No. **14-10092**

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

In the Matter of: JEFFREY BARON
Debtor;

SCHURIG JETEL BECKETT TACKETT; DEAN FERGUSON; POWERS TAYLOR, LLP; GARY LYON; JEFFREY HALL; ROBERT GARREY; PRONSKE & PATEL, P.C.; DAVID PACIONE,
Appellants,

vs.

JEFFREY BARON,
Appellee.

Appeal from the United States District Court, Northern District of Texas
Docket No. 3:09-cv-0988-L

APPELLEE'S BRIEF

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Appellee.

CERTIFICATE OF INTERESTED PERSONS

Pursuant to Fifth Circuit Rule 28.2.1, the undersigned counsel of record for Appellee, Jeffrey Baron, certifies that the following listed persons have an interest in the outcome of the case. These representations are made in order that the Judges of this Court may evaluate possible disqualification or recusal.

The Certificate of Interested Persons submitted by the Appellants appears to be correct in most respects. However, Appellee advises this Court that the following parties have intervened in this case:

Interveners:

- Novo Point, LLC
- Quantec, LLC

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STATEMENT REGARDING ORAL ARGUMENT

The Appellee respectfully requests an oral argument under Fed. R. App. P. 34(a). The Appellee believes this case meets the standards in Rule 34(a)(2) for oral argument in that:

a. Some of the dispositive issues raised in this appeal, in particular the unique issues of: (1) whether the existence of a receivership, ruled invalid by this Court, precludes application of the insolvency element, under 11 U.S.C. § 303(h), for an involuntary bankruptcy; and (2) the application of collateral estoppel from a proceeding *in rem* in an involuntary bankruptcy proceeding is permissible, have not been authoritatively decided within this Circuit; and

b. As described in this brief, the decisional process may be significantly aided by oral argument.

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TO THE HONORABLE JUDGES OF THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT:

Jeffrey Baron, respectfully submits this Appellee's Brief showing the following in support of upholding the judgment of the United States District Court reversing the Order for Relief entered by the United States Bankruptcy Court:

ISSUES PRESENTED

1. Whether, in reversing an order for relief based, in part, on a partial summary judgment, the district court was correct in rendering a judgment for dismissal when the key facts were so developed that the issues may properly be determined as a matter of law, making further fact finding no remand futile.

2. Whether the district court was correct in determining the Appellants lacked standing to be petitioning creditors due to the disputed nature of their claims.

3. Whether the district court was correct in determining that the petitioning creditors lacked standing, under 11 U.S.C. § 303(b), to bring an involuntary petition in bankruptcy due to bona fide disputes as to liability or as to the amount of their claims.

4. Whether the bankruptcy court erred in entering the Order for Relief against Jeffrey Baron.

5. Whether the district court erred in reversing the bankruptcy court's Order for Relief entered against Jeffrey Baron.

STATEMENT OF THE CASE

In *Netsphere, Inc. v. Baron*, this Court held that District Judge Royal Furgeson abused his discretion in imposing an equity receivership over Baron's assets—including assets exempt from unsecured creditors' claims under Texas law—over "unresolved claims" that had not been reduced to a judgment. 703 F.3d 296, 302, 306, 308 (5th Cir. 2012). The Court mandated an expeditious wind-down of the receivership and return of the receivership estate, less approved expenses of the receivership, to Baron. As to the wind-down, this Court stated:

> In light of our ruling that the receivership was improper, equity may well require the fees to be discounted meaningfully from what would have been reasonable under a proper receivership. Fees already paid were calculated on the basis that the receivership was proper. Therefore, the amount of all fees and expenses must be reconsidered by the district court. Any other payments made from the receivership fund may also be reconsidered as appropriate. . . .
>
> The new determination by the district court of reasonable fees and expenses to be paid to the receiver, should the amount be set at more than has already been paid, may be paid from the $1.6 million. To the extent the cash on hand is insufficient to satisfy fully what is determined to be the reasonable charges by the receiver and his attorneys, those charges will go unpaid. No further sales of domain names or other assets are authorized.
>
> *Id*. at 313–14. (internal citation omitted).

This case is about the *Netsphere* Appellees' attempt, in violation of the district court's injunction, to interfere with the wind-down of the receiver-

ship, a receivership that continues to operate to this very day, by the filing of a meretricious involuntary bankruptcy ***two hours*** after this Court issued its opinion in *Netsphere v Baron*.

A. Fee Order entered during the Receivership

While Baron immediately appealed the order appointing the Receiver, he was unable to obtain a stay of the order appointing the Receiver. (ROA.1374–95). Therefore, the Receiver commenced carrying out his duties. One of the district court's professed goals of the receivership "was for the Receiver to collect evidence of the Former Attorney Claims . . . and then, with the Court's guidance, instructions, and orders, disburse assets to resolve the Former Attorney Claims." (ROA.1398). Ultimately, the Receiver put forth a plan that would pay the claims sought by the Appellants, albeit a reduced amount. In all, the Receiver, with the aid of the Appellants themselves, gathered evidence of claims totaling $1,453,208.27 and proposed that the Receivership estate pay 60 percent of such fees—$870,237.19.[1] (ROA.1409–13). The district court approved payment of these fees, "once the Receiver has obtained cash to pay the Former Attorney Claims,"[2] provided that the Appellants waived further claims for amounts not approved

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[1] This amount reflects the fact the Appellants were previously paid $3,177,880.22. (ROA.4693–5945).

[2] ROA.1415.

by the court as well as their claims for punitive damages. (ROA.1416–17). The order also preserved Baron's rights to bring claims against the Appellants after the end of the receivership.[3] (ROA.1417).

