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Scope of Injunctive Relief Available To Foreign Proceedings Under Bankruptcy Code Section 304

In Hoffman v. Bullmore (In re Nat'l Warranty Ins. Risk Retention Group), No. 04-1754 (8th Cir. Sept. 24, 2004), the plaintiff was one of approximately 950,000 purchasers holding a Vehicle Service Contract ("VSC"), guaranteed by the debtor. The debtor's primary place of business was in Nebraska, and the debtor's business and all of its assets were located in the United States. Notwithstanding, the debtor transferred $24 million out of the U.S. to bank accounts in the Cayman Islands, and then filed for liquidation under Cayman law. The debtor's lone connection to the Cayman Islands appears to be that it was its place of incorporation.

The foreign filing was preceded by the plaintiff's lawsuit against the debtor, which she intended to convert into a class action, based upon the debtor's failure to perform under the VSC. After filing the Cayman liquidation proceeding, the debtor filed a petition under Bankruptcy Code § 304 seeking an injunction to halt all actions against assets involved in the Cayman liquidation. The plaintiff objected on behalf of herself and others similarly situated. The Bankruptcy Court granted the requested § 304 relief and the B.A.P. for the Eighth Circuit affirmed.

On appeal to the Eighth Circuit Court of Appeals, the plaintiff argued that: (i) the Cayman liquidation was not a "foreign proceeding" allowing relief under Section 304; (ii) the Bankruptcy Court abused its discretion in evaluating the Section 304 factors and determining to grant relief; and (iii) the scope of the injunction was too broad. As to the first challenge, the Eighth Circuit held that the Cayman Islands are the debtor's domicile because it is the place of incorporation, and thus the Cayman Islands are the debtor's domicile for Section 304 purposes. Next, the Court determined that the Bankruptcy Court did not abuse its discretion in evaluating the Section 304 factors and granting the relief, even though a class action is likely not possible under Cayman law, requiring each of the thousands of VSC holders to individually liquidate their claims in the Cayman Islands. Although "inconvenient" for the individual claimants, the court viewed Cayman law as capable of justly treating each claimant Finally, the plaintiff argued that the scope of the injunction was too broad as it prohibited discovery by third-party non-debtors and prevented a class action from going forward in the U.S. where all VSC claimants could more cost-effectively pursue their claims. The Eighth Circuit was not persuaded. It noted that, under Section 304, courts are "free to mold appropriate relief in near 'blank check' fashion."

Thus, the Eighth Circuit concluded that a bankruptcy court, properly evaluating the Section 304 factors, is free to fashion injunctive relief that effectively prevents a class action proceeding.

Debtor Lacks Standing In Adversary Proceeding Regarding Pre-Petition Dispute

In *In re* Harrison, Bankr. No. 04-6019SI (8th Cir. BAP Sept. 30, 2004), the Bankruptcy Appellate Panel for the Eighth Circuit held that the debtor did not have standing to assert pre-petition rights for payment of certain annuity payments because pre-petition claims of the debtor became property of the bankruptcy estate. The debtor was involved in pre-petition litigation which resulted in a settlement agreement that provided for periodic payments from an annuity. The debtor subsequently entered into a series of contracts with Signer Asset Finance

Company ("Finance Company") where she sold some or all of her rights to receive the annuity payments in exchange for immediate compensation. A dispute arose between the debtor and the Finance Company regarding the terms of the contracts. This dispute was unresolved at the time the debtor filed for Chapter 7 bankruptcy.

The debtor filed an adversary proceeding against the Finance Company because the debtor believed that the Chapter 7 bankruptcy Trustee ("Trustee") was not doing enough to prosecute the claim on behalf of the bankruptcy estate against the Finance Company. The Bankruptcy Court granted the Finance Company's motion to dismiss based on the debtor's lack of standing. The BAP affirmed the Bankruptcy Court's ruling because it concluded that the Trustee was properly asserting the rights of the bankruptcy estate, and that the annuity company responsible for making payments to either the debtor or the Finance Company had commenced an adversary proceeding in which it named the debtor, the Finance Company and the Trustee as parties in the declaratory judgment action. The BAP's opinion made it clear that a debtor's rights in a pre-petition dispute becomes property of the bankruptcy estate and the debtor therefore will not have standing to individually pursue those pre-petition rights.

