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FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF CALIFORNIA

In re:

ECS REFINING, INC.,

Debtor.

Case No. 18-22453-A-7

KIMBERLY J. HUSTED,

Plaintiff,

v.

KENNETH TAGGART et al.,

Defendants.

Adv. No. 20-02093-A

PH-2, DB-2

MEMORANDUM

Argued and submitted on November 24, 2020

at Sacramento, California

Honorable Fredrick E. Clement, Bankruptcy Judge Presiding

Appearances: Christopher D. Sullivan, Roxanne Bahadurji
and Quentin Roberts, Diamond McCarthy LLP
for Kimberly J. Husted, Chapter 7 trustee;
Howard M. Privette and Kay S. Kress,
Troutman Pepper Hamilton Sanders LLP for
Kenneth Taggart, James Taggart and Jack
Rockwood; Jamie P. Dreher and Joseph K.
Little, Downey Brand LLP for Sinclair
Partners LLC, ECS Big Town LLC, and All
Metals, Inc.

1 Directors of insolvent corporations owe fiduciary duties to
2 creditors. ECS Refining, Inc., was insolvent. It owed SummitBridge a
3 \$26 million secured debt. When SummitBridge refused to restructure
4 its debt, ECS Refining's directors employed bare-knuckled and, in some
5 instances self-interested, tactics designed to "take out"
6 SummitBridge. Caught in the crossfire, unsecured creditors' interests
7 suffered. After ECS Refining filed bankruptcy, the Chapter 7 trustee
8 brought an action against the directors. Has she stated a cause of
9 action?

10 **I. FACTS**

11 **A. The Preamble**

12 ECS Refining, Inc. ("ECS") is a Delaware corporation. It
13 conducted business in California, Oregon, Texas, Ohio, and Arkansas.
14 Founded in 1980, its primary business was the disposal and, in some
15 cases, re-furbishing and re-selling of post-consumer electronic goods.
16 Prior to filing bankruptcy, it employed 325 people and had been quite
17 profitable.

18 ECS was founded by Kenneth Taggart and James Taggart.
19 Collectively, the Taggarts were ECS's sole shareholders and
20 constituted its board of directors.¹ They also comprised the majority
21 of ECS's officers. James Taggart was its Chief Executive Officer and
22 Kenneth Taggart was its Executive Vice President. A third person,
23 Jack Rockwood (collectively the "Individual Defendants"), served as
24 its president.

25 ¹ Though not germane here, between 2012 and early 2018, another private
26 equity fund, ZS Fund L.P., owned a 50% interest in ECS and had "two
27 individuals associated with the ZS Fund" on ECS's board of directors.
28 First Am. Compl. 9:11-21. By the date that ECS filed bankruptcy, the
Taggarts were the sole shareholders and only members of the board of
directors. *Id.* at 9:23-24.

1 The Taggarts are the primary, if not exclusive, owners of--and
2 control--three entities with whom ECS regularly did business: Sinclair
3 Partners, LLC; ECS Big Town, LLC; and All Metals, Inc. (collectively
4 the "Insider Entity Defendants").

5 The Insider Entity Defendants had long-term real property leases
6 with ECS. Sinclair Partners, LLC, leased 262,000 square feet, known
7 as "the Stockton facility," to ECS under a 20-year lease. Rent was
8 \$90,000 per month, subject to a 3.25% cost of living adjustment each
9 year. ECS Big Town, LLC, leased 216,000 square feet, known as "the
10 Mesquite facility," to ECS under a 10-year lease. Rent for that
11 facility was \$51,000 per month. All Metals, Inc., also leased space
12 to ECS. Those facilities were larger than reasonably required for
13 ECS's operations conducted at those sites.

14 Butch and Sundance, LLC, is a limited liability company. It was
15 formed on the eve of ECS's bankruptcy and its only members are the
16 Taggarts. It was formed for the specific purpose of providing post-
17 petition financing to ECS to be secured by receivables, inventory,
18 cash and new equipment.

19 **B. The SummitBridge Loans**

20 In 2012, Bank of America made two loans to ECS: a \$15 million
21 revolving loan and a \$35 million term loan. Those loans were secured
22 by ECS's equipment, inventory, goods, works in process, proceeds,
23 fixtures, patents and trademarks and a pledge of stock in another
24 company, Regenesys Glass Processing, LLC.²

25 In 2017, Bank of America sold its interest in the loans, and
26 assigned its collateral securing those loans, to SummitBridge National

27 _____
28 ² The relationship of Regenesys Glass Processing, LLC, if any, to the
Taggarts and/or ECS is unclear.

1 Investments V LLC ("SummitBridge"), a private equity firm.

2 About the same time, ECS wanted to restructure its long-term
3 debt, now held by SummitBridge. To that end it retained MCA Financial
4 Group, Ltd. ("MCA") and the law firm of Snell & Wilmer LLP ("Snell &
5 Wilmer") to negotiate restructuring the SummitBridge loan. MCA and
6 Snell & Wilmer did secure a forbearance agreement for ECS from
7 SummitBridge through December 31, 2017.

8 However, as the forbearance agreement neared expiration, it
9 became clear that the Taggarts and SummitBridge were at an impasse
10 with respect to ECS's ultimate goal of long-term restructuring of
11 SummitBridge's debt. The Taggarts insisted that they have control of
12 ECS and at least 40% ownership each; SummitBridge was agreeable to
13 further concessions but wanted further equity in ECS. Finding
14 SummitBridge's demands unacceptable, the Taggarts, MCA and Snell &
15 Wilmer developed a plan to "take out" Summit Bridge. But they needed
16 time to identify and implement that strategy. So, from January
17 through April 2018, Snell & Wilmer LLP and MCA engaged in "duplicitous
18 negotiations" with SummitBridge without any intention of giving it
19 additional equity in ECS while the Taggarts positioned ECS for
20 bankruptcy.

21 **C. Preparing for ECS's Bankruptcy**

22 While occupying SummitBridge with restructuring discussions, the
23 Taggarts employed a tripartite strategy designed to subdue
24 SummitBridge and to maximize Taggarts' control over ECS during and
25 after the bankruptcy process. First, the Taggarts weakened ECS's
26 overall financial health by minimizing ECS's cash position.
27 Commercial rental payments to the Insider Entity Defendants were
28 increased. For example, during the negotiations with SummitBridge the

1 Taggarts, acting through ECS Big Town, increased rent for the Mesquite
2 facility from \$31,679 per month to \$51,332 per month. They also
3 increased the rent for the Stockton facility by \$3,000 per month to
4 \$112,583 per month. ECS also paid unnecessarily high salaries and
5 wages to its employees. Trustee Husted complained that the Taggarts
6 failed to address the "bloated overhead by adequately trimming the
7 workforce" and made the "irrational decision to keep over" 325 full
8 time employees. First Am. Compl. 13:15-17, ECF No. 28. ECS also paid
9 vendors at rates greater than historical norms.

10 Second, the Taggarts undermined SummitBridge's position as a
11 secured creditor. Trustee Husted described the Taggarts efforts as "a
12 scheme to minimize ESC's assets that were subject to [its] security
13 interest [in the days] leading up to the bankruptcy." *Id.* 12:18-20.
14 As one of ECS's financial advisors described the strategy,

15 *Well, the strategy...is a great way to put the screws to*
16 *Summit by squeezing of as much of the [accounts receivable]*
17 *as possible before filing. Summit is limited to collecting*
18 *from and receiving proceeds from the [accounts receivable]*
19 *at the time of filing ONLY. That will include cash on hand*
at the time of filing. So that means once collected it
should immediately be used to pay down critical expenses
otherwise the money will need to be held FBO Summit.

20 *Id.* at 14:23-27 (emphasis added).

21 This strategy involved collecting accounts receivable, spending
22 available cash and ceasing production, and segregating incoming
23 inventory. Because a large portion of SummitBridge's collateral for
24 the loan was "inventory goods, works in progress, fixtures, and
25 proceeds of the foregoing," stepping down the aggregate value of these
26 assets increased its unsecured debt relative to its secured debt and
27 marginalized its influence as a creditor.

1 **D. Chapter 11**

2 After positioning itself, ECS filed Chapter 11 bankruptcy. ECS's
3 counsel of choice in the Chapter 11 was Snell & Wilmer, as well as
4 Ringstad & Sanders LLP.

5 At the time ECS sought bankruptcy protection, SummitBridge was
6 owed \$26.690 million.³ The collateral securing that debt had a value
7 of \$5 million. *Id.*

8 Third, the Taggarts attempted to capitalize on their pre-
9 bankruptcy strategies with a loan from their new-formed company Butch
10 and Sundance, LLC. Under the control of the Taggarts, ESC filed a
11 first-day motion to authorize it to obtain post-petition financing
12 from Butch and Sundance, LLC, of up to \$6 million, granting it liens
13 and superpriority administrative claims, and authorizing the use of
14 cash collateral. Emergency Ex Parte Mot. for Order Authorizing Post-
15 Petition Financing 2:3-4:25, *In re ECS Refining, Inc.*, No. 2018-22453
16 (Bankr. E.D. Cal. April 24, 2018), ECF No. 12. That motion
17 represented:

18 There is no dispute that, without substantial post-petition
19 financing, the Debtor will be forced to immediately cease
20 business operations and engage in a fire sale of its assets
21 without the ability to maximize their value through its
22 planned organization, which it plans to effectuate within
23 the exclusivity period, if not sooner, and will benefit all
24 creditors.

25 First Am. Compl. 20:6-9.

26 At the initial hearing of the motion there was "no disclosure that

27 ³ The court takes judicial notice of (1) the existence of Proof of
28 Claim No. 327-2, *In re ECS Refining, Inc.*, No. 18-22453 (Bankr. E.D.
29 Cal. November 16, 2018), filed by SummitBridge; and (2) the absence of
30 objection to that proof of claim. Fed. R. Evid. 201; *Burbank-
31 Glendale-Pasadena Airport Auth. v. City of Burbank*, 136 F.3d 1360,
32 1364 (9th Cir. 1998) (court may take judicial notice of court
33 filings). Absent objection, the Proof of Claim is deemed allowed and
34 presumptively valid. 11 U.S.C. § 502(a); Fed. R. Bankr. P. 3001(f).

1 Butch & Sundance LLC was purely self-funded and operated by the
2 Taggarts." *Id.* 20:10-11.

3 The motion was supported by the unsigned declaration of ECS
4 president, Jack Rockwood, who declared the terms were "fair,
5 reasonable and adequate." *Id.* 20:17-19. But that is not true. For
6 example, the proposed order approving the loan stated that the loan
7 was "negotiated in good faith and at arm's length" between ECS and
8 Butch and Sundance, LLC. Ex Parte Motion 32:9-10. Notwithstanding
9 its claim of evenhandedness, Butch and Sundance, LLC, conditioned its
10 willingness to make the loan on terms that were one-sided: (1) waiver
11 of the trustee's surcharge rights, 11 U.S.C. § 506(c); freeing post-
12 petition acquired property from any security interests granted to a
13 pre-petition lender, i.e., SummitBridge, 11 U.S.C. § 552; (2)
14 automatic stay relief on default; and (3) preclusion of any person
15 from using post-petition loan proceeds to "investigate, assert, join,
16 commence, support or prosecute any action" for "any avoidance action
17 or other actions arising under Chapter 5 or Section 724(a)." *Id.*
18 39:18-40:5, 40:27-41:24, 42:4-19.

19 Under the terms of the proposed post-petition financing, in
20 exchange for a loan of up to \$ 6 million, Butch and Sundance LLC would
21 receive a superpriority administrative expenses claim, 11 U.S.C. §
22 364(c); a first priority security interest against "any unencumbered
23 pre-petition assets and all post-petition assets of the debtor"; a
24 security interest "on any and [all] pre-petition assets, subject only
25 to any existing as of the Petition Date, valid, perfected and
26 unavoidable liens"; and a first priority security interest against
27 "any and all claims arising under Chapter 5 of the Bankruptcy Code,
28 including without limitation Sections 502(d), 544, 547, 548, 549, 550

1 and 553." *Id.* 2:28-4:6.

2 In response to ECS's motion, SummitBridge informed the court that
3 the Taggarts were, in fact, the owners of Butch and Sundance, LLC.

4 **E. Conversion to Chapter 7**

5 Six months after the Chapter 11 case was filed, the court ordered
6 it converted to a case under Chapter 7. Kimberly J. Husted ("Husted")
7 was appointed as the trustee.

