The Automatic Stay

I. Effect and Purpose of the Automatic Stay

A. The automatic stay, codified in § 362(a) of the Bankruptcy Code, is one of the most essential safeguards provided by the Code. In re Enron Corp., 306 B.R. 465, 475 (Bankr. S.D.N.Y. 2004).

B. Although the automatic stay does not eliminate or liquidate any debt, it does function as an ex parte injunction. Hudson Valley Cablevision Corp. v. Route 202 Developers, Inc., 170 B.R. 798, 532 (S.D.N.Y. 1994). In other words, the automatic stay shields debtors from creditors' attempts to obtain money for a specified amount of time.

C. The automatic stay allows debtors to have "a breathing spell" from creditors, and it prevents creditors from dissecting the bankruptcy estate before the bankruptcy trustee can distribute the assets equally. Koolik v. Markowitz, 40 F.3d 567, 568 (2d Cir. 1994). The stay promotes an organized and systematic method for administration of the debtor's estate. In re Colonial Realty Co., 980 F.2d 125, 133 (2d Cir. 1992).

D. The automatic stay is construed broadly and any exceptions are construed narrowly. In re Enron Corp., 306 B.R. 465, 475 (Bankr. S.D.N.Y. 2004).

II. The Scope of the Automatic Stay

A. Section 362(a) of the Bankruptcy Code applies to all entities including persons, estates, trusts, and governmental units. 11 U.S.C. § 101(15)

B. "[A]ll legal and equitable interests of the debtor in property" as of the filing of the bankruptcy petition are covered by the automatic stay provision. See In re Lankford, 305 B.R. 297, 301 (Bankr. N.D. Iowa 2004). For example, the automatic stay generally applies to insurance policies. In re Adelphia Communs. Corp., 298 B.R. 49, 55 (S.D.N.Y 2003). However, if the debtor purchased the insurance policy after filing for bankruptcy, then the policy is not subjected to the automatic stay. In re Plexus Enter., 289 B.R. 778, 779 (Bankr. M.D. Fla. 2002).

C. In addition, if the debtor has an interest in an unexpired lease, it is considered property of the bankruptcy estate. In re Ames Dep't Stores, 287 B.R. 112, 127 n. 13 (Bankr. S.D.N.Y. 2002). In other words, evictions are stayed if the lease did not expire prior to the filing of the bankruptcy petition. See id; In re Village Rathskeller, Inc., 147 B.R. 665, 669 (Bankr. S.D.N.Y. 1992).

D. Upon the filing of a bankruptcy petition, a number of actions, including judicial proceedings, are automatically stayed. Eastern Refractories Co. v. Forty Eight Insulations, 157 F.3d 169, 172 (2d Cir. 1998). For example, the commencement or continuation of any lawsuits against the debtor is stayed. 11 U.S.C. § 362(a)(1)

E. The stay also prohibits the implementation, against a debtor, of a judgment acquired before the filing of the bankruptcy petition. 11 U.S.C. § 362(a)(2)

F. In addition, the automatic stay applies to foreclosure actions that were commenced before the debtor filed the bankruptcy petition. LaBarge v. Vierkant, 240 B.R. 317, 322 (B.A.P. 8th Cir. 1999).

G. Section 362(a) operates as an automatic stay of any act to acquire ownership of, or to exercise dominion over, property of the bankruptcy estate. 11 U.S.C. § 362(a)(3).

H. Any setoff against the estate's property is stayed. 11 U.S.C. § 362(a)(7).

I. The stay also prevents any act to create, perfect, or enforce a lien against the debtor's property. 11 U.S.C. § 362(a)(4).

J. Any action to obtain, asses, or recover a claim against the debtor that arose before the filing of the bankruptcy petition is stayed. 11 U.S.C. § 362(a)(6).

K. In other words, the automatic stay prevents any act that would negatively affect the property of the estate. 11 U.S.C. § 362(a).

L. According to §362(c) of the Bankruptcy Code, the automatic stay continues until one of the following occurs: (1) the case is closed; (2) the case is dismissed; or (3) the debtor is granted or denied a discharge. 11 U.S.C. §§ 350, 524, 707, 1112, 1307.

M. If any acts are taken prior to the termination of the automatic stay or in violation of it, those acts are void. In re Best Payphones, No. 01-15472, 2002 Bankr. LEXIS 1939, at *14 (Bankr. S.D.N.Y. June 24, 2002). A violation is punishable as contempt of court, and the violating party may be sanctioned. Ball v. A.O. Smith Corp., 321 B.R. 100, 109 (N.D.N.Y 2005).

III. Exceptions and Exclusions from the Automatic Stay

A. Section 362(b) of the Bankruptcy Code lists 28 exclusions and exceptions to the automatic stay. 11 U.S.C. §362(b)

B. If the debtor filed a bankruptcy petition within the last year or had a case dismissed, then the automatic stay may not apply. 11 U.S.C. §§ 362(b)(21), 109(g), 362(c)(3) and 362(d)(4).

C. Criminal proceedings can commence and continue without the automatic stay provision being violated. 11 U.S.C. § 362(b)(1); United States v. Colasuonno, 697 F.3d 164, 173 (2d Cir. 2012).

D. The automatic stay does not prevent child custody, visitation rights, and domestic violence proceedings from continuing. 11 U.S.C. § 362(b)(2). As long as a

divorce does not divide the bankruptcy estate's property, divorce proceedings are not stayed. Id.

E. Although the IRS cannot collect taxes when a debtor files a bankruptcy petition, the IRS may still perform tax audits, request tax returns, and assess taxes; the automatic stay does not apply to these acts. 11 U.S.C. §362(b)(9); see generally Richmond v. United States, 172 F.3d 1099 (9th Cir. 1999).

F. Civil litigation brought by the debtor may commence and continue without violating the automatic stay provision. Koolik v. Markowitz, 40 F.3d 567, 568 (2d Cir. 1994).

G. The automatic stay does not prevent governmental units from enforcing their police and regulatory powers. 11 U.S.C. § 362(b)(4). In other words, governmental entities are not prohibited from commencing or continuing an action against a debtor to enforce its police or regulatory power. In re Synergy Development Corp., 140 B.R. 958, 959 (Bankr. S.D.N.Y. 1992).

1. Examples of regulatory or police power include preventing fraud and protecting consumers, the environment, public health, public welfare, and public safety. Lockyer v. Mirant Corp., 398 F.3d 1098, 1109 (9th Cir. 2005).

2. An action brought under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 ("CERCLA") is not stayed; the purpose of CERCLA is to protect the public's health, safety and welfare. 11 U.S.C. § 362(b)(4); New York v. Mirant N.Y., Inc., 300 B.R. 174, 179 (S.D.N.Y. 2003).

3. For example, if the government brings an action to recuperate costs of cleaning up a toxic spill and to enforce civil fines against a Chapter 11 debtor in possession, then the government's action is not stayed. See United States v. Mattiace Industries, Inc., 73 B.R. 816 (E.D.N.Y. 1987).

4. However, the government may not merely seek to collect a debt; these pecuniary actions are not exempt from the automatic stay. S.E.C. v. Brennan, 230 F.3d 65, 71 (2d Cir. 2000).

5. In order to decide whether the government's lawsuit involves a pecuniary interest or a public policy interest, courts apply the pecuniary purpose test and the public policy test. United States ex rel. Fullington v. Parkway Hosp., 351 B.R. 280, 282-83 (E.D.N.Y 2006). The pecuniary test examines whether the purpose of the government's proceeding is to protect its financial interest as a creditor. Id. at 283. If that is the purpose of the proceeding, then the action is stayed. Id. The public policy test assesses whether the government's proceedings are intended to implement public policies or to adjudicate private rights. Id. Proceedings aimed to

implement public policies are not stayed; however, actions brought to adjudicate private rights are stayed. Id.

IV. Third Parties

A. Section 362(a)(1) of the Bankruptcy Code typically only applies to the debtor filing a bankruptcy petition. Reliant Energy Servs. v. Enron Can. Corp., 349 F.3d 816, 825 (5th Cir. 2003).

B. Co-debtors, including guarantors and affiliates, are not automatically protected by the stay, unless the debtor is a Chapter 12 or 13 debtor. 11 U.S.C. §§ 1201, 1301; In re Moore, 410 B.R. 439, 441 (Bankr. E.D. Va. 2009).

1. In a Chapter 12 or 13 bankruptcy case, there are limits on the co-debtor stay. Saleh v. Bank of Am., 427 B.R. 415, 422 (Bankr. S.D. Ohio 2010); In re Circle Five, Inc., 75 B.R. 686, 688 (Bankr. D. Idaho 1987). For example, the co-debtor stay does not protect a limited liability company or a corporation. Id. In addition, it only applies to consumer debt, which is defined as "debt incurred by an individual primarily for a personal, family, or household purpose." Morris v. Zabu Holding Co., 385 B.R. 823, 829 (E.D. Va. 2008); In re Circle Five, Inc., 75 B.R. 686, 688 (Bankr. D. Idaho 1987).

C. The automatic stay does not apply to the non-debtor officers, directors, stockholders, and principals of a debtor corporation. Gucci, Am. Inc. v. Duty Free Apparel, Ltd., 328 F. Supp. 2d 439, 441 (S.D.N.Y 2004). Collecting from the personal assets of the debtor's officers, directors, or stockholders does not negatively effect the debtor corporation. In re Nashville Album Productions, Inc., 33 B.R. 123 (M.D. Tenn. 1983).

D. The automatic stay typically does not protect co-defendants. Queenie, Ltd. V. Nygard Int'l, 321 F.3d 282, 287 (2d Cir. 2003). For example, if one defendant in a multiple defendant personal injury action files a bankruptcy petition, the personal injury action is stayed only for the debtor.

E. Courts will occasionally grant stay to a third party. In re Adelphia Communs. Corp., 298 B.R. 49, 54-55 (S.D.N.Y 2003).

