WRITTEN DECISION - NOT FOR PUBLICATION

ENTERED 4-14-14
FILED
APR 14 2014
CLERK, U.S. BANKRUPTCY COURT
SOUTHERN DISTRICT OF CALIFORNIA
BY me DEPUTY

UNITED STATES BANKRUPTCY COURT

SOUTHERN DISTRICT OF CALIFORNIA

In re QUALITYBUILT.COM, a California corporation, Debtors, LESLIE T. GLADSTONE, Chapter 7 Trustee, Plaintiff, v. ELIZABETH MICHAELIS and GARTH MICHAELIS, Defendants.	Case No. 09-12113-PB7 Adv. No. 14-90005-PB ORDER ON DEFENDANTS' MOTION TO DISMISS ALL CLAIMS

Defendants are a former principal and employee of the Debtor in the underlying bankruptcy case. Plaintiff, the trustee in the underlying case, has filed a complaint asserting several causes of action based upon allegations that defendants improperly

converted and transferred debtor's assets for their personal use.

Defendants have moved to dismiss the complaint on the grounds that some of the claims are no longer property of the estate and that all of the claims are barred by the applicable statutes of limitations. For the reasons set forth below, the motion is granted in part and denied in part.

BACKGROUND

Defendant Elizabeth Michaelis and Stanley Luhr were the co-owners and officers of QualityBuilt.Com (Debtor). Defendant Garth Michaelis is the husband of Elizabeth, and a former employee of Debtor. On August 14, 2009, Elizabeth filed a petition of behalf of the Debtor. On March 12, 2010, the Court approved a sale of substantially all of the assets of the Debtor to newly formed Quality Built, LLC (QBLLC). Elizabeth is the president of QBLLC. On August 2, 2011, the Court entered an order approving a stipulation between the Debtor and Elizabeth that the "limitations period provided by 11 U.S.C. § 546(a)(1) for the commencement of an avoidance action to avoid and recover alleged preferential transfers against Elizabeth Michaelis is extended up to and including August 14, 2012." The order is at Docket No. 255.

On October 25, 2012, the case was converted to chapter 7 and Leslie Gladstone was appointed trustee (Trustee). At a 341(a) meeting held on April 26, 2013, the Trustee discovered that Luhr had sued Elizabeth in California state court, alleging, in part, that Elizabeth, while at the helm of the Debtor, made improper

distributions to herself and her family members including Garth (Luhr Action). On June 28, 2013, the Trustee served Rule 2004 subpoenas on Defendants. Defendants have yet to respond.

On January 10, 2014, the Trustee filed a complaint commencing this adversary proceeding (Complaint). The Complaint is based upon the same allegations of improper distributions included in the Luhr Action. The Complaint consists of ten claims for relief. The First through Fifth Claims for Relief are state law claims for breach of fiduciary duty, conversion and accounting (the Common Law Claims). The Seventh through Ninth Claims for Relief are fraudulent conveyance claims under Bankruptcy Code §§ 544 & 548. The Tenth Claim is an objection to claim based upon the fraudulent conveyance allegations. The Sixth seeks equitable tolling of the limitations period on the fraudulent conveyance claims. These Sixth through Tenth Claims are collectively referred to as the Avoidance Claims.

Defendants have moved to dismiss the Common Law Claims on the ground that those claims were sold to QBLLC, and thus the Trustee lacks standing to assert them, and that they are time barred by the state law statute of limitations. The Trustee disagrees, contending that the claims were excepted from the sale, and that the statute of limitations is tolled by the "discovery rule".

Defendants seek dismissal of the Avoidance Claims on the ground that the applicable limitations period has lapsed. The Trustee acknowledges that the time period has passed, but seeks

equitable tolling. The Court heard argument and took the matter under submission.

DISCUSSION

Common Law Claims

The Trustee does not dispute that she cannot pursue a claim that she does not hold. Thus, if the Common Law Claims were included in the sale of assets to QBLLC the Trustee lacks standing to assert them.

The terms of the sale of Debtor's assets to QBLLC were set out in the Amended and Restated Asset Purchase Agreement (APA). The APA identified those assets purchased by QBLLC (Purchased Assets) and those retained by the bankruptcy estate. Under paragraph 1.1(j) of the APA, Purchased Assets included:

> Except for those assets described in paragraph 1.2 below, all litigation rights, causes of action, choses in action and rights of action of recovery and counterclaims and setoff and recoupments rights, whether known or unknown and including proceeds thereof, including without limitation any and all claims, deposits and other security, prepayments, prepaid assets, refunds, cause of action, rights of recovery, rights of setoff and rights of recoupment arising from or relating to the Purchased Assets, Intellectual Property, and/or the Purchased AR...

