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Business Bankruptcy Case Developments

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Withdrawal of the Reference Does Not End the Bankruptcy Court's Docket Control.
Powers v. Stomberg (In re S. Luxury Motorcars, LLC), 2022 WL 2719732 (Bankr. S.D. Tex. May 31, 2022) (Norman, J.)

The bankruptcy court recommended withdrawal of the reference in an adversary proceeding involving *mostly* state law claims for conversion, unjust enrichment and breach of fiduciary duty (there was also a claim for turnover under 11 U.S.C. § 542(a)). The court found no evidence of forum shopping by the movant and no prejudice to either party by a withdrawal of the reference. In recommending withdrawal of the reference, the bankruptcy court reiterated that it "stands willing and ready to resolve any pre-trial matters including dispositive motions."

Considerations for Permissive Abstention Under 28 U.S.C. § 1334(c)(1)
Viper Prods. & Servs., LLC v. Diamondback E&P LLC (In re Viper Prods. & Servs., LLC), No. 21-50187-RLJ11V, 2022 WL 2707879 (Bankr. N.D. Tex. July 11, 2022) (Jones, J.)

Diamondback is an upstream oil and gas company, which entered into an agreement with Viper, an oilfield equipment provider and servicer. After learning that Viper may have violated the parties' agreement by, among other things, fraudulently billing Diamondback for work performed for Viper's president, Diamondback notified Viper that it would conduct an audit of the parties' transactions.

Diamondback refused to pay Viper until the audit was complete. Viper, however, refused to allow an audit and sued Diamondback for, among other things, breach of contract, suit on sworn account, quantum meruit, and promissory estoppel. A few months later, Viper filed a voluntary chapter 11 petition and removed the state court lawsuit to the bankruptcy court.

Diamondback filed a proof of claim in Viper's bankruptcy case, asserting, among other things, claims for breach of contract and declaratory judgment. It also requested that the bankruptcy court permissively abstain from hearing the state court lawsuit and remand the case back to state court.

Under 28 U.S.C. § 1334(c)(1), bankruptcy courts may permissively abstain from hearing a case "in the interest of justice, or in the interest of comity with State courts or respect for State law." In making such determination, courts examine fourteen factors, although no factor is dispositive and the court may give greater weight to some factors compared to others.

In large part because Judge Jones concluded that the removed lawsuit included only non-core, state law claims, he held that abstention was warranted. His opinion provides a helpful reminder that it is the *substance*, rather than *form* of a claim that matters for abstention purposes—even though the resolution of Diamondback's claims would be part of the claims allowance process in the bankruptcy court, the claims themselves were state law causes of action. Thus, characterizing Diamondback's claim as core under 28 U.S.C. § 157(b)(2)(B)[1] did little to tip the scale in favor of retaining jurisdiction.

Judge Jones also found that only 28 U.S.C. § 1334 provided a jurisdictional basis for the removal (which weighed in favor of abstention) and both parties had waived their jury trial rights (which weighed against abstention). Notably, the Court also explained that if Viper was definitely intending to reorganize, the potential for a substantial recovery from Diamondback through the lawsuit would be "a critical factor favoring abstention or remand." However, in an earlier hearing, Viper's counsel indicated that Viper may seek to convert its case to chapter 7. The Court found that impact on the administration of Viper's estate would be minimal in chapter 7—it may impact the return to Viper's creditors, but not the *administration* itself. He found that the remaining factors were neutral.

All in all, Judge Jones found that the factors weighed in favor of abstention and remanded the case to state court.

[1] Listing as "core," the "allowance or disallowance of claims against the estate…"

Motion to Withdraw Reference Denied by District Court Following Bankruptcy Court Recommendation

Covia Holdings Corp. v. Sand Revolution II, LLC (In re Covia Holdings Corp.), No. 22-02260, 2022 Bankr. LEXIS 2062 (S.D. Tex. July 27, 2022) (Eskridge, J.)

The U.S. Bankruptcy Court for the Southern District of Texas considered the six *Holland*[2] factors in considering a motion for withdrawal of the reference. This adversary case dealt with a debtor that produced sand for oil and gas operations and its contract counterparty was a vendor that provided logistical services for sand delivery. The crux of the adversary proceeding related to a $15 million deposit made by the debtor to the defendant vendor and the debtor's demand for the return of the sum. The defendant argued that the Court should permissively withdraw the reference.

Holland outlines the six factors for determining whether a court should permissively withdraw the reference. Those factors are: (i) the presence of a jury trial; (ii) whether the proceeding is core or non-core; (iii) whether withdrawal would promote uniformity in bankruptcy administration; (iv) whether withdrawal would expedite the bankruptcy process; (v) whether withdrawal produces forum shopping and confusion; and (vi) whether withdrawal would foster a more economical use of the parties' resources. Of these factors, the Court explained that all but one of the factors supported denial of the motion to withdraw the reference, and that the fourth factor (whether withdrawal would expedite the bankruptcy process) was neutral since the bankruptcy court had already confirmed a plan in the main bankruptcy case. The bankruptcy court recommended that the motion to withdraw the reference be denied, and on July 27, 2022, the District Court adopted the recommendation.

District Courts Cannot Refer Bankruptcy Appeals to Magistrate Judges

S. Central Houston Action Council v. Oak Baptist Church (In re South. Central Houston Action Council), 38 F.4th 471 (5th Cir. 2022) (Jones, J.)

Central Care Integrated Health Services (the "Debtor") appealed an order granting summary judgment to Fountain of Praise, a church, in a breach of contract adversary proceeding from the Bankruptcy Court to the District Court. The District Court, however, reassigned the appeal to a magistrate judge under 28 U.S.C. § 636(c) at the request and with the consent of the parties. The magistrate judge affirmed the bankruptcy court's summary judgment order.

The Fifth Circuit found that the District Court improperly referred the bankruptcy appeal to a magistrate judge under existing Fifth Circuit precedent. Specifically, the Fifth Circuit previously held that 28 U.S.C. § 158 governs appeals from a bankruptcy court and the plain meaning of 28 U.S.C. § 158 only allows bankruptcy appeals to be taken in either (a) the District Court or (b) to a panel of bankruptcy judges.[3] If Congress intended its bankruptcy appellate scheme to include a referral to a magistrate judge, it would have done so. The Fifth Circuit thus vacated the magistrate judge's opinion and remanded the case to district court for further proceedings. On October 18, 2022, the magistrate judge issued a memorandum and recommendation that the District Court affirm the bankruptcy court's judgment in accordance with the Fifth Circuit's remand.

Remand Upheld under Class Action Fairness Act's Local Controversy and Home State Exceptions.

Stewart v. Entergy Corp., 35 F.4th 930 (5th Cir. 2022) (per curiam)

Following Hurricane Ida, certain individuals filed a class action lawsuit in Louisiana state court against Entergy Corporation and certain affiliates (collectively, "Entergy"), alleging that Entergy negligently designed, operated, and maintained a electricity transmission system that resulted in severe power outages. After Entergy removed the case to federal district court, upon request of the individuals the case was remanded back to state court. Though a remand order is typically non-appealable, actions removed under the Class Action Fairness Act ("CAFA") allow for appellate courts to accept an appeal filed within ten days of the remand order. Entergy timely filed an appeal challenging the court's CAFA jurisdiction under the local controversy and home state

[2] *Holland Am. Ins. Co. v. Succession of Roy*, 777 F.2d 992, 999 (5th Cir. 1985).
[3] *See Minerex Erdoel, Inc. v. Sina, Inc.*, 883 F.2d 781, 786 (5th Cir. 1988).

Title search: Business Bankruptcy Case Developments

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