U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS
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IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

IN RE:	§	
	§	
EOTL SYSTEMS, INC.,	§	**CASE NO. 03-31017-BJH-7**
	§	
	§	
Debtor.	§	
	§	
HIBERNIA BANK,	§	
	§	
Plaintiff,	§	**ADV. PRO. 03-3507-BJH**
- against -	§	
	§	
THE STRUCTURED ADVANTAGE, INC., JOHNNY K. WASHINGTON, and DANIEL A. FISHER,	§	
Defendants.	§	
	§	
WILLIAM CLAXTON and QUINLAN ANIMAL CLINIC, P.C., JOHNNY K. WASHINGTON, INC.,	§	
Intervenors	§	

Memorandum Decision and Order

On August 1, 2002, Hibernia Bank ("Hibernia") filed a petition in interpleader in the District Court, 296th Judicial District, Collin County, Texas ("State Court Action") naming as parties The Structured Advantage, Inc., ("TSA"), Johnny K. Washington ("Washington") and Daniel A. Fisher ("Fisher"). The State Court Action alleges that Hibernia is or may be subject to multiple liability with respect to two bank accounts in TSA's name because of potential rival claims by TSA, Fisher and Washington and that Hibernia is an innocent stakeholder with no interest in the accounts. Upon the filing of the State Court Action, Hibernia deposited approximately $75,000 with the clerk, representing the proceeds of the disputed accounts, and the petition asks that Hibernia be released

and discharged from all liability to the defendants with respect to the accounts and that it recover its attorneys fees.

TSA, Fisher and Washington answered the petition. Thereafter, William Claxton and Quinlan Animal Clinic, P.C. (collectively, "Claxton") intervened,[1] as did J. Washington Company, Inc. ("JWCO").[2]

On January 29, 2003, EOTL Systems, Inc. ("EOTL" or the "Debtor"), formerly known as TSA, filed a voluntary petition for relief under Chapter 11 in this Court. On April 16, 2003, the Debtor filed a notice of removal of the State Court Action, removing it to the United States District Court for the Eastern District of Texas.[3] Almost immediately, Washington and JWCO moved for remand or abstention with respect to the State Court Action, as did Claxton (the "Motions"). After removal, the action was referred to the United States Bankruptcy Court for the Eastern District of Texas, and the Debtor moved to transfer venue to this Court. On May 21, 2003, the motion was granted and the State Court Action was transferred to this Court, prior to rulings on the Motions,

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[1] The petition in intervention alleges that TSA and Fisher represented to Claxton that they were knowledgeable in tax laws and that they structured Claxton's business and prepared its tax returns in such a way as to obtain significant tax refunds, from which TSA and Fisher received a percentage. It further alleges that unbeknownst to Claxton, the tax scheme was unlawful, Claxton's refunds have been disallowed, and Claxton must return the refunds and pay further amounts to the IRS. It further alleges that some or all of the interpled funds are funds that TSA or Fisher received from Claxton. The petition alleges claims for violation of the Texas Deceptive Trade Practices Act, negligence, breach of warranty, constructive trust and a request for injunctive relief against release of the interpled funds.

[2] The petition in intervention by JWCO alleges that in January 2001, TSA contracted with JWCO for JWCO to provide certain services related to TSA's business, but that TSA breached the agreement and refused to pay sums owed in the approximate amount of $193,000. The petition seeks damages for breach of contract, interest, attorneys' fees, and the imposition of a constructive trust upon the funds which Hibernia has deposited with the Court.

[3] At the time the State Court Action was removed, it appears that there were several motions pending: (i) to strike the petitions in intervention, (ii) for expedited discovery, (iii) to consolidate the State Court Action with another which had been earlier filed by TSA against JWCO, Washington and others, and (iv) for summary judgment. It does not appear that there were rulings on these motions prior to the removal to federal court.

which are currently before the Court.