8 **II. PROCEDURE**

9 Trustee Husted filed a complaint against the Individual
10 Defendants and the Insider Entity Defendants. Those defendants filed
11 motions to dismiss the complaint and the trustee exercised her right
12 to amend the complaint. Fed. R. Civ. P. 15(a)(1)(B), *incorporated by*
13 Fed. R. Bankr. P. 7015.

14 Plaintiff Husted's First Amended Complaint included 12 causes of
15 action: breach of fiduciary duty; corporate waste; avoidance of
16 preferences; avoidance of actual fraudulent transfers; avoidance of
17 constructively fraudulent transfers; avoidance of unauthorized post-
18 petition transfers; recovery of avoided transfers; equitable
19 subordination; and objection to Proofs of Claim.

20 The Individual Defendants now move under Rule 12(b)(6) to dismiss
21 the First Amended Complaint. The Insider Entity Defendants now move
22 under Rule 12(b)(6) to dismiss the First Amended Complaint or, in the
23 alternative, under Rule 12(e) for a more definite statement.

24 Plaintiff Husted opposes the motion.⁴

25 ⁴ The trustee does not oppose the motion as to (1) first and second
26 causes of action: defendant Jack Rockwell; (2) the third cause of
27 action: as to Sinclair Partners and ECS Big Town; (3) the sixth cause
28 of action: all defendants; or (4) the eighth through twelfth causes of
action: all defendants. As a result, the motion will be granted
without leave as to that defendant and those causes of action.

1 **III. JURISDICTION**

2 This court has jurisdiction. 28 U.S.C. §§ 1334(a)-(b), 157(b);
3 see also General Order No. 182 of the Eastern District of California.
4 Because all parties have consented to entry of final orders and
5 judgments, this court need not decide whether the matters presented
6 are core or non-core. 28 U.S.C. § 157(b)(3); *Wellness Int'l Network,*
7 *Ltd. v. Sharif*, 135 S.Ct. 1932, 1945-46 (2015); First Am. Compl. 7:21-
8 22, ECF # 28; Mot. to Dismiss 5:16-17, August 19, 2020, ECF No. 41;
9 Mem. P. & A. 9:8-10, August 19, 2020, ECF No. 50.

10 **IV. LAW**

11 **A. Rule 12(b)(6)**

12 Under Federal Rule of Civil Procedure 12(b)(6), a party may move
13 to dismiss a complaint for “failure to state a claim upon which relief
14 can be granted.” Fed. R. Civ. P. 12(b)(6), *incorporated by* Fed. R.
15 Bankr. P. 7012(b). “A Rule 12(b)(6) dismissal may be based on either
16 a lack of a cognizable legal theory or the absence of sufficient facts
17 alleged under a cognizable legal theory.” *Johnson v. Riverside*
18 *Healthcare Sys., LP*, 534 F.3d 1116, 1121-22 (9th Cir. 2008); *accord*
19 *Navarro v. Block*, 250 F.3d 729, 732 (9th Cir. 2001).

20 “After *Iqbal* and *Twombly*, courts employ a three-step analysis in
21 deciding Rule 12(b)(6) motions. At the outset, the court takes notice
22 of the elements of the claim to be stated. *Eclectic Properties East,*
23 *LLC v. Marcus & Millichap Co.*, 751 F.3d 990, 997 (9th Cir. 2014).
24 Next, the court discards conclusions. *Ashcroft v. Iqbal*, 556 U.S. 662,
25 679 (2009); *United States ex rel. Harper v. Muskingum Watershed*
26 *Conservancy District*, 842 F.3d 430, 438 (6th Cir. 2016) (the complaint
27 failed to include “facts that show how” the defendant would have known
28 alleged facts). Finally, assuming the truth of the remaining well-

1 pleaded facts, and drawing all reasonable inferences therefrom, the
2 court determines whether the allegations in the complaint "plausibly
3 give rise to an entitlement to relief." *Iqbal*, 556 U.S. at
4 679; *Sanchez v. United States Dept. of Energy*, 870 F.3d 1185, 1199
5 (10th Cir. 2017). See generally, *Wagstaff Practice Guide: Federal*
6 *Civil Procedure Before Trial*, Attacking the Pleadings, Motions to
7 Dismiss § 23.75-23.77 (Matthew Bender & Company, Inc. 2019)." *Aluisi*
8 *v. Jorgensen (In re Jorgensen)*, No. 19-01026, 2019 WL 6720418, at *4
9 (Bankr. E.D. Cal. Dec. 10, 2019)

10 "Plausibility means that the plaintiff's entitlement to relief is
11 more than possible. *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 556, 570
12 (2007) (the facts pled "must cross the line from conceivable to
13 plausible"); *Almanza v. United Airlines, Inc.*, 851 F.3d 1060, 1074 (11
14 Cir. 2017). Allegations that are "merely consistent" with liability
15 are insufficient. *Iqbal*, 556 U.S. at 662; *McCauley v. City of Chicago*,
16 671 F.3d 611, 616 (7th Cir. 2011)." *Aluisi v. Jorgensen*, 2019 WL
17 6720418, at *4.

18 "If the facts give rise to two competing inferences, one of which
19 supports liability and the other of which does not, the plaintiff will
20 be deemed to have stated a plausible claim within the meaning
21 of *Iqbal* and *Twombly*. *Houck v. Substitute Tr. Servs., Inc.*, 791 F.3d
22 473, 484 (4th Cir. 2015); *16630 Southfield Ltd. P'hsip v. Flagstar*
23 *Bank, F.S.B.*, 727 F.3d 502, 505 (6th Cir. 2013); see also, *Wagstaff*,
24 Motion to Dismiss at § 23.95. But if one of the competing inferences
25 is sufficiently strong as to constitute an "obvious alternative
26 explanation," that inference defeats a finding of plausibility and the
27 complaint should be dismissed. *Marcus & Millichap Co.*, 751 F.3d at 996
28 ("Plaintiff's complaint may be dismissed only when defendant's

1 plausible alternative explanation is so convincing that the
2 plaintiff's explanation is implausible."); *New Jersey Carpenters*
3 *Health Fund v. Royal Bank of Scotland Group, PLC*, 709 F.3d 109, 121
4 (2nd Cir. 2013)." *Aluisi v. Jorgensen*, 2019 WL 6720418, at *4.

5 In addition to looking at the facts alleged in the complaint, the
6 court may also consider some limited materials without converting the
7 motion to dismiss into a motion for summary judgment under Rule 56.
8 Such materials include (1) documents attached to the complaint as
9 exhibits, (2) documents incorporated by reference in the complaint,
10 and (3) matters properly subject to judicial notice. *United States v.*
11 *Ritchie*, 342 F.3d 903, 908 (9th Cir. 2003); accord *Swartz v. KPMG LLP*,
12 476 F.3d 756, 763 (9th Cir. 2007) (per curium) (citing *Jacobson v.*
13 *Schwarzenegger*, 357 F.Supp.2d 1198, 1204 (C.D. Cal. 2004)). A
14 document may be incorporated by reference, moreover, if the complaint
15 makes extensive reference to the document or relies on the document as
16 the basis of a claim. *Ritchie*, 342 F.3d at 908.

17 **B. Rule 12(e)**

18 Under Federal Rule of Civil Procedure 12(e), a party may move to
19 dismiss a complaint "for a more definite statement." Fed. R. Civ. P.
20 12(e), incorporated by Fed. R. Bankr. P. 7012(b). Rule 12(e) is
21 proper where the complaint is sufficiently conclusory, confused or
22 unclear that a defendant cannot properly be expected to respond.
23 *Balderrama v. Pride Indus., Inc.*, 963 F.Supp.2d 646, 667 (W.D. TX
24 2013).

25 **C. Internal Affairs Doctrine**

26 "A federal court sitting in diversity must look to the forum
27 state's choice of law rules to determine the controlling substantive
28 law." *Mazza v. Am. Honda Motor Co.*, 666 F.3d 581, 589 (9th Cir. 2012)

1 (quoting *Zinser v. Accufix Research Inst., Inc.*, 253 F.3d 1180, 1187
2 (9th Cir. 2001), *opinion amended on denial of reh'g*, 273 F.3d 1266
3 (9th Cir. 2001). The internal affairs doctrine is a conflict of law
4 principle that "recognizes that only one State should have the
5 authority to regulate a corporation's internal affairs--matters
6 peculiar to the relationships among or between the corporation and its
7 current officer, directors, and shareholders--because otherwise a
8 corporation could be faced with conflicting demands." *Edgar v. MITE*
9 *Corp.*, 457 U.S. 624, 645 (1982); *Drulias v. 1st Century Bancshares,*
10 *Inc.*, 30 Cal.App.5th 696, 705 (2018); *Greb v. Diamond Int'l Corp.*, 56
11 Cal.4th 243, 264-269 & fn. 35 (2013).

12 Well aware of the conundrum articulated by *Edgar*, California has
13 codified the internal affairs doctrine.

14 The directors of a foreign corporation transacting
15 intrastate business are liable to the corporation, its
16 shareholders, creditors, receiver, liquidator or trustee in
17 bankruptcy for the making of unauthorized dividends,
18 purchase of shares or distribution of assets or false
19 certificates, reports or public notices or other violation
of official duty according to any applicable laws of the
state or place of incorporation or organization, whether
committed or done in this state or elsewhere. Such
liability may be enforced in the courts of this state.

20 Cal. Corp. Code § 2116.

21 California's treatment of the issue is consistent with the
22 Restatement (Second) of Conflicts of Laws treatment of the problem.

23 The local law of the state of incorporation will be applied
24 to determine the existence and extent of a director's or
25 officer's liability to the corporation, its creditors and
26 shareholders, except where, with respect to the particular
27 issue, some other state has a more significant relationship
under the principles stated in § 6 to the parties and the
transaction, in which event the local law of the other
state will be applied.

28 *Restatement (Second) of Conflict of Laws* § 309 (1971), cited with

1 approval by *Edgar*, 457 U.S. at 645.

2 The outermost reach of the internal affairs doctrine is not well
3 defined. But as applied to directors and corporate officers the
4 doctrine applies to acts "which closely affect the organic structure
5 or internal administration of the corporation," as opposed to acts
6 that can "practicably be decided differently in different states,"
7 such as "causing the making of a contract or the commission of a
8 tort." Rest.2d § 309, Comment (c).

9 Exceptions to the rule exist where a state other than the state
10 of incorporation has "a more significant relationship" to the parties
11 and the transaction, Rest.2d § 309, Cal. Corp. Code § 2115;⁵ *Lidow v.*
12 *Superior Court (International Rectifier Corp.)*, 206 Cal.App.4th 351,
13 359 (2012) (recognizing the common law "more significant relationship"
14 exception); *Vaughn v. LJ Int'l, Inc.*, 174 Cal.App.4th 213, 225-226
15 (2009) or where the interests of justice so require. Rest.2d § 302 et

16
17 ⁵ California Corporations Code § 2115 provides a statutory exception to
the "internal affairs doctrine." In the pertinent part it provides:

- 18 (a) A foreign corporation (other than a foreign
19 association or foreign nonprofit corporation but
20 including a foreign parent corporation even though it
21 does not itself transact intrastate business) is
22 subject to the requirements of subdivision (b)
23 commencing on the date specified in subdivision (d)
24 and continuing until the date specified in subdivision
25 (e) if:
26 (1) The average of the property factor, the payroll
27 factor, and the sales factor (as defined in Sections
28 25129, 25132, and 25134 of the Revenue and Taxation
Code) with respect to it is more than 50 percent
during its latest full income year and
(2) more than one-half of its outstanding voting securities
are held of record by persons having addresses in this
state appearing on the books of the corporation on the
record date for the latest meeting of shareholders held
during its latest full income year or, if no meeting was
held during that year, on the last day of the latest full
income year....

1 seq.; *Gillis v. Pan Amer. Western Petroleum Co.*, 3 Cal.2d 249, 252
2 (1935).

3 **V. DISCUSSION**

4 The effect of Taggarts' actions was to restrict SummitBridge's
5 collateral to the \$5 million of collateral it held on the date ECS
6 filed for bankruptcy protection and to relegate the remainder of the
7 debt, i.e., \$21.690 million, to that of unsecured debt. 11 U.S.C. §§
8 506(a), (d), 552(a) ("[P]roperty acquired by the estate or by the
9 debtor after the commencement of the case is not subject to any lien
10 resulting from any security agreement entered into by the debtor
11 before the commencement of the case"); Emergency Ex Parte Mot. for
12 Order Authorizing Post-Petition Financing 2:28-4:6, *In re ECS*
13 *Refining, Inc.*, No. 2018-22453 (Bankr. E.D. Cal. April 24, 2018), ECF
14 No. 12 (interposing an intervening lien).