1. The third party must demonstrate that he will likely succeed on the merits and that he is likely to suffer irreparable harm. See Auto. Club of N.Y., Inc. v. Port Auth. Of N.Y. & N.J., 842 F. Supp. 2d 672, 676 (S.D.N.Y. 2012).

F. Obtaining Relief from Stay

G. Section 362(d) of the Bankruptcy Code permits a party to seek relief from the automatic stay on three grounds. 11 U.S.C. § 362(d).

H. The following are the three grounds for obtaining relief: (1) for cause; (2) when the debtor does not have equity in property and such property is unnecessary for an effective reorganization; or (3) when the property is "singe asset real estate." 11 U.S.C. §§ 362(d), 101(51B).

I. The word "cause" is not defined in the Bankruptcy Code. In re B.G. Petroleum, LLC, 525 B.R. 260, 278 (Bankr. W.D. Pa. 2015). Thus, courts consider three factors in order to determine whether relief should be granted for cause: (1) the likelihood the debtor will endure prejudice; (2) the probability the party will succeed on the merits; and (3) the weighing of hardships among the parties. Id.

Release and Discharge

I. Purpose and Effect of a Bankruptcy Discharge

A. A bankruptcy discharge relieves a debtor from all prepetition debts. 11 U.S.C. §§ 524, 727(a), 1228, 1328, 1141(d). In addition, judgments holding a debtor personally liable for dischargeable debts are void. 11 U.S.C. §§ 524(a)(1); See In re Elmes, 289 B.R. 100, 107-08 (Bankr. N.D. Ill. 2003).

B. A discharge functions as an injunction against the continuance or commencement of any action "to collect, recover or offset any debt." 11 U.S.C. §§ 524(a)(2); Garfield v. Ocwen Loan Servicing, LLC, 526 B.R. 471, 475-76 (W.D.N.Y. 2015). Thus, if a creditor files suit in state court over a previously discharged debt, the creditor violated the discharge injunction and may be held in contempt. Polysat, Inc. v. Union Tank Car Co., 152 B.R. 886, 894 (Bankr. E.D. Pa. 1993); In re Barrup, 53 B.R. 215 (1985).

C. The primary purpose of a bankruptcy discharge is to assist financially distraught debtors and to allow them to have "a fresh start." Lebron v. St. Vincent Med. Ctr., 21 Misc. 3d 1147(A) (Sup. Ct. 2008). In other words, debtors should be relieved from the "weight of oppressive indebtedness." In re Lin, 499 B.R. 430, 435 (Bankr. S.D.N.Y. 2013). However, the bankruptcy discharge is a privilege and not a right.

D. In addition, the bankruptcy discharge should be strictly construed against the creditor. Corrales v. Sanchez, 365 B.R. 414, 417 (Bankr. S.D.N.Y. 2007). In other words, the exceptions should be construed liberally in favor of the debtor. Id.

II. Effect of a Bankruptcy Discharge on Third Parties

A. Some circuits have held that bankruptcy discharges do not change or alter the liability of any third party individuals or entities. 11 U.S.C. § 524(e). Thus, guarantors and co-debtors are still liable for their debts and creditors may collect from them without violating the discharge. Green v. Welsh, 956 F.2d 30 (2d Cir. 1992); Grant v. Progressive Ins. Co., 535 F. Supp. 2d 296, 299 (D. Conn. 2008).

B. However, other circuits have held that third party injunctions are permitted under certain circumstances. In re Mahoney Hawkes, LLP, 289 B.R. 285, 297-98 (Bankr. E.D. Mass. 2002); In re Master Mortgage Inv. Fund, 168 B.R. 930, 935 (W.D. Mo. 1994). Courts consider the following factors to determine if a third party injunction is permissible:

a. There is "an identity of interest between the debtor and the third party" such that a claim against the third party is a claim against the debtor;

b. The third party contributed a significant amount of money to the reorganization plan;

c. The third party injunction is crucial to the reorganization plan;

d. A majority of the creditors agreed to the third party injunction and the proposed reorganization plan; and

e. The creditors affected by the third party injunction will receive payments for all or substantially all of the claims. Id.

III. Specific Code Sections Concerning Bankruptcy Discharges

A. Section 727(a) of the Bankruptcy Code only applies to Chapter 7 bankruptcy cases. Wahrman v. Bajas, 443 B.R. 768, 775 (2011). The bankruptcy discharge order is automatically submitted within 60 days of the first date of the section 341 meeting unless a party files a dischargeability proceeding. Id. at 773; See Fed. R. Bankr. 4004(a), (c).

B. Section 1141(d) governs the scope of the bankruptcy discharge for Chapter 11 debtors, where a plan was established and completed. 11 U.S.C. § 1141(d). A corporate or partnership debtor is not entitled to a discharge if its reorganization plan proposes liquidation and a discontinuance of its business activities. See 11 U.S.C. § 1141(d)(3); In re S. Canaan Cellular Invs., 427 B.R. 44, 85 (Bankr. E.D. Pa. 2010).

C. Section 1228 of the Bankruptcy Code governs discharges in Chapter 12 cases. 11 U.S.C. § 1228. Chapter 12 discharges are contingent upon the debtor completing the reorganization payment plan. 11 U.S.C. § 1228(a).

D. Section 1328 applies to discharges for Chapter 13 debtors. 11 U.S.C. § 1328. Unless a hardship discharge is obtained, a discharge under section 1328 is dependent upon the debtor completing all of the payments in the reorganization plan. 11 U.S.C. § 1328(b).

1. A hardship discharge is granted only if a Chapter 12 or Chapter 13 debtor cannot complete his reorganization payment plan and the following conditions are established:

a. The debtor should not be held responsible for the circumstances that prevented him from completing the payments;

b. The value paid under the reorganization plan for each unsecured claim is equal to or more than the total that would have been distributed for such a claim if the debtor's estate had been liquidated under Chapter 7; and

c. Post-confirmation modification is not a realistic option. 11 U.S.C. §§ 1228(b), 1328(b).

IV. General Objections to an 11 U.S.C. § 727 Discharge

A. Typically, a bankruptcy discharge should be granted unless an exception applies or the debtor deliberately attempted to defraud a third party. Pan Am. World Airways v. Chiasson, 183 B.R. 293, 295 (Bankr. M.D. Fla.1995). In order for the court to deny a discharge, the party opposing the discharge must establish an exception by a preponderance of the evidence. Peterson v. Scott, 172 F.3d 959, 966-67 (7th Cir. 1999); In re Marra, 308 B.R. 628, 630 (D. Conn. 2004).

B. Under section 727(a) of the Bankruptcy Code, there are various general exceptions to a discharge. 11 U.S.C. § 727(a).

1. A discharge should not be granted to non-individuals such as corporations or partnerships because bankrupt businesses likely will not have "future property accumulation." 11 U.S.C. § 727(a)(1); Wolinsky v. Oak Tree Imaging, 362 B.R. 770, 780 (S.D. Tex. 2007); In re Push & Pull Enterprises, Inc, 84 B.R. 546, 548 (N.D. Ind. 1979).

2. If a debtor intended to "hinder, delay or defraud" a creditor and thus "removed, destroyed, mutilated, or concealed" any of his property or any property of the estate, a bankruptcy discharge should be denied. 11 U.S.C. § 727(a)(2).

3. A debtor who has "concealed, destroyed, mutilated, or falsified" documents should not receive a bankruptcy discharge. 11 U.S.C. § 727(a)(3).

4. A discharge also should not be granted to a debtor who knowingly and fraudulently submitted a false claim, made a false statement, withheld pertinent financial information, or "gave, offered, [or] received" money, property, or an advantage "for acting or forbearing to act." 11 U.S.C. § 727(a)(4).

5. When a debtor refuses to obey a lawful court order or refuses to respond or testify to a material question that was approved by the court, the court will not grant a discharge. 11 U.S.C. § 727(a)(6).

6. Lastly, if the debtor does not satisfactorily explain the deficiency of assets to meet the debtor's liabilities, a court will deny a discharge. 11 U.S.C. § 727(a)(5).

C. In other words, section 727(a) of the Bankruptcy Code enumerates several exceptions to the universal rule that courts should always grant discharges. Republic Credit Corp. v. Boyer, 328 F. App'x 711, 715 (2d Cir. 2009). Most of the exceptions consist of two components: (1) an act or forbearance of an act (transfer, destruction, mutilation, or concealment) and (2) intent (to hinder, delay, or defraud creditors). Id.

D. When there are grounds for denial or an exception applies, courts have discretion to decide whether or not to grant a discharge. Union Planters Bank, N.A. v. Connors, 273 B.R. 764, 773 (S.D. Ill. 2002). Since denying a bankruptcy discharge is a "harsh and drastic" penalty, the reasons for disallowing a discharge must be "real and substantial." Fokkena v. Smith, 373 B.R. 895, 900 (N.D. Iowa 2007).

V. Revocation of 11 U.S.C. § 727 Discharge

A. A trustee, a creditor, or the United States trustee may request that a court revoke the debtor's discharge. 11 U.S.C. § 727(d). There are four reasons a discharge will be revoked. 11 U.S.C. § 727(d).

1. If the debtor used fraud to acquire the discharge and the requesting party had no knowledge of the fraud until after the discharge was granted, then the discharge must be revoked. 11 U.S.C. § 727(d)(1).

2. The discharge also must be revoked if the debtor obtained or became entitled to obtain property of the estate and knowingly and fraudulently refused to report the acquisition or entitlement to the trustee. 11 U.S.C. § 727(d)(2).

3. In addition, the court must revoke a discharge when a debtor refuses to obey a lawful court order or refuses to respond or testify to a material question that was approved by the court. 11 U.S.C. § 727(d)(3).

4. If the debtor did not satisfactorily justify a material misstatement in an audit or a failure to disclose all necessary documents requested for an audit, then the court must revoke the discharge. 11 U.S.C. § 727(d)(4).

