



ENTERED

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The following constitutes the order of the Court.

Signed September 1, 2005

United States Bankruptcy Judge

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

IN RE: §
§
VECTRIX BUSINESS SOLUTIONS, § CASE NO. 01-35656-SAF-11
INC., §
§
D E B T O R. §

MEMORANDUM OPINION AND ORDER

Mark Lynd moves the court for payment of \$65,000 from funds held by J. James Jenkins, trustee of the Vectrix Business Solutions Liquidating Trust. The trustee opposes the motion. The court conducted a hearing on the motion on July 26, 2005.

Lynd seeks payment based on his proof of claim. The trustee objected to the claim. The allowance and payment of a proof of claim constitutes a core matter over which this court has jurisdiction to enter a final order. 28 U.S.C. §§ 157(b)(2)(B) and 1334. This memorandum opinion contains the court's findings of fact and conclusions of law. Bankruptcy Rules 7052 and 9014.

Lynd had been the chief executive officer, president, and

chairman of the board of directors of Vectrix Business Solutions, Inc., the debtor. On November 11, 2001, Lynd filed a proof of claim, claim no. 84, for an unknown amount based on corporate indemnification obligations. On January 15, 2002, Jenkins became the trustee of the Vectrix Liquidating Trust pursuant to Vectrix's First Amended Plan of Liquidation. On February 19, 2003, the trustee filed an amended objection to Lynd's claim.

Lynd and Jenkins negotiated an interim agreement regarding the claim. On May 2, 2003, the court entered an agreed order. The court continued the objection to Lynd's claim indefinitely. The court directed the trustee to reserve \$75,000 to cover "any amounts that may be allowed for Claimant[] . . . Lynd [and two other claimants]." The court ordered that the trustee "not make payments at this time to Lynd [and the other two claimants] on the basis of their unresolved claims" without prejudice to Lynd's participation in future distributions and to his status as an insured under Vectrix's directors and officers insurance policy. The court held that "the Trustee [or] Lynd . . . may request a setting on the Objections" and that

Lynd [and the other two claimants] may seek the allowance of their claims in full, but in no instance would such claims receive total distributions in excess of the amount of the \$75,000 reserved by the Trust. The Trustee retains all rights to object to the claims filed by Lynd [and the other two claimants].

The trustee retained the \$75,000 pursuant to the agreed order. Other claims covered by the agreed order have been

resolved, with \$65,000 remaining in the reserve. But for this reserve, the Vectrix case has been fully administered and is ready to be closed. See 11 U.S.C. § 350.

On March 11, 2005, Lynd filed an amended proof of claim for \$65,000, based on corporate indemnifications for expenses for lawsuits based on his actions before July 29, 2001. Also on March 11, 2005, Lynd filed his motion for payment of the claim from the reserved funds.

Lynd asserts that his indemnification rights under the Vectrix articles of incorporation entitle him to recover his expenses to defend two lawsuits and to prosecute his proof of claim, as amended. The trustee objects to the claim for several reasons. The trustee asserts that Lynd has failed to document his legal fees and expenses; that the fees should be covered by the liability insurance policy of the Vectrix directors and officers; that the corporate indemnification does not cover the requested expenses; that the claim should be disallowed under 11 U.S.C. § 502(e)(1)(B); and that the claim should be subordinated under 11 U.S.C. § 510.

Article IX of the Vectrix articles of incorporation provides that Vectrix "shall indemnify any person" who has been named a party in a civil law suit "by reason of the fact that such person is or was a director, officer, employee or agent of [Vectrix]" for "all judgments, penalties, . . . fines, settlements and expenses (including attorneys' fees and court costs) actually and

reasonably incurred by such person in connection with such action, suit or proceeding to the fullest extent permitted by any applicable law." If expenses had not yet been actually incurred, the director or officer could seek an advance upon delivery to Vectrix of an undertaking. The bylaws provide that the indemnified person act "in good faith and in a manner the person reasonably believed to be in or not opposed to the best interest of [Vectrix]." Ex. 6, Certificate of Incorporation of Vectrix Business Solutions, Inc., Art. VIII, § 8.1.