On April 28, 2011, the district court conducted a hearing on the on the Receiver's application for approval of the Appellant's claims. A copy of the transcript of the hearing was later submitted as summary judgment evidence in the involuntary bankruptcy proceedings against Baron. (ROA.1419–1527). At the commencement of this hearing, Gary Schepps, an attorney who had been assisting Baron in the *Netsphere* appeal, made a limited appearance and advised the court that Baron did not have the ability to pay counsel, expert witnesses, or conduct discovery because all of his assets were tied up in the receivership. (ROA.1434–36, 1676–79). Moreover, the Receiver had taken control of all of Baron's business records. (ROA.1434–40, 1453, 1465–66, 1676). Schepps also advised the court that he was not being paid and could not continue to represent Baron during the hearing because trial work was not his area of expertise. (ROA.1677–78).

The Receiver admitted that he did not provide any funds for Baron to pay counsel or expert witnesses. (ROA.1434). Instead, the Receiver argued

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[3] In the event Baron brings legal malpractice claims against the Appellants, then the Appellants' waivers would be of no effect and they would be entitled to bring counterclaims for the fees not allowed by the court as well as counterclaims for punitive damages, if available under applicable law. (ROA.1417).

that a summary proceeding was a low cost way to settle the Appellants' claims. (ROA.1456, 1462, 1514).

Schepps brought Christopher Payne, a board-certified trial attorney, to the hearing, but the court declined to approve his retention. (ROA.1465). As a result, Baron was not represented at the hearing. Baron initially stood by his controverting affidavit to contest the Receiver's evidence. However, when the court informed him that he would have to be subject to cross examination by the Appellants who, the day before, made allegations of criminal conduct, Baron declined to testify without representation. (ROA.1493–94). As a result, Baron's affidavit was withdrawn and the evidence regarding the Appellants' claims was uncontested. (ROA.1413–14). Ultimately, no witnesses, including the Appellants, testified at the hearing. (ROA.1419–1527).

The *Findings of Fact, Conclusions of Law, and Order on Assessment and Disbursement of Former Attorney Claims* ("Fee Order") was approved on May 18, 2011. (ROA.1396–1417). Six days later, Judge Furgeson stayed enforcement of the Fee Order, and the stay was never lifted.[4] (ROA.1671–73).

---

[4] Other orders confirmed that the Fee Order was stayed. For example, on May 24, 2011, Judge Furgeson stated, "Having consulted with the Clerk of the U.S. Court of Appeals for the Fifth Circuit, the Court advises the parties that it is STAYED from taking further action in the various matters involved in the instant appeal." (ROA.7017). On June 5, 2011, Judge Furgeson stated, "I failed to mention that I would stay . . . orders concerning fees to be paid to the Baron attorneys pending appeal." (ROA.7020).

Originally, one of the issues in *Netsphere* was the appeal of the Fee Order; however, it was not ruled on by this Court because the matter was still before the district court on a motion for reconsideration, which was filed by Carrington, Coleman, Sloman & Blumenthal, L.L.P., one of the attorney creditors. *Netsphere*, 703 F.3d at 305 n. 1; *see also Baron v. Schurig*, No. 3:13-CV-3461-L, 2014 WL 25519, at *3 (N.D. Tex. Jan. 2, 2014) (further explaining the procedural history of the Fee Order). The district court never entered an order on the motion for reconsideration. Thus, the Fee Order was not only stayed, it was interlocutory in nature. Ultimately, it was vacated by Judge Sam A. Lindsay on January 2, 2014. *Baron*, 2014 WL 25519, at *15.

Of particular note, the receivership still has not concluded.[5] *See Id.* at *16.

B. Involuntary bankruptcy proceedings

Prior to Judge Lindsay vacating the Fee Order on January 2, 2014, it, along with all of its ambiguities, formed the foundation of the Appellants' misguided attempt to force Baron into an involuntary bankruptcy. The in-

[5] "While the receivership established in 2010 has taken on a life of its own, as aptly noted by Judge Furgeson after the Fifth Circuit issued its December 18, 2012 ruling, it was never intended to continue indefinitely. The court will therefore direct the Receiver, in a subsequent order to follow, to wind down the receivership and return all receivership assets to Baron or the entities from which the assets were received so that the receivership and the litigation regarding it can brought to a close." *Baron*, 2014 WL 25519, at *16.

voluntary petition was filed two hours after this Court issued its opinion in *Netsphere*. Early in the case, the Appellants admitted their motivations:

> The Petitioning Creditors immediately filed a Chapter 7 Involuntary Petition against Baron after entry of the Fifth Circuit Order on December 18, 2012 out of the concern that Baron might divest assets from the jurisdiction of the United States Courts and beyond the reach of creditors with significant claims against Baron.
>
> (ROA.273).

These motivations were similar to the motivations behind the receivership in the fist place. *See Netsphere*, 703 F.3d at 308. Yet, this Court found that there was no such evidence. *Id.* at 307. ("there was no record evidence brought to our attention that any discrete assets subject to the settlement agreement were being moved beyond the reach of the court.").

1. *Baron's motion to dismiss is denied*

On January 9, 2013, Baron filed a motion to dismiss. (ROA.161). Baron argued that the Appellants lacked standing under Section 303(b)(1) and that by filing an involuntary petition, the Appellants violated the district court's injunction. (ROA.161–63).

This motion was denied on April 5, 1993, after the bankruptcy court had the opportunity to review the Appellants' motion for summary judgment and hear arguments of counsel regarding the same.[6] (ROA.2303–04).

2. *Appellants' motion for summary judgment on the standing element under Section 303(b) is granted*

On February 1, 2013, the Appellants filed a motion for summary judgment, seeking to dispose of all elements under Section 303 as a matter of law. (ROA.457). The motion was supported by 994 pages of evidence, consisting mostly of detailed time sheets. (ROA.481–711, 751–1005, 1045–1299, 1339–1595). Baron's Motion to Dismiss, which challenged the Petitioning Creditors' standing, was pending at the time.