VI. Specific Creditors Objections to Discharge 11 U.S.C. § 523

A. The nineteen exceptions enumerated in section 523(a) of the Bankruptcy code do not apply to non-individuals debtors including partnerships and corporations. In re MF Global Holdings Ltd., No. 11-15059, 2012 Bankr. LEXIS 897, at *9-10 (Bankr. S.D.N.Y. Mar. 6, 2012).

B. The following categories of debt are excluded from the general rule of dischargeability. 11 U.S.C. § 523(a).

1. For example, debts for money, property, or services that were obtained by false pretenses, false representations, actual fraud, or false financial statements may not be discharged. 11 U.S.C. §§ 523(a)(2)(A), 523(a)(2)(B).

2. Debts for "an educational benefit overpayment or loan made, insured, or guaranteed by a governmental unit, or made" by a nonprofit institution or any program funded by a governmental unit may not be discharged. 11

U.S.C. § 523(8)(A). Debts to repay money obtained as an educational benefit, scholarship, or stipend also are not dischargeable. Id.

3. Debts incurred by an intoxicated debtor who unlawfully operated a vehicle and injured or killed an individual are not dischargeable. 11 U.S.C. § 523(9).

4. Debts for fines, penalties, and forfeitures "payable to and for the benefit of" a governmental unit are not discharged. 11 U.S.C. § 523(7).

5. Discharge of debt does not affect the debtor's liability for domestic support obligations. 11 U.S.C. § 523(a)(5). Domestic support obligations include alimony, maintenance, or any debt to a spouse, former spouse, or child of the debtor. 11 U.S.C. § 101(14A).

6. When the debtor willfully and maliciously injures another person or that person's property and incurs a debt, that debt is not dischargeable. 11 U.S.C. § 523(a)(6).

7. Debts incurred by embezzlement, larceny, or for fraud while the debtor was acting as a fiduciary are not included in a discharge. 11 U.S.C. § 523(a)(4).

8. In addition, debts for specific kinds of taxes or customs duties are not dischargeable. 11 U.S.C. § 523(a)(1)(A)-(C). For example, debts for taxes or customs that are designated as third or eighth priorities are not discharged. 11 U.S.C. § 523(a)(1)(A). If a debtor filed a fraudulent return or willfully attempted to evade the taxes, then those debts are not dischargeable. 11 U.S.C. § 523(a)(1)(C).

C. Congress established these exceptions to protect creditors. When an exception applies, the creditors' interests in recuperating the full amount of the debt outweighs the debtor's interest in a fresh start. Alibatya v. New York Univ., 178 B.R. 335, 337 (1995).

D. Additionally, the exceptions enumerated in section 523(a) of the Bankruptcy Code should be narrowly construed. Denton v. Hyman, 502 F.3d 61, 65 (2d Cir. 2007). In other words, the exceptions should be construed liberally in favor of the debtor. See Garland v. Lawton, No. 99-10120, 2001 Bankr. LEXIS, at *21-22 (Bankr. D. Vt, 2001).

E. Under 11 U.S.C. § 523, the party contesting the dischargeability of a debt has the burden of proof to establish that the debt should not be discharged by a preponderance of the evidence. Pereira v. Young, 346 B.R. 597, 606 (E.D.N.Y. 2006). In addition, when debts are denied discharge under 11 U.S.C. § 523, the party who contested the dischargeability is the only creditor who benefits from the denial.

VII. Reaffirmation

A. A reaffirmation agreement is an agreement between a creditor and a debtor. 11 U.S.C. § 524(c). In the agreement, the debtor waives discharge for a debt that typically is dischargeable. Id. Reaffirmation agreements are enforceable if the following conditions are established:

1. The agreement was made prior to the granting of a discharge;

2. The debtor received the disclosures described in 11 U.S.C. § 523(k) at or before the time the agreement was signed by the debtor;

3. The agreement and an affidavit was filed with the court (the affidavit must state that the debtor was fully informed and acted voluntarily, that "the agreement does not impose an undue hardship on the debtor," and that the lawyer fully counseled the debtor of the legal consequences);

4. The debtor did not rescind the agreement before the discharge was granted or within sixty days after the agreement was filed with the court;

5. The provisions concerning the discharge hearing have been complied with; and

6. The court approved the agreement if the debtor was not represented by a lawyer. 11 U.S.C. § 524(c)(1)-(6).

B. Reaffirmation agreements must comply with the statute in order to be valid. See Whitehouse v. Laroche, 277 F.3d 568, 575 (1st Cir. 2002). The statutory requirements protect and prevent debtors from "compromising their fresh start" and from being pressured to sign an agreement. In re Ripple, 242 B.R. 60, 64 (Bankr. M.D. Fla. 1999).

<u>Successor Liability</u>

I. The "Free and Clear" Rule

A. Under New York law, federal law, and traditional common law, a purchaser is generally not liable for a seller's torts or other liabilities. 11 U.S.C. § 363(f); Schumacher v. Richards Shear Co., 59 N.Y.2d 239, 244 (1983).

B. The purpose of the free and clear rule is to protect purchasers from liabilities they did not assume and to maximize "the fluidity of corporate assets." Vernon v. Schuster, 688 N.E.2d 1172, 1175 (Ill. 1997).

C. Although the doctrine of successor liability often is used as a defense in product liability cases, it is also used in cases concerning breaches of contract, the Employee Retirement Income Security Act (ERISA), the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), labor and employment law violations, and security trading actions.

1. For example, the Second Circuit held that a purchaser could be held liable for the selling corporation's delinquent contributions to a benefit plan. Stotter Div. of Graduate Plastics Co. v. Dist. 65, United Auto. Workers, 991 F.2d 997 (2d Cir. 1993). ERISA fiduciary duties and retiree health promises are also subject to ERISA successor liability. See Bish v. Aquarion Servs. Co., 289 F. Supp. 2d 134 (D. Conn. 2003).

2. Several circuit courts have determined that a successor company may be liable for a predecessor company's CERCLA violations, including the Second Circuit. See New York v. N. Storonske Cooperage Co., 174 B.R. 366, 374 (Bankr. N.D.N.Y. 1994). According to the Second Circuit, the continuity of enterprise test is the correct test to determine successor liability under CERCLA. Durham Mfg. Co. v. Merriam Mfg. Co., 294 F. Supp. 2d 251, 273 (D. Conn. 2003).

3. In addition, the Supreme Court held that a successor employer was not bound by the substantive terms of a pre-existing Collective Bargaining Agreement (CBA). NLRB v. Burns Int'l Sec. Servs., 406 U.S. 272 (1972); Fall River Dyeing & Finishing Corp. v. NLRB, 482 U.S. 27 (1987). However, successor companies may have an obligation to bargain with the union if the majority of the workforce is comprised of employees who worked for the predecessor company. Local 348-S, UFCW, AFL-CIO v. Meridian Mgmt. Corp., 583 F.3d 65, 73 (2d Cir. 2009). To determine whether a successor employer has an obligation to bargain with the union, courts should consider the following factors: (1) whether the business is the same; (2) whether the employees of the successor business perform the same duties and work under the same supervisors; and (3) whether the successor business has "the same production process, produces the same products, and basically has the same body of costumers." Local 348-S,

UFCW, AFL-CIO v. Meridian Mgmt. Corp., 583 F.3d 65, 74 (2d Cir. 2009).

4. Successor liability also has been applied in cases dealing with federal labor or employment laws such as the Fair Labor Standards Act (FLSA). EEOC v. N. Star Hospitality, Inc., 777 F.3d 898, 901-02 (7th Cir. 2015). According to the Seventh Circuit, courts should consider the following five factors in determining whether a successor company is liable for violations of federal labor and employment laws: "(1) whether the successor had notice of the pending lawsuit; (2) whether the predecessor could have provided the relief sought before the sale or dissolution; (3) whether the predecessor could have provided relief after the sale or dissolution; (4) whether the successor can provide the relief sought; and (5) whether there is continuity between the operations and work force of the predecessor and successor." Id. However, the Second Circuit has not addressed what test should be used to determine successor liability in FLSA cases. Garcia v. Serpe, No. 3:08cv1662, 2012 U.S. Dist. LEXIS 14026, at *31 (D. Conn. 2012); Battino v. Cornelia Fifth Ave., LLC, 861 F. Supp. 2d 392, 402 (S.D.N.Y. 2012).

II. Traditional Exceptions to Successor Liability

A. There are several well-known exceptions to the successor liability doctrine. Kasem v. BNC Storage, LLC, 816 N.Y.S.2d 375, 376 (2d Dep't 2001).

B. For example, a purchaser is responsible for a seller's liabilities if the purchaser expressly or impliedly assumes the liabilities of the seller. Id. To determine whether a purchaser assumed a seller's liabilities, courts should look at the language of the purchase agreement. Id.

C. If a purchaser and a seller merge or consolidate, then the purchaser is responsible for the seller's liabilities. Van Nocker v. A.W. Chesterton, Co., 789 N.Y.S.2d 484, 486 (1st Dep't 2005). A purchase-of-assets may be included in this exception as a de facto merger if it contains the following factors:

1. Continuity of ownership;

    a. Continuity of ownership occurs when the seller's shareholders become direct or indirect shareholders of the buyer.

2. A cessation of ordinary business operations and the dissolution of the seller's company as soon as possible after the transaction;

3. An assumption of any liabilities that are necessary to continue the seller's business uninterrupted; and

4. The continuation of management, personnel, physical location, assets, and general business operation. Id.

a. Hiring various employees of the seller is not sufficient to constitute a continuity of management. See Kretzmer v. Firesafe Prods. Corp., 805 N.Y.S.2d 340, 241 (1st Dep't 2005).

