Delaware Bankruptcy American Inn of Court CLE Program

Title of Program: Involuntary Bankruptcy Filings

Location: United States Bankruptcy Court for the District of Delaware, 824 Market Street, 5th Floor, Courtroom No. 5, Wilmington, Delaware

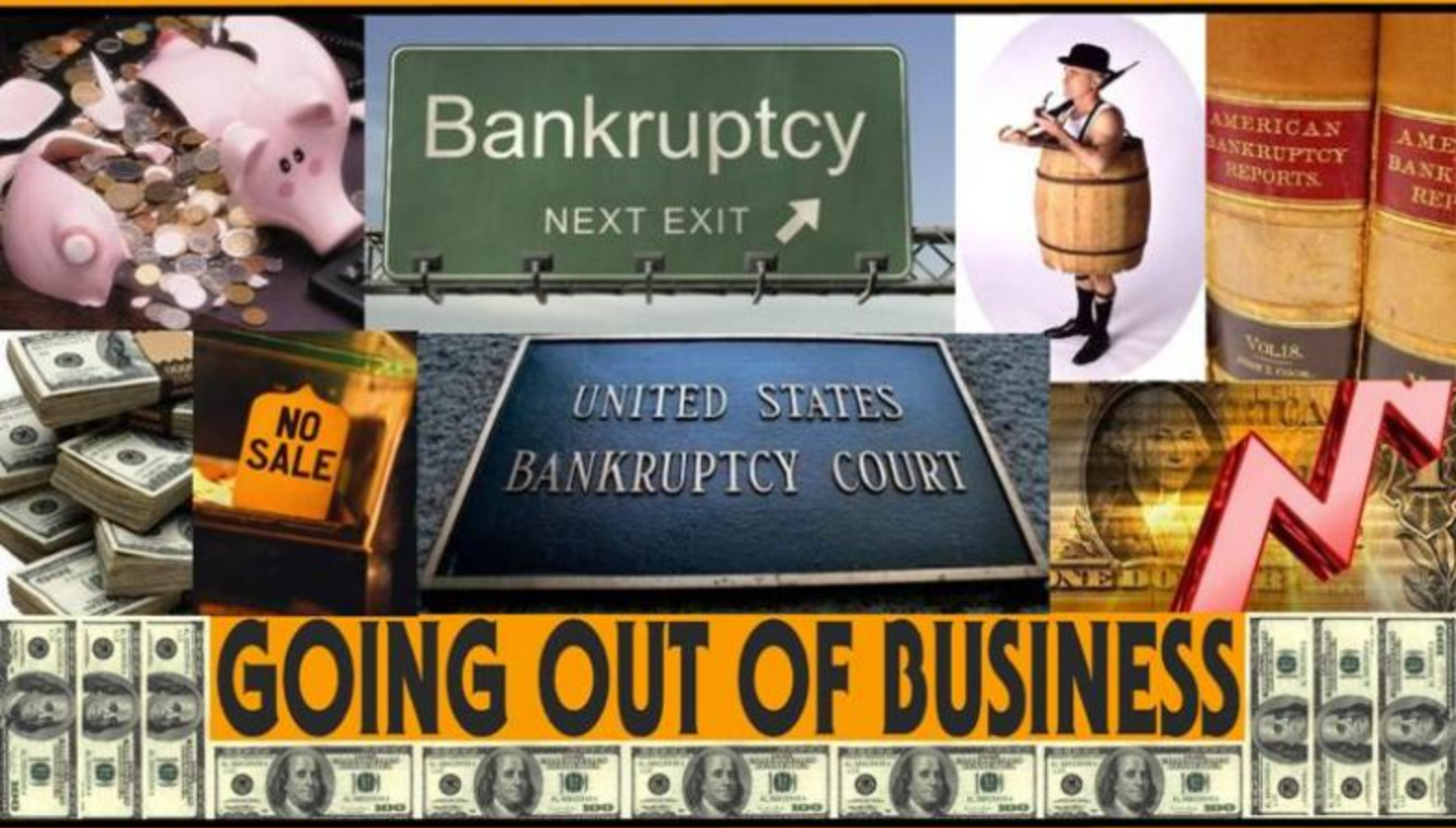
Date: January 19, 2010

Time: 5:30 p.m. to 7:00 p.m.

