion of the trial judge.").

28 Although the subjective test pre-dates the 1978 Bankruptcy  
Code, according to the Ninth Circuit, it is still an appropriate  
basis for surcharge where the secured lender expressly or  
impliedly consents to or causes administrative expenses. See

1 Compton Impressions, 217 F.3d at 1260 (holding that, under  
2 § 506(c), a trustee or debtor-in-possession must demonstrate that  
3 the expenses sought to be surcharged are reasonable, necessary and  
4 beneficial to the secured creditor or "that the [secured creditor]  
5 caused or consented to those expenses"), citing In re Cascade  
6 Hydraulics & Utility Serv., Inc., 815 F.2d 546, 548 (9th Cir.  
7 1987) (emphasis added).

8         The objective test arrived with the language of the 1978  
9 Code. As expressed in § 506(c), the trustee or debtor-in-  
10 possession may recover "the reasonable, necessary costs and  
11 expenses for preserving or disposing of" the secured creditor's  
12 collateral, "to the extent of any benefit" to the creditor. In  
13 our circuit, the case law makes clear that the objective test is  
14 not easily satisfied:

15                 The parties seeking the surcharge must prove  
16                 that the expenses were reasonable, necessary  
17                 and provided a quantifiable benefit to the  
18                 secured creditor. [Citations omitted.] This is  
19                 not an easy standard to meet. It is the party  
20                 seeking the surcharge that has the burden of  
21                 showing a "concrete" and "quantifiable"  
22                 benefit.... The § 506 recovery is limited to  
23                 the amount of the benefit actually proven. .  
24                 . . . Furthermore, because the amount of a  
25                 surcharge is limited to the amount of the  
26                 benefit and must be proven with specificity,  
27                 the deserving party is easily ascertainable.

22 In re Debbie Reynolds, 255 F.3d at 1068.

23         The objective test received particular attention after the  
24 Supreme Court's decision in Hartford Underwriters. As discussed  
25 earlier, Hartford Underwriters held that only a trustee or debtor-  
26 in-possession, and not an administrative claimant, has standing to  
27 pursue a surcharge. The Supreme Court in that case emphasized  
28 that the language of § 506(c) is plain and unambiguous. Hartford

1 Underwriters, 530 U.S. at 6. Since § 506(c) does not include  
2 reference to a "consent" standard, it may well foreshadow the  
3 ultimate abandonment of the subjective test. But though the  
4 objective test appears to be in the ascendant, we have no clear  
5 direction from our Court of Appeals or the Supreme Court whether  
6 the subjective test has continuing vitality.<sup>22</sup>

7 Under these circumstances, therefore, it was understandable  
8 that the bankruptcy court in this case applied both tests in its  
9 extensive Memorandum Decision. For this reason, we will also  
10 review the bankruptcy court's decision under both standards.

11 B.

12 Regarding the subjective test, the bankruptcy court recited  
13 fourteen pages of fact findings to support its conclusion that  
14 Comerica caused and consented to the surcharged expenses. For  
15 example, the bankruptcy court found that Comerica alone sought the  
16 appointment of an examiner to take control of GTI's cash and to  
17 guard against alleged fraudulent activities by GTI's management  
18 that could threaten its collateral. It was Comerica that  
19 persuaded the bankruptcy court to expand Examiner's authority  
20 beyond mere investigation and reporting to analyze equipment  
21 leases so as to prevent erosion of Comerica's collateral position.  
22 Comerica then succeeded in convincing the bankruptcy court to  
23 expand Examiner's powers to enable him to liquidate GTI's assets  
24 as a going concern, a goal consistent with Comerica's internal

---

25  
26 <sup>22</sup> The Ninth Circuit decided Compton Impressions, wherein it  
27 reaffirmed that satisfying either the subjective or objective  
28 tests could serve as the basis for a surcharge, in July 2000,  
about six weeks after the Supreme Court decided Hartford  
Underwriters. The Ninth Circuit's decision does not cite or  
discuss Hartford Underwriters.