Lynd claims attorney's fees and expenses of \$65,000 covered by these indemnification provisions for law suits brought against him for pre-bankruptcy activities and for representation in prosecuting his proof of claim. However, and curiously, Lynd did not contract for legal services related to the law suits or this bankruptcy case until March 2005. This was the only retainer agreement presented to the court. The contract provides for a \$65,000 retainer to be paid from the trustee's reserve. The trustee suggests that legal fees could not have been "actually . . . incurred" as required by the articles of incorporation for indemnification. Lynd did not post an undertaking to receive advances under the indemnification for costs not yet actually incurred.

Lynd has been named by reason of his director and officer position with Vectrix as a defendant in two law suits: Joann Panko v. Mark C. Lynd, case no. 03-02308, in the 95th Judicial

District Court, Dallas County, Texas, and Ferrer, et. al. v. Mark C. Lynd, case no. 04-5139, in the 134th District Court, Dallas County, Texas. The Vectrix directors and officers liability policy covered the Panko case. Lynd could have sought defense under the policy. His contract with counsel recognizes that coverage by limiting counsel's role to consultation with the insurance-provided defense counsel. The insurance policy fulfilled Vectrix's contractual indemnification obligation. As a result, Lynd did not "reasonably" incur Panko defense costs to be paid under the indemnification provision of the articles of incorporation.

The directors and officers policy does not extend to the Ferrer case. Lynd presented evidence of invoices received from counsel. The court has reviewed the invoices *in camera*. The attorney time records contain vague descriptions of the work performed, with only limited references to work actually performed in the Ferrer case, even though several invoices reference the Ferrer case in the invoice heading. The Ferrer suit was filed in July 2004. Lynd actually incurred legal fees for the Ferrer suit of \$240 on February 16, 2005, and \$210 on February 17, 2005. The invoices reflect no fees for the Ferrer suit thereafter. Consequently, the court finds that Lynd has actually incurred \$450 for the defense of the Ferrer case.

Lynd's attorneys aver that Lynd will ultimately incur

expenses between \$60,000 and \$100,000 to defend the lawsuit. Lynd testified that he has been invoiced for a total of \$34,000 for legal services related to the two lawsuits and the bankruptcy case. He estimated \$31,000 would be needed to resolve the Ferrer litigation. Lynd argues that the court may estimate his claim to allow the trustee to make the final distributions in the case and then close the case. See 11 U.S.C. § 502(c). The court may estimate claims to permit final distributions. Id. But other than counsel's averment, the court has no basis to estimate a claim of actual expenses of \$65,000 for the Ferrer suit. After thirteen months of litigation, Lynd has actually incurred only \$450 for that lawsuit. Lynd testified differently than his counsel concerning estimated remaining fees. The timing and terms of the March 2005 retention agreement suggest that Lynd has structured the retention to match the funds held by the trustee pursuant to the May 2, 2003, agreed order, thereby undermining counsel's averment of the estimated defense costs. Nevertheless, Lynd must defend the suit. The allegations of the suit fall within the indemnification agreement. Without evidence of the issues and pre-trial work and settlement efforts in the litigation, the court may only estimate a minimal cost. The court will estimate the indemnification amount at \$5,000.

The trustee argues that Lynd cannot establish that he acted in good faith as required by the Vectrix bylaws for indemnification. The trustee suggests that the allegations of

the Ferrer complaint imply a lack of bad faith. For purposes of this claims allowance process, the court considers that the defense of the suit falls within the indemnification ambit.

The trustee contends that any amount must be disallowed under § 502(e)(1)(B). That section provides:

Notwithstanding subsections (a), (b), and (c) of this section and paragraph (2) of this subsection, the court shall disallow any claim for reimbursement or contribution of an entity that is liable with the debtor on . . . the claim of a creditor, to the extent that - such claim for reimbursement or contribution is contingent as of the time of allowance or disallowance of such claim for reimbursement or contribution.