In their summary judgment motion, the Appellants argued that the district court's evidentiary hearing that led to the approval of the Fee Order was collateral estoppel in the bankruptcy court. In particular, the Appellants asserted that the evidence heard in the district court precluded Baron from contesting the amount of liability or whether the claims were subject to bona fide disputes in the bankruptcy court.

Despite the district court's order being clear as to the amount of fees it was awarding, the Appellants sought a summary judgment on the full

[6] The same day, the bankruptcy court granted the Appellants' motion for summary judgment. (ROA.2301–02).

amount of the fees they claimed in the district court, rather than the "compromised" amount set forth in the Fee Order. These findings were made following a hearing where all interested parties were initially given an opportunity to cross examine witnesses; however, Baron ended up being unrepresented due to the court prohibiting him from paying counsel. Moreover, this was a summary proceeding[7] where Baron was not able to fully litigate his disputes related to the claims. Instead, the court preserved Baron's right to litigate his legal malpractice claims against the Appellants after the termination of the receivership. (ROA.1417).

After the filing of the motion for summary judgment, the parties entered into a written stipulation which provided, in relevant part:

> The Petitioning Creditors and the Alleged Debtor hereby stipulate and agree that the sole summary judgment issue to be presented to the Court with respect to the bona fide dispute issue shall be whether prior orders issued in the District Court and this Court in a related bankruptcy matter legally foreclose any argument as to the existence of a bona fide dispute as to the Petitioning Creditors' claims. . . .
>
> The Petitioning Creditors and the Alleged Debtor further hereby stipulate and agree that nothing herein shall prevent the Petitioning Creditors from reurging the evidence of their underlying claims at a later hearing, including a hearing on a second motion for summary judgment.
>
> (ROA.1732–33).

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[7] ROA.1401–02.

At the hearing on the motion for summary judgment, the bankruptcy court and the litigants understood that the stipulation reduced the scope of the motion to a single, narrow issue. (ROA.1888–89).

The order granting the summary judgment was entered on April 5, 2013, and held, in part, "the claims of the Petitioning Creditors are not contingent as to liability or the subject of a bona fide dispute as to liability or amount."[8] (ROA.2302). This left the insolvency element under Section 303(h) as the only issue for trial.

After the trial, the bankruptcy court made findings of fact relating to the standing element under Section 303(b), the subject of the earlier motion for summary judgment. (ROA.4366, 4380–93).

3. *Trial on the insolvency element under Section 303(h) is held*

The bankruptcy court ordered a trial of the remaining elements under Section 303, "including whether or not . . . [Baron] is generally paying his debts as they become due." (ROA.2308–09). It further ordered that the evidence would be declarations, with attachments, and that the parties would be able to cross-examine, re-direct, and re-cross witnesses as necessary, subject to the court's time limitations. (ROA.2309–10).

The bankruptcy court opined:

[8] The Order Denying Baron's Motion to Dismiss was entered on the same day, April 5, 2013. (ROA.2303–04).

> But the final question in this court's mind is whether this should all be analyzed differently, since Mr. Baron's assets have been tied up in a Receivership for almost three years (a Receivership that was overturned by the Fifth Circuit) and, arguably, Mr. Baron has not had the ability to generally pay his debts as they become due? This court does not believe Mr. Baron has a persuasive argument in this regard. The evidence reflected that there was more than enough value from the assets in the Receivership to pay the legal fees (if Mr. Baron had wanted to pay the fees and cease the Receivership at any time). Moreover, the history here (partially discussed earlier) cannot be ignored.
>
> (ROA.4400–01).

As shown below, this interpretation of the law is erroneous.

4. *Order for Relief & appeal to the district court*

On June 26, 2013, the bankruptcy court entered an order for relief. (ROA.4404). Baron perfected an appeal of the order for relief to the district court on July 8, 2013. (ROA.6027–37) (Am. Notice of Appeal).

After full briefing by the parties, the district court entered its final judgment on January 2, 2014. (ROA.8090). Accompanying the final judgment is the *Amended Memorandum Opinion and Order*. (ROA.8061–89). *See also Baron*, 2014 WL 25519.

SUMMARY OF THE ARGUMENT

In an involuntary bankruptcy, petitioning creditors must prove that they have standing *and* that the debtor is not paying his debts as they come due. Under the facts of this case, standing requires that petitioning creditor

hold claims that are not contingent or subject to a bona fide dispute as to liability or amount. Likewise, insolvency requires a showing that the debtor is not paying debts, which are not subject to a bona fide dispute, as they come due.

The district court committed no error in ordering the bankruptcy court to dismiss the involuntary bankruptcy case against Jeffrey Baron. When a summary judgment is reversed by an appellate court, a remand is not necessarily required, and this case is one of those situations. An appellate court is entitled to rely on fully developed, undisputed facts and reframe the legal issues. In the present case, no evidence that the Appellants might introduce on remand can overcome the legal impediments to them having standing to be petitioning creditors in an involuntary bankruptcy.

First, the Appellants cannot overcome the fact that this Court recognized the disputed nature of their claims in *Netsphere v. Baron*. Second, the nature of the receivership proceeding where the district court entered the Fee Order, which formed the foundation of the Appellants' position on standing, was a proceeding *in rem*. The involuntary bankruptcy was a proceeding *in personam*, and where one action is *in rem* and the other is *in personam*, there is no preclusive effect from one proceeding to the other. Moreover, the Fee Order was interlocutory in nature, and it was stayed by Judge Furgeson. Thus, it is irrelevant whether Baron controverted the evi-

dence in the hearing giving rise to the Fee Order. Third, the existence of known counterclaims that the district court was allowing Baron to assert after the termination of the receivership creates a bona fide dispute as to the amount of the claim as a matter of law. Finally, in filing an involuntary petition just hours after this Court issued its opinion in *Netsphere*, the Appellants violated the district court's injunction prohibiting creditors from instituting or continuing legal proceedings affecting the receivership.