The Court heard argument on the Motions on October 28, 2003, but deferred its rulings pending the outcome of a motion by the Office of the United States Trustee to dismiss the Debtor's bankruptcy proceeding or convert it to Chapter 7. On November 5, 2003, the Court entered an order granting the U.S. Trustee's motion and converting the Debtor's case to one under Chapter 7. The Court requested that the Chapter 7 Trustee submit a written recommendation to the Court with respect to the Motions to remand, following which the Court would take them under advisement. On November 18, 2003, the Chapter 7 Trustee filed his written recommendation and the Court took the Motions under advisement.

The Parties' Arguments

Washington and JWCO have moved for abstention or remand. First, they argue that the Court *must* abstain under 28 U.S.C. § 1334(c)(2) because this is a non-core proceeding which is merely related to the bankruptcy case and adjudication of the State Court Action would deprive them of their right to a jury trial. In the alternative, they assert that discretionary abstention is appropriate under 28 U.S.C. § 1334(c)(1). Lastly, they argue that the Court should remand on equitable grounds pursuant to 28 U.S.C. § 1452(b). Claxton's motion is essentially a mirror image of the motion by Washington and JWCO.

The Debtor has opposed the Motions, arguing that since the bank accounts are in the Debtor's name, they are presumptively property of the estate which this Court must administer. It asserts that the interpleader is a core proceeding, since it concerns a determination of property of the estate. The Debtor argues that a ruling on the interpleader action assists in the liquidation of the estate, and the Debtor itself could have brought a turnover action seeking recovery of the disputed funds.

The Chapter 7 Trustee points out that the Debtor's own pleadings and proposed liquidating plan (filed while the Debtor was in Chapter 11) state that the primary assets of this estate are litigation claims. The Chapter 7 Trustee asserts that the estate has no liquid assets with which to pursue such litigation, which continues to proliferate. The Chapter 7 Trustee notes that there are few third-party, non-client trade creditors, and the Debtor's receivables are of questionable value, since the United States has filed a complaint against the Debtor and others seeking a permanent injunction under the Internal Revenue Code for promoting an abusive tax shelter and aiding and abetting understatements of tax liability, engaging in conduct subject to penalties under the Internal Revenue Code and unlawfully interfering with enforcement of the Internal Revenue Code.[4] The Trustee observes that the bankruptcy case may well serve no purpose as a means of recovery for non-insider, non-client creditors, and that if the Court does retain jurisdiction, it will only serve as a delay mechanism since it appears that some of the parties possess a right to a jury trial.

Analysis

Remand

Removal of a civil action to bankruptcy court is governed by 28 U.S.C. § 1452 which provides, as relevant here, that a party may remove any claim to the district court for the district where such claim is pending, if the district court has jurisdiction of such claim under section 1334 of title 28. It further provides that the court to which such claim is removed may remand it on any equitable ground. 28 U.S.C. § 1452. The removing parties bear the burden of establishing federal jurisdiction. *See Frank v. Bear Stearns & Co.*, 128 F.3d 919, 921-22 (5th Cir. 1997).

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[4] The Debtor attempted to remove the United States's action for injunctive relief to this Court, but on December 18, 2003, this Court ruled that the Notice of Removal must be stricken, since 11 U.S.C. § 1452(a) expressly prohibits the removal of claims "brought by a governmental unit to enforce such governmental unit's police or regulatory power."

Thus, the first question is whether this Court has jurisdiction over the claims asserted in the State Court Action under 28 U.S.C. § 1334. In addition to "cases under title 11," which refers to the original bankruptcy petition and is not at issue here, section 1334 lists three types of proceedings over which the court has jurisdiction – those "arising under title 11," those "arising in" a case under title 11, and those "related to" a case under title 11. *See Wood v. Wood (In re Wood)*, 825 F.2d 90, 92 (5th Cir. 1987).[5] Claims that "arise under" or "arise in" a bankruptcy case are "core" matters. *WRT Creditors Liquidation Trust v. C.I.B.C. Oppenheimer Corp.*, 75 F.Supp. 2d 596, 606 (S.D. Tex. 1999). Claims that "relate to" a bankruptcy case, but do not arise under the Bankruptcy Code or arise in a bankruptcy case are "non-core" matters. *Id.*