Length: 1.5 hours

Empty Pocket Productions
Presents

INVOLUNTARY



One Night Only at the Bankruptcy Court Theater

824 MARKET STREET - WILMINGTON, DE 19801

January 19, 2010 at 5:30 p.m.

The Broken Piggy Bank Theater Company

Production Staff

Executive Producer ..... Ed Kosmowski
Executive Director ..... Karen McKinley
Act One Producer ..... Matt McGuire
Act Two Producers ..... Shelly Kinsella and Maris Finnegan
Act Three Producer ..... Kim Lawson

Production Designers

Act One ..... Matt McGuire
Act Two ..... Shelly Kinsella and Donna Harris
Act Three ..... Kim Lawson
Briefs ..... Mark Chehi and Howard Cohen

Writers

Medical Organization Incorporated Brief ..... Howard Cohen, Kevin Collins and Zachary Haupt
Vaccine Corporation Brief ..... Mark Chehi, Doug Herrmann and Yosef Ibrahimi
Court's Opinion ..... Ron Gellert and Marisa Terranova

Cast

Act I
Medical Organization Incorporated CEO ..... Kelly Conlan
Medical Organization Incorporated Bankruptcy Counsel ..... Julie Finocchiaro
Medical Organization Incorporated Litigation Counsel ..... Nathan Catchpole

Act II
Vaccine Corporation CEO ..... Alissa Gazze
Vaccine Corporation Bankruptcy Counsel ..... Shelly Kinsella

Act III
Vaccine Corporation Bankruptcy Counsel ..... Seth Brostoff
Medical Organization Incorporated Bankruptcy Counsel ..... Kristine Grigorian
United States Trustee ..... Terri Brown-Edwards
Bankruptcy Judge ..... Ron Gellert
Law Clerk ..... Marisa Terranova

The Broken Piggy Bank Theater Company
and Empty Pocket Productions
proudly present

INVOLUNTARY

ACT I ..... A Plan Is Hatched
Scene: The Boardroom of Medical Organization Incorporated
The CEO of Medical Organization Incorporated meets with Bankruptcy and Litigation Counsel to discuss the possibility of filing an Involuntary against Vaccine Corporation.

ACT II ..... What Now?
Scene: The Boardroom of Vaccine Corporation
The CEO of Vaccine Corporation meets with Bankruptcy Counsel to discuss options now that Medical Organization Incorporated has filed an Involuntary naming Vaccine Corporation as the alleged debtor.

ACT III ..... The Courtroom Drama
Scene: United States Bankruptcy Court
The Courtroom drama unfolds after Medical Organization Incorporated files its Brief in Support of the Involuntary and Vaccine Corporation files its Motion to Dismiss the Involuntary.

WRITTEN MATERIALS

INVOLUNTARY
FACT PATTERN

Vaccine Corporation ("VC") is a privately held company that develops and manufactures vaccines. VC has two lines of business: (i) the development and manufacture of vaccines and (ii) the development of new technology (the "IP") which permits production of new vaccines at an accelerated rate. VC is an operating company with 100 employees, many customers and many trade suppliers. Its original capitalization (a combination of debt and equity) was the result of investment by its current Chief Executive Officer ("CEO") and current Chief Operating Officer ("COO"), but since that time many other investors, both individual and institutional, have provided equity investment in VC.

VC has been developing a promising new swine flu vaccine ("Vaccine"), which is currently in the clinical trials phase and showing excellent results. While both the Vaccine and the IP are promising, VC has been having financial trouble for the past two years due to unexpected costs and delays in obtaining FDA approval for the Vaccine, as well as unexpected costs of developing the IP. While these investments appear to be on the verge of paying off, VC has been unable to pay some debts that recently became due, and certain of its creditors are losing patience.