15 These allegations give rise to the inference that the Taggarts
16 intended to use plan confirmation to force SummitBridge to restructure
17 its debt. Bifurcating SummitBridge's claim positioned ECS for
18 confirmation fight with SummitBridge by: (1) reducing the amount that
19 must be paid under the best interests test, i.e., \$5 million, 11
20 U.S.C. § 1129(a)(7)(A)(ii); (2) denying SummitBridge an absolute
21 priority rule objection as to its secured claim by proposing a plan
22 that called for the sale of SummitBridge's now diminished collateral,
23 11 U.S.C. §§ 1129(b)(1),(2)(A)(ii) (which overrides a 11 U.S.C. §
24 1111(b) election), 1111(b)(1)(B)(ii)); *Cf. RadLAX Gateway Hotel, LLC*
25 *v. Amalgamated Bank*, 566 U.S. 639 (2012) (construing 11 U.S.C. §
26 1129(b)(2)(A)(iii)); 7 *Collier on Bankruptcy* ¶ 1111.03[5][c] (Alan N.
27 Resnick & Henry J. Sommer eds., 16th ed. 2020); and (3) minimizing any
28 argument that the absolute priority rule is violated as to unsecured

1 creditors by reducing the amount of the “new value” contribution
2 necessary to overcome that objection. 11 U.S.C. § 1129(b)(2)(B); *In*
3 *re Bonner Mall Partnership*, 2 F.3d 899, 906 (9th Cir. 1993), *abrogated*
4 *on other grounds by Bullard v. Blue Hills Bank*, 575 U.S. 496 (2105).

5 But neither federal, nor state, i.e., Delaware, law authorizes
6 the trustee to act solely on behalf of an individual creditor, i.e.,
7 SummitBridge. *Caplin v. Marine Midland Grace Trust Co. of New York*,
8 406 U.S. 416 (1972) (a bankruptcy trustee may not pursue a claim for
9 injury solely to benefit one creditor or one class of creditors);
10 *Williams v. Cal. 1st Bank*, 859 F.2d 664, 666 (9th Cir. 1988); *Mixon v.*
11 *Anderson (In re Ozark Rest. Equip. Co.)*, 816 F.2d 1222, 1227-28 (8th
12 Cir. 1987); *N. Am. Catholic Educ. Programming Found., Inc. v.*
13 *Gheewalla*, 930 A.2d 92, 99 (Del. 2007) (creditors do not hold a direct
14 right of action against directors for breach of a fiduciary duty);
15 *Nemec v. Shrader*, 991 A.2d 1120, 1129 (Del. 2010).⁶

16 The question is whether the Taggarts’ actions, which were aimed
17 at SummitBridge, incidentally and unlawfully injured ECS’s unsecured
18 creditors.

19 **A. First Cause of Action: Breach of Fiduciary Duties**

20 Plaintiff Husted alleges that defendants Taggarts’ actions
21 breached their fiduciary duties of loyalty, care and good faith.

22 **1. Choice of Law: Delaware or California**

23 *Edgar* and California Corporations Code § 2116 specifically
24 contemplate the breed of cat now before this court. Section 2116
25

26 ⁶ Because *Caplin v. Marine Midland Grace Trust Co. of New York*, 406
27 U.S. 416 (1972), precludes the trustee from acting on behalf of but a
28 single creditor the Individual Defendants’ motion to dismiss the First
Amended Complaint will be granted without leave to amend insofar as
the trustee seeks to recover for injuries unique to SummitBridge.

1 applies to a director's liability to "the corporation, its
2 shareholders, creditors, receiver, liquidator or trustee in
3 bankruptcy." By the same measure it applies to directors' actions
4 "for the making of unauthorized dividends, purchase of shares or
5 distribution of assets or false certificates, reports or public
6 notices or other violation of official duty." Efforts by the board of
7 directors to restructure debt or to posture the corporation for
8 reorganization in Chapter 11 are "official duties" within the meaning
9 of § 2116. The Chapter 7 trustee contends the directors Taggarts'
10 actions were overly zealous or self-interested.

11 Moreover, California and federal courts have had little
12 difficulty finding a breach of fiduciary duty that affects the organic
13 structure of the corporation and, as a result, that Delaware law
14 provides the rule of decision. *Vaughn v. LJ Int'l, Inc.*, 174
15 Cal.App.4th 213, 223-25 n. 5 (2009) (apply internal affairs doctrine
16 to breach of fiduciary duty); *Banjo Buddies, Inc. v. Renosky*, 399 F.3d
17 168, 179 n. 10 (3rd Cir. 2005); *Gabriel v. Preble*, 396 F.3d 10, 13
18 (1st Cir.2005); *Hollis v. Hill*, 232 F.3d 460, 465-66 (5th Cir. 2000);
19 *Nagy v. Riblet Products Corp.*, 79 F.3d 572, 576 (7th Cir. 1996);
20 *Hausman v. Buckley*, 299 F.2d 696, 703 (2d Cir.1962) ("the internal
21 affairs rule has been applied repeatedly in order to determine the
22 fiduciary duty of a foreign corporation's directors").

23 Plaintiff Husted argues that California has a more significant
24 relationship to the parties and the transaction than Delaware has to
25 the parties and the transaction. Rest.2d § 309. If *Edgar*, and its
26 progeny, admit such an exception, *VantagePoint Venture Partners 1996*
27 *v. Examen, Inc.*, 871 A.2d 1108, 1115-1118 (Del. 2005) (holding
28 California Corp. Code § 2115, the codification of the more significant

1 relationship exception, unconstitutional), this is not it. The laws
2 of the state of incorporation presumptively provide the rule of
3 decision and it is the "unusual case" where the forum state has a more
4 significant relationship to the parties and the occurrence." *Mukamal*
5 *v. Bakes*, 378 Fed.Appx. 890, 897 (11th Cir. April 30, 2010). In
6 determining whether the forum state has a more significant
7 relationship to the parties and the transaction, the court should
8 consider:

9 (a) the needs of the interstate and international systems,
10 (b) the relevant policies of the forum, (c) the relevant
11 policies of other interested states and the relative
12 interests of those states in the determination of the
13 particular issue, (d) the protection of justified
14 expectations, (e) the basic policies underlying the
15 particular field of law, (f) certainty, predictability and
16 uniformity of result, and (g) ease in the determination and
17 application of the law to be applied.

18 Restatement (Second) Conflicts of Laws § 6 (1971).

19 The trustee attempts to characterize this dispute as one that is
20 rooted deeply, perhaps even exclusively, in California. But that is
21 not true. As the trustee herself characterizes ECS's operations it
22 conducted business in five states and employees 325 persons. Its
23 creditors come from throughout the United States and themselves have
24 national presences. Under the guidance of a national law firm, Snell
25 & Wilmer, the Taggarts employed a companywide strategy to take over
26 ECS. The strategy involved keeping SummitBridge talking about
27 restructuring its debt while the Taggarts prepared for ECS's
28 bankruptcy; weakening ECS companywide by reducing cash, work in
progress, and accounts receivable; and undermining SummitBridge's
position as a secured creditor by using its collateral without
replacing it. After placing ECS in peril, Taggarts, acting through
their wholly-owned entity, Butch and Sundance, LLC, purported to

1 rescue ECS with a post-petition loan which falsely purported to be on
2 terms that were "fair, reasonable and adequate." Adding insult to
3 injury neither ECS, nor Taggarts, initially disclosed their ownership
4 in that entity. The simple point is that California's tie to this
5 case is far weaker than the trustee believes, and that fragile
6 connection weighs heavily in favor of the rule, i.e., application of
7 Delaware law, and against application of California law.

8 Moreover, justified expectations also suggest application of the
9 rule, and not the exception. Taggarts certainly expected, even
10 bargained for, application of Delaware law. Sophisticated creditors
11 (who now speak through trustee Husted) contemplating business with ECS
12 are fairly charged with knowledge of the law, including the internal
13 affairs doctrine, and must have expected application of well-trenched
14 choice of law rules against them.

15 Finally, certainty, predictability and uniformity of result weigh
16 in favor of the application of Delaware law. ECS had a presence in
17 five states: California, Oregon, Texas, Ohio and Arkansas. Its
18 Chapter 11 petition might well have been proper in any of those
19 venues. 28 U.S.C. § 1408. Literal application of the internal
20 affairs doctrine will produce certainty and uniformity in the choice
21 of law analysis. Deviating from it undercuts uniformity and certainty
22 with respect to the standard by which the Individual Defendants'
23 actions would be judged.

24 For these reasons, the court believes that Delaware, and not
25 California, law controls.

26 **2. Corporate directors and their duties**

27 Delaware law imposes fiduciary duties on corporate directors. 1
28 R. Frank Balotti & Jesse A. Finkelstein, *Delaware Law of Corporations*

1 *and Business Organizations* § 4.14 (3rd ed. 2020-2 Supplement). As a
2 rule, that duty requires directors to exercise due care and loyalty
3 toward the corporation and its shareholders. *Mills Acquisition Co. v.*
4 *Macmillan, Inc.*, 559 A.2d 1261, 1280 (Del. 1989); Balotti &
5 Finkelstein, *supra*, at § 4.14.⁷

6 Directors must exercise due care, both in decision making by
7 acting on an informed basis and in “other aspects of their
8 responsibilities.” Balotti & Finkelstein, *supra*, at § 4.15. As a
9 rule, in managing corporate affairs directors of a corporation must
10 exercise “that amount of care which ordinarily careful and prudent men
11 would use in similar circumstances.” *Graham v. Allis-Chambers Mfg.*
12 *Co.*, 188 A.2d 125, 130 (1963). But as applied to decision-making,
13 Delaware courts have applied a gross negligence standard. *Stone v.*
14 *Ritter*, 911 A.2d 362, 369 (Del. 2006); *Brehm v. Eisner*, 746 A.2d 244,
15 259 (Del. 2000); *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984). As
16 used in this context gross negligence means a “reckless indifference
17 to or a deliberate disregard of the whole body of stockholders or
18 actions which are without the bounds of reason.” *Tomczak v. Morton*
19 *Thiokol, Inc.*, No. 7861, 1990 WL 42607, at *12 (Del. Ch. Apr. 5,
20 1990).

21 As one source summarized that duty:

22 Judicial inquiry into whether directors have exercised “due
23 care” in the decision-making context (citation omitted)
24 involves an examination of whether the directors informed
25 themselves, before “making a business decision, of all
26 material information reasonably available to them.” The
27 directors' judgment must be “informed . . . , with the
28 inquiry directed to the material or advice the board had

⁷ Good faith is not a separate subspecies of fiduciary duty but is a subsidiary element of the duty of loyalty. *Stone v. Ritter*, 911 A.2d 362, 369-70 (Del. 2006); Balotti & Finkelstein, *supra*, at § 4.14 fn. 624.

1 available to it and whether it had sufficient opportunity
2 to acquire knowledge concerning the problem before acting.

3 Balotti & Finkelstein, *supra*, at § 4.15.

4 Directors also act with loyalty toward the corporation in their
5 management of corporate affairs and personal dealings with the
6 corporation. *Id.* at § 4.16 (describing it as a “companion obligation
7 to the duty of care”). This duty arises from the premise that “the
8 directors are duty-bound to the true owners of the corporation, the
9 stockholders.” *Id.* That duty precludes a director from “stand[ing]
10 on both sides” of a transaction and from obtaining “any personal
11 benefit through self-dealing.” *Andarko Petroleum Corp. v. Panhandle*
12 *E. Corp.*, 545 A.2d 1171, 1174 (Del. 1988); *QC Commc’ns, Inc. v.*
13 *Quartone*, No. 8218-VCG, 2014 WL 3974525, at *11 (Del. Ch. Aug. 15,
14 2014); *Pers. Touch Holding Corp. v. Glaubach*, No. 11199-CB, 2019 WL
15 937180, at *19 (Del. Ch. Feb. 25, 2019) (“[I]n a typical self-dealing
16 transaction, the fiduciary is the recipient of an allegedly improper
17 personal benefit, which usually comes in the form of obtaining
18 something of value or eliminating a liability.”); Balotti &
19 Finkelstein, *supra*, at § 4.16. The standard is not a subjective one.
20 See *AC Acquisitions Corp. v. Anderson, Clayton & Co.*, 519 A.2d 103,
21 114-15 (Del. Ch. 1986).

22 As the same commentator described the duty:

23 In effect, it mandates that a director not consider or
24 represent interests other than the best interests of the
25 corporation and its stockholders in making a business
26 decision. The duty of loyalty also “encompasses cases where
the fiduciary fails to act in good faith,” including the
duty of oversight.