"Arising under" jurisdiction involves causes of action created or determined by a statutory provision of title 11. *Wood*, 825 F.2d at 96. "Arising in" jurisdiction is not based on a right expressly created by title 11, but is based on claims that have no existence outside bankruptcy. *Id.* at 97. "Related to" jurisdiction exists if "the outcome of that proceeding could *conceivably* have any effect on the estate being administered in bankruptcy." *Celotex Corp. v. Edwards,* 514 U.S. 300, 307 n. 6 (1995); *In re Wood*, 825 F.2d at 93. The Fifth Circuit has further stated that "an action is related to bankruptcy if the outcome could alter the debtor's rights, liabilities, options or freedom of action (either positively or negatively) and . . . in any way impacts upon the handling and administration of the bankrupt estate." *Feld v. Zale Corp. (In re Zale Corp.)*, 62 F.3d 746, 753 (5th Cir. 1995) (internal citations omitted).

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[5] The Fifth Circuit has held that "[f]or the purpose of determining whether a particular matter falls within bankruptcy jurisdiction, it is not necessary to distinguish between proceedings 'arising under,' 'arising in a case under,' or 'related to a case under,' title 11. These references operate conjunctively to define the scope of jurisdiction. Therefore, it is necessary only to determine whether a matter is at least 'related to' the bankruptcy." *Wood,* 825 F.2d at 93. The distinction is relevant, however, for determining whether a proceeding is core or non-core.

Proceedings "related to" the bankruptcy "include . . . suits between third parties *which have an effect on the bankruptcy estate.*" *Celotex*, 514 U.S. at 308 n. 5 (citing 1 *Collier on Bankruptcy* ¶ 3.01[1][c][iv], at 3-28 (Lawrence P. King ed., 15th ed. 1994)) (emphasis added). Regarding third-party actions, the Fifth Circuit noted that the:

> large majority of cases reject the notion that bankruptcy courts have 'related to' jurisdiction of third-party actions. Those cases in which courts have upheld 'related to' jurisdiction over third-party actions do so because the subject of the third-party dispute is property of the estate, or because the dispute over the asset would have an effect on the estate. Conversely, courts have held that a third-party action does not create 'related to' jurisdiction when the asset in question is not property of the estate and the dispute has no effect on the estate.

Zale, 62 F.3d at 753 (internal citations and footnotes omitted).

The Court concludes that it has jurisdiction over the State Court Action and that it was therefore properly removed, since it is undisputed that the bank accounts which are the subject of dispute are in the Debtor's name and may well be property of its estate. The Court agrees with the Debtor that this is a core proceeding,[6] and that, at a minimum, there is "related to" jurisdiction under section 1334.

Despite proper removal, however, the Court may still remand the case on any equitable ground. 28 U.S.C. § 1452(b). In deciding this issue, the Court will consider the following factors:

> (1) the duplication or uneconomical use of judicial resources;
> (2) whether remand will adversely affect the bankruptcy estate's effective administration;
> (3) whether the case involves questions of state law better addressed by state courts;
> (4) comity;
> (5) prejudice to the parties;
> (6) whether remand lessens the possibility of inconsistent results; and
> (7) whether the court where the action originated has greater expertise.

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[6] In addition, although no party has raised it, the Court also notes that under 28 U.S.C. § 1334(e), the court has exclusive jurisdiction of "all of the property, wherever located, of the debtor as of the commencement of such case, and of property of the estate."

