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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NOT FOR PUBLICATION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

5	In re:	)	BAP No. NC-11-1426-DHSa
		)	
6	SWIFT INSTRUMENTS, INC.,	)	Bk. No. 06-50896-CN
		)	
7	Debtor.	)	Adv. No. 09-5335-CN
		)	
8	_____	)	
		)	
9	CAROLYN WU, Chapter 7 Trustee,	)	
		)	
10	Appellant,	)	
		)	
11	v.	)	<b>M E M O R A N D U M</b> <sup>1</sup>
		)	
12	STEPHEN H. SWIFT TRUST; ANNE	)	
	H. SWIFT; STEPHEN H. SWIFT;	)	
13	SAMUEL H. SWIFT; QTIP TRUST #2)	)	
	OF HUMPHREY H. SWIFT TRUST -	)	
14	1966 U/I DATED AUGUST 1, 1966,	)	
		)	
15	Appellees.	)	
		)	

Submitted on January 19, 2012  
at San Francisco, California

Filed - March 8, 2012

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

Honorable Charles Novak, Bankruptcy Judge, Presiding

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Appearances: Kevin W. Coleman of Schnader Harrison Segal & Lewis  
LLP for Appellant Carol Wu; Marcia Gerston of Trepel  
Greenfield Sullivan & Draa, LLP for Appellee QTIP

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<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 Trust #2 of Humphrey H. Swift Trust, 1966 U/I Dated  
2 August 1, 1966; and Dennison Gallaudet, Trustee of  
the Stephen H. Swift Trust, pro se.

3  
4 Before: DUNN, HOLLOWELL, and SALTZMAN,<sup>2</sup> Bankruptcy Judges.

5 On the record submitted to the Panel, we AFFIRM the bankruptcy  
6 court's summary judgment determination that certain claims are not  
7 subject to subordination pursuant to § 510(b).<sup>3</sup>

8 I. FACTS

9 By agreement dated June 19, 1952 ("1952 Stock Restriction  
10 Agreement"), Swift and Anderson, Inc., predecessor in interest to  
11 Swift Instruments, Inc. ("Debtor"), agreed to repurchase and pay for  
12 all the stock held by stockholders Stephen H. Swift ("Stephen") and  
13 Humphrey H. Swift ("Humphrey") upon their deaths. The terms of  
14 repayment were to be "one-fifth of the purchase price in cash and  
15 [the Debtor's] promissory note or notes for four-fifths of the  
16 purchase price payable in four equal annual installments with  
17 interest at five per cent upon the unpaid balance. . . ." By an  
18 amendment ("1993 Amendment") to the 1952 Stock Restriction  
19 Agreement, dated June 25, 1993, the terms of repayment were changed  
20 to provide that one-twelfth of the purchase price was payable in

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22 <sup>2</sup> Hon. Deborah J. Saltzman, United States Bankruptcy Judge  
23 for the Central District of California, sitting by designation.

24 <sup>3</sup> Unless otherwise specified, all chapter and section  
25 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and  
26 all "Rule" references are to the Federal Rules of Bankruptcy  
Procedure, Rules 1001-9037. The Federal Rules of Civil Procedure  
are referred to as "Civil Rules."

1 cash, with the eleven-twelfths balance to be paid by the Debtor's  
2 promissory note or notes in eleven equal installments with simple  
3 interest at five percent on the unpaid balance. The 1993 Amendment  
4 stated that the 1952 Stock Restriction Agreement was "still in  
5 effect solely with respect to [Stephen]." <sup>4</sup> The 1993 Amendment was  
6 acknowledged and agreed to by the Stephen H. Swift and Caroline H.  
7 Swift Settlement Trust dated March 17, 1969 ("Divorce Settlement  
8 Trust"), and by the beneficiaries under the Divorce Settlement  
9 Trust: Stephen Hyde Swift, Anne Hathaway Swift and Samuel Hyde  
10 Swift. As relevant to this appeal, the Divorce Settlement Trust was  
11 funded by some of Stephen's shares in the Debtor.

12 Stephen died in 1997. Under his will, the 1000 Debtor shares  
13 Stephen still owned personally were transferred to the Stephen H.  
14 Swift Trust ("SHS Trust"). At the time of Stephen's death the stock  
15 was valued at \$100.65 per share. In accordance with the 1952 Stock  
16 Restriction Agreement and the 1993 Amendment, the Debtor was  
17 obligated to repurchase the SHS Trust's shares for a total purchase  
18 price of \$110,650. One-twelfth of that amount was paid in cash, and  
19 the Debtor issued a promissory note dated December 1, 1997 for the  
20 \$101,429.13 balance. <sup>5</sup>

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22 <sup>4</sup> Notwithstanding this statement, Humphrey still was living  
23 and remained a party to the 1952 Stock Restriction Agreement.