This Court ordered that the receivership be wound down in an expeditious manner. The fact that the automatic stay was imposed upon the filing of the bankruptcy petition and that the bankruptcy court attempted to gain control of the receivership estate under control of the district court, caused delays in the wind-up of the receivership that continues to this very day. The Appellants' unauthorized involuntary petition caused the Receiver to incur further expenses of administration. Therefore, this Court should not allow the Appellants to continue this involuntary bankruptcy that has violated this Court's mandate in *Netsphere v. Baron* and the district court's orders, causing delay in the wind-down of the receivership.

Finally, the Appellants should not be allowed to place Baron into an involuntary bankruptcy under a judicially-created "special circumstances" doctrine which perverts the express provisions of the bankruptcy code. The harm that a bad faith involuntary petition can do is enormous; therefore,

Congress enacted numerous safeguards and requirements into the Bankruptcy Code. This Court should not endorse any doctrine that violates the express provisions of Section 303 of the Bankruptcy Code. Moreover, the Appellants' justification for placing Baron into an involuntary bankruptcy, the accusation that he was transferring assets outside of the court's jurisdiction, was debunked by this Court in *Netsphere*.

ARGUMENT

In reviewing the decision of a district court sitting as an appellate court, this Court applies the same standards of review to the bankruptcy court's findings of fact and conclusions of law as applied by the district court. *Caillouet v. First Bank & Trust (In re Entringer Bakeries, Inc.)*, 548 F.3d 344, 348 (5th Cir. 2008).

The bankruptcy court's conclusions of law and mixed questions of fact and law are reviewed *de novo*. *Randall & Blake, Inc. v. Evans (In re Canion)*, 196 F.3d 579, 584 (5th Cir. 1999). Findings of fact are reviewed under a clearly erroneous standard. *Beaubouef v. Beaubouef (In re Beaubouef)*, 966 F.2d 174, 178 (5th Cir. 1992). "A finding is 'clearly erroneous' when, although there is evidence to support it, the reviewing court on the entire record is left with the definite and firm conviction that a mistake has been

committed." *United States v. United States Gypsum Co.*, 333 U.S. 364, 395 (1948).

I.

The district court was correct in ordering dismissal of the involuntary bankruptcy case and remanding only the question of attorneys' fees under 11 U.S.C. § 303(i)

The Appellants' argument is predicated on the assumption that that the district court allegedly erred by rendering a judgment rather than remanding the case to the bankruptcy court for further proceedings. This might be the case if there were fact issues that the bankruptcy court should try on remand. Instead, a remand would be futile because the Appellants lack standing under Section 303(b) as a matter of law. That a cross-motion for summary judgment was not filed does not deprive the district court from properly rendering a judgment directing dismissal of the involuntary bankruptcy petition.

A. Despite reversing a partial summary judgment, the Appellants cannot prove, as a matter of law, that they have standing to force Baron into an involuntary bankruptcy

The Appellants seek a remand so that they may get a second chance to put on evidence when they had previously stipulated, after filing a motion for summary judgment that was potentially fully dispositive, that they could reurge the evidence supporting their alleged claims. (ROA.1733). In

this case, the facts are fully developed; a remand would be futile. No matter what evidence the Appellants could present to the bankruptcy court, overriding issues of law doom the Appellants' case.

1. *Prior to the filing of the involuntary petition, other courts recognized the existence of a bona-fide disputes clouding the Appellants' claims*

This case illustrates one of the occasions where a remand is not required after the reversal of a partial summary judgment.

In effectively rendering a judgment, the district court decided any disputed issues of fact that may have been evident in the record in addition to reviewing the bankruptcy court's conclusions of law. When reviewing a summary judgment, it is well established that appellate courts will decide mixed questions of fact and law, where, as in the instant case, no further development of facts is required in order to resolve the mixed question and where a remand is neither necessary nor prudent. *Miles v. Great N. Ins. Co.*, 634 F.3d 61, 66 (1st Cir. 2011); *see also Societe Des Produits Nestle, S.A. v. Casa Helvetia, Inc.*, 982 F.2d 633, 642 (1st Cir. 1992) (where trial court "supportably 'made the key findings of fact' but applied the wrong rule of law, the [appellate court] ha[s] the power, in lieu of remanding, simply to regroup the findings 'along the proper matrix.'").

In *Miles*, the First Circuit quoted its decision in *Williams v. Poulos*, which has particular relevance to this case. *Id.* at 66–67. *Williams* stated:

> [I]t is not ordinarily the province of appellate courts to make findings of fact or to resolve, in the first instance, mixed questions of law and fact. *Yet, where only one resolution of a predominantly fact bound question would, on a full record, be sustainable, courts of appeals can, and often should, decline to remand where there has been an error committed*.
>
> *Williams v. Poulos*, 11 F.3d 271, 280–81 (1st Cir. 1993) (emphasis added).

Miles has been followed by this Court. When the Court is "sufficiently informed as to the district court's rationale, and the record contains undisputed facts which support the court's ruling, a remand for findings of fact and conclusions of law is unnecessary." *Silver Star Enters. v. M/V Saramacca*, 19 F.3d 1008, 1014 n. 11 (5th Cir. 1994) ("stating that a remand for failure to comply with Fed. R. Civ. P. 52(a) is not required if a complete understanding of the issues may be had without the aid of separate findings").

Clearly, a remand would be futile because, as a matter of law, the very claims that formed the basis of the involuntary petition were indeed subject to a bona fide disputes as of the date of the filing of the involuntary petition. Moreover, the fact that the Fee Order was vacated subjects the Appellants' claims to a bona fide dispute, at least as to amount.