1 plans concerning these loans. And, after the sale, Comerica  
2 supported another grant of authority to Examiner to conduct a  
3 course of "shuttle diplomacy" with other creditors, hopefully to  
4 settle the amounts to be paid on their claims, and presumably  
5 because it appreciated that compromising administrative claims as  
6 originally planned in the Term Sheet would likely generate a net  
7 saving in its litigation costs.

8       None of the bankruptcy court's fact findings that Comerica  
9 caused or consented to Examiner's authority and actions in  
10 administering these estates, and incurring the expenses in  
11 question here, are clearly erroneous. Indeed, it appears to us  
12 from our review of the record that Comerica, from early on in the  
13 bankruptcy case, decided it was beneficial to employ an examiner  
14 with expanded powers to divest GTI's management from control of  
15 GTI's finances, to sell the assets, and later, to settle  
16 administrative claims, including those of the personal property  
17 lessors. It is also apparent that Comerica appreciated, from  
18 almost the inception of Examiner's service, based upon the  
19 extensive financial information being supplied by Examiner and  
20 otherwise available to Comerica, that it was possible, if not  
21 probable, that the asset liquidation would not net sufficient  
22 amounts to pay administrative expenses and Comerica's secured  
23 claim in full.

24       In other words, when it appears that a secured creditor in a  
25 reorganization case holding a lien on nearly all of the debtor's  
26 assets secures and promotes the services of an examiner, not only  
27 to investigate the debtor's financial affairs, but also to sell  
28 the debtor's business as a going concern and to settle outstanding



1 claims, while all the time appreciating that the debtor may be  
2 administratively insolvent, the bankruptcy court may properly  
3 conclude that the secured creditor impliedly consented that the  
4 costs of administering that bankruptcy estate be paid from its  
5 cash collateral. Here, there is ample competent evidence to  
6 support the bankruptcy court's conclusion that Comerica caused and  
7 consented to Examiner's professional expenses, and to the payments  
8 for certain essential leased personal property,<sup>23</sup> sought to be  
9 recovered in the surcharge motions. If the subjective test  
10 remains valid, the bankruptcy court properly applied it, and did  
11 not err in ordering the surcharge.

12 C.

13 Even if the subjective test has been abrogated by adoption of  
14 § 506(c), the abrogation is of no consequence in this appeal.

---

15  
16 <sup>23</sup> Although most attention in this appeal has been placed on  
17 the surcharge of expenses for the Examiner and his professionals,  
18 there can be little doubt that Comerica also, and consistently,  
19 consented to incurring the lessors' expenses. Comerica had early  
20 in the case agreed to pay administrative expenses out of its  
21 alleged collateral, but opposed payment to lessors unless an  
22 Examiner was appointed and pared down the number of lessors and  
23 amount of payments. Examiner in fact did recommend rejection of  
24 30 leases, which the court approved on July 28, 2003, and the  
25 court later ruled that Comerica would not be surcharged for  
26 expenses resulting from those rejections. The Examiner's report  
27 on leases identified 26 other leases that were "necessary to  
28 operation of the debtor" and these leases continued in effect  
after July 28, 2003. The court correctly found that Comerica  
consented, not only to the leases that were in place on August 1,  
2003, but to payment of those leases out of its alleged  
collateral. When several of those leases were subsequently  
rejected between August 1, 2003, and the sale of the debtors'  
assets, the court could properly conclude that "Comerica indeed  
caused the estates to incur the Unpaid Lease Claims by consenting  
to the lease payments, choosing the remedy of the Examiner with  
expanded powers, and pursue a going concern sale of the Debtors'  
Property through the Examiner" and that "Comerica should be  
surcharged for that portion of the Unpaid Lease Claims relating to  
those leases rejected by the Debtors for the period from August 1,  
2003 through the closing on the sale transaction." Memorandum  
Decision at 85-86.

1 This is because the bankruptcy court also correctly analyzed and  
2 granted the surcharge requests under the objective test.

3 The objective test has three components. "The parties  
4 seeking surcharge must prove that the expenses were reasonable,  
5 necessary and provided a quantifiable benefit to the secured  
6 creditor." In re Debbie Reynolds, 255 F.3d at 1068. The  
7 bankruptcy court provided extensive findings of fact in this case  
8 as to the reasonableness and necessity of the expenses, and as to  
9 the quantifiable benefit bestowed upon Comerica.