Unless expressly excepted, the Common Law Claims would clearly fall under this broad list of litigation rights. The Trustee

\\\

\\\

\\\

\\\

\\\

argues that they were in fact excepted from the sale under paragraph 1.2 which retained to the bankruptcy estate:

> (f) any property of the Bankruptcy estate, including, without limitation, litigation rights arising under or related to claims, and choses of action arising under Chapter 5 of the Bankruptcy Code("Avoidance Action"), which is not specifically included in Section 1.1 above.

The Trustee argues "under the language of Section 1.2(f), the Common Law Claims are 'related to claims... arising under Chapter 5 of the Bankruptcy Code.'" In the Trustee's view paragraph 1.2(f) excepted avoidance actions and all claims arising under or related thereto. The Court does not share that view. Paragraph 1.2(f) of the APA did not except from the sale avoidance actions and any causes of action "arising under or related [to the avoidance actions]." This interpretation proposed by the Trustee is undercut by the comma between "litigation rights arising under or related to claims" and "and choses arising under Chapter 5 of the Bankruptcy Code...." As the Court reads the APA, all of Debtor's litigation rights were sold to QBLLC, with the exception of two categories - first, "rights arising under or related to claims" and second, "choses of action arising under Chapter 5." The result of paragraphs 1.1(j) and 1.2(f) is that it unambiguously excepted only Chapter 5 avoidance actions and causes of action related to claims against the estate. It did not except any general claims which happen to arise from the same facts as the avoidance actions.

\\\

The Trustee also argues that even if she did not have standing to assert the Common Law Claims on behalf of the estate, she "also has standing to pursue the claims on behalf of creditors." This too is unavailing. If the Common Law Claims were sold to QBLLC, then neither the bankruptcy estate nor the creditors thereof have any remaining interest therein except as nonbankruptcy law might otherwise provide.

This disposes of the Trustee's argument that the Common Law Claims were reserved to the estate as actions related to the Avoidance Claims. However, the Court's interpretation, which differs from that of both parties, gives rise to an issue which has not yet been addressed. That is, whether the Common Law Claims are "litigation rights arising under or related to claims [against the bankruptcy estate]."

Elizabeth filed ten or more proofs of claim. Perhaps the argument can be made that the Common Law Claims arise under or relate to Elizabeth's claims against the estate whether as defenses or setoffs, and were thus excepted from the sale. However, since neither party has addressed this issue, the Court will not do so at this time. Rather, the motion to dismiss the Common Law Claims will be granted without prejudice to the Trustee amending the Complaint to assert standing to pursue the claims on the theory that they relate to or arise under the claims Elizabeth has asserted against the estate.

Defendants also argue that the Common Law Claims are barred by the 4 year California statute of limitations. In her

opposition the Trustee argued for application of the Discovery Rule, which provides that the statue does not *begin to run until* the facts supporting the claims are discovered. In the Complaint the Trustee alleges that the transfers were not discovered until May 2011, which, if established, would make the filing within 4 years thereof timely. Defendants did not respond to this argument in the reply. Assuming the facts as plead to be accurate, and not challenged by the Trustee, the motion to dismiss the Common Law Claims on the statute of limitations argument is denied.

Time to File Limitations on Avoidance Actions

The Avoidance Actions were clearly retained by the estate under the APA. The issue as to these claims is whether they are barred by the time under § 546(a) within which to file. The Trustee does not dispute that the time period within which to file the Avoidance Claims expired on August 11, 2012, well before the Complaint was filed on January 10, 2014. She argues, though, that the time limit ought to be equitably tolled.

Equitable tolling is a remedy applied in limited situations. "As a general rule, statutes of limitations are strictly construed. [Citation omitted] In extreme circumstances, however, under the doctrine of equitable tolling, a court may extend equitable relief to a claimant by suspending the applicable statute of limitations." In re Hosseinpour-Esfahani, 198 B.R. 574, 577-78 (9th Cir.BAP 1996). In order to invoke equitable tolling, the party must establish not only that it was

diligent in investigating the potential action, but also that he or she was not "dilatory after discovering the existence of a claim." Id. at 579. On the undisputed facts in this case, the Court finds that the Trustee was indeed dilatory after discovering the facts underlying the Avoidance Claims, and that there are no extreme circumstances which warrant equitable tolling to save the Trustee from the time limitations.