Due to VC's difficulty paying its debts, VC entered into negotiations and signed a letter of intent, subject to shareholder approval, to sell all of its assets (the "MOI APA") to Medical Organization Incorporated ("MOI").[1] In anticipation of the potential sale and in order to aid cash flow, MOI loaned VC $50 million evidenced by a promissory note (the "Note") secured by a lien on substantially all of VC's assets. The MOI APA included a "no shop" provision that

1 CEO and COO, who each hold a 10% interest in VC, do not believe the MOI APA is in the best interest of VC's shareholders.

prohibited VC from soliciting competitive transactions. It also prohibited the disclosure of any financial information and/or the business plans of VC.

Over the objections of CEO and COO, the VC Board approved the MOI deal, which also required shareholder approval. Although several board members felt pressured to vote in favor of going forward with the MOI APA due to VC's financial situation, one board member, Ms. Barbara Boardmember, was overheard saying she believed that if the deal goes through, MOI is getting "the deal of the century."

Unfortunately, the VC shareholders did not approve the proposed asset sale of VC as many shareholders believe that VC has significantly more value than the MOI deal attributes to it. MOI subsequently sued VC in state court alleging that the CEO and COO had fraudulently obtained shareholder disapproval. For its part, VC accused MOI of disavowing critical portions of its LOI. Needless to say, there was no love lost between VC and MOI, and VC did not pay the Note when it became due. VC attempted to line up several investors willing to purchase MOI's debt at full price, but MOI refused to cooperate with any of the potential investors.

While that action was pending, VC signed a multi-million dollar contract with the U.S. government for the development of the Vaccine (the "Government Contract"). The Government Contract has a base value of $37 million, and may be worth a total of $147 million to VC. Final approval of the Government Contract however is contingent upon a showing of financial stability by VC. The award of the Government Contract has dramatically increased the likelihood that VC will be able to obtain similar contracts from other governmental entities around the world, thereby bringing in significant revenues to VC. In fact, negotiations are underway with several countries to license VC's technology. Contingent on final approval of the Government Contract, France has offered a $2 million up-front payment to license VC's proprietary technology to

produce the vaccine. Other licenses, with up to $18 million in up-front payments, are currently under negotiation.

The day after VC signed the Government Contract, MOI filed an involuntary petition (the "Involuntary Petition") under chapter 7 of the Bankruptcy Code naming VC as the alleged debtor. MOI was joined by in its petition by Clinical Testing, Inc. ("Testing") and Consulting Services, LP ("Consulting"). MOI alleges that it is owed $51.5 million based on the note. Testing is owed $1,200,000 in connection with some clinical testing services it provided to VC and Consulting is owed $300,000 in connection with consulting services it provided to VC in connection with the potential sale to MOI. The $300,000 owed to Consulting is based upon three monthly invoices of $100,000 each. ($100,000 is due 30 days from the date the Involuntary Petition was filed, $100,000 is currently due, and $100,000 is 30 days past due.) Although the Consulting invoices are due thirty (30) days from receipt (thereafter a 1% per month late charge may be assessed), VC has in the past paid some Consulting invoices between 30 and 60 days from receipt with no late charges ever assessed by Consulting. As for Testing, although VC had not previously notified Testing, VC believes it has a valid dispute for $20,000 of the $1,200,000 claim alleged by Testing.[2] Other than the foregoing, VC does not dispute the claims of MOI, Testing, or Consulting. Additionally, VC has been slow paying many of its trade creditors.

VC believes that the filing of the Involuntary Petition has been orchestrated by MOI as a litigation tactic to either (i) put pressure on VC shareholders to approve the MOI APA or (ii) take control of VC through the chapter 7 proceeding. An independent financial report indicates that VC is worth substantially more as a going concern as opposed to if its assets were liquidated.

2 As part of the agreement with Testing, VC was to receive a clinical testing report, to which both parties stipulate is valued at $20,000. Testing has not provided the report to VC.