Creditor Failed to Establish Affirmative Defenses to Preference

In Shodeen v. Airline Software, Inc. (In re: Access Air, Inc.), Case No. 04-6020SI (8th Cir. B.A.P. Sept. 22, 2004), the Bankruptcy Appellate Panel for the 8th Circuit affirmed the Bankruptcy Court's holding that a creditor's receipt of in excess of $100,000.00 in payments during the 90-day preference period constituted an avoidable preference under 11 U.S.C. § 547(b), and that the creditor failed to establish that the payments were unavoidable pursuant to § 547(c)(2) or § 547(c)(4).

The defendant, Airline Software, Inc. ("Airline Software") provided airline management software to the debtor. As part of the licensing arrangement, the debtor made monthly payments. Six such payments were made during the preference period. The parties stipulated that the payments satisfied the elements of § 547(b), so the trial was solely on the merits of Airline Software's affirmative defenses. At trial, Airline Software's president, Mr. Rosen, testified that he was unable to produce any of his company's records relating to its payment history with the debtor because they were destroyed. As a result, the Bankruptcy Court specifically found that Rosen was not a credible witness for either subjective ordinary course of business standard under Section 547(c)(2)(B) or the objective "industry standard" under Section 547(c)(2)(C).

However, in addition, the Court also found that even if Rosen's testimony was credible, Rosen failed to provide objective evidence of the industry standard. The Court noted that the creditor only provided testimony of the creditor's own subjective experience which is insufficient by itself to establish the range of terms prevailing within the industry as required by Section 547(c)(2)(C). In addition, the debtor's director of management information systems also testified as to the debtor's payment history to its other creditors. The Court found again that the debtor's subjective payment history with its other creditors was also insufficient evidence as it was not objective evidence of the range of terms for billing with the relative industry as required by Section 547(c)(2)(C). "The transferee must establish the general range of industry practice by introducing objective evidence

outside it or the debtor's subjective experience to satisfy its burden of proof under Section 547(c)(2)(C)."

Though not required for its holding, it is not exactly clear whether the Bankruptcy Appellate Panel is essentially requiring that a creditor needs to use a third party expert witness to establish the industry standard under Section 547(c)(2)(C).

NEWS

Court Migrating to CM/ECF in 2005

The U.S. Bankruptcy Court is currently in the process of migrating from its locally developed Electronic Records System (ERS) to the Case Management and Electronic Case Filing (CM/ECF) program developed by the Administrative Office of the United States Courts. Conversion to the new system will occur in 2005.

Filers will notice many similarities between the two systems, including a required user name and password, data input screens, drop-down menus, pdf files, and real time filing. The Court is also incorporating some of the most popular features from ERS, such as the screen help text and "unlisted document," into CM/ECF.

CM/ECF will include some changes, including more case filing options, a judge/trustee assignment feature, automatic email notification of interested parties when there is docket activity in a case, and on-line credit card payment of filing fees. The most notable change is that CM/ECF requires users to pay for viewing and downloading information.

Court staff are currently developing and testing docket events for the new system. Internal staff training is also underway with attorney training to begin in 2005. Several training options will be offered for attorneys and their staff, and training information will be emailed to attorneys and will also be posted on the Court's web site, www.mnb.uscourts.gov as it is available.

For a preview of the new electronic filing program, click "ECF 101" from the drop-down menu at CM/ECF on the Court's home page. The September 2004 ***CM/ECF Update,*** also found on the drop-down menu, provides more detailed information about the similarities and differences between ERS and CM/ECF.