24 <sup>5</sup> At the time of Stephen's death, Stephen Hyde Swift, Anne  
25 Hathaway Swift and Samuel Hyde Swift each received individual  
26 promissory notes for their respective interests attributable to  
Stephen's stock owned by the Divorce Settlement Trust. Stephen Hyde  
Swift, Anne Hathaway Swift and Samuel Hyde Swift although named as  
appellees did not participate in this appeal.

1 After Stephen's death, Humphrey and the remaining shareholders  
2 of the Debtor executed an "Amended and Restated Stock Restriction  
3 Agreement" dated October 12, 1999 ("1999 Restated Agreement").<sup>6</sup>  
4 Substantial changes were made to the terms for required repurchase  
5 and payment for Humphrey's stock upon his death.

6 Humphrey died on January 20, 2002. Upon his death, his estate  
7 sold his shares<sup>7</sup> to the Debtor in accordance with the 1999 Amended  
8 and Restated Agreement. The Debtor made a partial payment of  
9 \$788,560.44 to Humphrey's estate, using proceeds from a life  
10 insurance policy bought for that purpose.<sup>8</sup> The Debtor then executed  
11 two promissory notes, payable to Humphrey's estate for the balance  
12 of the repurchase price for his shares. The first note, dated

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14 <sup>6</sup> Paragraph 14 of the 1999 Restated Agreement recited that  
15 prior stockholder agreements, including the 1952 Stock Restriction  
16 Agreement and other agreements dated October 10, 1960 and April 28,  
17 1975, previously were rescinded and cancelled. The 1999 Restated  
18 Agreement purported to amend and restate the agreement dated  
19 September 15, 1977 between the Debtor and certain shareholders  
20 regarding the transfer of stock. Only the 1952 Stock Restriction  
21 Agreement is included in the record on appeal.

19 <sup>7</sup> Excluded from Humphrey's shares subject to repurchase by  
20 the Debtor were shares that Humphrey left to his daughter, Alison,  
21 who succeeded to Humphrey's position as Chief Executive Officer of  
the Debtor upon his death.

22 <sup>8</sup> The 1999 Restated Agreement required the Debtor, upon the  
23 death of Humphrey, to use the entire proceeds of the "key man" life  
24 insurance policy on Humphrey to redeem in cash all stock held by  
25 shareholder Harold Mercer. Any remaining proceeds were to be used  
26 to purchase Humphrey's stock. As a result, Humphrey's estate  
received a cash payment equivalent to 25% of the value of Humphrey's  
stock at the time of his death, rather than the one-twelfth cash  
payment otherwise contemplated.

1 June 24, 2002, was in the amount of \$1,635,551.21; the second note,  
2 dated March 13, 2003, was in the amount of \$337,238.68. These notes  
3 were consolidated into a single note dated April 15, 2003, in the  
4 amount of \$2,012,749.89, made payable to the QTIP Trust #2 of The  
5 Humphrey H. Swift Trust - 1966 u/I, dated August 1, 1966 ("HHS  
6 Trust"), based upon an assignment, also dated April 15, 2003.

7 As early as October 2002, the Debtor began negotiations with  
8 the holders of the promissory notes representing the unpaid balances  
9 for the repurchase of Stephen and Humphrey's shares to alter their  
10 terms. Between 1998 and 2002, Debtor's overall sales declined by  
11 27% with no corresponding decline in its operating expenses. By  
12 letter dated November 29, 2002, the Debtor advised Humphrey's estate  
13 that it would be unable to make the payments due in June 2003 on the  
14 outstanding promissory notes without creating an "emergency  
15 liquidation situation." In March 2003, the Debtor proposed to  
16 convert 75% of the outstanding balances on the promissory notes due  
17 Humphrey's estate to equity. Instead, the parties agreed to  
18 restructure the obligation reflected in the note, now payable to the  
19 HHS Trust, by deferring principal payments for approximately four  
20 years. In exchange for the deferral, the HHS Trust was given a  
21 warrant for 10% of the amount of the Debtor's current outstanding  
22 stock at a \$1.00 per share exercise price. To effectuate the  
23 restructuring, the Debtor executed a Restated Promissory Note  
24 payable to the HHS Trust, dated January 31, 2004, in the amount of

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1 \$2,177,402.87.<sup>9</sup>

2 The Debtor made the quarterly interest only payments on the  
3 restated promissory notes to Stephen Hyde Swift, Anne Hathaway  
4 Swift, Samuel Hyde Swift, and the HHS Trust through the payment due  
5 September 2005.