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	:	
	:	Involuntary Chapter 7
Vaccine Corporation,	:	
	:	Case No. 10-12345 (RG)
Alleged Debtor.	:	
	:	

Vaccine Corporation's Pretrial Brief

ARGUMENT

I. THE INVOLUNTARY PETITION FAILS TO MEET THE REQUIREMENTS OF 11 U.S.C. § 303

Testing,[1] Consulting and MOI (the "Petitioning Creditors") cannot satisfy the three part test of 11 U.S.C. § 303 necessary to sustain an involuntary petition against VC. That test requires that (i) three or more creditors (where the alleged debtor has 12 or more creditors) each hold a claim "that is not contingent as to liability or the subject of a bona fide dispute as to liability or amount," (ii) the creditors' "noncontingent undisputed claims" must be undersecured by at least $13,475 in the aggregate; and (iii) the purported debtor "is generally not paying [its debts as they become due] unless such debts are the subject of a bona fide dispute as to liability or amount." *See* 11 U.S.C. §§ 303(b)(1), (h)(1).

Accordingly, the involuntary case commenced against VC must be dismissed with its costs and reasonable attorneys' fees being borne by the Petitioning Creditors. *See* 11 U.S.C. § 303(i)(1). Moreover, the Court should grant a judgment in favor of VC for punitive and consequential damages based on MOI's bad faith. *See* 11 U.S.C. § 303(i)(2).

1 Capitalized terms not defined herein shall have the meaning as prescribed in the Statement of Facts.

A. Testing's and Consulting's Claims are the Subject of Bona Fide Disputes

Neither Testing nor Consulting qualify as petitioning creditors because their purported claims are subject to bona fide disputes. Since neither qualify, the first prong of Section 303(b)(1) cannot be met and the Involuntary Petition should be dismissed.

Although the Bankruptcy Code does not define the term "bona fide dispute," the Third Circuit has held that a bona fide dispute exists:

> If there is a genuine issue of material fact that bears upon the debtor's liability, or a meritorious contention as to the application of law to undisputed facts. Under this standard, the bankruptcy court must determine whether there is an objective basis for either a factual or a legal dispute as to the validity of debt.

In re AMC Investors, LLC, 406 B.R. 478, 483-84 (Bankr. D. Del.) (*citing B.D.W. Assoc. v. Busy Beaver Bldg. Ctrs.*, 865 F.2d 65, 66 (3d Cir. 1989)) (additional internal citations omitted). "The burden is on the petitioning creditor to first establish a prima facie case that no bona fide dispute exists." *In re AMC Investors, LLC*, 406 B.R. at 484 (*citing In re Busick*, 831 F.2d 745, 750 (7th Cir. 1987)). Only after the petitioning creditors establish a prima facie case does "the burden shift[] to the alleged debtor to demonstrate the existence of a bona fide dispute." *In re AMC Investors, LLC*, 406 B.R. at 484 (*citing Key Mechanical, Inc. v. BDC 56, LLC, In re BDC 56 LLC*, 330 F.3d 111, 118 (2d Cir. 2003)).

Under 11 U.S.C. § 303(b)(1), as amended by the Bankruptcy Abuse and Consumer Protection Act of 2005 ("BAPCPA"), a bona fide dispute may relate to either "liability or amount." Prior to BAPCPA, a dispute limited to the amount was not a "bona fide dispute" as to the entire claim under Section 303(b)(1). *See, e.g., In re Focus Media, Inc.* 378 F.3d 916, 926 (9th Cir. 2004) ("a dispute as to the amount of the claim gives rise to a bona fide dispute only when (1) it does not arise from a wholly separate transaction and (2) netting out the claims of the debtors could take the

petitioning creditors below the amount threshold of § 303"); *In re BDC 56 LLC*, 330 F.3d at 120 (2d Cir. 2003) (bona fide dispute exists "where a claim for offset arises out of the same transaction and is directly related to the creditor's underlying claim, and, if valid, could serve as a complete defense to that claim.").