10 In regards to reasonableness, the court pointed to the 300  
11 pages of detailed billings and extensive analysis of Examiner's  
12 and his professionals' time. The court described these services  
13 as "excellent" and the time spent and rates "reasonable." These  
14 findings are not clearly erroneous. The court also noted that  
15 Comerica has submitted no evidence to show the professional fees  
16 and expenses were not reasonable.

17 The bankruptcy court next addressed the necessity requirement  
18 of § 506(c). The court carefully audited the services provided  
19 and expenses sought to be surcharged. That it performed a proper  
20 necessity analysis is evidenced by its explanation of how certain  
21 identified services and expenses were not necessary to preserve or  
22 dispose of Comerica's claimed collateral. For example, the court  
23 identified \$39,761.00 from Examiner's attorneys' First and Second  
24 Fee Applications which were not necessary under § 506(c). Based  
25 on the record, the bankruptcy court likewise declined to surcharge  
26 \$142,561.00 in fees and costs requested by Examiner's counsel in  
27 its Third Fee Application, and all costs in all three fee  
28 applications. The court also excluded \$20,816 of fees of Examiner

1 and his environmental consulting firm which it determined were not  
2 necessary to preserve or dispose of Comerica's collateral.  
3 Finally, it determined that all services of Examiner's  
4 environmental consulting firm were necessary within the meaning of  
5 § 506(c).

6 The bankruptcy court provided greatest attention to a  
7 detailed analysis of benefits to Comerica resulting from the  
8 efforts of Examiner and his professionals, and from the lease  
9 payments. In a six page section of its decision, the court  
10 explained how Comerica received direct, substantial and  
11 quantifiable benefit from all Examiner's and professional services  
12 in investigating GTI's dealings, preparing the Preliminary Report,  
13 cash management, sales and marketing of the assets, collection of  
14 outstanding accounts receivable, and settlement of administrative  
15 expense claims.

16 Much of the factual findings detailing these benefits was  
17 derived by the bankruptcy court from the testimony of Examiner and  
18 Goodman. The bankruptcy court noted that while Comerica called  
19 McDonald, a bank officer, to testify, she knew "little to nothing  
20 about what transpired in these cases and knew virtually nothing  
21 about Comerica's institutional experiences on key issues related  
22 to the benefits that Comerica might have obtained from the efforts  
23 of the Examiner and his professionals." Memorandum Decision at  
24 81-82. Comerica has an especially difficult burden in asking us  
25 to disregard any testimony because of the deference we give the  
26 bankruptcy court's opportunity to weigh the importance of witness  
27 testimony and judge the credibility of witnesses. See Rule 8013  
28 (On appeal, "due regard shall be given to the opportunity of the

1 bankruptcy court to judge the credibility of witnesses.”).

2 Summing up its conclusions about the benefit to Comerica, the  
3 bankruptcy court noted that:

4 Comerica was the primary beneficiary, and in  
5 many respects, the sole beneficiary of the  
6 efforts of the Examiner and his professionals.  
7 In a case where general unsecured creditors  
8 will almost certainly never receive a  
9 distribution and administrative expense  
10 claimants are faced with an uphill battle to  
11 receive more than a fraction of the amount of  
12 their claims, Comerica’s argument that the  
13 efforts of the Examiner and his professionals  
14 benefitted everyone, and not primarily  
15 [Comerica], is sophistry.

16 Memorandum Decision at 83. We agree with the bankruptcy court’s  
17 analysis.

18 Before leaving the objective test issues, we must review the  
19 objective test as it applies to the amounts Comerica was  
20 surcharged for unpaid rent and taxes under the leases. The  
21 bankruptcy court noted that the very first task Comerica expected  
22 Examiner to complete after his initial appointment was to pare  
23 down the personal property leases to those covering essential  
24 equipment. He did so. It is undisputed that Examiner reported to  
25 Comerica, and promptly and significantly reduced the number of  
26 leases and their attendant expenses which could strain Comerica’s  
27 cash collateral. The leases not rejected as part of this initial  
28 review covered only those items that Comerica agreed were  
essential equipment.

