

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF:)	CASE NO. BK98-80382
)	
CONTEMPORARY INDUSTRIES)	
CORPORATION,)	CH. 11
)	
Debtor.)	
-----)	
CONTEMPORARY INDUSTRIES)	ADV. NO. A99-8135
CORPORATION,)	
)	
Plaintiff,)	
)	
vs.)	
)	
TERRY G. FROST, et al.,)	
)	
Defendants.)	

MEMORANDUM

This matter is before the court on the motion for summary judgment (Fil. #195) filed by the defendants, and a resistance thereto filed by the plaintiff (Fil. #210). T. Randall Wright, Paul Bennett Bran, and Robert V. Ginn represent the plaintiff, and Craig F. Martin, Frank M. Schepers, and William M. Lamson Jr. represent the defendants. The motion was taken under advisement as submitted without oral arguments. This memorandum contains findings of fact and conclusions of law required by Federal Rule of Bankruptcy Procedure 7052 and Federal Rule of Civil Procedure 52. This is a core proceeding as defined by 28 U.S.C. § 157(b)(2)(H).

I. Background

Contemporary Industries Corporation (“CIC”), the debtor operating pursuant to a confirmed plan, filed this fraudulent transfer, unjust enrichment, and illegal/excessive distribution action against former shareholders of CIC (“Defendants”). The CIC seeks avoidance of payments made to Defendants in return for the sale of their stock. Statutory authority for the complaint is 11 U.S.C. § 544, 11 U.S.C. § 550, and the Nebraska Uniform Fraudulent Transfer Act, Neb. Rev. Stat. §§ 36-701 to -712.

Defendants have moved for summary judgment pursuant to the “settlement payment” exception to avoidance of a fraudulent conveyance as contained in 11 U.S.C. § 546(e). The facts are undisputed for purposes of this motion. The interpretation of a statute is a question of law. Banks v. Griffin (In re Griffin), 352 B.R. 475, 476 (B.A.P. 8th Cir. 2006).

II. Decision

The motion for summary judgment is granted.

III. Summary Judgment Standard

Summary judgment is appropriate only if the record, when viewed in the light most favorable to the non-moving party, shows there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law. Fed. R. Civ. P. 56(c) (made applicable to adversary proceedings in bankruptcy by Fed. R. Bankr. P. 7056); *see, e.g., Celotex Corp. v. Catrett*, 477 U.S. 317, 322-23 (1986); *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 249-50 (1986); *Aviation Charter, Inc. v. Aviation Research Group/US*, 416 F.3d 864, 868 (8th Cir. 2005); *Ferris, Baker Watts, Inc. v. Stephenson (In re MJK Clearing, Inc.)*, 371 F.3d 397, 401 (8th Cir. 2004).

When reviewing the record, the court is required to draw all reasonable inferences in favor of the non-movant; however, the court is “not required to draw every conceivable inference from the record – only those inferences that are reasonable.” *Auto Mart, Inc. v. Wendt (In re Wendt)*, 355 B.R. 769, 771 (Bankr. W.D. Mo. 2006) (quoting *Bank Leumi Le-Israel, B.M. v. Lee*, 928 F.2d 232, 236 (7th Cir. 1991)). A summary judgment motion should be interpreted by the court to dispose of factually unsupported claims and defenses. *Tiffany v. Speck Enter., Ltd.*, 418 F. Supp. 2d 1120, 1123 (S.D. Iowa 2006).

Essentially, the test is “whether the evidence presents a sufficient disagreement to require submission to a jury or whether it is so one-sided that one party must prevail as a matter of law.” *Anderson v. Liberty Lobby, Inc.*, 477 U.S. at 251-52. Moreover, although under Federal Rule of Civil Procedure 56 due deference must be given to the rights of litigants to have their claims adjudicated by the appropriate finder of fact, equal deference must be given under Rule 56 to the rights of those defending against such claims to have a just, speedy and inexpensive determination of the action where the claims have no factual basis. *Celotex Corp. v. Catrett*, 477 U.S. at 327.

IV. Statement of Facts

Defendants sold their stock in CIC to an investor group. A new company, Contemporary Industries Holding (“CIH”), was created to acquire the shares. The funds to finance the transaction came from lenders and an equity investment from the investor group. All of the debtor’s assets were pledged as collateral for the loans which financed the purchase of Defendants’ stock. CIH then caused approximately \$26.5 million of these funds to be deposited with First National Bank of Omaha and Defendants deposited their shares with First National Bank of Omaha. CIH, Defendants, and First National Bank of Omaha entered into an escrow agreement concerning the distribution of these funds to Defendants.