Post enactment, a majority of courts considering the effect of BAPCPA as to the bona fide dispute element of Section 303(b)(1) have determined that "[a]s a result of the amendment, any dispute regarding the amount that arises from the same transaction and is directly related to the underlying claim should render the claim subject to a bona fide dispute." *In re Reg'l Anesthesia Assocs.*, 360 B.R. 466, 470 (Bankr. W.D. Pa. 2007); *see also Riverview Trenton R.R. Co. v. DSC Ltd. (In re DSC, Ltd.)*, 486 F.3d 940, 947 (6th Cir. 2007) (holding Congress made clear its intent to disqualify creditors when any legitimate basis, factual or legal, existed for debtor not to pay claim); *In re Euro-American Lodging Corp.*, 357 B.R. 700, 712 (Bankr. S.D.N.Y. 2007) (holding that, under BAPCPA, any dispute arising from same transaction should render a claim subject to a bona fide dispute); *In re Orlinsky*, 2007 WL 1240207, at *1 (Bankr. S.D. Fla. April 24, 2007) (creditors whose claims are partially disputed "are creditors whose claims are 'the subject of a bona fide dispute as to liability or amount' as that term is used in § 303(b)(1)"); *In re Tobacco Rd. Assocs., L.P.*, 2007 U.S. Dist. LEXIS 22990 (E.D. Pa. Mar. 30, 2007) (noting same); *In re Hentges*, 351 B.R. 758 (Bankr. N.D. Okla. 2006) (disqualifying petitioning creditor because the portion of its claim pertaining to attorney's fees and costs was subject to bona fide dispute).[2]

2 There are a few bankruptcy courts that have interpreted BAPCPA's addition of the words "as to liability or amount" to Section 303(b)(1) as not effecting a change in the meaning of the statute. Those cases are inconsistent with the principles of statutory interpretation. The courts in each of those cases refused to presume that Congress intended to disqualify claims that were partially disputed without committee comments or other supporting legislative history. *See In re Demirco Holdings, Inc.*, No. 06-70122, 2006 WL 1663237 (Bankr. C.D. Ill. June 9, 2006), *In re Mylotte, David & Fitzpatrick*, No. 07-11861, 2007 WL 2033812 (Bankr. E.D. Pa. July 12, 2007) and *In re Knight*, 380 B.R. 67 (Bankr. M.D. Fla. 2007). As the United States Supreme Court has made clear, however, "[t]he starting point in discerning congressional intent [] is the existing statutory text, and not predecessor statutes." *Lamie v. United States Trustee*, 540 U.S. 526, 527 (2004). Furthermore, the general presumption is that a

1. Testing's Claim is Subject to a Bona Fide Dispute as to Amount

Testing asserts a claim for $1,200,000 for testing services that it provided VC. VC disputes a portion of the claim because Testing failed to provide a certain report with a stipulated value of $20,000. The failure to produce the required report renders Testing's claim subject to a bona fide dispute as to amount. The fact that the disputed amount does not reduce Testing's total claim to less than $13,475 is immaterial. Section 303(b)(1) provides that any dispute arising from the same transaction and directly related to the underlying claim renders that claim subject to a bona fide dispute. *See, e.g.*, *In re Reg'l Anesthesia Assocs.*, 360 B.R. 466, 470 (Bankr. W.D. Pa. 2007) ("any dispute regarding the amount that arises from the same transaction and is directly related to the underlying claim should render the claim subject to a bona fide dispute.").

Under the parties' agreement, Testing was required to prepare the testing report for VC. Therefore, the report is part of the transaction giving rise to Testing's right to payment and also, therefore, directly related to Testing's underlying claim. Additionally, VC may have counterclaims against Testing for any direct and consequential damages VC has suffered due to Testing's failure

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> legislature enact[ing] an amendment indicates that it intended to change the original act by creating a new right or withdrawing an existing one. Therefore, any material change in the language of the original act is presumed to indicate a change in legal rights…. The presumption of change is not conclusive and may be overcome by more persuasive considerations. Although generally, a statutory amendment is presumed to have been intended to change the law, legislative history may indicate that the amendment was intended as a clarification…. The legislature is presumed to know the prior construction of terms in the original act, and an amendment substituting a new term or phrase for one previously construed indicates that the judicial or executive construction of the former term or phrase did not correspond with the legislative intent and a different interpretation should be given the new term or phrase…. An amendment of an unambiguous statute indicates an intent to change the law.

See Norman Singer and J.D. Shambie Singer, *Sutherland on Statutory Construction*, §22:30.