11 U.S.C. § 502(e)(1)(B). The concept of reimbursement includes indemnity. In re Wedtech Corp., 85 B.R. 285, 289 (Bankr. S.D.N.Y. 1988); see In re GCO Servs., LLC, 324 B.R. 459, 465 (Bankr. S.D.N.Y. 2002); In re Drexel Burnham Lambert Group, 148 B.R. 982, 985-86 (Bankr. S.D.N.Y. 1992). The co-liability requirement mandates a finding that the causes of action in the underlying lawsuit assert causes of action upon which, if proven, the debtor could be liable but for the automatic stay. Wedtech Corp., 85 B.R. at 290.

The Ferrer plaintiffs allege claims against Lynd under the Texas Blue Sky Act. See Ex. 3, Plaintiff's Original Petition 6 (alleging causes of action under Texas Revised Civil Statutes Art. 581-33(A) and 581-33 (f)(I)). Both Vectrix and its control persons, including Lynd, could be liable under that act. At the time of the filing of the bankruptcy case, both the debtor's and

Lynd's liability had been contingent. Under the Bankruptcy Code, Lynd's indemnification claim is considered a reimbursement or contribution claim. Berlinder Handels-Und Frank-Furter Bank v. E. Texas Steel Facilities, Inc. (In re E. Texas Steel Facilities, Inc.), No. Civ. A. 3:90-CV-2042-J, 2000 U.S. Dist. LEXIS 4106, at *11 (N.D. Tex. Mar. 30, 2000). Consequently, a claim by Lynd for indemnification for any liability in the Ferrer law suit would be disallowed under § 502(e)(1)(B).

But Lynd only seeks an indemnification claim for his attorney's fees incurred in defending the lawsuit. Vectrix would not be co-liable with Lynd to the Ferrer plaintiffs for Lynd's attorney's fees in the Ferrer suit. Vectrix would only be co-liable for Lynd's liability to the Ferrer plaintiffs on the merits of their securities law claim. Lynd's indemnification claim for attorney's fees is therefore not subject to § 502(e)(1)(B).

Lastly, the trustee contends that Lynd's claim should be subordinated to other unsecured creditors under 11 U.S.C. § 510(b) and (c). Lynd does not premise his claim on his position as an interest holder in the debtor nor on a security transaction. See 11 U.S.C. § 510(b). The trustee has not filed an adversary proceeding to establish the elements for equitable subordination under § 510(c). Fabricators, Inc. v. Technical Fabricators, Inc. (In re Fabricators), 926 F.2d 1458, 1464-65 (5th Cir. 1991); Benjamin v. Diamond (In re Mobile Steel Co.),

563 F.2d 692, 699-702 (5th Cir. 1977). Accordingly, the trustee has not established a basis to subordinate the claim.

Lynd also seeks indemnification recovery for his attorney's fees incurred in prosecuting his claim in this bankruptcy case. Lynd's bankruptcy-related expenses do not arise from expenses in a civil or criminal action brought against Lynd by reason of the fact that he had been a director or officer of Vectrix that he has actually and reasonably incurred in connection with that action. Lynd's bankruptcy-related expenses do not fall within the ambit of his indemnification rights under Vectrix's articles of incorporation. Lynd, like all unsecured creditors, may not recover his bankruptcy-related expenses. The Bankruptcy Code only provides for recovery of post-bankruptcy petition legal fees for over secured creditors. See 11 U.S.C. § 502(b). Lynd's claim for indemnification for his legal fees incurred in prosecuting his indemnification claim is disallowed.

Order

Based on the foregoing,

IT IS ORDERED that Mark Lynd's motion for payment of claim no. 84 is **GRANTED IN PART** and **DENIED IN PART**.

IT IS FURTHER ORDERED that Mark Lynd is allowed a general unsecured claim of \$5,000 to be paid by J. James Jenkins, trustee of the Vectrix Liquidating Trust, out of the \$65,000 held pursuant to the order entered on May 2, 2003.

IT IS FURTHER ORDERED that in all other respect Mark Lynd's claim is **DENIED**.

IT IS FURTHER ORDERED that the balance of the funds held by Trustee Jenkins pursuant to the order entered on May 2, 2003, are released from that order for use in the payment of administrative expenses and claims in this case.

###END OF ORDER###