6 On May 24, 2006, the Debtor filed a voluntary chapter 11  
7 petition. The following claims were filed based upon the promissory  
8 notes for Debtor's repurchase of Stephen and Humphrey's stock:

9 - Claim No. 25, filed by Anne Hathaway Swift, asserting a general  
10 unsecured claim in the amount of \$299,020.19.

11 - Claim No. 29, filed by the SHS Trust, asserting a general  
12 unsecured claim in the amount of \$80,336.63.

13 - Claim No. 39, filed by Stephen Hyde Swift, asserting a general  
14 unsecured claim in the amount of \$234,746.90.

15 - Claim No. 49, filed by Samuel Hyde Swift, asserting a general  
16 unsecured claim in the amount of \$226,407.09.

17 - Claim No. 31, filed by the HHS Trust, asserting a general  
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19 <sup>9</sup> The record on appeal suggests that with respect to the  
20 promissory notes relating to the repurchase of Stephen's stock, the  
21 promissory notes held by Stephen Hyde Swift, Anne Hathaway Swift and  
22 Samuel Hyde Swift also were restructured on January 31, 2004, but  
23 not the promissory note held by the SHS Trust. See (1) allegations  
24 in the complaint (paragraphs 15-17, 23 and 29), (2) the answers  
25 filed by the SHS Trust, by Stephen Hyde Swift, and by Samuel Hyde  
26 Swift (if Anne Hathaway Swift filed an answer to the complaint, it  
is not included in the record on appeal), and (3) SHS Trust's  
memorandum in support of its motion for summary judgment ("The SHS  
Trust was not asked to participate and did not participate in this  
exchange [for a restated promissory note] and holds no warrants to  
purchase stock of the Debtor.").

1 unsecured claim in the amount of \$2,265,095.53.

2       The bankruptcy court entered an order converting the case to  
3 chapter 7 on November 28, 2007, and Carol Wu was appointed the  
4 chapter 7 trustee ("Trustee"). On December 16, 2009, the Trustee  
5 filed her complaint pursuant to § 510(b) of the Bankruptcy Code,  
6 seeking to subordinate the claims represented by the promissory  
7 notes to claims of general unsecured creditors.<sup>10</sup> In their answers  
8 to the complaint, all defendants asserted that the Trustee was not  
9 entitled to equitable subordination of their claims pursuant to  
10 § 510(b) because not only were they not, nor had they ever been,  
11 equity owners and/or shareholders of the Debtor, but the Stock  
12 Repurchase Agreement by its terms precluded them from being  
13 shareholders.

14       The Trustee, the SHS Trust and the HHS Trust all filed cross-  
15 motions for summary judgment. None of the summary judgment motions  
16 are in the record on appeal. The only pleadings filed in connection  
17 with the summary judgment motions included in the record before the

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19       <sup>10</sup> The Trustee's claim for relief for avoidance of transfers  
20 (the quarterly interest payments in the year before the Debtor filed  
21 its bankruptcy petition) against Stephen Hyde Swift, Anne Hathaway  
22 Swift, Samuel Hyde Swift, and the HHS Trust, were dismissed as  
23 untimely pursuant to § 546. No appeal was taken from that  
24 determination of the bankruptcy court.

25       The Trustee also sought to disallow the claims of Stephen  
26 Hyde Swift, Anne Hathaway Swift, Samuel Hyde Swift, and the HHS  
Trust on the basis that they failed to return the alleged  
preferential transfers. The bankruptcy court did not grant summary  
judgment on this claim for relief. However, the Trustee has  
stipulated to the dismissal of this claim for relief as to all  
defendants.

1 Panel are: the memorandum of the SHS Trust in support of its motion  
2 for summary judgment, the identical declarations of Preston H.  
3 Saunders filed (1) September 3, 2010 in support of HHS Trust's  
4 motion for summary judgment and (2) October 10, 2010 in opposition  
5 to the Trustee's motion for summary judgment, and the identical  
6 declarations of Alison C. Swift filed (1) September 3, 2010 in  
7 support of HHS Trust's motion for summary judgment and  
8 (2) October 10, 2010 in opposition to the Trustee's motion for  
9 summary judgment.

10 On December 14, 2010, the bankruptcy court entered its  
11 Memorandum Decision and Order Granting Motion for Summary Judgment  
12 ("Memorandum Decision"), stating that all parties have agreed that  
13 no questions of fact exist regarding the Trustee's § 510(b) claim  
14 for relief, and that "this court's sole task is to interpret that  
15 code section and apply it to the undisputed facts." Holding that  
16 § 510(b) is "aimed at equity interests attempting to elevate their  
17 claim," the bankruptcy court ruled that, in light of the mandate in  
18 the 1952 Stock Restriction Agreement that the Debtor repurchase  
19 Stephen and Humphrey's shares upon their deaths, the defendants were  
20 seeking only to enforce their debt instruments, i.e. the promissory  
21 notes, and were not asserting claims that relied on or were tied to  
22 the value of the Debtor's stock, or to recharacterize a securities  
23 or equity claim as debt. On July 25, 2011, the bankruptcy court  
24 entered judgment in favor of the defendants on the Trustee's  
25 § 510(b) claim for relief, and the Trustee timely appealed.