27 Balotti & Finkelstein, *supra*, at § 4.16 at fn. 747, citing *Revlon,*
28 *Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173, 182 (Del.

1 1986); *Weinberger v. UOP, Inc.*, 457 A.2d 701, 710 (Del. 1983); *Guth v.*
2 *Loft, Inc.*, 5 A.2d 503, 510 (Del. 1939) ("The rule that requires an
3 undivided and unselfish loyalty to the corporation demands that there
4 shall be no conflict between duty and self-interest."); *In re infoUSA,*
5 *Inc. S'holders Litig.*, 953 A.2d 963, 996 (Del. Ch. 2007) ("If
6 defendants actually engaged in this form of wasteful legerdemain in
7 order to help [the Chief Executive Officer] acquire the company at an
8 inequitable price, it constitutes a violation of their fiduciary duty
9 of loyalty, even if it did not succeed.").

10 That same commentator stated:

11 While the general concept underlying the duty of loyalty--
12 that a director refrain from self-dealing--is simple,
13 application of the loyalty principle can be difficult,
14 especially in complex transactions involving corporate
15 control. In such circumstances, this application can become
16 a highly fact-intensive exercise. This is in part because,
17 in those circumstances, *the courts interpret the duty of*
18 *loyalty as involving not only a duty to refrain from self-*
dealing but also a duty to deal "fairly" with the
stockholders when directors have an interest in the
transaction. As the Delaware Supreme Court stated . . .
'[w]hen directors of a Delaware corporation are on both
sides of a transaction, they are required to demonstrate
their utmost good faith and the most scrupulous inherent
fairness of the bargain.'

19 Balotti & Finkelstein, *supra*, at § 4.16 (emphasis added).

20 A corollary to the duties of care and loyalty is the duty of
21 disclosure. Balotti & Finkelstein, *supra*, at § 4.18 ("The duty of
22 disclosure--also known as the duty of candor--is not really a separate
23 fiduciary duty; it stems from the fiduciary duties of due care and
24 loyalty"). When shareholders ask for corporate action, they must
25 disclose any and all material information requested and must provide
26 "a balanced, truthful account of all matters disclosed in the
27 communications with shareholders." *Id.*, citing *Malone v. Brincat*, 722
28 A.2d 5, 12 (Del. 1998); see also *Shell Petroleum, Inc. v. Smith*, 606

1 A.2d 112, 114 (Del. 1992); *Stroud v. Milliken Enters., Inc.*, 552 A.2d
2 476, 480 (Del. 1989); *Lynch v. Vickers Energy Corp.*, 383 A.2d 278,
3 279, 281 (Del. 1978). Materiality is determined by whether there is a
4 substantial likelihood that it would affect the shareholders'
5 decision.

6 The Delaware courts use the same materiality standard used
7 by the U.S. Supreme Court: "An omitted fact is material if
8 there is a substantial likelihood that a reasonable
9 shareholder would consider it important in deciding how to
vote." That is, directors are only required to disclose
facts that significantly alter the "total mix" of
information available to the stockholder.

10 Balotti & Finkelstein, *supra*, at § 4.18.

11 Even in instances where shareholder action is not sought, if
12 directors "knowingly disseminate false information that results in
13 corporate injury or damage to an individual shareholder," the
14 directors have breached their fiduciary duty. *Malone v. Brincat*, 722
15 A.2d 5, 9 (Del. 1998). "When the directors are not seeking
16 shareholder action, but are deliberately misinforming shareholders
17 about the business of the corporation, either directly or by a public
18 statement, there is a violation of fiduciary duty." Balotti &
19 Finkelstein, *supra*, at § 4.18.

20 A director's fiduciary duty is limited by the "business judgment
21 rule." Balotti & Finkelstein, *supra*, at § 4.19. The business
22 judgment rule is a "presumption that in making a business decision the
23 directors of a corporation acted on an informed basis, in good faith
24 and in the honest belief that the action taken is in the best
25 interests of the company." *Id.* at § 4.19 fn. 1090, citing *Aronson v.*
26 *Lewis*, 473 A.2d 805, 812 (Del. 1984); see also *Citron v. Fairchild*
27 *Camera & Instrument Corp.*, 569 A.2d 53, 64 (Del. 1989) ("The
28 presumption initially attaches to a director-approved transaction

1 within a board's conferred or apparent authority in the absence of any
2 evidence of fraud, bad faith, or self-dealing in the usual sense of
3 personal profit or betterment."); *John Hancock Capital Growth Mgmt.*
4 *Inc. v. Aris Corp.*, 9920, 1990 WL 126656, at *1 (Del. Ch. Aug. 24,
5 1990). When applicable, the business decisions of the board of
6 directors "will not be disturbed if they can be attributed to any
7 rational business purpose. A court under such circumstances will not
8 substitute its own notions of what is or is not sound business
9 judgment." Balotti & Finkelstein, *supra*, § 4.19 fn. 1091, citing
10 *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720 (Del. 1971); see also
11 *Brazen v. Bell Atl. Corp.*, 695 A.2d 43, 49 (Del. 1997) ("Courts give
12 deference to directors' decisions reached by a proper process, and do
13 not apply an objective reasonableness test in such a case to examine
14 the wisdom of the decision itself.").

15 The Delaware Court of Chancery described the business judgment
16 rule as having three elements: "a threshold review of the objective
17 financial interests of the board whose decision is under attack (i.e.,
18 independence), a review of the board's subjective motivation (i.e.,
19 good faith), and an objective review of the process by which it
20 reached the decision under review (i.e., due care)." *Delaware Law of*
21 *Corporations*, Fiduciary Duties § 4.19 fn. 1091, citing *In re RJR*
22 *Nabisco, Inc. S'holders Litig.*, No. 10389, 1989 WL 7036, at *1156
23 (Del. Ch. Jan. 31, 1989).

24 The business judgment rule operates as a "procedural guide" and
25 "a substantive rule of law." *Citron v. Fairchild Camera & Instrument*
26 *Corp.*, 569 A.2d 53, 64 (Del. 1989). Among its procedural aspects is
27 the presumption that the directors have acted properly, placing the
28 burden of proof on the plaintiff. "The burden falls upon the

1 proponent of a claim to rebut the presumption by introducing evidence
2 either of director self-interest, if not self-dealing, or that the
3 directors either lacked good faith or failed to exercise due care."
4 *Id.*

5 Finally, only limited persons have standing to prosecute a claim
6 for breach of fiduciary duty against a corporate director.
7 Ordinarily, those rights belong exclusively to the corporation and its
8 shareholders. *Guth v. Loft*, 5 A.2d 503, 510 (Del.1939); *Malone v.*
9 *Brincat*, 722 A.2d 5, 10 (Del.1998). Shareholders may act only
10 derivatively. As the Supreme Court of Delaware explained:

11 It is well established that the directors owe their
12 fiduciary obligations to the corporation and its
13 shareholders. While shareholders rely on directors acting
14 as fiduciaries to protect their interests, creditors are
15 afforded protection through contractual agreements, fraud
16 and fraudulent conveyance law, implied covenants of good
17 faith and fair dealing, bankruptcy law, general commercial
law and other sources of creditor rights. Delaware courts
have traditionally been reluctant to expand existing
fiduciary duties. Accordingly, "the general rule is that
directors do not owe creditors duties beyond the relevant
contractual terms."

18 *N. Am. Catholic Educ. Programming Found., Inc. v. Gheewalla*, 930 A.2d
19 92, 99 (Del. 2007). As a consequence, the directors of solvent
20 corporations are wholly protected against actions, direct or indirect,
21 by aggrieved creditors.

22 Corporations that are not yet insolvent but are in financial
23 jeopardy are referred to as "within the zone of insolvency." Like
24 solvent corporations, creditors hold no right of action for breach of
25 fiduciary duties against directors for corporations operating within
26 the zone of insolvency. *Id.*; *Quadrant Structured Products Co., Ltd.*
27 *v. Vertin*, 115 A.3d 535, 546 (Del. Ch. 2015).

28 By contrast, the creditors of "insolvent" corporations do hold a

1 derivative action against the corporation and, by extension, its
2 directors, under the "so-called trust fund doctrine." Balotti &
3 Finkelstein, *supra*, at § 5.2. Insolvency is measured on the date the
4 action is filed, *Quadrant Structured Products*, 115 A.3d at 543-556,
5 and will be adjudged by the balance sheet test ("deficiency of assets
6 below liabilities"), *Gheewalla*, 930 A.2d at 98, citing *Production Res.*
7 *Group v. NCT Group, Inc.*, 863 A.2d 772, 782 (Del.Ch. 2004); *Geyer v.*
8 *Ingersoll Publ'ns Co.*, 621 A.2d 784, 789 (Del.Ch. 1992); *McDonald v.*
9 *Williams*, 174 U.S. 397, 403 (1899), or by the cash flow test ("an
10 inability to meet maturing obligations as they fall due in the
11 ordinary course of business"). *Gheewalla*, 930 A.2d at 98, citing
12 *Production Res. Group v. NCT Group, Inc.*, 863 A.2d 772, 782 (Del. Ch.
13 2004).

14 A creditor's right to pursue an action against directors is best
15 described by the Delaware Supreme Court:

16 When a corporation is solvent, those duties may be enforced
17 by its shareholders, who have standing to bring derivative
18 actions on behalf of the corporation because they are the
19 ultimate beneficiaries of the corporation's growth and
20 increased value. *When a corporation is insolvent, however,*
21 *its creditors take the place of the shareholders as the*
22 *residual beneficiaries of any increase in value.*

23 Consequently, the creditors of an insolvent corporation
24 have standing to maintain derivative claims against
25 directors on behalf of the corporation for breaches of
26 fiduciary duties. The corporation's insolvency makes the
27 creditors the principal constituency injured by any
28 fiduciary breaches that diminish the firm's value.
Therefore, equitable considerations give creditors standing
to pursue derivative claims against the directors of an
insolvent corporation. Individual creditors of an insolvent
corporation have the same incentive to pursue valid
derivative claims on its behalf that shareholders have when
the corporation is solvent.

27 *Gheewalla*, 930 A.2d at 98 (emphasis added); see also *Quadrant*
28 *Structured Products*, 115 A.3d at 546-47 ("[Directors] continue to owe

1 fiduciary duties to the corporation for the benefit of all of its
2 residual claimants, a category which now includes creditors.").

3 **3. Plausibility**

4 As applied here, plausibility requires trustee Husted to make a
5 three-part factual showing: standing, i.e., that ECS was insolvent at
6 the time the adversary proceeding was commenced; inapplicability of
7 the business judgment rule, i.e., fraud, bad faith or self-dealing;
8 and breach of fiduciary duty. She has done so.

9 Plaintiff Husted has standing to assert derivative claims for
10 breach of fiduciary duties. As of the date of Husted's adversary
11 proceeding ECS was a Chapter 7 debtor and was not paying its bills in
12 the ordinary course. *Geyer v. Ingersoll Publication Co.*, 621 A.2d 784
13 789 (Del. Ch. 1991) (cash flow test); 11 U.S.C. §§ 704(a)(9), 726;
14 Fed. R. Bankr. P. 5009(a) (contemplating distribution after full
15 administration of the case). Moreover, courts have long recognized
16 the authority of Chapter 7 trustees to assert derivative claims for
17 breach of fiduciary duty against members of the board of directors of
18 a corporate debtor. *Bovay v. H.M. Byllesby & Co.*, 38 A.2d 808 (Del.
19 1944); *Trenwick Am. Litig. Trust v. Ernst & Young, L.L.P.*, 906 A.2d
20 168, 189 (Del. Ch. 2011) (litigation trust); *In re USDigital, Inc.*,
21 443 B.R. 22, 43 (Bankr. D. Del. 2011) (Chapter 7 trustee); *In re Scott*
22 *Acquisition Corp.*, 344 B.R. 283, 290 (Bankr. D. Del. 2006). As a
23 result, Husted has standing to pursue this claim.

24 The business judgment rule does not bar this action. While that
25 rule assumes appropriate conduct by the board of directors, that
26 presumption may be rebutted by pleading facts that show self-interest,
27 self-dealing, lack of good faith or the failure of due care. *Citron*
28 *v. Fairchild Camera & Instrument Corp.*, 569 A.2d 53, 64 (Del. 1989).

1 Here, the trustee has plead facts from which the inference of self-
2 dealing or the lack of good faith might be inferred. Those facts
3 include: increased rental payments to the Insider Entity Defendants;
4 the cessation of operations to reduce cash flow and receivables, an
5 expressed desire to “put the screws to Summit[Bridge]”; and the
6 failure to disclose to creditors the Taggarts’ ownership of Butch and
7 Sundance, LLC, the proposed post-petition lender. As a result, the
8 trustee has plead around the business judgment rule.