5. A de facto merger may occur even if some of the factors are excluded from the asset purchase agreement. Id. In other words, the factors should be analyzed in a flexible manner, and the court should determine whether the purchaser intended to continue the seller's business. Matter of AT&S Transp., LLC v. Odyssey Logistics & Tech. Corp., 803 N.Y.S.2d 118, 119 (2d Dep't 2006). However, a continuity of ownership is essential and should be established before the other factors are analyzed. Id.

D. A successor company may also be responsible for a predecessor's liabilities if the successor is a mere continuation of the predecessor. Matter of Seventh Judicial Dist. Asbestos Litig., 788 N.Y.S.2d 579, 581-82 (Sup. Ct. 2005). The mere continuation exception concerns corporate reorganizations where the predecessor is dissolved and only the successor company survives the purchase agreement. Id. If the predecessor company continues to exist after the purchase agreement, the mere continuation exception does not apply. Id.

1. Since the mere continuation exception and the de facto merger exception are similar, they are often viewed as one exception. Douglas v. Stamco, 363 F. App'x 100, 102 (2d Cir. 2010).

E. If a purchaser and a seller fraudulently executed a purchase agreement in order to escape liabilities and obligations, then the purchaser may be held liable. Kasem v. BNC Storage, LLC, 816 N.Y.S.2d 375, 376 (2d Dep't 2001). Although New York courts acknowledge the fraud exception, no court has considered the contours of it. Jeffrey M. Alexander & Sarah Shannon Carlins, *Successor Liability in New York Post-Berger*, 14 N.Y. ST. B.A. HEALTH L.J. 51, 53 (2009).

III. Non-Traditional Exceptions to Successor Liability

A. Some courts have adopted the continuity-of-enterprise exception. See Turner v. Bituminous Cas. Co., 244 N.W.2d 873 (Mich. 1976). Under the continuity-of-enterprise exception, an asset purchase agreement would bind a purchaser to a seller even if the two companies' shareholders differed. Id. The following three elements are necessary to impose continuity-of-enterprise liability on a purchaser:

1. A continuation of management, personnel, physical location, assets, and general business operations;

2. A cessation, liquidation, or dissolution of the seller as soon as practically and legally possible; and

3. An assumption of the seller's liabilities and obligations in order for the normal business operations to continue uninterrupted. Id. at 879.

B. In other words, the continuity-of-enterprise exception is the de facto merger exception without the continuity-of-shareholders requirement. See Kretzmer v. Firesafe Prods. Corp., 805 N.Y.S.2d 340, 241 (1st Dep't 2005).

C. At minimum, one New York Supreme Court has adopted this exception. See Salvati v. Blaw-Knox Food & Chem. Equip., Inc., 497 N.Y.S.2d 242 (N.Y. Sup. Ct. 1985). However, the New York Court of Appeals has not discussed this exception since 1983 when it chose not to adopt it. Schumacher v. Richards Shear Co., 59 N.Y.2d 239 (1983).

D. Other courts have adopted the product line exception to successor liability. See Ray v. Alad Corp., 560 P.2d 3 (Cal. 1977). If a purchaser produces the same products as the seller corporation and exploits the seller's goodwill, name, and customer lists, then the purchaser may be responsible for the predecessor corporation's liabilities. Id. The following three elements are necessary to impose product liability on a purchaser:

1. A lack of remedies against the predecessor corporation because of the transaction;

2. The purchaser's ability to spread risk; and

3. The fairness of forcing a purchaser to assume liabilities for defective products that was "a burden necessarily attached to the original manufacturer's goodwill being enjoyed by the successor in the continued operation of the business." Salvati v. Blaw-Knox Food & Chem. Equip., Inc., 697 N.Y.S.2d 242, 244-45 (Sup. Ct. Queens Cnty. 1985).

E. In 2006, the New York Court of Appeals rejected the product line exception. Semenetz v. Sherling & Walden, Inc., 7 N.Y.3d 194, 201 (2006).

IV. The GM Bankruptcy Case

A. By a Sale Order dated July 05, 2009, General Motors Corp. (Old GM) sold the majority of its assets to General Motors LLC (New GM) free and clear of successor liability claims.

B. In 2014, the following three classes of plaintiffs filed class action lawsuits: (1) economic loss plaintiffs; (2) pre-closing accident plaintiffs; and (3) non-ignition switch plaintiffs. In re Motors Liquidation Co., 529 B.R. 510, 521-23 (Bankr. S.D.N.Y 2015). The economic loss plaintiffs sought to recover money for damages related to the product recalls, and the pre-closing accident plaintiffs sued to recover damages for accidents that happened before the sale order. Id. The non-ignition switch plaintiffs sought to recover damages for having GM cars (that had no ignition switch problems), alleging that the brand was damaged (their claims were deferred for later consideration). Id.

C. Since Old GM failed to give the plaintiffs actual notice of the deadline to file proofs of claim in its bankruptcy case, the court held the plaintiffs were "denied the notice due process requires." Id. at 560. The pre-closing accident plaintiffs did not suffer prejudice because similarly situated creditors had received notice and asserted the same arguments that the plaintiffs did. Id. at 572-73. However, the economic loss plaintiffs were prejudiced because no similarly situated creditor, who had received notice, had argued that the Sale Order was excessively broad. Id. at 566.

D. Thus, the U.S. Bankruptcy Court for the Southern District of New York held that the economic loss plaintiffs could assert claims against New GM if the claims were based upon New GM's conduct. Id. at 598. However, the pre-closing accident plaintiff's claims were barred against New GM because successor liability claims are barred under the free-and-clear doctrine. Id.

E. Since appellate relief has not been exhausted, the ultimate outcome is unknown.

LIMITATION OF FEDERAL COURTS TO REVIEW
<u>FINAL STATE COURT JUDGMENTS</u>

I. The *Rooker Feldman Doctrine*.

A. Federal courts' jurisdiction to review final state court judgments is limited pursuant to the Principles articulated in two Supreme Court cases; *Rooker v Fidelity Trust Co.*, 263 U.S.413 (1923) and *District of Columbia Court of Appeals v Feldman,* 460 U.S. 462 (1983). Also, recently applied in *Exxon Mobil Corp. v Saudi Basic Industries Corp.,* 544 U.S. 280 (2005).

B. As enunciated by the Second Circuit Court of Appeals, four criteria must be satisfied for the *Rooker- Feldman* principle to be applied as follows; [1] the party raising the claim must have lost in the state court, [2] the aggrieved party's injuries were caused by the state court judgment, [3] the party's claims must invite the district court to review and reject the state court judgment, and [4] the stat ecourt judgment must have been issued before the commencement of the federal court proceedings. <u>See</u>, *Hoblock v Albany County Board of Elections,* 422 F.3d 77 (2nd Cir. 2005).

C. Good illustration of *Rooker-Feldman* in attached Bankruptcy Court Opinion in *In re Dommer Construction Corporation* Case # 10-12764 (Bankr. W.D.N.Y. 2011); affirmed *Business Funding Group v Dommer Construction Corp.* Case # 11-cv-565S (U.S.Dist. Ct., 2012). Both decisions are attached.

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NEW YORK

In re

DOMMER CONSTRUCTION CORPORATION — Case No. 10-12764 K

Debtor

AMENDED OPINION AND ORDER

INTRODUCTION

Most (if not all) states provide a comprehensive means of assuring that money paid or loaned to improve land finds its way first to suppliers of labor or materials that are incorporated into the improvements. In New York, that is the "Lien Law," which imposes a statutory trust on the money, for the benefit of such suppliers.

But New York Lien Law recognizes that some contractors or subcontractors may have to borrow in order to perform the contract. Because a lender to a contractor cannot lien the building contractually (as it is not in privity with the landowner), and because only the suppliers themselves may lien the building statutorily, lending to contractors is done by "factors." Factors loan on the security of the payments the contractor will receive during the progress of the improvement project.

When factors are not involved, but a construction loan secured by a mortgage is involved, the Lien Law imposes filing requirements such that a possible supplier of labor or materials may assess the chances of getting paid, and the likely timing of payments (based on the schedule of advances on the loan), so that a decision can be made as to whether to supply labor or

materials on credit.

When a factor is involved, other filing requirements are imposed for the same purpose. If a factor does everything correctly, it can "prime" a supplier. Therefore, notice of the terms of the factoring arrangement might be critical to a possible supplier's decision whether to get involved in the project or not.

This issue extends itself throughout the ladder of subcontracts, sub-subcontracts, etc.

The Debtor here is a contractor which, in engaging a "sub," knew that the sub was borrowing from a factor, and knew that it (the Debtor) must ordinarily make its progress payments for the sub to the factor, not the sub.

In the midst of construction, the Debtor learned that not all of the sub's suppliers were getting paid in full and on-time. In order to avoid economic injury under its own obligations, it may have disregarded its obligation to the factor,[1] and paid its sub's suppliers directly, jumping over the factor. At some point (seemingly after the payments) it was learned that the factor had not properly filed its agreement under the Lien Law.

After the project was completed, and with the Debtor facing the imminent entry of a state court judgment in favor of the factor for the full amount of what the Debtor owed to the sub, with no offsets for amounts paid directly to the sub's suppliers, the Debtor/contractor filed here for relief under Chapter 11, and the factor has filed a Proof of Claim for that full amount,

[1]Whether it actually had such obligation is still undecided, as discussed below.

without offsets, supported solely by state court decisions that might otherwise have become "final judgments" that would bind this Court under *Kelleran v. Andrejevic*, 825 F.2d 692 (2d Cir. 1987).

This Objection to Claim followed. After much oral argument, the parties stipulated that this Court is not bound by the non-final decisions of the state court, but would give "great deference" to that court's findings of fact, so that this Court would not "re-try" evidentiary matters decided by the state court, and would order evidentiary hearing only as to matters as to which this Court believes that the state court should have heard evidence, but refused to hear it.