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II. JURISDICTION

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

III. ISSUE

Whether the bankruptcy court erred when it ruled that the claims of the SHS Trust, Stephen Hyde Swift, Anne Hathaway Swift, Samuel Hyde Swift, and the HHS Trust were not subject to subordination under § 510(b).

IV. STANDARDS OF REVIEW

We review de novo a decision to grant summary judgment. See FTC v. Stefanchik, 559 F.3d 924, 927 (9th Cir. 2009). De novo review requires that we view the case from the same position as the bankruptcy court. See Lawrence v. Dep't of Interior, 525 F.3d 916, 920 (9th Cir. 2008). In our review of the grant of a motion for summary judgment, we are governed by the same standard used by the bankruptcy court under Civil Rule 56(c), applicable in the adversary proceeding pursuant to Rule 7056. See Suzuki Motor Corp. v. Consumers Union, Inc., 330 F.3d 1110, 1131 (9th Cir.), cert. denied, 540 U.S. 983 (2003). Summary judgment may be appropriate when a mixed question of fact and law involves undisputed underlying facts. See EEOC v. UPS, 424 F.3d 1060, 1068 (9th Cir. 2005).

We also review de novo the bankruptcy court's interpretation of a statute, including provisions of the Bankruptcy Code. See Beeman v. TDI Managed Care Svcs., 449 F.3d 1035, 1038 (9th Cir. 2006).

1 V. DISCUSSION

2 At the outset, we note the difficulty imposed on us by the  
3 Trustee's failure to provide a complete record of what was presented  
4 to the bankruptcy court. Although "[c]omprehensive briefs were  
5 filed and an extended oral argument took place"<sup>11</sup> before the  
6 bankruptcy court, the only summary judgment pleadings we have in the  
7 record before us are (1) the memorandum filed by the SHS Trust in  
8 response to the Trustee's motion for summary judgment, and (2) two  
9 declarations, without the referenced exhibits attached, that were  
10 filed in support of HHS Trust's position in opposition to the  
11 Trustee's motion for summary judgment and in support of its own. We  
12 have no transcript of the "extended oral argument" on the cross-  
13 motions for summary judgment. The Trustee's failure to provide a  
14 complete record of material pleadings and documents, as well as the  
15 hearing transcript, in itself constitutes a basis to dismiss this  
16 appeal or summarily affirm the bankruptcy court's decisions. See  
17 Kyle v. Dye (In re Kyle), 317 B.R. 390, 393 (9th Cir. BAP 2004);  
18 Ehrenberg v. Cal. State Univ., Fullerton Found. (In re Beachport  
19 Entm't), 396 F.3d 1087-88 (9th Cir. 2005) (When the inadequacy of  
20 the record provided to the Panel affords little choice but to  
21 summarily affirm, we may do so.).

22 The problem created by the lack of record manifests itself, in  
23 part, in this way: "Ordinarily, we do not consider arguments that  
24 were neither raised nor addressed before the bankruptcy court."

25 \_\_\_\_\_  
26 <sup>11</sup> HHS Trust's Opening Brief on Appeal at p. 6.

1 Charlie Y., Inc. v. Carey (In re Carey), 446 B.R. 384, 393 (9th Cir.  
2 BAP 2011), citing Cooper Indus., Inc. v. Aviall Servs., Inc., 543  
3 U.S. 168-69 (2004). Because we do not have before us any memorandum  
4 the Trustee may have filed either in support of her own motion for  
5 summary judgment or in opposition to the cross motion filed by the  
6 HHS Trust or the transcript of the argument on the cross motions, we  
7 do not know what arguments included in the Trustee's Opening Brief  
8 on Appeal ("Trustee's Opening Brief") were presented to the  
9 bankruptcy court.