Because the Fee Order was vacated, none of the district court's findings of fact and conclusions of law relating to the Fee Order should be determinative of whether there is a bona fide dispute for purposes of a subsequent proceeding under Section 303 of the Bankruptcy Code. At most the district

court's findings would be collateral estoppel as to the amount of the claims *before* taking into account any offsets or counterclaims, the existence of which were most definitely acknowledged by the district court when it originally entered the Fee Order. (ROA.1417). That the district court said that Baron could not bring such claims until after the conclusion of the receivership does not lessen the genuineness of the claim. Moreover, this Court recognized the disputed nature of the claims in its *Netsphere* opinion. *See* 703 F.3d at 306 ("the receivership was deemed imposed for unresolved claims").

The Appellants argue that in the receivership proceeding where the district court heard evidence on the Appellants' claims that collateral estoppel establishes there is no bona fide dispute for purposes of Section 303(b). This is because the district court found the evidence to be essentially uncontroverted. (ROA.1413–15). To apply collateral estoppel in such a circumstance requires the Court to ignore the exact nature of the receivership proceeding.

A receivership action is an action *in rem*. *Sumrall v. Moody*, 620 F.2d 548, 550 (5th Cir. 1980). The fees established during the hearing on the Fee Order related to a proceeding where the Court was applying rules of equity and conducted a summary proceeding. (ROA.1401–02). Any rulings did not establish Baron's personal liability to the Appellants. *See Shaffer v. Heit-*

ner, 433 U.S. 186, 199 (1977). Where an action is *in rem*, orders establishing rights over property are not binding *in personam*. *Id.* Moreover, there is no *in personam* preclusive effect to the Fee order. *See Hoxsey v. Hoffpauir*, 180 F.2d 84, 87 (5th Cir. 1950).

That the evidence supporting the district court's Fee Order may have been uncontroverted cannot establish, through principles of collateral estoppel, that there was no bona-fide dispute as to the amount of the debt. This was properly recognized by the district court in reversing the Order for Relief. *See Baron*, 2014 WL 25519, at *13.

Finally, the existence of a counterclaim or offset to the Appellants' claims, renders the claim subject to a bona fide dispute as to the amount of the claim. *See Credit Union Liquidity Serv., L.L.C. v. Green Hills Dev. Co. (In re Green Hills Dev. Co.)*, 741 F.3d 651, 660 (5th Cir. 2014). Therefore, as a matter of law, a remand would be futile; the district court was correct in ordering dismissal of the involuntary case, something the bankruptcy court should have done after Baron filed his motion to dismiss.

2. *The Appellants' filing of an involuntary petition violated the district court's injunction & delayed the wind-down of the receivership, contrary to this Court's opinion in* **Netsphere v. Baron**

The involuntary petition should never have been filed during the receivership without leave of the district court. The Appellants were enjoined from doing so by the very order that established the receivership. During

the pendency of the receivership, all other persons and entities were stayed from:

> 1. Commencing, prosecuting, continuing, entering, or enforcing any suit or proceeding. . . .
>
> 3. Executing, issuing, serving or causing the execution, issuance or service of, any legal process including, but not limited to, attachments, garnishments, subpoenas, writs of replevin, writs of execution, or any other form of process whether specified in this Order or not; and
>
> 4. Doing any act or thing whatsoever to interfere with the Receiver taking custody, control, possession, or management of the assets or documents subject to this receivership, or to harass or interfere with the Receiver in any way, or to interfere in any manner with the exclusive jurisdiction of this Court over the assets or documents of the Receivership Party.

(ROA.6935–36).

Clearly, by initiating an involuntary bankruptcy proceeding, seeking the appointment of an interim trustee, and ultimately seeking an order for relief, the Appellants violated the district court's order in an attempt to assert control of the receivership asserts.

There is no absolute right for a creditor to file an involuntary petition in bankruptcy, particularly in light of a federal court receivership. Creditors may be enjoined from seeking relief in bankruptcy courts. *See S.E.C. v. Byers*, 609 F.3d 87, 91–92 (2nd Cir. 2010) (noting such authority should be exercised sparingly); *see also Liberte Capital Group, LLC v. Capwill*, 462 F.2d 543, 551–52 (6th Cir. 2006); *S.E.C. v. Wencke*, 622 F.2d 1363, 1369, 1371

(9th Cir. 1980) (the power of federal courts to issue stays does not depend on specific congressional authorization or the Bankruptcy Code); *but see Gilcrest v. General Elec. Capital Corp.*, 262 F.3d 295, 300–01 (4th Cir. 2001) (injunction prohibiting the filing of an involuntary bankruptcy cannot be enforced against nonparties).

While *Netsphere* required the receivership to be expeditiously wound-down, the mere filing of the involuntary petition interfered with the receivership. *See* 11 U.S.C. § 362(a) ("a petition filed under section . . . 303 . . . of this title . . . operates as a stay . . ."); *see also Gilcrest*, 262 F.3d at 303–04 (the automatic stay under the Bankruptcy Code stays federal court receiverships).

The fact that an involuntary bankruptcy was filed before the wind-down of the receivership actually interfered with the receivership and prevented the district court from carrying out this Court's mandate for almost a year while the Appellants were prosecuting their involuntary petition and Baron was appealing the same. Only because the Appellants have been

unable to obtain a stay pending appeal, has the district court been able to begin the process of winding down the receivership.[9]

By ignoring the effect of injunction, the bankruptcy court erred when it failed to dismiss the case after Baron filed his motion to dismiss.