And so the issue presented is a bankruptcy issue only. Has the Rule 3001(f) presumption of validity and amount of a Proof of Claim successfully been rebutted? This Court rules that the presumption has so been rebutted, and that the Proof of Claim must be amended, without prejudice to an appeal of this Decision at an appropriate time.

This Court goes further by instructing the factor as to the appropriate elements of its amended Proof of Claim. Offsets in favor of the Debtor are indeed available, and the burden falls upon the factor to file a claim that no longer relies upon the non-final state court decisions.

It is a heavy burden indeed, because it may depend, in significant part, on many evidentiary matters that have never even been the subject of discovery, let alone trial. For example: Which suppliers to the sub actually knew about the factoring arrangement despite the failure to properly file it? As to each such sub-sub who did know, did the knowledge come before or after a decision by the sub-sub to provide labor or materials? Is a certain non-binding decision of a lower state court decision persuasive to this Court?

Because this Court now rules, with great respect for the state court judge in this difficult case, that the state court's decision was incorrect, the factor must amend its claim downwards, without prejudice to its right eventually to appeal.

PROCEDURAL POSTURE

The procedural posture of this case is somewhat unusual. This matter was litigated in state court and was the subject of two decisions written by the state court judge. But the Debtor filed its Chapter 11 Petition before a final judgment could be entered. The state court had ruled against the Debtor in an amount over $400,000. However, after the Petition was filed, the Debtor made a strategic decision to permit the judgment to be entered so that it could appeal it through the state court system. When the prevailing party failed to move for relief from the stay to enter the judgment, the Debtor itself moved for lift of stay to permit the judgment to be entered against it, so that it could appeal the judgment.

At hearing on that motion, this Court advised the parties that it would be willing to hear the matter in the context of a claims objection, and in an effort to avoid having to fully re-litigate the matter, would give "great deference" to the state court's Findings of Fact and would rule *de novo* on disputes regarding the law. The parties then stipulated to this Court's denial of the Debtor's Motion to Lift Stay.

The prevailing party in the state court, BFG, Inc., filed its Proof of Claim. The Debtor filed its objection to the claim. The Court then directed the parties to "annotate" the state court's decisions from each side's perspective. From the Debtor's perspective, that meant, of

course, pointing out those parts of the state court's decisions that the Debtor felt constituted error, with an explanation of the Debtor's arguments in that regard. From BFG's perspective, of course, it meant simply explaining why it agreed with the state court's rulings, together with any points that BFG wished to make in support of the various rulings made by the state court, which the state court might have included in its decisions, but did not.

After appropriate exchanges and submissions, the matter came before this Court for oral argument on January 21, 2011. At the close of oral argument, this Court took the matter under submission.

In sum, then, this Court deems the procedural posture of the matter to be this: Claimant BFG, Inc. filed a Proof of Claim in the amount of $438,725.17, supported by the entire record of the state court proceeding and the rulings by the state court judge which never took the form of a final judgment; this Court will review the state court's Conclusions of Law *de novo* and will give "great deference" to the state court's Findings of Fact except to the extent that the state court's findings of "mixed fact and law" were premised on an incorrect interpretation of law; the matter will not be re-litigated here, except that evidence may be reopened and heard here if this Court determines that an error of law within the state court decisions compels a fuller evidentiary record.[2]

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[2]Though it might appear that this Court is purporting to sit "in review" of the state court decisions, that is not a correct interpretation. Rather, it would be fully within the authority of this Court to disregard the state court proceedings entirely, since they never resulted in a Final Judgment. In that event, a full evidentiary record would have to be made here, which would be wasteful for the parties. Hence, this Court is attempting to derive as much guidance as possible from the state court record and the state court's rulings, as this Court attempts to reach the same conclusion it would reach if the state court proceedings were ignored entirely, and the matter fully retried here in the context of this claims objection.

ISSUE PRESENTED

The issue presented here is uniquely a bankruptcy issue. In the state court the issue was whether, under general principles of contract law, common law and under particular New York Statutes appertaining to the commercial construction industry, claimant BFG was damaged when the Debtor construction company chose to dishonor $292,000 worth of assignments that the Debtor's subcontractor, MBE, had made to the claimant, and instead made those payments directly to unpaid suppliers of labor or materials to MBE, which suppliers could otherwise have placed liens on particular projects.

In this Court the question is how a claimant must support a Proof of Claim in this regard, once the non-binding state court decision on the matter has been determined to fail as such support.

FACTUAL BACKGROUND

The Debtor is a small company. Paul Dommer is its principal.

At some point prior to December 5, 2003, the Buffalo Public School System decided to renovate eight Buffalo Public Schools. It named Louis P. Ciminelli Management Company, Inc. to be the "Program Provider" (i.e., general contractor) for this effort. On September 17, 2003, Ciminelli chose the Debtor, Dommer Construction Corporation, to be the "primary subcontractor" with regard to work on two of the schools. The dollar amount of that subcontract was $1,884,000.

Under Article 16 of that subcontract, Dommer was required to provide a performance bond and a labor and material payment bond in that total amount, and Dommer did so. (This was also required by statute because this was a "public improvement" project.)

In December of 2003, Dommer chose the MBE Group, Inc. to perform $1.4 million of the work (much of which involved studding and drywall work).

In the sub-subcontract between Dommer and MBE, Dommer reserved "the right to withhold and to recover any and all amounts necessary to cover costs that may be incurred by [Dommer] as a result of [MBE's] unsatisfactory job progress, including costs associated with supplementation of [MBE's] work forces; defective construction not remedied; disputed work; third-party claims filed or reasonable evidence that such claims may be filed; failure of [MBE] to make timely payments for labor, equipment, and materials, reasonable evidence that the [sub subcontract] cannot be completed for the unpaid balance of the [sub subcontract] amount and retainage."

Such language was not gratuitous. New York Lien Law § 70 imposes a statutory trust on any payments that a contractor or subcontractor receives on a job, in favor of suppliers of labor or materials on the contract. Moreover, a condition of the statutorily required payment bond was that Dommer "shall promptly make payment to all claimants . . . for all labor and material used or reasonably required for use in the performance of the subcontract," and defined "claimant" to be "any contractor, supplier, materialman or worker providing labor, materials, or both, used or reasonably required for use in the performance of the subcontract."

Based on substantial judicial experience, this Court takes judicial notice of the fact that to the extent that the bonding company had to pay any such claimant under the bond, the bonding company had a right of indemnification from Dommer.

MBE needed to borrow money in order to be able to perform its sub-subcontract with Dommer. With Dommer's permission, MBE entered into a factoring arrangement with the claimant here, BFG. Despite the trust fund status of payments that Dommer would receive on the contract and the trust obligations that MBE would have with respect to payments it received from Dommer, factoring arrangements are permitted under New York law in a carefully circumscribed way set forth in New York Lien Law § 73. Consequently, Dommer entered into direct negotiations with BFG to assist MBE in obtaining the funds it needed to perform the sub-subcontract, and to make sure that to the extent that Dommer would be making payments to BFG rather than MBE, Dommer would not violate the Lien Law.[3]

The only documents which would be signed as between Dommer and BFG would be "Notices of Assignment" of accounts receivable, which would be signed by MBE, BFG, and Dommer, with respect to each progress payment that Dommer would otherwise make to MBE. The "Notices of Assignment" are abbreviated "NOAs" for purposes of this litigation.

The first five NOAs went through without a hitch. Each of those was a single side of one page. Paragraph 1 of each contained the following "boiler plate:" "As of the date hereof the amount owing on the attached invoice by the Undersigned to Assignor, and the amount to be

[3]The last is not a finding of fact, but rather a supposition that is open to attack by BFG, if evidence will be taken here, as discussed below.

paid to BFG pursuant to the obligations of the Undersigned is $. The undersigned represents to BFG that no portion of such sum represents retainage. *Payment condition (sic) upon receipt of payment from Contractor and confirmation of payment to suppliers and prevailing wage supplements."* [Emphasis added.]

Over $400,000 was disbursed by Dommer to BFG pursuant to those five NOAs.

The three NOAs at issue here were materially different, though they were not conspicuously distinct from the first five. The statement that payment was conditioned upon "confirmation of payment to suppliers and prevailing wage supplements" was deleted and replaced with the language "Such sum is owed absolutely and the Undersigned now, in the past, or in the future, has or will have no defense to and no right of counterclaim, contra claim, set-off or any other right of deduction from such sum, all of which are hereby waived as to BFG by the Undersigned."

The first four NOAs were signed by the project manager for Dommer, but not Paul Dommer himself. The last four were signed by Dommer's Comptroller. All eight of the NOAs were drafted by BFG and submitted to the Dommer company. The principal of BFG testified in state court that he never spoke to Paul Dommer about the change in language, but that he did communicate with some unnamed person at Dommer to the effect that BFG would be making the change.[4] Although the Dommer comptroller might not have been called to the stand in state court, she apparently attested in an affidavit that she had been unaware that the language had been

[4]Actually, his testimony was not quite that clear. After first testifying that he did speak with Mr. Dommer about the change, he later changed his testimony to make it clear that he had not done so. But he left the impression that he had communicated with someone at Dommer.

changed and did not observe the change when she signed the NOA's that she signed. She did attest that no-one misled her, as described below.

Before Dommer sent any money to BFG in connection with the three NOAs in question, Dommer received notification that some of MBE's key suppliers were not receiving timely or full payments.

It is not clear to this Court whether decisionmakers in Dommer were aware that they had, in NOA numbers 6, 7 and 8, waived the right (that they had possessed under NOA numbers 1 through 5 and under the sub-subcontract terms between Dommer and MBE), to withhold payments otherwise owed to MBE (or its assignee)) to make sure that the trust fund rights of MBE's suppliers were honored. But Dommer paid more than $250,000 directly to five major suppliers of MBE and took other steps to assist MBE to complete its work on the sub-subcontract.