10 The Trustee makes three arguments in this appeal. First, the  
11 bankruptcy court erred in its interpretation and application of the  
12 Ninth Circuit's decision in In re Betacom of Phoenix, 240 F.3d 823  
13 (9th Cir. 2001), which the Trustee characterizes as "[t]he  
14 controlling law in this Circuit regarding the possible subordination  
15 of promissory notes arising from a sale of securities." Trustee's  
16 Opening Brief at pp. 11-12. Second, the Trustee asserts that the  
17 assignment of the claims subject to subordination does not alter the  
18 Betacom analysis. Id. at pp. 16-19. Third, although she concedes  
19 that the bankruptcy court correctly identified the policy underlying  
20 § 510(b), the Trustee contends that the bankruptcy court erred when  
21 it focused on the form of the claim rather than analyzing the risk  
22 represented by the claim. Because the bankruptcy court's Memorandum  
23 Decision contains no discussion of the legal effect of assignment,  
24 we presume the argument was not raised by the Trustee and therefore

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1 conclude that the Trustee waived that argument on appeal.<sup>12</sup>

2 We therefore limit our de novo review to the bankruptcy court's  
3 interpretation and application of § 510(b).

4 Section 510(b) provides:

5 For the purpose of distribution under this title, a claim  
6 arising from rescission of a purchase or sale of a  
7 security of the debtor or of an affiliate of the debtor,  
8 for damages arising from the purchase or sale of such a  
9 security, or for reimbursement or contribution allowed  
10 under section 502 on account of such a claim, shall be  
11 subordinated to all claims or interests that are senior to  
12 or equal the claim or interest represented by such  
13 security except that if such security is common stock,  
14 such claim has the same priority as common stock.

15 The principal cases in this circuit with respect to § 510(b)  
16 are Betacom and American Wagering.<sup>13</sup> In Betacom, the Ninth Circuit  
17 ruled that a claim for damages for breach of a merger agreement was  
18 properly subordinated under § 510(b) where the alleged breach was  
19 the corporation's failure to convey shares of stock. In reaching  
20 that decision, the Ninth Circuit suggested that assessing the  
21 application of § 510(b) to any claim requires an analysis of "the  
22 two main rationales for mandatory subordination: 1) the dissimilar

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23 <sup>12</sup> In any event, it appears that the issue of assignment is  
24 irrelevant in the bankruptcy court's analysis. The bankruptcy court  
25 points out that, "No one contests that the notes result from the  
26 Stock Restriction Agreement purchases." Memorandum Decision at p. 6  
n.7. The bankruptcy court also states that the defendants, "and  
their predecessors in interest," i.e., Stephen and Humphrey's  
respective estates which last held actual stock, "removed themselves  
as equity holders when the company issued the promissory notes."  
Id. at 8:6-7.

<sup>13</sup> In re Am. Wagering, Inc., 493 F.3d 1067 (9th Cir. 2007).

1 risk and return expectations of shareholders and creditors; and  
2 2) the reliance of creditors on the equity cushion provided by  
3 shareholder investment." See, generally, Betacom, 240 F.3d at  
4 828-30.

5 American Wagering concerned a claim based upon a judgment debt  
6 held by a financial advisor who had performed services relating to  
7 the initial public offering of the stock of debtor's predecessor-in-  
8 interest. Under his employment agreement, the financial advisor was  
9 to be paid \$150,000 cash plus "4.5 percent of the final evaluation  
10 in the form of . . . common stock." Overruling this Panel's  
11 decision (326 B.R. 449 (9th Cir. BAP 2005)), the Ninth Circuit  
12 determined that the financial advisor's claim was not subject to  
13 subordination under § 510(b), because he never contracted to hold  
14 shares of stock, only to receive compensation measured against the  
15 value of stock. He therefore never undertook the risks of a  
16 shareholder.

17 The Trustee asserts on appeal that under Ninth Circuit  
18 precedent, the claims of the SHS Trust, Stephen Hyde Swift, Anne  
19 Hathaway Swift, Samuel Hyde Swift, and the HHS Trust are subject to  
20 "mandatory" subordination to the claims of the Debtor's general  
21 unsecured creditors pursuant to § 510(b). The Trustee cites Betacom  
22 for the proposition that claims based on fixed payment promissory  
23 notes must be subordinated under § 510(b) if they were "linked to"  
24 the stock repurchase. The Trustee contends that § 510(b) is to be  
25 read "broadly" to include claims in which "there exists some nexus  
26 or causal relationship between the claim and the purchase of the

1 securities. . . ." Am. Wagering, 493 F.3d at 1072.

2 In granting summary judgment against the Trustee, the  
3 bankruptcy court recognized that for purposes of § 510(b), the  
4 Debtor's repurchase of Stephen and Humphrey's stock constituted  
5 purchases of the Debtor's securities. Memorandum Decision at 5:26-  
6 27. The bankruptcy court further recognized that contract claims  
7 and even claims by persons or entities who are not and never were  
8 shareholders of the debtor are subject to § 510(b) subordination.  
9 Id. at 5:27-6:2. See also Betacom, 240 F.3d at 829 ("There is  
10 nothing . . . to suggest that Congress's concern with creditor  
11 expectations and equitable risk allocation was limited to cases of  
12 debtor fraud."), and ("Nothing in § 510(b)'s text requires a  
13 subordinated claimant to be a shareholder."). Finally, the  
14 bankruptcy court agreed that § 510(b) was to be interpreted broadly.  
15 Memorandum Decision at 6:6-8. However, the bankruptcy court further  
16 stated that the critical question it had to decide for purposes of  
17 § 510(b) was whether the claims for damages for breach of contract,  
18 i.e., for Debtor's failure to pay the notes, "arose" from the  
19 Debtor's repurchase of Stephen and Humphrey's stock.