Within in a little more than a year, CIC filed a voluntary petition for relief under Chapter 11, on February 17, 1998. A plan was confirmed which released the lenders and investors from any claims, including avoidance claims. The plan provided for liquidation of the assets of the debtor and authorized the debtor, through the Committee, to bring appropriate avoidance actions. CIC, in conjunction with the Committee, filed suit against the selling shareholder Defendants. The complaint alleges that the funds received by Defendants were avoidable fraudulent transfers from CIC. The complaint further alleges that Defendants were unjustly enriched to the extent of the receipt of transfers, and that the tender of Defendants’ stock constituted excessive and/or illegal distributions under applicable non-bankruptcy law.

V. Conclusions of Law and Discussion

The Bankruptcy Code, at 11 U.S.C. § 544, permits the debtor-in-possession to bring a fraudulent transfer complaint based upon state law. Using such statutory authority, CIC filed the complaint in this action. However, 11 U.S.C. § 546(e) provided, in pertinent part, at the time the complaint was filed, as follows: “Notwithstanding sections 544 . . . the trustee may not avoid a transfer that is a . . . settlement payment, as defined in section 101 or 741 of this title, made by or to a . . . financial institution.”

The motion for summary judgment depends upon the above-quoted statutory section. Defendants claim the cash transfers made to CIC’s shareholders were “settlement payments” and that those payments were made by a financial institution. The Bankruptcy Code, at 11 U.S.C. § 741(8), defines a “settlement payment” as “a preliminary settlement payment, a partial settlement payment, an interim settlement payment, a settlement payment on account, a final settlement payment, or any other similar payment commonly used in the securities trade”

Three circuit courts of appeal and other courts have concluded that the definition of a settlement payment is “extremely broad.” See Lowenschuss v. Resorts Int’l, Inc. (In re Resorts Int’l, Inc.), 181 F.3d 505, 515-16 (3rd Cir.), cert. denied, 528 U.S. 1021 (1999); Jonas v. Resolution Trust Corp. (In re Comark), 971 F.2d 322, 326 (9th Cir. 1992); Kaiser Steel Corp. v. Pearl Brewing Co. (In re Kaiser Steel Corp.), 952 F.2d 1230, 1239 (10th Cir. 1991) (“Kaiser II”), cert. denied, 505 U.S. 1213 (1992); Official Comm. of Unsecured Creditors v. Fleet Retail Fin. Group (In re Hechinger Inv. Co. of Delaware), 274 B.R. 71 (D. Del. 2002); Walsh v. The Toledo Hosp (In re Fin’l Mgmt. Scis., Inc.), 261 B.R. 150, 154 (Bankr. W.D. Pa. 2001); Biggs v. Smith Barney, Inc. (In re David), 193 B.R. 935, 940 (Bankr. C.D. Cal. 1996).

“In the securities industry, a settlement payment is generally the transfer of cash or securities made to complete a securities transaction.” Resorts Int’l, Inc., 181 F.3d at 515 (citing Kaiser Steel Corp. v. Chas. Schwab & Co., Inc., 913 F.2d 846, 849 (10th Cir. 1990) (“Kaiser I”). The Tenth Circuit appellate court consulted reference materials on the usage of terms in the financial business to determine whether certain transfers were settlement payments in Kaiser I: “Settlement is ‘the completion of a securities transaction[,]’” 913 F.2d at 849 (quoting A. Pessin & J. Ross, Words of Wall Street: 2000 Investment Terms Defined 227 (1983)) and “[settlement is the] ‘[t]ransfer of the security (for the seller) or cash (for the buyer) in order to complete a security transaction.’” Id. (quoting D. Scott, Wall Street Words 320 (1988)). See also Fin’l Mgmt. Scis., Inc., 261 B.R. at 154 (“In general, any transfer of cash or securities made to complete a securities transaction is considered a settlement payment by the securities industry.”) (citing Kaiser I, 913 F.2d at 849).

Both the Third Circuit Court of Appeals in Resorts International and the Tenth Circuit Court of Appeal in the Kaiser cases applied the definition of settlement payment to the type of transaction involved in this case and found that the payment of funds in exchange for shares or securities of the leveraged company were clearly “settlement payments.” See Resorts Int’l, 181 F.3d at 516 (“A payment for shares during an LBO is obviously a common securities transaction, and we therefore hold that it is also a settlement payment for the purposes of section 546(e).”); Kaiser I, 913 F.2d at 849 (“[I]nterpreting ‘settlement payment’ to include the transfer of consideration in an LBO is consistent with the way ‘settlement’ is defined in the securities industry.”); Kaiser II, 952 F.2d at

1237-39. In fact, even “[t]he Securities and Exchange Commission has taken the position . . . that the consummation of an LBO is a ‘settlement payment’ exempted from avoidance by section 546(e).” Kaiser I, 913 F.2d at 849-50.