9 Finally, plaintiff Husted has plead plausible claims for breach
10 of the duty of care and of loyalty. Fed R. Civ. P. 10(b) (allowing
11 aggregating theories in a single count), *incorporated by* Fed. Bankr.
12 P. 7010.

13 Husted’s first theory is that Taggarts engaged in bad faith acts
14 that deepened ECS’s insolvency. Delaware law does not recognize “an
15 independent cause of action for deepening insolvency.” *Trenwick Am.*
16 *Litig. Trust v. Ernst & Young, L.L.P.*, 906 A.2d 168, 205 (2006);
17 *Quadrant Structured Products Co., Ltd.*, 115 A.3d at 547 (“Directors
18 cannot be held liable for continuing to operate an insolvent entity in
19 the good faith belief that they may achieve profitability...”). But
20 Delaware does require that a director’s actions be undertaken in “good
21 faith.” *Id.* A court may infer the lack of good faith where a
22 director “intentionally acts with a purpose other than advancing the
23 best interests of the corporation.” *In re Walt Disney Co. Derivative*
24 *Litig.*, 906 A.2d 27, 67 (Del. 2006). Moreover, *Trenwick* specifically
25 reserved to the corporation--and by extension, creditors--breach of
26 fiduciary duty claims where the board of directors acted in a way that
27 made the corporation’s situation more dire:

28 The rejection of an independent cause of action for

1 deepening insolvency does not absolve directors of
2 insolvent corporations of responsibility. Rather, it remits
3 plaintiffs to the contents of their traditional toolkit,
which contains, among other things, causes of action for
breach of fiduciary duty and for fraud.

4 *Trenwick*, 906 A.2d at 205.

5 Here, the plaintiff has plead facts from which a plausible claim
6 for breach of the fiduciary duty of due care that resulted in ECS's
7 still deeper insolvency. Decisions by the board of directors are
8 reviewed under a "gross negligence" standard. *Stone v. Ritter*, 911
9 A.2d 362, 369 (Del. 2006); *Brehm v. Eisner*, 746 A.2d 244, 259 (Del.
10 2000). Gross negligence means "reckless indifference to or a
11 deliberate disregard of the whole body of stockholders [here,
12 creditors] or actions that are without of the bounds of reason."
13 *Tomczak v. Morton Thiokol*, No. 7861, 1990 WL 42607, at *12 (Del. Ch.
14 April 5, 1990). The Taggarts deliberately weakened ECS's financial
15 condition to force concessions from SummitBridge. Two inferences are
16 possible. One inference is that the Taggarts' actions designed to
17 tame an unruly secured creditor were, in fact, in the best interests
18 of unsecured creditors. The other inference was the weakening
19 strategy is employed without due consideration of its impact on
20 unsecured creditors. Given the use of a counterintuitive strategy,
21 i.e., weakening an already frail corporation, and self-dealing,
22 *Trenwick Am. Litig. Trust*, 906 A.2d at 205 (requiring good faith in
23 the exercise of due diligence), the court infers reckless indifference
24 to the interests of unsecured creditors. *Morton Thiokol*, 1990 WL
25 42607, at *12. Moreover, in deciding a Rule 12(b)(6) motion the court
26 should not weigh competing inferences in deciding the plausibility of
27 well-plead facts, unless one inference is so strong as to constitute
28 an obvious alternative explanation. *Marcus & Millichap Co.*, 751 F.3d

1 at 996. In light of actions specifically contrary to the corporate
2 best interests that benefitted the Taggarts personally, the court will
3 not find the existence of an obvious alternative explanation.

4 Husted's second theory is that the Taggarts' breached their duty
5 of loyalty by attempting to improve their position as equity holders
6 vis-à-vis unsecured creditors. In this instance, unsecured creditors
7 were harmed by decreasing the availability of unencumbered assets
8 available to pay unsecured creditors, Emergency Ex Parte Mot. for
9 Order Authorizing Post-Petition Financing 2:28-4:6, *In re ECS*
10 *Refining, Inc.*, No. 2018-22453 (Bankr. E.D. Cal. April 24, 2018), ECF
11 No. 12, and by increasing the pool of unsecured creditors by \$21.69
12 million, 11 U.S.C. § 506(a), (d).

13 Butch and Sundance, LLC's lien survives dismissal of the case.
14 11 U.S.C. § 349(b); see also, *Production Credit Ass'n of the Midlands*
15 *v. Farm & Town Indus., Inc.*, 518 N.W.2d 339, 343 (Iowa 1994). It also
16 survives conversion to Chapter 7 and is not assailable by the Chapter
17 7 trustee. 11 U.S.C. §§ 348(d), 364(c), (e), 549(a) (limiting the
18 trustee's ability to attack post-petition transactions); *Cf. Sapir v.*
19 *C.P.Q. Colorchrome Corp. (In re Photo Promotion Assoc., Inc.)*, 881
20 F.2d 6, 8 (2nd Cir. 1989) (trustee entitled to recover under § 549(a)
21 funds paid by the debtor to a trade creditor where § 364(c)
22 authorization not obtained); *Terry Oilfield Supply Co., Inc. v.*
23 *American Security Bank, N.A.*, 195 B.R. 66, 72 (S.D. TX 1996)
24 (exception transactions approved under §§ 303(f) and 542(c), post-
25 petition transactions approved by the court are not subject to §549(a)
26 avoidance). It also gave Butch & Sundance, LLC, a better right to
27 ECS's assets, at least to the extent of the lien. *Hartford*
28 *Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 4-5

1 (2000) (wholly encumbered assets may not be used to pay administrative
2 claims); *In re KVN Corp., Inc.*, 514 BR 1, 5-6 (9th Cir. BAP 2014)
3 (fully encumbered assets should be abandoned); *In re Traverse*, 753
4 F.3d 19, 25-26 (1st Cir. 2014). If the case did not dismiss or
5 convert but continued in Chapter 11 it reduced the minimum amount due
6 unsecured creditors. 11 U.S.C. § 1129(a)(7)(A)(ii) (best interests
7 test).

8 Moreover, if the Chapter 11 continued to contested plan
9 confirmation the Taggarts' actions have increased their ability to
10 cramdown the plan at the expense of unsecured creditors. The primary
11 impediment to nonconsensual plan confirmation is the absolute priority
12 rule. *Northern Pac. R.R. Co. v. Boyd*, 228 U.S. 482, 504 (1913);
13 *Caplin v. Marine Midland Grace Trust Co. of New York*, 406, U.S. 416,
14 436 fn. 2 (1972) (Douglas, J. dissenting). It is codified at 11
15 U.S.C. § 1129(b) and provides that the court may confirm a plan over
16 objection of a creditor if "the plan does not discriminate unfairly,
17 and is fair and equitable, with respect to each class of claims or
18 interests that is impaired under, and has not accepted, the plan."
19 "[D]iscriminate unfairly" is a "horizontal comparative assessment"
20 that determines whether other similarly situated creditors are
21 inappropriately advantaged vis-à-vis the nonaccepting class; "fair and
22 equitable" is a vertical measurement that "regulates priority among
23 classes of creditors having higher and lower priority for payment. *In*
24 *re Tribune Co.*, 972 F.3d 228, 232 (3d Cir. 2020), quoting Bruce A.
25 Markell, *A New Perspective on Unfair Discrimination in Chapter 11*, 72
26 Am. Bankr. L.J. 227, 227-28 (1998). Fair and equitable means that all
27 senior classes of creditors, e.g., unsecured creditors, must be paid
28 in full before any junior class may receive or retain any property

1 under the plan. *Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 202
2 (1988); *Carson Nugget, Inc. v. Green (In re Green)*, 98 B.R. 981, 982
3 (9th Cir. BAP 1989).

4 The "new value" rule is an exception to the absolute priority
5 rule. It allows equity holders to retain their interest to the extent
6 that they contribute new value to the estate, even though senior
7 classes are not paid in full. *In re Bonner Mall P'ship*, 2 F.3d 899,
8 906 (9th Cir. 1993), *abrogated on other grounds by Bullard v. Blue*
9 *Hills Bank*, 575 U.S. 496 (2015); *In re Coltex Loop Central Three*
10 *Partners, L.P.*, 138 F.3d 39, 46 (2nd Cir. 1998)); *In re U.S. Truck*
11 *Co., Inc.*, 800 F.2d 581, 588, 590 (6th Cir. 1986). The new value
12 contributed must be reasonably equivalent to the interest received or
13 the property retained. *In re Ambanc La Mesa Ltd. P'ship*, 115 F.3d
14 650, 654-656 (9th Cir. 1997). That value, in this case ECS's stock,
15 is generally determined by the "going concern" value, *Consolidated*
16 *Rock Products Co. v. Du Bois*, 312 U.S. 510, 525-26 (1941), and is
17 based on the estimated future earnings discounted to present value.
18 *In re Muskegon Motor Specialties*, 366 F.2d 522, 525 (6th Cir. 1966).
19 The simple point is that reducing pre-petition earnings and
20 profitability, even in the few months before filing, will reduce the
21 new value payment necessary to force non-consensual plan confirmation.

22 These facts give rise to an inference that the Taggarts
23 intentionally sought to advance a purpose other than the best
24 interests of "all residual claimants, a category which now includes
25 creditors". *Quadrant Structed Products Co., Ltd. v. Vertin* 115 A.3d
26 at 546-47. As a result, trustee Husted has stated a plausible claim
27 for breach of fiduciary duty, i.e., due care and loyalty.
28

1 **4. Full protection Under 8 Delaware Code § 141(e)**

2 Delaware law provides directors who rely on appropriate
3 professional advice a safe harbor.

4 A member of the board of directors, or a member of any
5 committee designated by the board of directors, shall, in
6 the performance of such member's duties, be fully protected
7 in *relying in good faith* upon the records of the
8 corporation and *upon such information, opinions, reports or*
9 *statements* presented to the corporation by any of the
10 corporation's officers or employees, or committees of the
11 board of directors, or by any other person *as to matters*
12 *the member reasonably believes are within such other*
13 *person's professional or expert competence and who has been*
14 *selected with reasonable care by or on behalf of the*
15 *corporation.*

16 8 Del. C. § 141(e) (emphasis added).

17 As a rule, the protections of § 141(e) are an affirmative
18 defense. *Manzo v. Rite Aid Corp.*, 2002 WL 31926606, at *3 n. 7 (Del.
19 Ch. Dec. 19, 2002); *Ogus v. SportTechie, Inc.*, 2020 WL 502996, at *14
20 (Del. Ch. January 31, 2020). Generally, an affirmative defense cannot
21 be raised by a Rule 12(b)(6) motion. *Xechem, Inc. v. Bristol-Myers*
22 *Squibb Co.*, 372 F.3d 899, 901 (7th Cir. 2004). But where the
23 allegations of the complaint disclose a bar to the action, i.e.,
24 affirmative defense, the issue may be raised by motion. *Weisbuch v.*
25 *County of Los Angeles*, 119 F.3d 778, 783 fn. 1 (9th Cir. 1997);
26 *Hensley Mfg. v. ProPride, Inc.*, 579 F.3d 603, 613 (6th Cir. 2009); see
27 also, *Brehm v. Eisner*, 746 A.2d 244, 262 (Del. 2000) (applying the
28 rule to 8 Del. C. § 141(e)).

 Here, the facts give rise to an inference that Taggarts' actions
fall outside the scope of § 141(e). At least an inference of the lack
of good faith reliance exists. First Am. Compl. 14:22-27 ("a great
way to put the screws to [SummitBridge]"), 16:13-16 (cessation of
operations). The complaint contains no allegations that the

1 Professional Advisors were "selected with reasonable care." Nor is
2 there indication that the Professional Advisors were acting "by or on
3 behalf of the corporation," as opposed to Taggarts personally. As a
4 result, § 141(e) is not a basis to dismiss the First Amended
5 Complaint.

6 **5. Exculpatory clauses in the Certificate of**
7 **Incorporation**

8 Delaware law allows a corporation's Certificate of Incorporation
9 to exculpate directors from a broad spectrum of liabilities.

10 In addition to the matters required to be set forth in the
11 certificate of incorporation by subsection (a) of this
12 section, the certificate of incorporation may also contain
13 any or all of the following matters:

14 ...