20 The bankruptcy court rejected the Trustee's assertion that  
21 Betacom and American Wagering required the application of a "but  
22 for" analysis, a mere nexus between the claim and the repurchase of  
23 stock. The bankruptcy court interpreted American Wagering as  
24 requiring not simply that § 510(b) be interpreted broadly as the  
25 Trustee suggested, but rather that it be interpreted broadly "to  
26 give effect to the statute's remedial goals." Id. at 6:6-7, citing

1 Am. Wagering, 493 F.3d at 1072. The bankruptcy court thus rejected  
2 a mandatory application of § 510(b) in the absence of a  
3 determination that subordinating the claims satisfied the purposes  
4 of § 510(b). Id. at 6:23-7:4, citing In re JTS Corp., 305 B.R. 529,  
5 545 (Bankr. N.D. Cal. 2003).

6 We agree with the bankruptcy court that it is not appropriate  
7 to adopt a rule that all claims based on stock redemption notes must  
8 be subordinated. The language of § 510(b) is not sufficiently clear  
9 to impose such a rule. The Tenth Circuit provides a good analysis  
10 both of the policies behind the addition of § 510(b) to the  
11 Bankruptcy Code and of the ambiguity of the language of § 510(b).  
12 See Allen v. Geneva Steel Co. (In re Geneva Steel Co.), 281 F.3d  
13 1173 (10th Cir. 2002).<sup>14</sup>

14 \_\_\_\_\_  
15 <sup>14</sup> In enacting § 510(b), Congress adopted the position  
16 articulated in "an influential article written by law professors  
17 John Slain and Homer Kripke. See John Slain & Homer Kripke, The  
18 Interface Between Securities Regulation and Bankruptcy-Allocating  
19 the Risk of Illegal Securities Issuance Between Security Holders and  
20 the Issuer's Creditors, 48 N.Y.U. L.Rev. 261 (1973)." Geneva Steel,  
21 281 F.3d at 1176.

22 Slain and Kripke criticized the favorable treatment that  
23 bankruptcy courts were extending to shareholder fraud  
24 claims. Their argument rested on the bargain and reliance  
25 interests formed by creditors and equity-holders. They  
26 pointed out that allowing equity-holders to become  
effectively creditors-by treating these two classes as  
though they were one-gives investors the best of both  
worlds: a claim to the upside in the event the company  
 prospers and participation with creditors if it fails. It  
 also dilutes the capital reserves available to repay  
 general creditors, who rely on investment equity for

(continued...)

1 In Betacom, the Ninth Circuit remanded two claims based on  
2 promissory notes to the bankruptcy court, with direction that the  
3 promissory note claims should be subordinated along with the claim  
4 for breach of the merger agreement, “[i]f the note claims are linked  
5 to the Merger Agreement.” Betacom, 240 F.3d at 832. Thus  
6 “[although Betacom indicates that promissory note claims can be  
7 subject to mandatory subordination under appropriate circumstances,  
8 it does not describe what type of circumstances justify  
9 subordination.” JTS Corp., 305 B.R. at 546. We therefore find no  
10 error in the bankruptcy court’s determination that it was required  
11 to decide whether subordinating the claims would satisfy the  
12 purposes of § 510(b).<sup>15</sup>

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14 \_\_\_\_\_  
15 <sup>14</sup>(...continued)

16 satisfaction of their claims. Giving shareholder claims  
17 the same priority as creditor claims, reasoned Slain and  
18 Kripke, eliminates this safety cushion.

19 Id.

20 <sup>15</sup> This approach is similar to that enunciated by the First  
21 Circuit in the context of equitable subordination under § 510(c).  
22 Noting the Supreme Court has stated that “‘categorical reordering of  
23 priorities that takes the place at the legislative level of  
24 consideration is beyond the scope of judicial authority’ with  
25 respect to equitable subordination under section 510(c),” the First  
26 Circuit rejected the “rule” that all claims based on stock  
redemption notes must be subordinated. Merrimac Paper Co., Inc. v.  
Harrison (In re Merrimac Paper Co., Inc.), 420 F.3d 53, 62 (1st Cir.  
2005) (quoting U.S. v. Reorganized CF & I Fabricators of Utah, Inc.,  
518 U.S. 213, 229 (1996)). Instead, a court sitting in equity must  
consider whether subordinating a particular claim would be fair  
based on the totality of the circumstances in the individual case.  
Merrimac, 420 F.3d at 63.