B. Because he was under an invalid receivership for two years, Baron was not insolvent within the meaning of Section 303(h)

While not part of the district court's analysis in *Baron v. Schurig*, the bankruptcy court erred in discounting the effect of the receivership on Baron's ability to pay his debts as they came due for over the approximately two years of the receivership. The court instead reasoned that the receivership assets that exceeded the amount of the Appellants' claims and the history of the case warranted a finding that Baron was insolvent under Section 303(h). (ROA.4396).

After setting aside the partial summary judgment, the district court did not consider the other issues in Baron's original appeal of the Order for Relief. The court stated, "The court's determination regarding the Order for Relief moots the parties' remaining grounds for relief and contentions."

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[9] On January 6, 2014, the district court entered an order directing the Receiver to take steps to wind-down the receivership and to file a final accounting and application for payment by March 7, 2014, or alternatively, to file a status report as to when the Receiver believes the receivership may be terminated. Currently, the court is taking the Receiver's final report and final fee application and the parties' various objections under advisement.

Baron, 2014 WL 25519, at *16. This was an issue that was fully briefed by Baron in the district court. (ROA.6770–72).

Nevertheless, the insolvency element under Section 303(h) is where the Appellants' case disintegrates. *See* 11 U.S.C. § 303(h)(1) ("debtor is generally not paying [his] debts as such debts become due unless such debts are subject to bona fide dispute"). The insolvency element was tried by the bankruptcy court in an abbreviated evidentiary hearing where the court considered written declarations and cross-examination of select witnesses. The bankruptcy court found that the Appellants satisfied this element, and it was one of the issues on appeal. *See Baron*, 2014 WL 25519 at *12. It was fully briefed by Baron. (Ex. E). Yet, in reversing the order for relief, the district court exclusively focused on the standing requirement under Section 303(b) and did not analyze the second element under Section 303(h). *See Baron*, 2014 WL 25519, at *16.

Because this error was properly preserved,[10] this Court, in conducting a *de novo* review of the lower courts' legal conclusions may certainly determine whether the bankruptcy court's findings under Section 303(h) were clearly erroneous. *See Booking v. General Star Mgmt. Co.*, 254 F.3d 414, 418–19 (2nd Cir. 2001) ("It follows that we have discretion to consider issues

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[10] *See Baron*, 2014 WL 25519, at *12.

that were raised, briefed, and argued in the District Court, but that were not reached there."). If this Court makes such a determination, the Appellants would not be entitled to a remand to retry their standing issues—it would be futile.

In determining insolvency under Section 303(h), the Court should examine the totality of the circumstances, balancing the interests of the debtor with those of the petitioning creditors. *Bartmann v. Maverick Tube Corp.*, 853 F.2d 1540, 1546 (10th Cir. 1988); *see also In re Norris*, 456 B.R. 437, 456 (Bankr. W.D. La. 1995) (identifying 4 factors many courts consider). Moreover, this determination as of the petition date. *Bartman*, 853 F.2d at 1546. In this case, that was the same day as this Court issued the *Netsphere* opinion—actually within two hours.

Insolvency under Section 303 is established when either:

1. the debtor is generally not paying such debtor's debts as such debts become due unless such debts are the subject of a bona fide dispute as to liability or amount; or
2. within 120 days before the date of the filing of the petition, a custodian . . . was appointed or took possession.

11 U.S.C. § 303(h).

Moreover, insolvency is determined as of the date of the filing of the involuntary petition. *Subway Equip. Leasing Corp. v. Sims (In re Sims)*, 994 F.2d 210, 222 (5th Cir. 1993). It is not determined at some earlier point.

The receiver was first appointed November 24, 2010. *Netsphere*, 703 F.3d at 304. The involuntary petition was not filed until some two years later. (ROA. 58–59, 6080). Therefore, insolvency may not be proved merely because a receivership had been in place for more than 120 days.[11] *Cf. In re Pallet Reefer Co.*, 233 B.R. 687, 691–92 (Bankr. E.D. La. 1999) (liquidator appointed less than 120 days before the filing of the involuntary petition). Moreover, the presumption of insolvency that occurs when a person is under receivership should not apply after 120 days. Nor should it apply when the receivership is determined to be invalid.

Yet curiously, the bankruptcy court found that the existence of a receivership for more than 120 days should matter in the determination of insolvency. (ROA.4396). This Court's December 18, 2012 determination that the receivership was invalid and the ultimate issuance of its mandate on April 19, 2013[12] does not allow a party to restart the clock under Section 303(h)(2).

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[11] "The legislative history observes that 'once a proceeding to liquidate assets has been commenced, the debtor's creditors have an *absolute right* to have the liquidation (or reorganization) proceed in the bankruptcy court and under bankruptcy laws with all of the appropriate creditor and debtor protections that those laws provide.'" *In re Colonial Ford, Inc.*, 24 B.R. 1014, 1021 n. 14 (Bankr. D. Utah 1982) (quoting H.R. Rep. No. 95-595, 95th Cong., 1st Sess. 220 (1977)). It stands to reason that when a receivership over substantially all of a debtor's assets has been in place for more than 120 days, the creditors should not be allowed to force a change in the forum or the controlling law.

[12] ROA.4384.

So, for over two years prior to the filing of the involuntary petition in Baron's case, Baron was still under a receivership, with all of his assets outside his control. In other words, on the petition date, Baron could not have paid the Appellants' alleged claims unless he wanted to be in contempt of court.[13] The decision to pay Baron's debts was firmly in the control of the Receiver and the district court on the date of the filing of the involuntary petition.[14] Therefore, as a matter of law, the Appellants did not prove, nor can they prove on remand, the insolvency element under Section 303(h).

In short, the district court was correct in ordering dismissal of the involuntary bankruptcy case against Baron.

[13] Baron was enjoined from, among other things: (1) "Transacting any of the business of the Receivership Party;" (2) Transferring, receiving, altering, selling, encumbering, pledging, assigning, liquidating, or otherwise disposing of any assets owned, controlled, or in the possession or custody of, or in which an interest is held or claimed by, the Receivership Party or the Receiver." (ROA.6932–33). "Receivership Party" was defined as Baron and various business entities. (ROA.6924).