In other words, Dommer's actions were consistent with (1) its duty to the general contractor, (2) its need to avoid liability under the payment bond, (3) the terms of NOA members 1 through 5, and (4) its understanding of the New York Lien Law.[5]

However, these actions were in direct violation of the pertinent language of NOA numbers 6, 7 and 8, assuming that those NOA's were binding, as discussed below.

BFG then sued Dommer, Ciminelli, and the Buffalo Public School System for various causes of action including the failure of Dommer to pay to BFG the amounts reflected in

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[5]See footnote 3 above as to the fact that the last of these statements might still be open to attack, if evidence is to be heard here.

NOA numbers 6, 7 and 8. At issue here are only the non-final rulings against the Debtor.

At some time after Dommer made the disbursements to MBE's suppliers and before the state court took the matter under submission, Dommer discovered that BFG had failed to perfect its interest under Lien Law § 73 because BFG had failed to file its factoring agreement in both of the required places.

THE STATE COURT'S DECISIONS

First, this Court will address the March 29, 2010 Decision of the state court. In that Decision, that court held that the fact that BFG failed to perfect its priority as against suppliers of labor and materials (because BFG did not comply with the filing requirement of Lien Law § 73) did not avail Dommer. Citing substantial case law, the state court stated that "the case law makes clear that the courts have construed the defense of invalidity of an assignment to be available only to the intended beneficiaries of the statute, i.e. laborers and material men . . . ." The present Court agrees.

Next, the state court addressed Dommer's argument that it is subrogated to the rights of the trust fund beneficiaries it paid on MBE's behalf. The state court stated "the key question . . . is whether Dommer Construction is entitled to advantage itself of [the invalidity of the assignment as against Lien Law beneficiaries] through common law subrogation to defend against BFG's breach of contract claims, assuming the contracts are enforceable." And the state court turned to the latter question first - - the enforceability of NOAs 6 through 8. That court concluded that the relationship between BFG and Dommer was contractual in nature, and not

statutory, and it rejected Dommer's request that the court consider parol evidence regarding the terms of the "meeting of the minds" between Dommer and BFG as to the language that was to be contained in all of the NOAs. That court instead concluded that

> "There is no dispute that Dommer Construction executed NOAs numbers 6 through 8 and that they were executed by a properly authorized person. There was no testimony by [Dommer's comptroller] that there was any fraud in the factum . . . with respect to the documents or that she was in any way subjected to deceptive machinations by BFG with respect to the contents of the documents. To the extent that anyone on behalf of Dommer Construction failed to appreciate the change in the language to NOAs numbers 6 through 8, they cannot now be heard to complain after they executed the documents and are presumed to know the contents thereof. There can be no doubt that Dommer Construction and its principal, Dommer, are experienced in the construction field and cannot legitimately assert that they did not understand the significance of the legal document Dommer Construction was executing and the obligations it was thereby undertaking.
>
> "The only argument raised by Dommer Construction to avoid the application of the clear terms of the contracts (including the 'estoppel language') is that it should not be bound by the change in the relevant three . . . NOAs because the change in those contracts as to the right of setoff was not brought to its attention. However, a written agreement between sophisticated business people cannot be changed based on an assertion that it did not express one party's unilateral understanding of it . . . . The Court therefore concludes that NOAs numbers 6 through 8 are enforceable according to their terms, including as to the waiver of the right of setoff, and that Dommer Construction has failed to sustain any valid affirmative defense negating the enforcement of those contracts."

[Citations omitted.]

Because the present Court disagrees with a different holding by the state court, as set forth below, and because this Court is ordering further proceedings as a consequence, this Court will not presently state whether it agrees or disagrees with the above-quoted holding. The further proceedings which the present Court orders may or may not lead to an evidentiary

hearing. If an evidentiary hearing is warranted, the present Court will then decide whether the state court should have accepted Dommer's offer to produce parol evidence regarding a "meeting of the minds."

The state court then addressed what it described as the "key question" which, again, "is whether Dommer Construction is entitled to advantage itself of [BFG's failure to perfect its priority] through common law subrogation to defend against BFG's breach of contract claims." It concluded that Dommer was not obligated under statute to make payments to MBE's trust fund beneficiaries; and that Dommer's subcontract with MBE afforded Dommer Construction only the *right, but not the obligation*, to pay MBE's contractors. Thus, the state court ruled that "because its payments were voluntary, . . . Dommer Construction is not entitled to be subrogated to the rights of MBE's trust fund beneficiaries."

For reasons to be set forth below, this Court disagrees with that conclusion.

The state court then acknowledged that that particular holding rested on "unsettled" principles, and considered whether, if Dommer had not *voluntarily* paid and was therefore entitled to subrogation, it could use this right to offset the damages sought by BFG. That Court then extended another state court's holding - - - the case of *Matter of Dick's Concrete Company v. K. Hovhamian*, 2008 WL 427 4481; 17 Misc. 3rd 1136 (Sup. Ct. Orange Co. 9/17/2008). - - - in a way with which the present Court disagrees. The *Dick's* case, like the present case, involved a factor who failed to perfect its priority properly. But the plaintiff in the *Dick's* case was a trust fund beneficiary who had actual knowledge of the factoring arrangement. It was that actual knowledge that defeated the beneficiary's ability to subordinate the unperfected

factoring agreement to its own priority rights.[6]

The state court in this Dommer case found that "Dommer Construction's actual notice of the assignments, of which it had no knowledge at the time might be invalid as to trust fund beneficiaries under Lien Law § 16, negates its ability to elevate its equitable subrogation rights above the lawful contracts it voluntarily entered into with MBE. . . . This conclusion is supported by the practical observation that any other determination would allow a contractor to evade its contractual obligations to a factor by making payments directly to its subcontractor's trust fund beneficiaries. This would not only impair the contractual relationship between the contractor and the factor, but also between the assignor and assignee. Such an easy means of excusing contractual performance should not be sanctioned by the courts."

The present Court believes that this holding by the state court misinterprets the *Dick's* case holding, as discussed below. Moreover, the *Dick's* case is not binding.

On a motion for reconsideration, the state court rendered a second decision, on June 15, 2010. Because of the present Court's disposition of the matter before it, it is not necessary for the present Court to address the contents of that second decision, at this time.

ANALYSIS

The governing principle is this:

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[6]The present Court today incorporates its Bench Ruling that the mere fact MBE's suppliers were receiving payments from BFG does not establish "actual knowledge" that BFG was a factor that could prime the supplier. To a supplier, BFG could have simply been a lender without priority, or an entity that owed money to MBE, or some affiliate of MBE's, etc.

"A party seeking subrogation can establish that its payments were not voluntary either by pointing to a contractual obligation ***or to the need to protect its own legal or economic interests.***" 23 N.Y.Jur.2d, Contribution, Indemnity, and Subrogation, § 174. [Emphasis added.]

It is the view of the present Court that the state court made too much of its perceived distinction between Dommer's "right" to pay MBE's debts (such as under the terms of Dommer's sub-subcontract with MBE) and the type of "obligation" to pay those debts that the state court believed was necessary for Dommer to avoid being a mere volunteer.

To be sure, BFG has argued before this Court that Dommer's proper recourse upon learning that some of MBE's suppliers were not being paid was to escrow the funds or to commence an interpleader. Were this a simpler case, this Court would heartily agree. But this was an ongoing construction project and the problem arose before it was completed.

Dommer clearly had an interest to protect in avoiding being defaulted on its contract with Ciminelli; avoiding claims upon its bond, for which it would have to indemnify the surety (and might suffer difficulty thereafter in obtaining bonds for other projects); and in protecting itself from, perhaps, other forms of economic injury such as injury to its reputation or other "fall-out" had MBE's suppliers ceased providing to MBE and had Dommer not stepped in to assist MBE in completing work on the sub-subcontract.[7]

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[7]The present Court notes that one of the bases for Dommer's motion to reconsider the initial state court decision was the assertion that the issue of whether Dommer was a mere volunteer had never been briefed or argued in the state court. In the decision upon reconsideration the state court stated "it is inaccurate to assert that equitable subrogation principles were not raised prior to the Trial Decision. . . . A subrogation analysis was not a surprise to anyone in this case. In addition, principles of subrogation, as discussed in the Trial Decision, necessarily involved an analysis of the voluntariness of the payments." This writer has great respect for the state court judge, and accepts his explanation. As a matter of personal judicial philosophy, however, this writer would have invited further briefing on

HOLDING

"Obliged" is too technical a word to use in determining whether one is a mere volunteer. The term connotes an obligor and an obligee. But the law, as defined above, is clear that if one acts to protect an interest, one is not a mere volunteer, at least where, as here, the payor itself would have suffered powerful economic damages had it failed to protect its interests.

Dommer was at risk of claims upon the bond (and consequent liability to the bonding company, perhaps risking its future bondability), was at risk of being defaulted on its contract with Ciminelli, and was at risk of general injury to its reputation, which might have threatened its future viability. Further, it perceived itself to be at risk (rightly or wrongly) of violating its trust fund responsibilities under the Lien Law.[8]

Hence, contrary to the state court's rulings, Dommer was not a mere volunteer. But assuming arguendo that NOAs 6 - 8 were binding, finding that it was not a volunteer does not mean that Dommer's obligations to BFG were a nullity. The notion that NOAs 1 through 5 represented a "meeting of the minds," between BFG and Paul Dommer, but that NOAs 6 through 8 did not, seems to lack an evidentiary basis right now. No evidence has been pointed out to this writer even to suggest that Paul Dommer ever cared a whit about the NOAs that actually were signed for Dommer by others authorized to sign for it, let alone thought them to violate a

the question of "volunteerism," because it arguably was dispositive.

[8]See footnote 3 above.

"meeting of the minds."[9] Rather it appears that the only reason that Dommer bypassed BFG was that at about the same time that BFG changed the language, Paul Dommer learned that MBE's suppliers were not all being paid in full and on time. That motivated the Debtor to protect itself against liability as set forth above. There is no evidence that Paul Dommer looked at the language of the NOAs, consulted legal counsel, consulted BFG, or made any demand upon BFG.