The Trustee became aware of the alleged transfers by Elizabeth no later than April 26, 2013 when she learned of the Luhr Complaint. She knew then that the time to file an avoidance action had expired, yet she did not seek relief and she waited nine months to file the Complaint. The Trustee complains that Defendants failed to respond to her 2004 exam discovery requests. However, she did not need their responses to file her complaint - all of the necessary facts were laid out in the Luhr Complaint. In fact the Trustee did file her complaint without input from the Defendants - just nine months later.

The Trustee may be suggesting that she did not want to file a complaint until she verified the facts through her 2004 exam. Even so, at the very least the Trustee should have sought relief from the time limitation and/or filed the complaint once it became clear Defendants were nonresponsive - 28 days after the June 28, 2013 discovery requests were served.

The Trustee also relies upon a line of cases which have applied a Delaware court-created tolling to toll the state law statute of limitations where a corporate fiduciary engaged in

secret self-dealing to the detriment of shareholders. See In re Sheffield Steel, 320 B.R. 405 (Bankr.N.D.Okla. 2004). Even if we assume that the Delaware law would apply to the time limitations provided in Bankruptcy Code § 546, that tolling provision is subject to the same restrictions discussed above. The equitable considerations "include whether the plaintiff failed to act promptly upon learning of the fiduciary's wrongdoing...." Sheffield Steel, 320 B.R. at 418. As discussed above, the Trustee did not act promptly. She filed the Complaint nine months after she learned of the Luhr Complaint, which contained all of the factual allegations upon which her Complaint is based. Under the facts of this case, the Trustee did not act with reasonable promptness, and is not entitled to equitable tolling under either line of cases. The motion to dismiss the Avoidance Claims is granted on the ground that they are barred by the time limitation of § 546(a).

CONCLUSION

For the foregoing reasons, Defendants' motion to dismiss the Common Law Claims is granted without prejudice. The Trustee has leave to amend the Complaint within thirty (30) days of the date of service of this Order to allege standing on the grounds that those causes of action arise under or relate to Elizabeth's claims against the estate. The Defendants motion to dismiss the Avoidance Actions is granted on the ground that they are barred

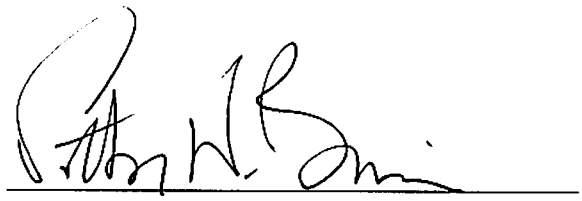
\\\

\\\

by the applicable statute of limitations and the Trustee is not entitled to equitable tolling.

IT IS SO ORDERED.

DATED: APR 14 2014



PETER W. BOWIE, Judge
United States Bankruptcy Court

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF CALIFORNIA
325 West F Street, San Diego, California 92101-6991

In re Bankruptcy Case: Qualitybuilt.com Case No.: 09-12113-PB7
Adversary: Leslie T. Gladstone v. Elizabeth and Garth Michaelis Adv. No.: 14-90005-PB

CERTIFICATE OF MAILING

The undersigned, a regularly appointed and qualified clerk in the office of the United States Bankruptcy Court for the Southern District of California, at San Diego, hereby certifies that a true copy of the attached document, to wit:

ORDER ON DEFENDANTS' MOTION TO DISMISS ALL CLAIMS

was enclosed in a sealed envelope bearing the lawful frank of the bankruptcy judges and mailed to each of the parties at their respective addresses listed below:

Geraldine A. Valdez
401 Via Del Norte
La Jolla, CA 92037

Sean A. O'Keefe
Garrick A. Hollander
660 Newport Center Dr., 4th Fl.
Newport Beach, CA 92660

Said envelope(s) containing such document was deposited by me in a regular United States Mail Box in the City of San Diego, in said District on April 14, 2014.

Lisa Cruz, Deputy Clerk

Notice Recipients

District/Off: 0974−3	User: melimu	Date Created: 4/14/2014
Case: 14−90005−PB	Form ID: pdfO1	Total: 5

Recipients of Notice of Electronic Filing:

pla	Leslie T. Gladstone	candic@flgsd.com
aty	Garrick A. Hollander	ghollander@winthropcouchot.com
aty	Geraldine A. Valdez	geraldinev@flgsd.com

TOTAL: 3

Recipients submitted to the BNC (Bankruptcy Noticing Center):

dft	Elizabeth Michaelis	401 SE 12th Street, Suite 200	Fort Lauderdale, FL 33316
dft	Garth Michaelis	401 SE 12th Street, Suite 200	Fort Lauderdale, FL 33316

TOTAL: 2