In addition to the Third and Tenth Circuits, the Fifth and Ninth Circuits have discussed the definition of “settlement payment” as covering a variety of transactional payments, including those in a leveraged buyout. See Williams v. Morgan Stanley Capital Group, Inc. (In re Olympic Natural Gas Co.), 294 F.3d 737, 742 (5th Cir. 2002) (this case was expressly decided only under § 101(51A) and not under § 741(8)), and Comark, 971 F.2d at 325. See also QSI Holdings, Inc. v. Alford (In re Quality Stores, Inc.), 355 B.R. 629 (Bankr. W.D. Mich. 2006) (payments to defendant shareholders resulting from a leveraged buyout were settlement payments from a financial institution and thus were exempt from avoidance based on the settlement payment exception established in § 546(e)).

In this case, the CIC shareholders tendered their shares to an escrow agent, First National Bank of Omaha, as set forth in their escrow agreement. The lenders and investors wired the funds to First National Bank of Omaha so that First National Bank of Omaha could “settle” the transaction by paying the shareholders when it received their share certificates.

To qualify for an exception to the trustee avoidance power, § 546(e) requires the settlement payment to have been made by or to a financial institution. A bank is a “financial institution.” See Resorts Int’l, 181 F.3d at 515-16; Hechinger Inv. Co., 274 B.R. at 87-88.

First National Bank of Omaha is a bank and is clearly a financial institution. It received the payments from the purchasers and it received the shares of stock from Defendant shareholders. It transferred the purchase price to the shareholders and the shares to the purchasers.

As discussed above, payments and shares were delivered to First National Bank of Omaha to settle the CIC transaction. This transaction appears to satisfy the requirements of 11 U.S.C. § 546(e) prohibiting the avoidance of transfers made by First National Bank of Omaha to Defendants.

As with most statutory provisions concerning the Bankruptcy Code, there are contrary decisions at the circuit level, and otherwise, taking the position that transfers such as those involved in the leveraged buyout in this case do not qualify for the exception under § 546(e). The Eleventh Circuit Court of Appeals in Munford v. Valuation Research Corp. (In re Munford), 98 F.3d 604 (11th Cir. 1996), cert. denied, 522 U.S. 1068 (1998), refused to apply the exception where the financial institution did not retain a beneficial interest in the funds, but acted only as an intermediary. However, there is nothing in the statutory language which requires the financial institution involved in a settlement of a securities transaction to take a financial interest in the matter. The Munford case stands in contrast to the plain reading of the statutory terms in the cases cited above.

Although Munford is the only circuit court refusing to apply § 546(e) exception to a leveraged buyout similar to this case, several other cases also suggest the § 546(e) exception is not applicable to private transactions but is only applicable to leveraged buyouts in the public commodities and securities market. See Kipperman v. Circle Trust F.B.O. (In re Grafton Partners, L.P.), 321 B.R. 527 (B.A.P. 9th Cir. 2005); Zahn v. Yucaipa Capital Fund, 218 B.R. 656, 676-77

(D.R.I. 1998); Wieboldt Stores, Inc. by and through Raleigh v. Schottenstein, 131 B.R. 655, 663-65 (N.D. Ill. 1991); Official Comm. of Unsecured Creditors v. Lattman (In re Norstan Apparel Shops, Inc.), ___ B.R. ___, 2007 WL 965963, at * 5 (Bankr. E.D.N.Y. Mar. 30, 2007); Official Comm. of Unsecured Creditors v. Asea Brown Boveri, Inc. (In re Grand Eagle Cos., Inc.), 288 B.R. 484, 494 (Bankr. N.D. Ohio 2003); Brandt v. Hicks, Muse & Co. (In re Healthco Int'l, Inc.), 195 B.R. 971, 983 (Bankr. D. Mass. 1996). Each of these cases looks beyond the statutory language and attempts to discern the intent of Congress when drafting the language. However, the United States Supreme Court has made it very clear that when language is plain, it should be enforced according to its terms. See Estate of Cowart v. Nicklos Drilling Co., 505 U.S. 469, 475 (1992) (“[W]hen a statute speaks with clarity to an issue judicial inquiry into the statute’s meaning, in all but the most extraordinary circumstance, is finished.”); Lamie v. United States Trustee, 540 U.S. 526, 534 (2004) (“It is well established that ‘when the statute’s language is plain, the sole function of the courts – at least where the disposition required by the text is not absurd – is to enforce it according to its terms.’”); United States v. Ron Pair Enter., Inc., 489 U.S. 235, 241 (1989) (“[W]here, as here, the statute’s language is plain, ‘the sole function of the courts is to enforce it according to its terms.’”) (quoting Caminetti v. United States, 242 U.S. 470, 485 (1917)).