[14] The district court also entered various stays prohibiting the enforcement of the Fee Order, pending final resolution of the *Netsphere* appeal. Due to the filing of the involuntary petition the Fee Order continues to be stayed. Moreover, the receivership estate had more assets than the amount allegedly due to the Appellants.

II.

Appellants' alternative argument that the record supports a finding that their claims were not subject to a bona fide dispute requires a distorted application of collateral estoppel

The Appellants correctly recite their statutory burden as petitioning creditors in pages 26–26 of their merits brief. However, they misstate the amendment to Section 303(b)(1) that occurred as a result of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005.[15] By inserting "as to liability *or amount*," counterclaims and offsets may make a claim disputed as to amount when no bona fide dispute existed under the prior law. *See Green Hills Dev. Co.*, 741 F.3d at 660.

The Appellants argue that their claims are not subject to a bona fide dispute because the testimony in the district court leading up to the entry of the Fee Order was undisputed. (ROA.1413–15). To apply collateral estoppel in such a circumstance requires the Court to ignore the exact nature of the receivership proceeding.

This Court has held that the offensive use of collateral estoppel cannot be used where the underlying order was interlocutory and subject to being modified or vacated. *See Avondale Shipyards, Inc. v. Insured Lloyd's*, 786 F.2d 1265, 1270 (5th Cir. 1986). This is because the trial court continues to have

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[15] Pub. L. No. 109-8, § 1234, 119 Stat. 23 (2005).

the plenary power to alter its order, in its sound discretion, without having to satisfy the requirements of Rule 60(b) of the Federal Rules of Civil Procedure, governing the modification of final orders. *Id*. at 1269.

When the district court vacated the Fee Order, any claims that the Appellants could rely on as collateral estoppel for the hearing on the Fee Order vanished. *Harris Trust and Sav. Bank v. John Hancock Mut. Life Ins. Co.*, 970 F.2d 1138, 1146 (2nd Cir. 1992) (a vacated order has no collateral estoppel effect). The district court closed the door on further attempts by the Appellants to spin some sort of preclusive effect regarding the lack of a bona fide dispute.

Moreover, as discussed on page, 18, *supra*, the fact that the Fee Order arose from a proceeding *in rem*, findings made in the receivership case cannot be collateral estoppel in an involuntary bankruptcy, which is an *in personam* proceeding. *Shaffer*, 433 U.S. at 199 (where an action is *in rem*, orders establishing rights over property are not binding *in personam*).

Finally the Fee Order should not preclude evidence of a bona fide dispute because it is clear that Baron was not represented during the hearing in which the district court heard evidence regarding the fee order. "A fundamental requirement of due process is 'the opportunity to be heard.' . . . It is an opportunity which must be granted at a meaningful time and in a meaningful manner." *See Armstrong v. Manzo*, 380 U.S. 545, 552 (1965) (in-

ternal citation omitted) (biological father prevented from participating in adoption case). In the proceedings where the Receiver sought entry of the Fee Order, the right to be heard was severely lacking.

III.

The Court should not sanction a judicially-created "special circumstances" exception to the strict requirements of Section 303 of the Bankruptcy Code

The Appellants' argument that that the judicially-created special circumstances exception to the statutory requirements for standing under Section 303(b) should be employed is something that should not be endorsed or condoned by this Court. The applicable standing requirements are clear:

> An involuntary case against a person is commenced by the filing with the bankruptcy court of a petition under chapter 7 or 11 of this title—
>
> (1) by three or more entities, each of which is either a holder of a claim against such person that is not contingent as to liability or the subject of a bona fide dispute as to liability or amount, or an indenture trustee representing such a holder, if such noncontingent, undisputed claims aggregate at least $15,325 more than the value of any lien on property of the debtor securing such claims held by the holders of such claims.[16]
>
> 11 U.S.C. § 303(b).

[16] Subsections 2–4 would not apply in this case as Baron did not have fewer than 12 creditors, excluding employees or insiders, described in Section 303(b)(1); he was not a partnership; nor was he involved in a foreign bankruptcy. *See* 11 U.S.C. §§ 303(b)(2), 303(b)(3), 303(b)(4).

The Bankruptcy Court for the Northern District of Texas first adopted the special circumstances exception to the standing requirement under Section 303(b) in *Norriss Bros. Lumber Co., Inc.* 133 B.R. 599, 609 (Bankr. N.D. Tex. 1991) (holding arguable fraudulent conveyances and arguable preferential transfers constitute special circumstances). In doing so, it relied on a series of cases from bankruptcy or district courts in Wisconsin, Ohio, New York, Nevada, and Colorado as well as a Sixth Circuit opinion,[17] stating that these Courts "have suggested the three creditor requirement may not be applicable in the event of trick, artifice, scam, or fraud." *Id.* at 608–09. The special circumstances exception has also been applied in the Northern District of Texas in two other reported decisions. The first is *In re Moss*, where the court found special circumstances in the case of alleged fraudulent transfers, failure to comply with a turnover order, an inability to explain the loss of significant sums of money, and an inability to identify the whereabouts of certain monies and assets. 249 B.R. 411, 424 (Bankr. N.D. Tex. 2000). The second is *In re Smith*, where special circumstances were found in the case of the transfer of the debtor's assets to an offshore trust with a spendthrift provision at the time a summary judgment was obtained

[17] *Concrete Pumping Serv., Inc. v. King Constr. Co. (In Concrete Pumping Serv., Inc.)*, 943 F.2d 627, 630 (6th Cir. 1991) (upholding an order for relief in a bankruptcy case where there was a single petitioning creditor and the debtor owed one debt due to likelihood of fraud, artifice, and/or scam).

by a creditors. 437 B.R. 817, 825 (Bankr. N.D. Tex. 2010). Neither *Norriss Bros. Lumber Co.*, *Moss*, or *Smith* were appealed, and this Court has never decided a reported case involving the special circumstances exception.