The Debtor had two competing interests, and it chose to disregard one - - its contract liability or potential liability to BFG, under contract. BFG is entitled to damages if NOA's 6 - 8 are binding. But BFG's claim that it is entitled to full payment upon NOA's 6 through 8 is absurd. It is premised on the argument that this Court must assume that every supplier to MBE (everyone whom Dommer paid) would lose-out as against BFG under the rationale of the *Dick's* case, so that BFG could have simply kept all the money received on NOA's 6 through 8 by choosing to "stiff" them all. If *Dick's* were so extended, then every factor which realizes that it failed to properly perfect under Lien Law § 73, could simply choose a good time to give all of the beneficiaries "actual knowledge" of the factoring agreement (presumably by registered mail), and keep all the trust funds it thereafter receives.[10] That cannot be the law, and

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[9]There is evidence that when the Debtor negotiated with BFG to help MBE to borrow from BFG, Paul Dommer and BFG had discussed the terms of the NOAs that would be used. Shown an NOA form for a different project, Paul Dommer wrote that he would "sign a similar letter (sic)." That form said this, in relevant part: "Such sum is owed absolutely: Undersigned has no defense to and no right of counterclaim, contraclaim, setoff or any right of deduction from such sum *which is unrelated to the above mentioned project. Undersigned and BFG will attain [sic] certified payrolls, lien releases for suppliers and union requirements for above total before approval of such total.*" [Emphasis added.] The italicized language did not appear in NOAs 6 - 8.

[10]This Court's interpretation of paragraph 4 of Lien Law § 73 is such that BFG would lose-out to any of MBE's suppliers who made an appropriate demand for payment against BFG, unless *Dick's* holding is correct and applies to defeat each such supplier. (Such a demand would squarely present the *Dick's* issue, because only a supplier with actual knowledge would make such a demand upon BFG, rather than MBE.)

this Court declines BFG's invitation so to extend the holding in the *Dick's* case.

If NOAs 6 - 8 are enforceable (a matter not yet decided here), BFG has an allowable claim here, but for how much? At a minimum, it would be lost profits on its deal with MBE, supposing that it had paid all of the MBE suppliers that it was required to pay, and as it presumably would have paid (given its failure to perfect its priority) if all of MBE's suppliers had no actual knowledge of the factoring agreement at any *relevant time*, and if all of MBE's suppliers had made appropriate demand for payment upon BFG under § 73, paragraph 4. That is the minimum claim allowable here.

The maximum BFG could claim here depends upon this Court's view of a different aspect of the *Dick's* holding. This Court is of the view that if the *Dick's* decision is correct at all, it is correct as to the *relevant time* for a beneficiary to lose-out under the *Dick's* holding. It must have gained actual knowledge *before* it supplied labor or materials for a project on which the factor might choose to assert its priority, to the supplier's loss.

BFG argues that Dommer's position to the effect that all of MBE's suppliers would have to have been paid by BFG is "too speculative." If the state court decisions were correct, then this Court would agree. However, BFG's proof of claim is the only matter before this Court, and that claim is based solely on the state court's non-final rulings, and this Court has now found that the state court reached the wrong decision as to whether Dommer was or was not a volunteer.

The state court's ruling obviated the need for that court to address the dollar

amount of offsets. Now, those amounts must be addressed. The Debtor is entitled to offsets because it was not a mere volunteer.

CONCLUSION

BFG must amend its claim, without prejudice to its right to appeal today's holding at an appropriate time. This is to say that the Rule 3001(f) command that a duly filed proof of claim enjoys a presumption of validity as to existence and amount, has been successfully rebutted. The Proof of Claim had justifiably been premised on the state court's non-final rulings. Now that the state court's rulings have been found to suffer an error of law, BFG must resort to the traditional means of supporting a Proof of Claim, as if the matter had not been decided by the state court at all.

BFG must examine its own records as to which suppliers to MBE had been given "actual knowledge" of the factoring arrangement before (and not after) they supplied labor or materials that Dommer, rather than BFG, paid for. BFG must also examine its own records as to whether any suppliers of labor or materials to MBE made any appropriate demand upon BFG under Lien Law § 73, paragraph 4.[11] BFG must also provide a copy of the factoring agreement, in case it provides useful information about its duties to MBE's suppliers.

[11]As noted above, the absence of a demand might indicate a supplier who had no actual knowledge of the factoring arrangement. The presence of a demand might directly implicate the correctness of the *Dick's* holding.

Proofs of claims that do not enjoy the benefit of being supported by a final state court judgment can be very expensive to prepare. However, the requirements of Title 18 U.S. Code §§ 152 and 3571 require great care.

The burden is on BFG to claim an amount that is a reasonable estimate of the amount it could actually have kept, lawfully, if it had received the trust funds from Dommer and then fulfilled its trust obligations, given the fact that it failed to perfect its priority.

This Court's rulings above as to the maximum extent to which this Court might be persuaded by the holding in the *Dick's* case, gives BFG guidance as to how to undertake the analysis necessary to amend its claim, without prejudice to its ability to appeal today's holding.

Today's holding is also without prejudice to Dommer's right to argue that NOA's 6 - 8 are unenforceable, and to argue that the *Dick's* case has no application at all here.

The parties are encouraged to undertake negotiations that might result in an agreement as to a reduced claim that would not be opposed by the Debtor.

BFG shall so amend its claim within 30 days, or else <u>its</u> claim will be disallowed as being too speculative.

In other proceedings here, BFG, as one holding a claim that has yet to be allowed or disallowed, is vigorously pursuing discovery as to possible avoiding actions as to transfers to the Debtor's insiders. This Court's Orders in that regard are hereby suspended. This is because the Debtor has proffered that if BFG is not actually a creditor, or is a creditor only in a much-reduced amount, the Debtor might have been solvent at all material times. Now having ruled that BFG's claim is not longer entitled to Rule 3001(f)'s presumptions, the Debtor's proffer might be

dispositive of such matters.

This matter is restored to the Court calendar for hearing at the U.S. Bankruptcy Court, Olympic Towers, 300 Pearl Street, Part 1, Buffalo, New York, on March 30, 2011 at 10:00 a.m., for a status report after the amended claim has been filed.

SO ORDERED.

Dated: Buffalo, New York
March 3. 2011

s/Michael J. Kaplan

U.S.B.J.

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF NEW YORK

BUSINESS FUNDING GROUP,

Appellant,

v.

DECISION AND ORDER
11-CV-565S

DOMMER CONSTRUCTION CORP.,

Appellee.

I. INTRODUCTION

Appellant and creditor, Business Financial Group ("BFG"), seeks reversal of the Order of the Hon. Michael J. Kaplan, United States Bankruptcy Judge, Western District of New York, which found that appellee and debtor, Dommer Construction Corp. ("Dommer"), could offset certain debt it owed BFG.[1] In rendering his judgment, Judge Kaplan expressly disagreed with a previous New York State court decision that came to a contrary conclusion. Specifically, BFG appeals Judge Kaplan's finding that the Rooker-Feldman doctrine did not apply, allowing him to come to a different conclusion than the New York State court. For the following reasons, Judge Kaplan's Order is affirmed.

II. BACKGROUND

The precise nature of Dommer's underlying petition in the bankruptcy court and the background explaining how Dommer became indebted to BFG are irrelevant to this action. It suffices to note that Dommer is a general contractor that became liable to BFG for loans that BFG provided to Dommer's subcontractor, MBE Group Inc. See In re Dommer Constr. Corp., No. 10-12764K, 2011 WL 832901, at *1 (W.D.N.Y. Mar. 3, 2011).

[1]BFG argues that Judge Kaplan's Order is final and therefore subject to appeal under Rule 8002 of the Federal Rules of Bankruptcy Procedure. To the extent that the Order is interlocutory, BFG is granted leave to appeal pursuant to Bankruptcy Rule 8003.

BFG eventually sued on this debt in New York State court. On March 29, 2010, the New York State Supreme Court, County of Erie, found Dommer liable in the amount of $438,725.17. Bus. Funding Grp., Inc. v. Dommer Constr. Corp., Index No. 2005-5161 (N.Y. Sup. Ct. Mar. 29, 2010) (unreported). Several months later, on June 22, 2010, the same court denied Dommer's motion for reconsideration and subsequently signed a judgment in BFG's favor for the aforementioned amount. (Dommer's Objection to BFG's Motion for Leave to Appeal ("Objection"), ¶ 6; Docket No. 4-11.) But before that judgment was entered at the Erie County Clerk's Office, Dommer filed for relief in the bankruptcy court under Chapter 11, thus automatically staying the entry of a final judgment. (Id., ¶ 11.) There is, therefore, no dispute that the judgment was not final and binding under New York State law. See N.Y. C.P.L.R. §§ 5017, 5018(a),(c) (McKinney 2011).

Thereafter, on July 26, 2011, Dommer filed a motion in the bankruptcy court requesting that the automatic stay be lifted to allow entry of the New York judgment, thus allowing Dommer to appeal the decision. (Objection, ¶ 11.) That motion was opposed by BFG, but the parties eventually agreed that because the judgment was not final, the bankruptcy court could review the state court decision. (Id., ¶ 13.)

Consequently, on March 3, 2011, Judge Kaplan issued an Order disagreeing with the state court as it applied to Dommer's debt and instructed BFG to amend its Proof of Claim, which was premised on the state-court decision. In re Dommer, 2011 WL 832901.

However, despite the earlier agreement and a subsequent order concerning the bankruptcy court's ability to review the state court's findings, BFG eventually reversed course, sought reconsideration of the March 3, 2011 Order, and argued that the bankruptcy court did not have subject-matter jurisdiction, pursuant to the Rooker-Feldman

doctrine, to review or alter the state court's decision as it applied to BFG's Proof of Claim in bankruptcy court.[2] (Objection, ¶ 20.) After oral argument, Judge Kaplan found that he was not barred by the doctrine and therefore denied BFG's motion for reconsideration on that ground. (Order on Motion for Reconsideration; Docket No. 3-16.)