1 Section 510 of the Bankruptcy Code is an integral part of  
2 the scheme established in subchapter I of chapter 5 of the  
3 Bankruptcy Code. That subchapter, consisting of sections  
4 501 through section 510, seeks to establish a fair  
5 allocation of estate assets among the many types of  
6 claimants in a liquidation or reorganization case.  
7 Subordination of a claim alters the otherwise applicable  
8 priority of that claim so that the subordinated claimant  
9 receives a distribution only after the claims of other  
10 identified creditors have been satisfied.

11 4 COLLIER ON BANKRUPTCY ¶ 510.01, at p. 510-3 (Alan N. Resnick &  
12 Henry J. Sommer, eds., 16th ed. 2011).

13 As the Ninth Circuit explained in American Wagering, § 510(b)  
14 "serves to effectuate one of the general principles of corporate and  
15 bankruptcy law: that creditors are entitled to be paid ahead of  
16 shareholders in the distribution of corporate assets." Am.  
17 Wagering, 493 F.3d at 1071. Betacom directs that we look to the  
18 origin of the promissory notes on which the claims are based to  
19 determine whether they should be subordinated. Betacom, 240 F.3d at  
20 832. However, merely because the debt represented in the promissory  
21 notes is from the repurchase of Stephen and Humphrey's stock does  
22 not automatically mean that it is subject to subordination. See  
23 4 COLLIER ON BANKRUPTCY ¶ 510.04[6] at pp. 510-15-16.

24 Generally, state law governs the rights and status of the  
25 claims of holders of promissory notes based on repurchased stock vis  
26 a vis other unsecured creditors of the corporation. See Butner v.  
U.S., 440 U.S. 48 (1979).

Property interests are created and defined by state law.  
Unless some federal interest requires a different result,  
there is no reason why such interests should be analyzed  
differently simply because an interested party is involved  
in a bankruptcy proceeding. Uniform treatment of property

1 interests by both state and federal courts within a State  
2 serves to reduce uncertainty, to discourage forum  
3 shopping, and to prevent a party from receiving "a  
4 windfall merely by reason of the happenstance of  
5 bankruptcy." Lewis v. Manufacturers Nat'l Bank, 364 U.S.  
6 603, 609 . . . .

7 Id. at 55.

8 The 1952 Stock Restriction Agreement, the 1993 Amendment, and  
9 the 1999 Restated Agreement all were executed in Massachusetts.  
10 Although only the 1999 Restated Agreement contains a choice of law  
11 provision ("[t]his agreement shall be construed under and governed  
12 by the laws of the Commonwealth of Massachusetts"), each version of  
13 the agreement to repurchase the shares of Stephen and/or Humphrey  
14 upon his death is governed by Massachusetts law. Each of the notes  
15 payable to the HHS Trust contains the following language: "The  
16 execution, delivery and performance of this Note shall be governed  
17 by and construed in accordance with the laws of the Commonwealth of  
18 Massachusetts."<sup>16</sup>

19 Under Massachusetts law, the effect on a corporation from a  
20 distribution to a shareholder which occurs by repurchase of a  
21 corporation's shares is measured by the earlier of (i) the date the  
22 debt was incurred by the corporation, or (ii) the date the  
23 shareholder ceased to be a shareholder with respect to the  
24 repurchase. Mass. Gen. Laws ch. 156D, § 6.40(e)(1). Further, a  
25 corporation's indebtedness to a shareholder created through a

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26 <sup>16</sup> The promissory notes issued in connection with the  
repurchase of Stephen's stock are not in the record on appeal.

1 distribution (repurchase of shares) is at parity with the  
2 corporation's indebtedness to its general, unsecured creditors  
3 except to the extent subordinated by agreement. Id. at § 6.40(f).  
4 However,

5 No distribution may be made by a corporation which is a  
6 going concern if, after giving it effect,  
7 (1) the corporation would not be able to pay its existing  
8 and reasonably foreseeable debts, liabilities and  
9 obligations, whether or not liquidated, matured, asserted  
or contingent, as they become due in the usual course of  
business. . . .