See, e.g., Browning v. Navarro, 743 F.2d 1069, 1077 n. 21 (5th Cir. 1984) (analyzing the predecessor to §1452); *Horton v. Nacogdoches Indep. Sch. Dist.*, 81 F.Supp. 2d 707, 711 (E.D. Tex. 2000); *Gabel v. Engra, Inc. (In re Engra, Inc.)*, 86 B.R. 890, 896 (S.D. Tex. 1988). The Court will also consider:

> (1) the jurisdictional basis, if any other than 28 U.S.C. § 1334;
> (2) the degree of relatedness or remoteness of the proceeding to the main case;
> (3) the substance rather than the form of the asserted 'core' proceeding;
> (4) the feasibility of severing state law claims from core bankruptcy matters to allow judgment to be entered in state court with enforcement left to the bankruptcy court;
> (5) burden of the bankruptcy court's docket;
> (6) the likelihood that the commencement of the proceeding in bankruptcy court involves forum shopping by one of the parties; and
> (7) the presence of nondebtor parties.

See Horton, 81 F.Supp. 2d at 711.

In this case, equitable remand is appropriate. As all of the parties appear to be citizens of Texas and no federal question is involved, there does not appear to be any basis for federal jurisdiction other than section 1334. State law issues predominate, since the determination of the parties' entitlement to the funds will turn on the resolution of claims for violation of the Texas Deceptive Trade Practices Act, negligence, breach of warranty, constructive trust, and breach of contract. There are several non-debtor parties involved in this action. The Debtor itself is no longer the proper party to participate, as its case has been converted to Chapter 7 and the Chapter 7 Trustee is now the representative of the estate. As the Chapter 7 Trustee points out, the primary asset of this estate appears to be litigation, and the estate has no funds with which to pursue claims. Most of the debt in the case is owed to insiders. There is little non-insider unsecured debt that is owed, and more than half of it is owed to one entity for disputed fees. It appears to be a waste of judicial resources for the bankruptcy court to retain jurisdiction over state law claims when the estate's representative

is unable to pursue them and the non-debtor parties may well have rights to a jury trial. Therefore, remand will not adversely affect the estate's effective administration.

Abstention

The determination of whether to abstain is a core proceeding. 28 U.S.C. § 157(b)(2)(A). Under 28 U.S.C. § 1334(c)(2), the court must abstain if (i) a party to the proceeding has filed a timely motion to abstain; (ii) the proceeding is based on a state law claim; (iii) the proceeding is a "related to" proceeding; (iv) there is no basis for federal court jurisdiction other than section 1334; (v) an action was pending in state court; and (vi) the state court action can be timely adjudicated. *In re Engra, Inc.,* 86 B.R. at 894.

The Court does not believe that 28 U.S.C. § 1334(c)(2) is applicable, because it finds that this is a "core" proceeding. However, under section 1334(c)(1), a court may, in its discretion, abstain from deciding either core or non-core proceedings if the interests of justice, comity, or respect for state law so require. *Gober v. Terra Corp. (In re Gober)*, 100 F.3d 1195, 1206 (5th Cir.1996).

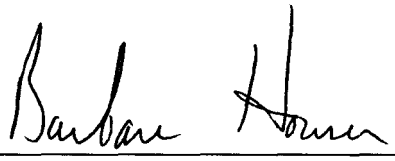
Courts have stated that the "starting point" in analyzing whether permissive abstention is appropriate is whether abstention "will impede or disrupt the bankruptcy court's 'exclusive and non-delegable control over the administration of the estate within its possession.'" *See Republic Reader's Serv., Inc. v. Magazine Serv. Bureau, Inc. (In re Republic Reader's Serv.)*, 81 B.R. 422, 426 (S.D. Tex. 1987) (quoting *Thompson v. Magnolia Petroleum Co.*, 309 U.S. 478, 483 (1940)). The Court may consider many of the same factors relevant to a determination of whether remand is appropriate, *Id.* at 429, and, for the reasons set forth above, the Court also concludes that permissive abstention is appropriate in this case.

For the foregoing reasons, the Motions are granted. The case is remanded on equitable

grounds, and the Court hereby abstains from hearing it pursuant to 28 U.S.C. § 1334(c)(1).

So Ordered.

SIGNED: January 12, 2004



Barbara J. Houser
United States Bankruptcy Judge