This appeal followed.

III. DISCUSSION

A. Standard of Review

Under its appellate jurisdiction, this Court conducts a *de novo* review of the law. In re Porges, 44 F.3d 159, 162 (2d Cir. 1995); Teufel v. Schlant, No. 02-CV-81S, 2002 WL 33008689, at *4 (W.D.N.Y. Sept. 25, 2002). The facts, which would be reviewed for clear error, are undisputed. See In re Alper Holdings USA, Inc., 398 B.R. 736, 747 (S.D.N.Y. 2008)

B. Rooker-Feldman Doctrine

Federal district and bankruptcy courts are "courts of limited jurisdiction." Exxon Mobil Corp. v. Allapattah Servs., Inc., 545 U.S. 546, 552, 125 S. Ct. 2611, 162 L. Ed. 2d 502 (2005) (internal quotations omitted). The Rooker-Feldman doctrine, named for a pair of Supreme Court cases, Rooker v. Fidelity Trust Co., 263 U.S. 413, 414-15, 44 S. Ct. 149, 68 L. Ed. 362 (1923) and District of Columbia Court of Appeals v. Feldman, 460 U.S. 462, 486, 103 S. Ct. 1303, 75 L. Ed. 2d 206 (1983), emphasizes the limited nature of this jurisdiction. Even if "otherwise [] empowered to adjudicate" a dispute, the doctrine bars all

[2]Such a reversal is not barred by waiver or estoppel as "[s]ubject-matter jurisdiction can never be waived or forfeited" and objections thereto "may be resurrected at any point in the litigation." Gonzalez v. Thaler, --- U.S. ---- 132 S. Ct. 641, 648, 181 L .Ed. 2d 619 (2012).

federal courts, except the Supreme Court, from hearing "cases brought by state-court losers complaining of injuries caused by state-court judgments rendered before the district court proceedings commenced and inviting district court review and rejection of those judgments." Exxon Mobil Corp. v. Saudi Basic Indus. Corp., 544 U.S. 280, 284, 291, 125 S. Ct. 1517, 161 L. Ed. 2d 454 (2005).

There is no dispute that the bankruptcy court was "otherwise [] empowered to adjudicate" the Proof of Claim at issue there. See Id., 544 U.S. at 291. However, BFG argues that because the state court already adjudicated that very issue, the bankruptcy court was divested of its jurisdiction by operation of the Rooker-Feldman doctrine. If BFG's argument is correct, the bankruptcy court would be precluded from disagreeing with state-court's findings and BFG's Proof of Claim would remain at $438,725.17. If not, BFG must amend its Proof of Claim and "must resort to the traditional means of supporting a Proof of Claim, as if the matter had not been decided by the state court at all" in accordance with Judge Kaplan's order. In re Dommer, 2011 WL 832901, at *9.

In this Circuit, the Rooker-Feldman doctrine has been consistently interpreted to impose four conditions, each of which must be met for it to apply: (1) the party raising the claim must have lost in state court; (2) that party's injuries must be caused by the state court judgment; (3) that party's claims must invite the district court to review and reject the state court judgment; and (4) the state court judgment must have been rendered prior to the commencement of the federal court proceedings. Hoblock v. Albany Cnty. Bd. of Elections, 422 F.3d 77, 85 (2d Cir. 2005).

BFG argues that each of the four elements have been met in this case. But the bankruptcy court, under an admittedly narrow understanding of the second factor, found,

as Dommer now argues, that no injuries were "caused by" the state court's judgment. Under recent Supreme Court and Second Circuit precedent, the bankruptcy court's position is correct.

In 1983, the Supreme Court held that district courts do not have jurisdiction "over challenges to state court decisions." Feldman, 460 U.S. at 462. Under that broad understanding, it would appear that the doctrine would have barred the bankruptcy court from hearing Dommer's claim, since it amounted to a challenge to a state-court decision. However, in 2005, in Exxon Mobil Corp., the Court made it clear that the doctrine should be "confined to cases of the kind from which the doctrine acquired its name: cases brought by state-court losers complaining of injuries *caused by* state-court." 554 U.S. 284 (emphasis added).

Soon thereafter, the Second Circuit had occasion to define Rooker-Feldman's reach in light of Exxon Mobil Corp. See Hoblock, 422 F.3d 77. It cautioned that the Rooker-Feldman doctrine is meant to occupy "narrow ground," and characterized the Supreme Court's holding as "paring back the Rooker-Feldman doctrine to its core." Id. at 85; see also Green v. Mattingly, 585 F.3d 97, 101 (2d Cir. 2009) (noting that before Exxon Mobil Corp., "[t]here was a time when this Circuit applied the Rooker-Feldman doctrine 'expansively,' viewing it as 'effectively coextensive with the doctrines of claim and issue preclusion'") (internal citations omitted). The Hoblock court then detailed the four requirements necessary for the doctrine to apply. Under the second requirement – the "caused by" requirement – the court noted that "an 'independent' (and therefore non-barred) claim may 'den[y] a legal conclusion' reached by the state court[,]" suggesting "that a plaintiff who seeks in federal court a result opposed to the one he achieved in state

court does not, for that reason alone, run afoul of Rooker–Feldman." 422 F.3d at 85 (quoting Exxon Mobil Corp., 544 U.S. at 293).

The Hoblock court then reiterated that the source of the injury must be the state-court judgment and provided an example:

> Suppose a plaintiff sues his employer in state court for violating both state anti-discrimination law and Title VII and loses. If the plaintiff then brings the same suit in federal court, he will be seeking a decision from the federal court that denies the state court's conclusion that the employer is not liable, but he will not be alleging injury from the state judgment. Instead, he will be alleging injury based on the employer's discrimination. The fact that the state court chose not to remedy the injury does not transform the subsequent federal suit on the same matter into an appeal, forbidden by Rooker-Feldman, of the state-court judgment.

Hoblock, 422 F.3d at 87-88.

In accordance with the above-stated example and explanation, Dommer was not seeking relief caused by a state-court judgment because the state court's judgment, as both parties agree, had no legal effect on Dommer until it was properly filed with the Erie County Clerk. Since it was not so filed, it cannot be said that Dommer sought relief caused by the state-court's ruling because the judgment caused no legally recognizable change in Dommer's bottom line. Certainly, Dommer sought a result "opposed to the one he achieved in state court" but under Hoblock, such relief does not implicate Rooker-Feldman. The bankruptcy merely "den[ied] a legal conclusion" reached by the state court, as it was free to do under Exxon and Hoblock.

Of course, once the state action is complete, "[d]isposition of the federal action . . . would be governed by preclusion law." Exxon Mobil Corp., 544 U.S. at 293. As the court explained, "[i]n parallel litigation, a federal court may be bound to recognize the claim- and

issue-preclusive effects of a state-court judgment, but federal jurisdiction over an action does not terminate automatically on the entry of judgment in the state court." Id. In other words, "Rooker-Feldman and preclusion are entirely separate doctrines." Hoblock, 422 F.3d at 85. But preclusion is inapplicable here because the preclusive effect of a state court's judgment is a matter of state law, see id., at 92-93, and there is no dispute that the state court's judgment does not have such an effect under New York law.

Accordingly, the Rooker-Feldman doctrine did not apply to the bankruptcy court's adjudication of BFG's Proof of Claim and the court properly exercised its subject-matter jurisdiction.[3]

C. Stern v. Marshall

On the final pages of its reply brief, BFG, for the first time, argues that the bankruptcy court did not have "jurisdiction to hear [Dommer's] subrogation claim" pursuant to the Supreme Court's holding in Stern v. Marshall, a decision that was issued before this appeal was commenced. 131 S. Ct. 2594, 180 L. Ed. 475 (2011). This issue was never raised in the bankruptcy court.

New arguments, however, may not be made in a reply brief and this Court accordingly declines to entertain this new theory. See Ernst Haas Studio v. Palm Press, Inc., 164. F.3d 110, 112 (2d Cir. 1999).

Moreover, even if this Court were to consider this argument, it has been prematurely and insufficiently raised [4] The Court in Stern held that a bankruptcy court cannot enter a

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[3]In an effort to argue that Judge Kaplan conducted an impermissible appeal of the state-court's ruling, BFG raises several concerns regarding the adequacy of his fact-finding process. But this issue, if it is an issue at all, is not presently before this Court.

[4]BFG's argument applying Stern to this case is limited to one paragraph.

judgment on a counterclaim that is based exclusively on a right assured by state law. But here, Judge Kaplan has not yet entered a judgment on Dommer's "subrogation claim," and, among other issues that go unaddressed by BFG, is it unclear whether BFG consented to the bankruptcy court's jurisdiction to hear Dommer's claim. See Stern,131 S. Ct. at 2621 (Scalia, J. concurring) (counting at least seven different factors, lack of consent among them, to be considered before ruling that an Article-III judge is required to adjudicate a lawsuit).

BFG's motion on this ground is therefore denied.

IV. CONCLUSION

For the foregoing reasons, this Court affirms the Order of the bankruptcy court.

V. ORDERS

IT HEREBY IS ORDERED, that the Order of the Bankruptcy Court, Western District of New York, is AFFIRMED.

FURTHER, that the appeal (Docket No. 1) is DENIED and DISMISSED.

FURTHER, that the Appellant's Motion to Stay is DENIED as moot.

FURTHER, that the temporary stay (Docket No. 9) is lifted.

FURTHER, that the Clerk of the Court shall take the steps necessary to close this case.

SO ORDERED.

Dated: March 26, 2012
Buffalo, NY

/s/William M. Skretny
WILLIAM M. SKRETNY
Chief Judge
United States District Court