9 Id. at 6.40(c).

10 Thus, outside of bankruptcy, the promissory notes were simply  
11 debt instruments entitled to be paid on the same basis as the  
12 Debtor's other unsecured creditors in the absence of an evidentiary  
13 record as to the Debtor's solvency or insolvency during the relevant  
14 time periods.<sup>17</sup> The question we must address is whether § 510(b)  
15 requires a different outcome once the Debtor corporation is in  
16 bankruptcy. In doing so, we evaluate the claims in light of the two  
17 main reasons for § 510(b) subordination identified in Betacom: the

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19 <sup>17</sup> While the record before us, particularly the  
20 correspondence from the Debtor to Humphrey's estate explaining that  
21 insolvency was imminent unless the terms of payment for the  
22 repurchased stock was restructured, suggests that the repurchase of  
23 Humphrey's shares may have been in violation of Mass. Gen. Laws ch.  
24 156D § 6.40(c), the Trustee made no effort to impose subordination  
on that basis, certainly not based on the record before us.  
25 Accordingly, we assume for purposes of our review that the notes  
26 issued to the HHS Trust are valid.

27 In contrast, in its summary judgment memorandum, the SHS Trust  
28 alleged that the equity cushion for the Debtor at the time the notes  
29 for the repurchase of Stephen's shares were issued was 2.9 times the  
30 amount of the debt incurred through the repurchase.

1 dissimilar risk and return expectations of shareholders and  
2 creditors, and the reliance of creditors on the equity cushion  
3 provided by shareholder investment.

4 Under Mass. Gen. Laws ch. 156D, § 6.40(e)(1), any right of  
5 Stephen to be a shareholder ended in 1997, when the Debtor issued  
6 the notes for the repurchase of Stephen's stock. Thus, as to the  
7 notes issued in 1997 to the SHS Trust, Stephen Hyde Swift, Anne  
8 Hathaway Swift and Samuel Hyde Swift, those parties held the risks  
9 and return expectations of creditors based only upon the terms of  
10 the notes they held. In addition, the bankruptcy court  
11 affirmatively found that the Trustee presented no evidence that  
12 creditors had relied upon equity created by Stephen's stock in  
13 deciding whether to extend credit to the Debtor.

14 Under Mass. Gen. Laws ch. 156D, § 6.40(e)(1), any right of  
15 Humphrey to be a shareholder ended in 2003, when the Debtor issued  
16 the notes for the repurchase of the then remaining shares of  
17 Humphrey's stock. Thus, as to the notes issued in 2002 and 2003 to  
18 the HHS Trust, it held the risks and return expectations of a  
19 creditor based only upon the terms of the notes it held. In  
20 addition, the bankruptcy court affirmatively found that the Trustee  
21 presented no evidence that creditors had relied upon equity created  
22 by Humphrey's stock in deciding whether to extend credit to the  
23 Debtor.

24 The Trustee contends that the fact that the claimants (except  
25 for the SHS Trust) held stock warrants issued in connection with the  
26 Debtor's issuance of the restated promissory notes in January 2004

1 changes the analysis. We disagree. Black's Law Dictionary defines  
2 a stock warrant as a "[c]ertificate[]" entitling the owner to buy a  
3 specified amount of stock at a specified time(s) for a specified  
4 price." Holding a stock warrant is not the equivalent of holding  
5 stock. In the January 2004 renegotiation of the notes, the Debtor  
6 issued stock warrants to Stephen Hyde Swift, Anne Hathaway Swift,  
7 Samuel Hyde Swift, and the HHS Trust. None of those stock warrants  
8 ever was exercised. Further, no claim for the value of any stock or  
9 stock warrants that might fall within the ambit of § 510(b) was ever  
10 filed. The mere existence of the stock warrants does not taint the  
11 claims based upon the promissory notes at issue in this appeal.  
12 Most importantly, § 101(49)(B)(iv) specifically excludes warrants  
13 from the definition of "security" for purposes of the Bankruptcy  
14 Code.

15 Summary judgment is appropriate where there is no genuine issue  
16 of material fact and the moving party is entitled to judgment as a  
17 matter of law. Civil Rule 56(c). The parties agreed that no  
18 questions of fact existed with respect to the Trustee's claim for  
19 § 510(b) subordination of the claims of the SHS Trust, Stephen Hyde  
20 Swift, Anne Hathaway Swift, Samuel Hyde Swift, and the HHS Trust.  
21 We have analyzed the claims under the standards set forth in Betacom  
22 and American Wagering, and we reach the same conclusion as did the  
23 bankruptcy court. The Trustee is not entitled to a judgment  
24 subordinating, pursuant to § 510(b), the Appellees' claims to the  
25 claims of other general unsecured creditors.

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VI. CONCLUSION

We AFFIRM the bankruptcy court's determination that the claims of the SHS Trust, Stephen Hyde Swift, Anne Hathaway Swift, Samuel Hyde Swift, and the HHS Trust were based on debt instruments and therefore not subject to subordination pursuant to § 510(b).