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.	§	
	§	
THE STRUCTURED ADVANTAGE, INC. and DANIEL A. FISHER,	§	
	§	
Plaintiffs,	§	**ADV. PRO. 03-3480-BJH**
- against -	§	
	§	
J. WASHINGTON COMPANY, INC. JOHNNY K. WASHINGTON, CDJ INVESTMENTS, INC., JOHN DURHAM, MARY LOU MURCHISON, JUDGE DEAN, THAD TATUM, and HIBERNIA NATIONAL BANK,	§	
	§	
Defendants.	§	
	§	
WILLIAM CLAXTON and QUINLAN ANIMAL CLINIC, P.C.,	§	
	§	
Intervenors	§	

Memorandum Decision and Order

On July 24, 2002, The Structured Advantage, Inc. ("TSA") and Daniel A. Fisher filed a petition in the District Court, 219th Judicial District, Collin County, Texas ("State Court Action") against J. Washington Company, Inc. ("JWCO"), Johnny K. Washington, CDJ Investments, Inc., John Durham, Mary Lou Murchison, Judge Dean, Thad Tatum and Hibernia National Bank ("Hibernia") (collectively, the "Defendants"). The State Court Action generally alleges a breach of contract claim against JWCO and Washington, a claim for breach of a lease and unlawful exclusion of a tenant against CDJ, breach of contract against Hibernia, and a claim for tortious interference

against Washington.[1] The petition further seeks an accounting, and a temporary restraining order and temporary and permanent injunctive relief against the Defendants from taking any action with regard to TSA's bank accounts, computer files, client lists, proprietary information and other assets, including the deletion, destruction or copying of TSA's files and a cessation of all contact with TSA's clients by Defendants.

The Defendants answered the petition. Thereafter, William Claxton and Quinlan Animal Clinic, P.C. (collectively, "Claxton") intervened.[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] The Debtor also filed a motion to transfer venue to this Court. Almost immediately, Washington, JWCO, CDJ, Murchison and Dean moved for remand or

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[1] Broadly speaking, the petition alleges that TSA contracted with JWCO for JWCO to provide TSA with operating space, telephone and message services, and tax preparation services coupled with data entry and submission of tax returns to federal and state authorities, but that JWCO failed to adequately provide such services and double-billed TSA for the services it did provide. It further alleges that there was a proposed merger of TSA and JWCO, pursuant to which Washington acted as President of TSA and thereafter took several actions detrimental to TSA. IT alleges that Fisher and Washington formed CDJ for the purpose of buying a building which both TSA and JWCO would occupy, that CDJ purchased the building and JWCO and TSA are tenants, but that Washington, JWCO, CDJ and others thereafter improperly changed the locks, froze TSA's accounts, and prevented TSA from accessing its client files. It further alleges that the furniture, fixtures and computer equipment being used by JWCO are owned by TSA, and that employees of JWCO are making false statements to TSA's clients.

[2] 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 funds paid into court by Hibernia in its action in interpleader 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.

[3] At the time the State Court Action was removed, it appears that there was a motion pending to consolidate the State Court Action with an interpleader action which had been filed by Hibernia. It does not appear that there was a ruling on this motion prior to the removal to federal court.

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. On May 19, 2003, the motion to transfer venue was granted and the State Court Action was transferred to this Court, prior to rulings on the Motions, 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, JWCO, CDJ, Murchison and Dean 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 the State Court Action alleges that the Defendants have locked the Debtor out of its premises, are using equipment which is property of the

estate and denying the Debtor access to its books and records, and interfering with its customer relationships. It asserts that the State Court Action is a core proceeding, since it concerns the Debtor's attempt to preserve its assets and have its books and records turned over.

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

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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."

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).

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

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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.

(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).

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 involves attempts by the Debtor to recover assets which it alleges are property of its estate. The Court agrees with the Debtor that this is a core proceeding,[6] and, 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;

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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."

(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.

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 Debtor's right to a return of property which it alleges belongs to it will turn on the state law issues of breach of contract and breach of a lease. There are primarily 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 very little non-insider unsecured debt owed, and more than half of it is owed to one entity for disputed fees.

It appears to be a waste of judicial resources and a burden on this Court's docket for this 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 (Bankr. 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