Despite these three cases from the Northern District of Texas, this Court has never been presented with an opportunity to express an opinion on this judicially-created exception to Section 303(b).

Outside the Northern District of Texas, the special circumstances exception has certainly been criticized. For example, in *In re Rothery*, the Ninth Circuit Bankruptcy Appeals Panel held "there is no exception to the requirement that an involuntary petition be joined in by at least three petitioners where the alleged debtor has 12 or more creditors." 211 B.R. 929, 934 (B.A.P. 9th Cir. 1997), *rev'd on other grounds*, 143 F.3d 546 (9th Cir. 1998). The Sixth Circuit has allowed a single creditor to maintain an involuntary petition when there is evidence of "'fraud, artifice, or scam.'" *Concrete Pumping Serv., Inc. v. King Constr. Co. (In Concrete Pumping Serv., Inc.)*, 943 F.2d 627, 630 (6th Cir. 1991). However, it later declined to extend such an exception then there is more than one creditor. *AZUR-US, Inc. v. DBH Ltd., Inc.*, No. 99-5970, 2000 WL 1478392, at *2 (6th Cir. Oct. 4, 2000) (not designated for publication). The most recent case to analyze a "special circumstances" exception is *In re Colon*, which determined that such an exception may only apply in cases where there is a single creditor and declined to ex-

tend it to the insolvency element under Section 303(h). 474 B.R. 330, 390 (Bankr. D. P.R. 2012).

While the present case involves one class of petitioning creditors with similar claims, there is certainly more than one petitioning creditor. Moreover, other deviations from the express standing requirements under Section 303(b) should not be allowed merely because the Appellants have suggested that they fear Baron might transfer his assets beyond the jurisdiction of this court. Such suggestions are not grounds for any such exceptions, especially when this Court has said there is no such evidence. *See Netsphere*, 703 F.3d at 308 ("We do not, though, find evidence that Baron was threatening to nullify the global settlement agreement by transferring domain names outside the court's jurisdiction.").

Creating such exceptions to the Bankruptcy Code's requirements is fraught with problems. This is especially true in an involuntary bankruptcy case where the mere filing of the petition creates the estate and imposes the automatic stay; therefore, the Bankruptcy Code and Rules provide "'numerous requirements and restrictions to curtail misuse and to insure that the remedy is sought only in appropriate circumstances.'" *Id*. at 361 (quoting Hon. Nancy C. Dreher & Hon. Joan N. Feeney, *Bankruptcy Law Manual*, § 14:2 (5th ed. 2011)). This Court should not add a fourth subsection to 11

U.S.C. § 303(b) when Congress did not legislate a "special circumstances" exception. Such judicially-created doctrines are inappropriate.

The most recent prohibition of such practice is in *Law v. Siegel*, where a unanimous Supreme Court held that a bankruptcy court had no statutory authority to impair or "surcharge" a debtor's property exemptions he is entitled to under the Bankruptcy Code. __ U.S. __, 134 S.Ct. 1188, 1195–96 (2014) ("The Code's meticulous—not to say mind-numbingly detailed—enumeration of exemptions and exceptions to those exemptions confirms that courts are not authorized to create additional exceptions.").

Accordingly, this Court should not endorse such a judicially-created expansion of Section 303 of the Bankruptcy Code.

Conclusion & Prayer

As shown above, the district court was correct in ordering dismissal of the involuntary bankruptcy case and remanding only the issue of attorneys' fees. This is because any further proceedings to determine whether the Appellants allegedly have standing under Section 303(b) would be futile. As a matter of law, the Appellants can not defeat the fact that this Court recognized the existence of a bona fide dispute, and that the claims Baron has against the Appellants creates a bona fide dispute at least as to the amount of the Appellants' claims. Moreover, the Appellants' filing of

an involuntary petition violated the district court's injunction and delayed the wind-down of the receivership, contrary to this Court's opinion in *Netsphere*.

The Court should not countenance the Appellants offensive use of collateral estoppel, especially in light of the fact that the receivership was found by this Court to be invalid, the Fee Order was interlocutory, the Fee Order was stayed, Baron was deprived of the right to paid counsel during the evidentiary hearing, and, most important, the Fee Order has been vacated by Judge Lindsay pursuant to the January 2, 2014 opinion in *Baron v. Schurig*.

Finally, this Court should not sanction a judicially-created "special circumstances" exception to the strict requirements of Section 303 of the Bankruptcy Code. In short, the Appellants should not be allowed to thumb their noses at this Court or the district court, or call for judicially created exceptions to section 303 of the Bankruptcy Code.

WHEREFORE, for the foregoing reasons, Jeffrey Baron requests this Court uphold the district court's judgment reversing the order for relief.

Respectfully Submitted,

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CERTIFICATE OF SERVICE

The undersigned certifies that the original of the Appellee's Brief was electronically filed with the Clerk of the United States Court of Appeals for the Fifth Circuit using the Appellate CM/ECF system. Accordingly, counsel who have entered an appearance in this case and are registered Appellate CM/ECF users will be served electronically by the Appellate CM/ECF system through their registered e-mail addresses.

The undersigned further certifies that a true and correct copy of this Appellants' Brief was served on counsel who do not participate in the Appellate CM/ECF system by courier in accordance with Fed. R. App. P. 25 and 5TH CIR. R. 25 on this 27th day of May 2014.

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CERTIFICATE OF COMPLIANCE WITH RULE 32(A)

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1. This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because this brief contains 7,972 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

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