As the bankruptcy court noted, had the leases not been  
preserved in a pared-down state, Comerica likely would not have  
obtained the direct, substantial and quantifiable benefit of the  
going concern sale of GTI’s business negotiated by Examiner.

1 Comerica's internal documents acknowledged that a going concern  
2 sale was beneficial to its position, and that a liquidation of the  
3 assets would likely return less value on its claim. Thus, the  
4 bankruptcy court concluded that the amounts due on the unpaid  
5 lease claims were reasonable, necessary and beneficial within the  
6 meaning of § 506(c). We agree.

7 Comerica argues that the leases rejected between August 1,  
8 2003, and the sale of the assets provided no benefit to Comerica.  
9 Comerica's argument appears to be in several parts. On the one  
10 hand, they insist that the leases rejected after August 1 are in  
11 exactly the same category as those leases rejected before August 1  
12 which the court acknowledged had provided no benefit to Comerica  
13 and that any amounts due on those leases could not be charged  
14 against Comerica. But Comerica does not explain how or why the  
15 leases rejected before August 1 are similar to those rejected  
16 after August 1.<sup>24</sup>

17 In any case, even if leases on either side of the dateline  
18 are identical, the issue is not the substance of the leases but  
19 the timing of the leases. The Examiner's lease report identified  
20 certain leases that, as of July 28, 2003, should be rejected, and  
21 another group of leases that, as of that date, were necessary to  
22 the continuing operation of the debtors. Leases rejected before  
23 August 1 provided no benefit to Comerica. Leases rejected after  
24 August 1 were deemed necessary for the continuing operation of the  
25 debtors and, thus, necessary to Comerica's and the Examiner's plan

---

26  
27 <sup>24</sup> We are also unable to conduct our own examination because  
28 we have little or no information in the record on the contents of  
the leases.

1 to sell the business as a going concern. That certain of the  
2 post-August 1 leases were eventually rejected does not mean that,  
3 while they were in effect, Comerica received no benefit from  
4 retention of the leased property.<sup>25</sup>

5 Comerica also argues that the benefit to Comerica accruing  
6 from these leases was not attributed by the bankruptcy court with  
7 sufficient specificity. Apparently, Comerica expected Examiner  
8 and the bankruptcy court to examine the benefit to Comerica for  
9 each lease.

10 An evaluation of the benefit of each lease to Comerica is not  
11 required. We believe the court correctly found that Comerica  
12 received a direct, substantial and quantifiable benefit because  
13 GTI's assets could be sold by Examiner as a going concern.  
14 Although the court noted that it was difficult to place a precise  
15 dollar amount on the benefit to Comerica derived from a going  
16 concern sale, it found that Comerica would not have received the  
17 benefit of the enhanced sale price without these leases. This  
18 finding is consistent with Comerica's own internal analysis and  
19 plans for liquidation of its collateral. The bankruptcy court's  
20 finding that Comerica benefitted from the leases was not clearly  
21 erroneous.

22 In sum, the bankruptcy court applied the correct legal  
23 standard under the objective test, and supported its conclusion  
24 that a surcharge was appropriate with ample findings of fact that  
25 are not clearly erroneous.

---

26  
27 <sup>25</sup> It must be remembered that while some leases were  
28 eventually rejected before the assets were sold, Comerica had  
consented to retention of the leases when Examiner made his  
original recommendations in July 2003.

1 D.

2 Comerica's arguments suggesting that the bankruptcy court  
3 erred in applying the burden of proof also lack merit. We agree  
4 with Comerica's assertion that GTI and Examiner bear the burden of  
5 proving the facts necessary to establish the right to surcharge  
6 its collateral. We disagree with Comerica's argument, however,  
7 that the bankruptcy court employed a presumption that all expenses  
8 could be surcharged against Comerica's collateral, and then  
9 shifted the burden of disproving surcharge to Comerica.