15 A provision *eliminating or limiting the personal liability*
16 *of a director* to the corporation or its stockholders for
17 monetary damages for *breach of fiduciary duty* as a
18 director, provided that such provision shall *not eliminate*
19 *or limit the liability* of a director: (i) For any *breach of*
20 *the director's duty of loyalty* to the corporation or its
21 stockholders; (ii) *for acts or omissions not in good faith*
22 or which involve intentional misconduct or a knowing
23 violation of law; (iii) under § 174 of this title; or (iv)
24 *for any transaction from which the director derived an*
25 *improper personal benefit.*

26 Del. Code Ann. tit. 8, § 102(b)(7) (2020) (emphasis added).

27 ECS's Certificate of Incorporation provides:

28 To the fullest extent permitted by the [General Corporation
Law of Delaware] as the same exists or may hereafter be
amended, a director of this Corporation shall not be
personally liable to the Corporation or its stockholders
for money damages for breach of fiduciary duty as a
director, provided that this Article shall not eliminate or
limit the liability of a director for (i) any breach of the
director's duty of loyalty to the Corporation or its
stockholders; (ii) acts or omissions not in good faith or
which involve intentional misconduct or a knowing violation
of the law, (iii) under section 174 of the [General
Corporation Law of Delaware], or (iv) for any transaction
from which the director derived an improper personal

1 benefit.

2 Certificate of Incorporation, Ninth Article.⁸

3 Plaintiff Husted's First Amended Complaint pleads plausible
4 claims for (1) breach of the duty of due care, i.e., bad faith
5 deepening insolvency; and (2) breach of the duty of loyalty, i.e.,
6 self-dealing arising from Taggarts' efforts to better their personal
7 interest in the Chapter 11 process at the expense of creditors. For
8 the purposes of pleading, the former falls within the lack of good
9 faith and/or improper personal benefit exceptions,
10 § 102(b)(7)(ii),(iv); the latter is excepted as under the duty of
11 loyalty exception, § 1207(b)(7)(ii).

12 As to the first count, the motion will be denied.

13 **B. Second Cause of Action: Corporate Waste**

14 Plaintiff Husted alleges that "[t]he excessive [insider]
15 commercial leases...unjustifiably high-cost payroll, and management
16 decisions leading to cash consumption, inventory segregation, and the
17 suspension of processing inventory" gives rise to a cause of action
18 for corporate waste against the Taggarts. First Am. Compl. 25:12-17.

19 Like actions against directors for breach of fiduciary duty,
20 actions for waste are governed by the internal affairs doctrine and
21 the law of the state of incorporation provides the rule of decision.
22 *In re Verisign, Inc., Derivative Litig.*, 531 F. Supp. 2d 1173, 1215
23 (N.D. Cal. 2007) (finding claims for waste as implicating the Internal
24 Affairs Doctrine); *Symington v. Guillen*, No. LACV1509809JAKPJWX, 2016
25 WL 7486603, at *8 (C.D. Cal. June 30, 2016). As a result, Delaware

26
27 ⁸ For the purposes of this motion the court assumes that ECS's
28 Certificate of Incorporation is a document incorporated by reference
in the complaint. *United States v. Ritchie*, 342 F.3d 903, 908 (9th
Cir. 2003).

1 law provides the rule of decision.

2 Moreover, in limited circumstances, Delaware law does recognize a
3 cause of action for corporate waste. Any action for waste will lie
4 where the plaintiff proves "that the exchange was 'so one sided that
5 no [businessperson] of ordinary, sound judgment could conclude that
6 the corporation has received adequate consideration." *In re Walt*
7 *Disney Co. Derivative Litig.*, 906 A.2d 27, 74 (Del. 2006). Waste will
8 only be found in the "rare, 'unconscionable case where directors
9 irrationally squander or give away corporate assets." *Id.* This
10 onerous standard for waste is a corollary of the proposition that
11 where business judgment presumptions are applicable, the board's
12 decision will be upheld unless it cannot be "attributed to any
13 rational business purpose." *Id.*

14 Moreover, Delaware courts have thoughtfully defined the contours
15 of corporate waste:

16 Roughly, a waste entails an exchange of corporate assets
17 for consideration so disproportionately small as to lie
18 beyond the range at which any reasonable person might be
19 willing to trade. Most often the claim is associated with a
20 transfer of corporate assets that serves no corporate
21 purpose; or for which no consideration at all is received.
22 Such a transfer is in effect a gift. *If, however, there is
any substantial consideration received by the corporation,
and if there is a good faith judgment that in the
circumstances the transaction is worthwhile, there should
be no finding of waste,* even if the fact finder would
conclude ex post that the transaction was unreasonably
risky....

23 *Brehm v. Eisner*, 746 A.2d 244, 263 (Del. 2000) (emphasis added).

24 As the Supreme Court of Delaware has articulated the doctrine of
25 waste, "a corporate waste claim must fail if 'there is any substantial
26 consideration received by the corporation and...there is a good faith
27 judgment that in the circumstances the transaction is worthwhile'."
28 *White v. Panic*, 783 A.2d 543, 554 (Del. 2001). Substantial

1 consideration and good faith must each exist to bring the directors'
2 actions within the business judgment rule and, therefore, bar an
3 action for waste. *Id.*

4 Plaintiff Husted has stated a plausible claim for waste. The
5 absence of substantial consideration received by the corporation and
6 the lack of good faith may form the basis of an action for waste. The
7 allegations of intentional weakening and self-dealing, i.e., Butch and
8 Sundance, LLC, loan sans full disclosure properly make plausible a
9 finding of lack of substantial consideration and/or lack of good
10 faith. As a result, the three part scheme aimed at SummitBridge also
11 provides sufficient inferences to support an action for waste,
12 sufficient to defeat a Rule 12(b)(6) motion.

13 As to the second count, the motion will be denied.

14 **C. Third Cause of Action: Preferential Transfers**

15 Plaintiff Husted asserts a preference action against All Metals,
16 Inc.

17 Preferential transfers exist as creatures of statute:

18 Except as provided in subsections (c) and (i) of this
19 section, the trustee may, *based on reasonable due diligence*
20 *in the circumstances of the case and taking into account a*
21 *party's known or reasonably knowable affirmative defenses*
22 *under subsection (c),* avoid any transfer of an interest of
23 the debtor in property--

24 (1) to or for the benefit of a creditor;

25 (2) for or on account of *an antecedent debt* owed by the
26 debtor before such transfer was made;

27 (3) made while the debtor was insolvent;

28 (4) made--

(A) on or within 90 days before the date of the filing
of the petition; or

(B) between ninety days and one year before the date of
the filing of the petition, if such creditor at the

1 time of such transfer was an insider; and

2 (5) that enables such creditor to receive more than such
3 creditor would receive if--

4 (A) the case were a case under chapter 7 of this title;

5 (B) the transfer had not been made; and

6 (C) such creditor received payment of such debt to the
7 extent provided by the provisions of this title.

8 11 U.S.C. § 547(b) (emphasis added).

9 Plaintiff Husted's third count predominantly pleads legal
10 conclusions. But it does include the following facts: (1) All Metals,
11 Inc., leased space to ECS "for its recycling operations," First Am.
12 Compl. 5:1-4;⁹ (2) All Metals, Inc., was an insider, *Id.*; (3) within
13 one year before the bankruptcy ECS made payments to All Metals on
14 account of "invoice[s]," *Id.* 26:11-16; and (4) those payments were
15 made on the following dates and in the following amounts, (A) August
16 31, 2017-\$400,000; (B) September 19, 2017-\$300,000; and (C) November
17 28, 2017-\$490,000. Exhibits to First Am. Compl. 8, ECF No. 30.

18 **1. Due diligence**

19 A conditions precedent is a "statutory prerequisite[]" to
20 litigation." 5 Arthur R. Miller et al., *Federal Practice and*
21 *Procedure* § 1303 (4th ed.). Section 547(b) now requires that the
22 trustee satisfy a condition precedent, i.e., reasonable due diligence
23 and consideration of known or knowable affirmative defenses. Small
24 Business Reorganization Act of 2019, Pub. L. No. 116-54 § 3(a),
25 effective February 19, 2020. "[T]he trustee may, based on reasonable
26 due diligence in the circumstances of the case and taking into account
27 a party's known or reasonably knowable affirmative defenses under

28 ⁹ The court cannot ascertain whether the payments were on account of
rent, First Am. Compl. 26:5-7, 14-16, or goods and/or services
rendered, *Id.* at 26:5-7.

1 subsection (c), avoid any transfer....” 11 U.S.C. § 547(b). This
2 condition precedent has three discrete subparts, which the trustee, or
3 someone acting on her behalf, must undertake prior to the commencement
4 of a preference action: (1) reasonable due diligence under “the
5 circumstances of the case”; (2) consideration as to whether a prima
6 facie case for a preference action may be stated; and (3) review of
7 the known or “reasonably knowable” affirmative defenses that the
8 prospective defendant may interpose. 11 U.S.C. § 547(b).

9 This court believes that this condition precedent, i.e., due
10 diligence and consideration of affirmative defenses, is an element of
11 the trustee’s prima facie case. 11 U.S.C. § 547. As a rule,
12 conditions precedent, or the lack thereof, may defeat jurisdiction,
13 *Henderson ex rel. Henderson v. Shinseki*, 562 U.S. 428, 436 (2011) (the
14 failure of a condition precedent only deprives federal courts of
15 jurisdiction where there is “clear indication that Congress wanted the
16 rule to be jurisdictional”); see also *U.S. E.E.O.C. v. Farmers Ins.*
17 *Co.*, 24 F.Supp.3d 956, 962–63 (E.D. Cal. 2014); serve as an element of
18 the prima facie case, *Walton v. Nalco Chemical Co.*, 272 F.3d 13, 21 n.
19 11 (1st Cir. 2001) (conditions precedents that are elements are those
20 that preclude a finding for the plaintiff); *U.S. ex rel. Krol v. Arch*
21 *Ins. Co.*, 46 F.Supp.3d 347, 356 (S.D. NY 2014) (exhaustion of
22 administrative remedies under Miller Act treated as an element);
23 *Pacific Dental Services, LLC v. Homeland Ins. Co. of New York*, 2013 WL
24 3776337, *4 (C.D. Cal. 2013) (contract claim); or constitute an
25 affirmative defense, *Albino v. Baca*, 747 F.3d 1162, 1168–69 (9th Cir.
26 2014). The effect of § 547(b)’s due diligence requirement has not
27 been resolved. *Harker v. Cummings (In re GYPC, Inc.)*, 2020 Bankr.
28 LEXIS 2384, *25 (Bankr. S.D. Ohio, August 4, 2020) (denying Rule

1 12(b)(6) motion without analysis); 5 *Collier on Bankruptcy* at ¶
2 547.02A (describing due diligence as an element or a condition
3 precedent).

4 The Supreme Court has provided guidance in determining whether a
5 condition precedent is an element or an affirmative defense. In *Jones*
6 *v. Bock*, 549 U.S. 199, 212-217 (2007), the court considered whether
7 the prison grievance procedures contained in the Prison Litigation
8 Reform Act of 1995 are “a pleading requirement the prisoner must
9 satisfy in his complaint or an affirmative defense the defendant must
10 plead and prove.” As the court explained, prison litigation
11 “account[s] for an outsized share of filings in federal district
12 courts.” Often, incarcerated persons bring actions under 42 U.S.C. §
13 1983 for wrongs, perceived or actual, arising from the conditions
14 associated with their confinement. In response, Congress enacted the
15 Prison Reform Act of 1995. 42 U.S.C. § 1997e. Among the reforms
16 contained in that statute were mandatory early judicial screening of
17 prisoner complaints and a requirement that incarcerated persons
18 exhaust prison grievance procedures before filing suit. The
19 requirement of exhausting grievance procedures states:

20 No action shall be brought with respect to prison
21 conditions under section 1983 or any other Federal law, by
22 a prisoner confined in any jail, prison or other
23 correctional facility until such administrative remedies as
24 are available are exhausted.

25 42 U.S.C. § 1997e(a).

26 The Prison Reform Litigation Act also gave courts sua sponte
27 powers to dismiss prisoner cases in some circumstances:

28 The court shall *on its own motion* or on the motion of a
party *dismiss any action* brought with respect to prison
conditions under section 1983 of this title, or any other
Federal law, by a prisoner confined in any jail, prison, or
other correctional facility *if the court is satisfied that*

1 *the action is frivolous, malicious, fails to state a claim*
2 *upon which relief can be granted, or seeks monetary relief*
3 *from a defendant who is immune from such relief.*

4 42 U.S.C. § 1997e(c)(1) (emphasis added).

5 As the Supreme Court articulated the issue before it:

6 There is no question that exhaustion is mandatory under the
7 [Prison Litigation Reform Act] and that unexhausted claims
8 cannot be brought in court. *What is less clear is whether*
9 *it falls to the prisoner to plead and demonstrate*
10 *exhaustion in the complaint, or to the defendant to raise*
11 *lack of exhaustion as an affirmative defense.*

12 *Jones*, 549 U.S. at 211 (emphasis added) (citations omitted).

