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WRITTEN DECISION - NOT FOR PUBLICATION

ENTERED JAN 10 2007
FILED
JAN 10 2007
CLERK, U.S. BANKRUPTCY COURT
SOUTHERN DISTRICT OF CALIFORNIA
BY _____ DEPUTY

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF CALIFORNIA

In re)	Case No. 04-09941-B7
)	Adv. No. 06-90468-B7
SD COMMUNICATIONS, INC. a)	
California corporation,)	
)	ORDER ON PLAINTIFF'S
Debtor.)	APPLICATION FOR
)	PRELIMINARY INJUNCTION
_____)	
AMERICAN COMMUNICATIONS)	
CORPORATION, a California)	
corporation,)	
)	
Plaintiff,)	
)	
v.)	
)	
ROBERT EDGECOMB, JENNIFER)	
LYNN JONES, and DOES 1-10,)	
)	
Defendant.)	
_____)	

This matter came on for hearing on plaintiff's motion for preliminary injunction, seeking to enjoin the defendants from pursuing any claimed interest in certain state court litigation, and from pursuing any claim that debtor made a fraudulent transfer of its assets.

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As made evident at the hearing, the Court has struggled with why the bankruptcy court has any interest, or jurisdiction to act in what at first blush appears to be a dispute between third parties. The oral argument was helpful in focusing on that issue, and the Court is persuaded it has subject matter jurisdiction pursuant to 28 U.S.C. § 1334 and General Order No. 312-D of the United States District Court for the Southern District of California. This is a core proceeding under 28 U.S.C. § 157(b)(2)(A), (H), (K), (N) and (O).

Discussion

As a threshold matter, defendants have argued this proceeding is an impermissible attempt to enjoin pending state court proceedings, in violation of 28 U.S.C. § 2283. The state court is not a party to the proceeding, and no relief is sought against it, so § 2283 is inapplicable. If injunctive relief is granted, it would run against named defendants and enjoin them from taking acts in violation of the terms of any such injunction, at risk of contempt of court and consequent sanctions.

The basic facts are not in dispute. Debtor commenced state court litigation against the Fontana School District for breach of contract and to recover money damages in 2002. In 2003, defendants sued debtor to recover damages from breach of debtor's contracts with them.

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1 On August 6, 2004 debtor entered into a "Consensual
2 Foreclosure Agreement" with certain of its secured creditors, by
3 which debtor acquiesced to the creditors' foreclosure of their
4 security interests in debtor's assets, thereby momentarily
5 becoming the owners of those assets. Contemporaneously, the
6 secured creditors entered into an agreement with American
7 Communications Corporation (plaintiff herein) and Silicon
8 Holdings, pursuant to which ACC became the owner of what had been
9 debtor's assets that had been the collateral for debtor's
10 obligations to the secured creditors.

11 Then, on or about August 18, 2004 the Superior Court
12 confirmed a June 14, 2004 Arbitration Award against debtor and in
13 favor of defendants. So, at that point in time, defendants
14 became judgment creditors of debtor. The next week, on or about
15 August 23, 2004 defendants filed a notice of lien in the Fontana
16 litigation, asserting a right to payment of their judgment
17 against debtor from any Fontana litigation proceeds to be paid to
18 debtor. At the center of plaintiff ACC's argument is that the
19 Fontana litigation no longer belonged to debtor but was
20 transferred to ACC back on August 6. Therefore, they argue,
21 there was no interest of debtor in the Fontana litigation to
22 which defendants' liens could attach.

23 The Court finds and concludes that it has no view on the
24 correctness of ACC's argument on that point. Further, resolution
25 of the issue appears to be purely one of state law, and the Court
26 denies at this time any request to enjoin the defendants from

1 seeking resolution of the specific issues involving whether
2 defendants' lien claims attached to any interest of the debtor
3 before the debtor's interests in the Fontana litigation were
4 transferred to the secured creditors on August 6, 2004.

5 That does not end the matter, however. On or about
6 November 18, 2004 debtor filed bankruptcy under Chapter 7 and
7 defendants were scheduled as creditors, and notice was given to
8 them and to their lawyers. Trustee Akers was appointed to
9 administer the estate.

10 In April, 2005 the trustee filed a pleading giving notice
11 that he reserved all rights to contest the validity of the August
12 2004 Consensual Foreclosure. The trustee served his "Statement
13 of Position" on counsel for defendants, among others. In the
14 "Statement" the trustee set out some of the foregoing events,
15 including making explicit reference to the Fontana litigation.
16 He then stated:

17 I am reviewing the prepetition
18 foreclosure conducted by creditors Hazen,
19 Ehlers and Garcia to determine if it is an
20 avoidable transfer under the Bankruptcy
21 Code or non-bankruptcy law. If the
22 foreclosure/transfer to Ehlers, Hazen and
23 Garcia is an avoidable transfer, then the
24 State Court Action would become property of
25 this bankruptcy estate. See 11 U.S.C.
26 541(a)(3).