10 As noted above, the bankruptcy court made extensive findings  
11 based on the evidence and testimony to support its conclusions  
12 that the expenses in question were reasonable and necessary, and  
13 of quantifiable benefit to Comerica. Where in its decision the  
14 bankruptcy court indicated that Comerica had not submitted  
15 credible evidence that expenses were unnecessary or unreasonable,  
16 it was not shifting the burden of proof to Comerica, but simply  
17 noting the absence of sufficient evidence in response to the proof  
18 provided by GTI and Examiner that those expenses were necessary or  
19 reasonable.

20 The bankruptcy court applied the correct burden of proof in  
21 ordering a surcharge of Comerica's collateral.

22 4. The bankruptcy court did not abuse its discretion when it  
23 excluded the expert report and testimony offered by Comerica.

24 The admission of expert testimony is governed by Federal Rule  
25 of Evidence 702:

26 If scientific, technical, or other specialized  
27 knowledge will assist the trier of fact to  
28 understand the evidence or to determine a fact  
in issue, a witness qualified as an expert by  
knowledge, skill, experience, training or

1 education, may testify thereto in the form of  
2 an opinion or otherwise, if (1) the testimony  
3 is based upon sufficient facts or data, (2)  
4 the testimony is the product of reliable  
principles and methods, and (3) the witness  
has applied the principles and methods  
reliably to the facts of the case.

5 Comerica offered the testimony and a report of Morris Aaron,  
6 CPA, as an expert witness on the subject of surcharge. The  
7 bankruptcy court allowed the witness to testify on direct  
8 examination, and withheld ruling on objections to his status as an  
9 expert witness and to admission of his testimony in evidence.  
10 After direct examination, Examiner's counsel questioned the  
11 witness and Aaron disclosed the following regarding his  
12 qualifications:

- 13 • He is a certified public accountant.
- 14 • He had not reviewed any bank records in his analysis.
- 15 • He had never communicated with Examiner, officers of GTI,  
16 Comerica, or any of the administrative creditors.
- 17 • He had only reviewed limited court filings and related  
18 documents provided to him by Comerica's counsel.

19 The bankruptcy court expressed two principal concerns  
20 regarding Aaron's testimony. First, the court did not believe  
21 that it required expert testimony on the surcharge issue. Second,  
22 the court questioned the methodology Aaron employed in preparing  
23 his testimony and report.

24 Ordinarily, a trial court's determination that it did not  
25 require expert testimony regarding a proposed surcharge would be  
26 dispositive.

27 The decision whether to admit expert testimony  
28 does not rest upon the existence or strength  
of an expert's opinion. Rather, the key



1 concern is whether the expert testimony will  
2 assist the trier of fact in drawing its own  
3 conclusion as to a "fact in issue."

3 United States v. Rahm, 993 F.2d 1405, 1411 (9th Cir. 1993).

4 Here, the bankruptcy court observed that it had presided over  
5 many cases in which surcharge was an issue and had never needed an  
6 expert witness on the subject. "It's just not something that the  
7 Court believes is an area where I need expert testimony." Tr.  
8 Hr'g 64:11-13 (June 29, 2005).

9 The bankruptcy court also expressed serious reservations  
10 about the methodology used by Aaron.

11 I have a great deal of concern about your  
12 reliance just on the court records. And if I  
13 understand your testimony correctly, that  
14 really was principally what you looked at. . .  
15 . The court normally is looking in expert  
16 testimony for the party really to go out and  
17 explore the field, and explore the factual  
18 information available.

16 Tr. Hr'g 66:11-20 (June 29, 2005). The court declined to allow  
17 Aaron's testimony in evidence. Comerica objects to the court's  
18 decision. Comerica is particularly concerned that the court  
19 refused Aaron's testimony but accepted, in Comerica's words, the  
20 "expert testimony" of Examiner regarding the propriety of a  
21 surcharge of his own fees and those of his professionals.

22 Comerica does not cite any legal authority on the subject of  
23 expert witnesses in either of its briefs. Further, Comerica's  
24 argument that Aaron's testimony was required to counter the  
25 testimony of Examiner misunderstands the function of expert  
26 testimony in the federal courts. Examiner was never presented as  
27 an expert witness under Rule 702. Examiner was a fact witness,  
28 not subject to Rule 702 restrictions.