13 A circuit split developed with respect to the pleading requirements
14 applicable to the Prison Litigation Reform Act. The Sixth Circuit
15 “adopted several procedural rules designed to implement this
16 exhaustion requirement and facilitate early judicial screening. These
17 rules require a prisoner to allege and demonstrate exhaustion in this
18 complaint...and require courts to dismiss the entire action” if
19 exhaustion had not been fully demonstrated in the complaint. Other
20 circuits declined to adopt those rules and treated the failure to
21 exhaust prison grievances as an affirmative defense that must be
22 raised in the answer, Fed. R. Civ. P. 8(c). The Supreme Court granted
23 certiorari. In resolving the issue, the Supreme Court noted the
24 Prison Reform Act of 1995 was “silent on the issue whether exhaustion
25 must be pleaded by the plaintiff or is an affirmative defense.” In
26 deciding whether exhaustion of administrative remedies was, in fact,
27 an affirmative defense, the Supreme Court focused on three things.
28 First, it noted that “the [Prison Litigation Reform Act] itself is not
29 a source of a prisoner’s claim; claims covered by the [Prison
30 Litigation Reform Act] are typically brought under 42 U.S.C. § 1983,
31 which does not require exhaustion at all.” Second, the parties to the

1 action did not dispute characterization of the grievance process as an
2 affirmative defense. Third, historically, exhaustion of
3 administrative remedies has been regarded as an affirmative defense.
4 Finally, the court observed,

5 The [Prison Litigation Reform Act] dealt extensively with
6 the subject of exhaustion, see 42 U.S.C. §§ 1997e(a),
7 (c)(2), but is silent on the issue whether exhaustion must
8 be pleaded by the plaintiff or is an affirmative defense.
9 This is strong evidence that the usual practice should be
10 followed, and the usual practice under the Federal Rules is
11 to regard exhaustion as an affirmative defense.

12 *Jones*, 549 at 212.

13 Once the court concluded that exhaustion of administrative remedies
14 was an affirmative defense, the Supreme Court had little difficulty in
15 deciding that a prisoner need not plead satisfaction of the condition
16 precedent to avoid the sua sponte dismissal provisions of the Prison
17 Litigation Reform Act. 42 U.S.C. § 1997e(c).

18 *Jones* provides a roadmap for consideration of the Small Business
19 Reorganization Act's amendments to § 547(b). Like the Prison
20 Litigation Reform Act, amended § 547(b) is silent on whether
21 satisfaction of the condition precedent is an element or an
22 affirmative defense and on whether satisfaction is a pleading
23 requirement.

24 But that is where the Small Business Reorganization Act of 2019
25 amendments to § 547(b) and the Prison Litigation Reform Act of 1995
26 part company. At least two significant differences exist. First, §
27 547(b) is the source of the trustee's substantive rights. It defines
28 those transactions that the trustee may avoid as preferential.
29 *Waldschmidt v. Ranier (In re Fulghum Construction Corp.)*, 706 F.2d 171
30 (6th Cir. 1983) ("[p]referential transfers which may be avoided by the
31 trustee are defined in 11 U.S.C. § 547(b)..."); *Levit v. Ingersoll*

1 *Rand Financial Corp.*, 874 F.2d 1186, 1194 (7th Cir. 1989) (“[s]ection
2 547(b) defines which transfers are ‘avoidable’”). When the
3 legislature elects to define a term, that definition is binding on the
4 courts. *Sturgeon v. Frost*, 139 S.Ct. 1066 (2019); *Digital Realty*
5 *Trust, Inc. v. Somers*, 138 S.Ct. 767 (2018); *United States v. Ron Pair*
6 *Enters., Inc.*, 489 U.S. 235, 242 (1989) (plain language of a statute
7 controls). In contrast, the Prison Litigation Reform Act merely
8 provided a procedural overlay to existing statutory rights, e.g., 42
9 U.S.C. § 1983, and applies to any action “with respect to prison
10 conditions under section 1983 of this title, or any other Federal
11 law.” 42 U.S.C. § 1997e(a). In part, *Jones* based its holding on the
12 fact that “[t]he [Prison Litigation Reform Act] itself is not a source
13 of a prisoner’s claims; claims covered by the [Prison Litigation
14 Reform Act] are typically brought under 42 U.S.C. § 1983, which does
15 not require exhaustion at all.” *Jones*, 549 U.S. at 212. As a result,
16 a legislative decision to include due diligence in the definition of
17 avoidable preferences undercuts one of the central pillars articulated
18 for the holding in *Jones*.

19 Second, unlike the Prison Litigation Reform Act (which is silent
20 on the issue), § 547 expressly requires that the trustee affirmatively
21 prove due diligence. Ordinarily, facts that the plaintiff must prove
22 at trial are elements of the prima facie case. *Flav-O-Rich Food*
23 *Service, Inc. v. Rawson Food Service, Inc. (In re Rawson Food Services*
24 *Inc.)*, 846 F.2d 1343 (11th Cir. 1988) (construing 11 U.S.C. § 546(c));
25 *Nayab v. Capital One Bank (USA), N.A.*, 942 F.3d 480, 493 (9th Cir.
26 2019) (“who bears the ultimate burden of proof and/or persuasion is
27 indicative of who bears the initial burden of pleading”); 5 Arthur R.
28 Miller et al., *Federal Practice and Procedure* § 1271 n. 23 (3d ed.).

1 Simply put, if the plaintiff bears the burden of proof of the fact at
2 trial, in most instances it is an element; if the defendant bears the
3 burden of proof at trial it is probably an affirmative defense.

4 Moreover, “[a] defense which demonstrates that plaintiff has not met
5 its burden of proof is not an affirmative defense.” *Zivkovic v. S.*
6 *California Edison Co.*, 302 F.3d 1080, 1088 (9th Cir. 2002).

7 Here, § 547(b) defines avoidable preferences; in contrast §
8 547(c) offers preference defendants nine affirmative defenses with
9 which they may resist the trustee’s effort to recover the offending
10 transfer. *Ensolv Co., Inc. v. Manpower, Inc. (In re Ensolv Co.,*
11 *Inc.)*, 64 B.R. 519, 521 (9th Cir. BAP 1986) (§ 547(c) is an exhaustive
12 list of affirmative defenses), *aff’d* 813 F.2d 1230 Mar. 19, 1987); *Ju*
13 *v. Liu (In re Liu)*, 611 B.R. 864, 880 (9th Cir. BAP 2020).

14 Congress has expressly allocated the burden of proof on the issue
15 of due diligence under § 547(b) to the trustee.

16 For the purposes of this section, *the trustee has the*
17 *burden of proving the avoidability of a transfer under*
18 *subsection (b) of this section*, and the creditor or party
19 in interest against whom recovery or avoidance is sought
has the burden of proving the nonavoidability of a transfer
under subsection (c) of this section.

20 11 U.S.C. § 547(g) (emphasis added).

21 Finally, the court believes that treatment of the due diligence
22 requirement as an element falls within the plain meaning rule. As a
23 consequence, that meaning controls unless “the literal application of
24 a statute will produce a result demonstrably at odds with the
25 intentions of its drafters.” *United States v. Ron Pair Enterprises,*
26 *Inc.*, 489 U.S. 235, 242, (1989). That is not the case here. The
27 Small Business Reorganization Act of 2019 made two changes to the
28 preference actions by: (1) adding a “reasonable due diligence”

1 requirement, 11 U.S.C. § 547(b); and (2) expanding the venue
2 protections for low dollar avoidance action defendants, 28 U.S.C. §
3 1409 (raising the dollar limit for actions that must be filed in the
4 defendant's district of residence from \$13,650 to \$25,000).
5 Legislative history does not explain the reason for these changes.
6 But a fair reading of these amendments is that Congress sought to curb
7 what it perceived as improper use of preference actions in some
8 instances. 5 *Collier on Bankruptcy* ¶ 547.02A (Alan N. Resnick & Henry
9 J. Sommer eds., 16th ed. 2020) (describing "preference mills," which
10 are law firms employed on a contingent basis, who file adversary
11 proceedings for small dollar actions in districts other than the
12 defendant's residence with little--or no--evaluation of the merits,
13 solely to force nuisance value settlements); see also American
14 Bankruptcy Institute, *Commission to Study the Reform of Chapter 11*,
15 148-151 (2014), <https://abiworld.app.box.com/s/vvircv5xv83aavl4dp4h>
16 (documenting preference action abuse, i.e., failure of merits
17 consideration before commencement of an action, and recommending
18 curative provisions, i.e., adding a due diligence requirement,
19 increasing the dollar limitation contained in the home district venue
20 provisions of 28 U.S.C. § 140(b), and requiring particularity in
21 preference pleadings). This court believes that treatment of due
22 diligence as an element of the prima facie case under § 547(b) is
23 consistent, rather than at odds, with Congressional intent.

24 Moreover, where applicable substantive law treats a condition
25 precedent as an element of the prima facie case, rather than an
26 affirmative defense, it must be plead. Fed. R. Civ. P. 9(c),
27 incorporated by Fed. R. Bankr. P. 7009; *Walton v. Nalco Chem. Co.*, 272
28 F.3d 13, 21 (1st Cir. 2001) ("Rule 9(c) governs not only contractual

1 conditions precedent, but statutory conditions precedent as well");
2 *Pacific Dental Services, LLC v. Homeland Insurance Co. of New York*,
3 2013 WL 3776337, *4 (C.D. Cal. 2013) (applying California substantive
4 law); see also, *Iqbal*, 556 U.S. at 679; *Twombly*, 550 U.S. at 556.

5 Even so, § 547(b) requires only "reasonable due diligence." The
6 standard is an objective one and is defined by a competent trustee
7 practicing before the specific jurisdiction involved. See *In re*
8 *Kayne*, 453 B.R. 372, 382 (9th Cir. 2011) (sanctioning attorney under
9 Fed. R. Bankr. 9011 for failing to perform due diligence), citing
10 *Smyth v. City of Oakland (In re Brooks-Hamilton)*, 329 B.R. 270, 283
11 (9th Cir. BAP 2005) (quoting *In re Grantham Bros.*, 922 F.2d 1438, 1441
12 (9th Cir.1991)), *aff'd in part and rev'd in part on other grounds*, 271
13 Fed. Appx. 654, 656 (9th Cir.2008).

14 Here, the plaintiff is the duly appointed Chapter 7 trustee. She
15 was appointed 18 months prior to the commencement of this adversary
16 proceeding. Absent allegations in the complaint suggesting otherwise,
17 post-petition she is deemed the custodian of ECS's regularly kept
18 records, 11 U.S.C. §§ 323, 541, 542, and she is fairly charged with
19 the knowledge of the facts that those records would reveal. The First
20 Amended Complaint does not expressly recite the efforts she undertook
21 to evaluate the merits of a prima facie case or reasonably knowable
22 affirmative defenses. Plaintiff Husted's use of pre-*Iqal/Twombly*
23 notice style pleadings and a very general nature of the allegations in
24 the First Amended Complaint suggest a lack of pre-filing due
25 diligence. Reasonable inferences do not suggest that trustee Husted
26 considered whether the debt was antecedent, 11 U.S.C. § 547(b)(2);
27 whether those transfers improved defendant's position, 11 U.S.C. §
28 547(b)(5), *Elliott v. Frontier Properties (In re Shurtleff, Inc.)*, 778

1 F.2d 1416, 1421 (9th Cir. 1985) (existing as a matter of law unless
2 case solvent); nor the inapplicability of all affirmative defenses,
3 known or reasonably knowable. 11 U.S.C. § 547(c).

4 **2. Antecedent debt**

5 Preference actions require payment on account of an antecedent
6 debt. 11 U.S.C. § 547(b)(2). An antecedent debt is one owed before
7 the transfer is actually made. *Id.* A debt is owed when one is
8 obligated by law to pay it. *Nolen v. Van Dyke Seed Co., Inc. (In re*
9 *Gold Coast Seed Co.)*, 751 F.2d 1118, 1119 (9th Cir. 1985).

10 The First Amended Complaint is unclear whether the payment was on
11 account of rent for commercial space or for goods provided and/or
12 services rendered. First Am. Compl. 26:5-7 ("goods, services and/or
13 commercial space"); see also, Exhibits to First Am. Compl. 8, ECF No.
14 30 (describing "[p]ayment of invoice"). Because the Insider Entity
15 Defendants have argued that the payment was for rent and because the
16 trustee has not resisted that characterization, the court assumes that
17 the disputed payments were for commercial space rent.