23 Then, in late July, 2005, the trustee served on all
24 creditors, including defendants and their attorneys, a notice
25 that he intended to enter into a settlement with ACC, Silicon
26 Holdings, Hazen, Garcia and Ehlers. The notice stated, in part:

1 The Trustee has asserted potential
2 claims against ACC, Silicon Holdings, Hazen,
3 Garcia, and Ehlers, including claims to avoid
 fraudulent transfers, to avoid fraudulent
 obligations

4 To settle all disputed claims raised by
5 the Trustee against ACC, Silicon Holdings,
6 Hazen, Garcia, and Ehlers . . . ACC and
7 Silicon Holdings have jointly agreed to pay
8 the Trustee \$130,000 . . . and, in addition,
9 to waive any and all claims they have or
10 could assert against Debtor's bankruptcy
11 estate . . . , in exchange for the Trustee's
12 waiver of any and all claims he has or could
13 assert against ACC, Silicon Holdings, Hazen,
14 Garcia, and Ehlers in Debtor's bankruptcy
15 estate.

16 The Notice of Intended Action gave any interested entity or
17 person 28 days to request a hearing and file objections to the
18 proposed action. No one did, and on October 4, 2005 an order was
19 entered by the Court approving the trustee's motion to settle.

20 Meanwhile, on or about December 21, 2004 defendants were
21 granted leave by the state court to intervene in the Fontana
22 litigation. In September, 2006 defendants sought leave to
23 amend their complaint in intervention, which was granted in
24 October, 2006. The First Cause of Action seeks to foreclose on
25 the lien as against ACC. As already discussed, this Court takes
26 no position on that issue, and grants no injunctive relief to
 prevent defendants from seeking resolution of the issue in state
 court.

 The Second Cause of Action seeks to set aside the Consensual
 Foreclosure as a fraudulent transfer under California law. The
 Third Cause of Action alleges a conspiracy to violate the Uniform

1 Fraudulent Transfer Act against Hazen, Ehlers and Garcia, and
2 others. Therein lies the crux of the issue before the Court.

3 Defendants have made no showing that at the time the debtor
4 filed bankruptcy any fraudulent transfer claim, whether available
5 to the trustee under bankruptcy law (11 U.S.C. § 548) or under
6 state law (by operation of 11 U.S.C. § 544) did not become a
7 claim that the trustee had the exclusive initial authority to
8 pursue. To the contrary, it appears all applicable law so
9 provides. Without question, the trustee has the "strong arm
10 power" under § 544 to utilize state fraudulent transfer law to
11 avoid transfers. The trustee is authorized to invoke that power
12 for the benefit of creditors of the debtor. Defendants herein
13 are creditors of the debtor, and their claim in the Fontana
14 litigation is solely as a way to collect on the debt owed to them
15 by the debtor.

16 Applicable law also establishes that once the bankruptcy is
17 filed, the trustee has the exclusive initial right to pursue any
18 such claims. See, e.g. In re Tessmer, 329 B.R. 776 (Bankr. M.D.
19 Ga. 2005). There is some authority for the notion that if a
20 trustee refuses to exercise the avoidance power, then a
21 bankruptcy court may authorize someone else to do so. But that
22 is not the present situation.

23 The record before the Court indicates that the trustee did
24 make a claim against ACC, Silicon Holdings, Hazen, Garcia and
25 Ehlers pursuant to his powers, asserting in part that a
26 fraudulent transfer had occurred. The trustee then settled those

1 claims against those parties on behalf of all creditors of the
2 debtor's bankruptcy estate, including creditors Jones and
3 Edgecomb, defendants here. They were given notice and the
4 opportunity to object to the proposed settlement, and apparently
5 elected to not do so. They cannot now be heard to say they have
6 an independent right to exercise for themselves the same state
7 law power the trustee has already exercised on behalf of all
8 creditors, including them.

9 Accordingly, plaintiff ACC has clearly demonstrated a high
10 probability of success on the merits of their complaint for
11 injunctive relief. In the Court's view public policy also favors
12 injunctive relief because Congress granted a bankruptcy trustee
13 the power to exercise the state law rights of creditors of a
14 bankruptcy estate, including avoidance powers, and the trustee in
15 this case did so after full notice and opportunity to be heard.
16 It is also clear that allowing defendants to go forward with
17 litigating their Second and Third Causes of Action as against
18 ACC, Silicon Holdings, Hazen, Garcia and Ehlers would impose an
19 expensive and time-consuming burden on them, and gives rise to at
20 least a theoretical risk that the state court may render a ruling
21 inconsistent or incompatible with this Court's approval of the
22 trustee's noticed settlement of the same claims on behalf of all
23 creditors of the estate, including defendants.

24 The Court understands defendants' contention that in effect
25 the secured creditors have removed debtor's assets from their
26 reach and left them holding an empty judgment against a debtor

1 with no ability to pay. The Court expresses no opinion on
2 whether that is what has been accomplished by the "Consensual
3 Foreclosure Agreement". The essential point is that defendants
4 have had full notice and opportunity to be heard if they wanted
5 to oppose the trustee's settlement of the estate's claims,
6 including the fraudulent transfer claim, on behalf of all the
7 creditors of the bankruptcy estate. They were accorded full due
8 process, and cannot now be heard to claim otherwise.

9 For all the foregoing reasons, plaintiff's motion for
10 preliminary injunction is granted pursuant to Bankruptcy Rule
11 7065. Counsel for plaintiff shall prepare and present to the
12 Court a proposed form of preliminary injunction order consistent
13 with the foregoing as to the Second and Third Causes of Action of
14 defendants' First Amended Complaint in Intervention as to
15 defendants therein ACC, Silicon Holdings, Hazen, Garcia and
16 Ehlers.

17 IT IS SO ORDERED.

18 DATED: JAN 10 2007

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22 PETER W. BOWIE, Chief Judge
23 United States Bankruptcy Court
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