Here, 11 U.S.C. § 546(e) is clear. It prohibits the avoidance of a settlement payment as defined in § 101 or § 741 of the Code, made to or by a financial institution. As a matter of law, the transaction may not be avoided as a fraudulent transfer.

In addition to the fraudulent transfer aspects of the complaint, Plaintiff asserts that the transaction should be set aside or Defendants should be required to pay back the funds received because they have been unjustly enriched by the transaction or have received illegal/excessive distribution. Defendants take the position that such claims are preempted by § 546(e). In support of their position, Defendants describe the Supremacy Clause of the United States Constitution, through the doctrine of preemption, as invalidating state laws that interfere with or are contrary to federal law. Ass’n of Int’l Auto. Mfrs., Inc. v. Abrams, 84 F.3d 602, 607 (2nd Cir. 1996) (quoting Hillsborough County v. Automated Med. Labs., Inc., 471 U.S. 707, 712 (1985)). The Second Circuit case stated that even where federal law does not expressly preempt state law, preemption may be implied “when the scope of a [federal] statute indicates that Congress intended federal law to occupy a field exclusively,” or “where state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.” Ass’n of Int’l Auto. Mfrs., 84 F.3d at 607 (quoting Freightliner Corp. v. Myrick, 514 U.S. 280, 287 (1995)).

In this case, CIC’s state law claims for unjust enrichment and illegal/excessive distribution are substantially identical to the avoidance claims barred by 11 U.S.C. § 546(e). Therefore, implied preemption principles should apply. See Hechinger Inv. Co., 274 B.R. at 95-98. In that case, the court found that § 546(e) prohibited the unsecured creditors committee from recovering funds paid by Hechinger to purchase stock from certain shareholders in connection with a leveraged buyout. It also preempted any attempt to recover the payments on a state law unjust enrichment theory.

Concerning Plaintiff’s “excessive/illegal distribution” claim, Plaintiff, in response to the argument of Defendants, suggests that case law with regard to illegal distributions under state law makes such illegal distributions void and therefore the claim against Defendants cannot be preempted. However, the cases cited by Plaintiff are in the minority. CIC was a Nevada corporation

and there is no Nevada case law that suggests ultra vires distributions would be treated as anything but voidable as a majority of the cases hold. The majority of state cases on the subject simply hold that stock repurchase agreements which may be unauthorized or ultra vires corporate acts are not void. See Am. Family Care, Inc. v. Irwin, 571 So. 2d 1053, 1060 (Ala. 1990); James v. J.F.K. Carwash, Inc., 628 S.W.2d 299, 300-01 (Ark. 1982); Triumph Smokes, Inc. v. Sarlo, 482 S.W.2d 696, 698 (Tex. Civ. App. 1972); Rainford v. Rytting, 451 P.2d 769, 771 n.5 (Utah 1969); La Voy Supply Co. v. Young, 369 P.2d 45, 49 (Idaho 1962) .

Since the unjust enrichment and excessive/illegal distribution claim are analogous to the fraudulent transfer claim, which is safe from avoidance by virtue of § 546(e), that statutory section preempts the unjust enrichment and excessive/illegal distribution claims.

VI. Conclusion

The Bankruptcy Code at 11 U.S.C. § 546(e) prohibits the trustee, debtor-in-possession, or Committee, in this case, from avoiding the transfers which are the subject matter of this adversary proceeding. The motion for summary judgment (Fil. #195) filed by the defendants is granted. Separate judgment shall be entered.

DATED: June 29, 2007

BY THE COURT:

/s/ Timothy J. Mahoney
Chief Judge

Notice given by the Court to:

T. Randall Wright	Paul Bennett Bran
Robert V. Ginn	*Craig F. Martin
*Frank M. Schepers	*William M. Lamson
U.S. Trustee	

Movant (*) is responsible for giving notice to other parties if required by rule or statute.

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Defendants.)	

JUDGMENT

This matter is before the court on the motion for summary judgment (Fil. #195) filed by the defendants, and a resistance thereto filed by the plaintiff (Fil. #210). T. Randall Wright, Paul Bennett Bran, and Robert V. Ginn represent the plaintiff, and Craig F. Martin, Frank M. Schepers, and William M. Lamson Jr. represent the defendants.

IT IS ORDERED: For the reasons stated in the Memorandum of today's date, the defendants' motion for summary judgment (Fil. #195) is granted. Judgment is hereby entered in favor of the defendants and against the plaintiff debtor.

DATED: June 29, 2007

BY THE COURT:

/s/ Timothy J. Mahoney
Chief Judge

Notice given by the Court to:

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Robert V. Ginn *Craig F. Martin
*Frank M. Schepers *William M. Lamson Jr.
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