18 Current rent payments are not on account of an antecedent debt;
19 late rent payments are on account of an antecedent debt. *In re*
20 *Upstairs Gallery, Inc.*, 167 B.R. 915, 918 (9th Cir. BAP 1994); *In re*
21 *Coco*, 67 B.R. 365, 371 (Bankr. S.D. NY 1986); *In re Garrett Tool &*
22 *Engineering, Inc.*, 273 B.R. 123, 126 (E.D. MI 2002); Cf. *In re Tanner*
23 *Family, LLC*, 556 F.3d 1194, 1197 & n. 2 (11th Cir. 2009) (lease
24 termination payment due when lease executed).

25 Here, there is no principled manner by which this court may
26 independently determine whether these three payments were made after
27 they were due. The complaint plead only a legal conclusion, "Rents
28 were made after they had come due..."). First Am. Compl. 26:11-16.

1 **3. Ordinary course defense**

2 Trustee Husted's action is not barred by the ordinary course
3 affirmative defense. 11 U.S.C. § 547(c)(2); *Ensolv Co., Inc. v.*
4 *Manpower, Inc. (In re Ensolv Co., Inc)*, 64 B.R. 519, 521 (9th Cir. BAP
5 1986), *aff'd*. 813 F.2d 1230 (9th Cir. Mar. 19, 1987); *Jue v. Liu (In*
6 *re Liu)*, 611 B.R. 864, 880 (9th Cir. BAP 2020). Section 547(c)(2)
7 provides:

8 The trustee may not avoid under this section a transfer--

9 ...

10 (2) to the extent that such transfer was in payment of a
11 debt incurred by the debtor in the ordinary course of
12 business or financial affairs of the debtor and the
transferee, and such transfer was--

13 (A) *made in the ordinary course of business or financial*
14 *affairs of the debtor and the transferee; or*

15 (B) *made according to ordinary business terms.*

16 11 U.S.C. § 547(c)(2) (emphasis added).

17 Since it is an affirmative defense, the plaintiff need not plead
18 around it and a Rule 12(b)(6) motion will lie only if the facts of the
19 transaction show that the payment was, in fact, made in the ordinary
20 course of "business or financial affairs of the debtor and the
21 transferee" or "according to ordinary business terms." 11 U.S.C. §
22 547(c)(2). Here, the irregular payment dates, i.e., August 31,
23 September 29, and November 28, 2017, and varying amounts of payment,
24 i.e., \$400,000, \$300,000, and \$490,000, do not reflect a bar to the
25 action and are sufficient to defeat, at least for pleading purposes,
an ordinary course defense.

26 As to the third count, the motion will be granted.

27 **D. Fourth Cause of Action: Fraudulent Transfers (Actual)**

28 Trustee Husted alleges that rental payments made to the Insider

1 Entity Defendants for rent for the Stockton Facility, Mesquite
2 Facility, and other rented facilities within one year before the
3 Chapter 11 filing constituted actual fraud. First Am. Compl. 27:3-
4 28:19; 75-177; Exhibits to First Am. Compl. 2-8, ECF No. 30.

5 A trustee may avoid a transfer for a debt incurred within two
6 years prior to the bankruptcy if the debtor "made such transfer or
7 incurred such obligation with actual intent to hinder, delay, or
8 defraud any entity to which the debtor was or became, on or after the
9 date that such transfer was made or such obligation was incurred,
10 indebted..." 11 U.S.C. § 548(a)(1).

11 Ordinarily the intent element of fraud is demonstrated by
12 circumstantial evidence. The Ninth Circuit has provided clear
13 guidance on this subject:

14 Among the more common circumstantial indicia of fraudulent
15 intent at the time of the transfer are: (1) actual or
16 threatened litigation against the debtor; (2) a purported
17 transfer of all or substantially all of the debtor's
18 property; (3) insolvency or other unmanageable indebtedness
19 on the part of the debtor; (4) a special relationship
20 between the debtor and the transferee; and, after the
21 transfer, (5) retention by the debtor of the property
involved in the putative transfer.

19 The presence of a single badge of fraud may spur mere
20 suspicion; the confluence of several can constitute
21 conclusive evidence of actual intent to defraud, absent
"significantly clear" evidence of a legitimate supervening
purpose.

22 *In re Acequia, Inc.*, 34 F.3d 800, 805-06 (9th Cir. 1994).

23 As is the case here, Rule 12(b)(6) motions frequently target the
24 sufficiency of the pleadings as to the defendant's intent to hinder,
25 delay or defraud creditors.

26 At least for the purposes of defeating a Rule 12(b)(6) motion,
27 plaintiff Husted has plead facts giving rise to at least two indicia
28 of fraud. The existence of unmanageable debt, *Acequia*, 34 F.3d at

1 805-06, is sufficiently plead by the retention of MCA Financial Group,
2 Ltd., as its financial advisor, and Snell & Wilmer, a national
3 insolvency firm, as its legal advisors, as well as its negotiation of
4 a forbearance agreement through December 31, 2017, and efforts to
5 restructure its debt. First Am. Compl. 10:24-11:5, 11:21-12:17. The
6 special relationship between the Insider Entity Defendants and ECS,
7 *Acequia*, 34 F.3d at 805-06, has been sufficiently plead. First Am.
8 Compl. 4:4-5:4, 6:15-20. Moreover, plaintiff Husted has plead facts
9 giving rise to the inference if an improper purpose, e.g., self-
10 dealing, may be inferred. *Id.* (“absent ‘significantly clear’ evidence
11 of a legitimate supervening purpose”).

12 As to the fourth count, the motion will be denied.

13 **E. Fifth Cause of Action: Fraudulent Transfers (Constructive)**

14 Husted alleges that prepayment for “goods and/or services
15 subsequently received” gives rise to a cause of action for
16 constructive fraudulent transfer. First Am. Compl. 28:25-28.

17 Constructive fraud is defined by statute.

18 (a)(1) The trustee may avoid any transfer... of an interest
19 of the debtor in property, or any obligation... incurred by
20 the debtor, that was made or incurred on or within 2 years
before the date of the filing of the petition, if the
debtor voluntarily or involuntarily—

21 ...

22 (B) (i) *received less than a reasonably equivalent value in*
23 *exchange for such transfer or obligation; and*

24 (ii)(I) was insolvent on the date that such transfer
25 was made or such obligation was incurred, or became
insolvent as a result of such transfer or obligation;

26 (II) was engaged in business or a transaction, or was
27 about to engage in business or a transaction, for which
any property remaining with the debtor was an
unreasonably small capital;

28 (III) intended to incur, or believed that the debtor

would incur, debts that would be beyond the debtor's ability to pay as such debts matured...

11 U.S.C. § 548(a)(1)(B) (emphasis added).

To plead a viable cause of action for constructive fraud the plaintiff must plead:

To plead plausible constructive fraudulent transfer claims against Defendants, Trustee had to allege facts to support the following four elements: (1) a transfer of [debtor's] interest in property; (2) the transfer was made or incurred within two years before the date of the bankruptcy petition; (3) [debtor] *received less than reasonably equivalent value in exchange for the transfer*; and (4) one of three alternatives:

(I) that [the debtor] was insolvent on the date the transfer was made or became insolvent as a result of the transfer;

(ii) that [the debtor] was engaged in business for which any property remaining was an unreasonably small capital; or

(iii) that [the debtor] intended to incur or believed it would incur debts beyond its ability to pay as such debts matured.

In re Blue Earth, Inc., No. 3:16-BK-30296-DM, 2019 WL 4929933, at *6 (9th Cir. BAP Oct. 2, 2019), *appeal docketed*, No. 19-60054 (9th Cir. October 30, 2019) (emphasis added).

Here, after incorporating by reference the preceding 181 paragraphs, Trustee Husted alleges constructive fraudulent transfers with respect to the Insider Entity Defendants arising out of (A) 24 payments to Sinclair Partners, LLC, characterized as "rent" aggregating \$1.473 million; (B) 27 payments to ECS Big Town, LLC, called "rent" aggregating \$551,737; and (C) 3 payments to All Metals, Inc., denominated "payment of invoice" aggregating \$1.190 million. First Am. Compl. 25:27-26:2; Exhibits to First Amend Compl. 8, ECF No. 30. The complaint then alleges:

To the extent one or more of the Transfers identified on

1 *Exhibit A were not made on account of an antecedent debt,*
2 *[and] was a prepayment for goods or services subsequently*
3 *received, Plaintiff pleads that the debtor did not receive*
reasonably equivalent value in exchange for such
transfer(s) and:

4 a) Debtor was insolvent as of the date of the Transfers or
5 became insolvent as a result of the Transfers; or

6 b) The Debtor was engaged in, or about to engage in
7 business or a transaction for which any property remaining
8 with the Debtors or for whose benefit the Transfer was made
9 was an unreasonably small capital; or

10 c) the Debtor intended to incur, or believed it would
11 incur, debts beyond their ability to pay upon maturity.

12 First Am. Compl. 28:25-29:7 (emphasis added).

13 Plaintiff Husted has not plead facts from which the court can
14 plausibly find that ECS did not receive "reasonably equivalent value."
15 Recitation of the statutory elements of a cause of action is
16 insufficient. *Id.* At a bare minimum, the complaint must "describe
17 the consideration and why the value of such consideration was less
18 than the amount transferred." *Sarachek v. The Right Place, Inc. (In*
19 *re Agriprocessors), Inc.*, No. Adv 10-09123, 2011 WL 4621741, at *6
(Bankr. N.D. Iowa Sept. 30, 2011); *Angel v. Ber Care Inc. (In re*
Caremerica), Inc., 409 B.R. 737, 756 (Bankr. E.D.N.C. 2009).

20 Here, the complaint falls short of the standards articulated in
21 *Iqbal* and *Twombly*. Paraphrased, the complaint is fairly read to state
22 that if the payments were not rent and if they were prepayment for
23 goods or services they are not of reasonably equivalent value. First
24 Am. Compl. 28:25-29:7. The First Amended Complaint makes no effort to
25 describe the consideration (or in the alternative, state that no
26 consideration was received) or to explain why the consideration
27 received was less than the amount transferred.

28 As to the fifth count, the motion will be granted.

1 **F. Seventh Cause of Action: Recovery of Avoided Transfers**

2 Plaintiff Husted's seventh cause of action seeks to recover
3 transactions avoided under 11 U.S.C. §§ 547, 548 and 549, i.e., the
4 third, fourth, fifth and sixth cause of action. 11 U.S.C. § 550(a).
5 Since § 550 recovery is dependent on the trustee prevailing on the
6 underlying cause of action and since this motion will be granted as to
7 the third, fifth and sixth causes of action, the motion will also be
8 granted as to those causes of action insofar as they are contained in
9 the seventh cause of action, and otherwise denied.

10 **G. Leave to Amend**

11 Federal Rule of Civil Procedure 15(a) provides that leave to
12 amend "shall be freely given when justice so requires." Circuit law is
13 well settled on this point. "In determining whether to grant leave to
14 amend the court should consider five factors: bad faith, undue delay,
15 prejudice, futility, and previous amendments. *Johnson v. Buckley*, 356
16 F.3d 1067, 1077 (9th Cir. 2004). "Futility alone can justify" denying
17 leave to amend. *Nunes v. Ashcroft*, 375 F.3d 805, 808 (9th Cir. 2004)."
18 *Aluisi v. Jorgensen (In re Jorgensen)*, No. 18-14586-A-13, 2019 WL
19 6720418, at *9 (Bankr. E.D. Cal. Dec. 10, 2019).

20 Bad faith, undue delay and prejudice are not present here.
21 Except as otherwise provided herein, this court believes that
22 plaintiff Husted may be able to cure the pleading deficiencies and
23 will grant leave to file a Second Amended Complaint.

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1 **VI. CONCLUSION**

2 For each of these reasons, the motions will be granted and denied
3 as provided herein. The court will issue an order from chambers.

4 **Dated:** December 15, 2020

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6 Fredrick E. Clement
7 United States Bankruptcy Judge
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Instructions to Clerk of Court
Service List - Not Part of Order/Judgment

The Clerk of Court is instructed to send the Order/Judgment or other court generated document transmitted herewith *to the parties below*. The Clerk of Court will send the document via the BNC or, if checked ____, via the U.S. mail.

Attorney for the Plaintiff(s)	Attorneys for the Defendant(s)
Bankruptcy Trustee (if appointed in the case)	Office of the U.S. Trustee Robert T. Matsui United States Courthouse 501 I Street, Room 7-500 Sacramento, CA 95814