The *Demirco* court and its progeny, therefore, erred in reasoning that some special showing of legislative history was needed to diverge from prior case law applying former § 303(b)(1). In fact, a special showing of legislative history would be required to establish that the BAPCPA amendment to Section 303(b) *did not change the meaning of that section*. The plain text of Section 303(b)(1), therefore, now excludes, for the purposes of determining whether an involuntary petition is proper, any consideration of claims that are subject to a bona fide dispute over amount. Giving effect to the plain meaning of this text does not lead to "absurd" results, because excluding consideration of claims that are the subject to a dispute over amount serves a legitimate Congressional purpose – preventing debtors from being dragooned into bankruptcy as a means of litigating a disputed claim. Indeed, there is no requirement that Congress enact an involuntary bankruptcy system, and so limiting the classes of creditors that may petition for an involuntary bankruptcy is well within Congress' power and discretion. Therefore, unless *all three* petitioning creditors establish that there is no bona fide dispute as to liability *or* amount on their claims Vaccine Corp. is entitled to dismissal.

to provide the required testing report. Those counterclaims may provide further amounts giving rise to a bona fide dispute in respect of Testing's claim. As a result of these disputes, there is no basis for the Court to consider only the undisputed portion of Testing's claim in determining whether Testing qualifies as a proper petitioning creditor.

2. Consulting's Claim is Subject to a Bona Fide Dispute as to Amount

Consulting alleges that it has a claim for $300,000 based on consulting services it provided VC in connection with the potential sale to MOI. Consulting evidences its claim using three monthly invoices, equal in value. The terms of payment under each of the invoices is thirty days from receipt with the right to impose a 1% late charge per month after an invoice is thirty days past due. At the time the involuntary bankruptcy petition was filed one invoice was due thirty days from petition date, one invoice was currently due and one invoice was thirty days past due. Based upon their course of dealing, the parties have altered the payment terms from thirty days after receipt of an invoice to payment being due sometime after thirty days but prior to sixty days after receipt. Consulting has not once assessed late charges upon VC either with respect to these consulting services or on prior consulting invoices that VC paid thirty or sixty days after receipt. This course of dealing makes clear that the payment terms on Consulting's invoices have been modified. Thus, Consulting's claim is subject to a bona fide dispute with payment on one invoice currently due and payment on the other two not yet due.

A course of dealing between parties "establishes the common basis of understanding" for interpreting the parties' expressions and conduct and "gives meaning to or supplements or qualifies [the parties'] agreement." Rest. Contracts 2d. § 223. Here, course of dealing between the parties, rather than the terms on the invoices, is a better gauge of the parties' understanding on terms of payment. At the time the involuntary petition was filed, only one of Consulting's invoices was

current. The other two were subject to a bona fide dispute based on the parties' clear course of dealing with payment terms of more than 30 days but less than 60 days. Any dispute as to amount gives rise to a bona fide dispute if it arises from the same transaction and is related to the petitioning creditor's underlying claim. *In re Reg'l Anesthesia Assocs.*, 360 B.R. 466, 470 (Bankr. W.D. Pa. 2007); *In re Euro-American Lodging Corp.*, 357 B.R. 700, 712 (Bankr. S.D.N.Y. 2007). VC's dispute over payment of the two unmatured invoices arises from the same transaction (the provision of consulting services) and is intrinsically related to Consulting's underlying claim for consulting services. As a result, Consulting does not qualify as a proper petitioning creditor.[3]

B. MOI's Claim is Fully Secured and Therefore Does not Meet the Aggregation Requirement

Even assuming Testing and Consulting qualify as petitioning creditors – which they do not – the requirements of Section 303 still are not met because MOI's noncontingent, undisputed claim does not meet the requirement set forth in Section 303(b)(2) because in the aggregate it is less than "at least $13,475 more than the value of any liens on property of the debtor securing the [petitioning creditor's] claims."

In anticipation of the potential sale of VC to MOI and in order to aid VC's cash flow, MOI loaned VC $50 million evidenced by the Note. MOI secured the Note by a lien on substantially all of VC's assets. As such, MOI is a fully secured creditor. Fully secured claims do not count towards the aggregation requirement of 11 U.S.C. §§ 303(b)(1) or (b)(2).[4] *See In re AMC Investors, LLC*, 406 B.R. at 483 (Bankr. D. Del. 2009) (holding that where there are fewer than 12

[3] Moreover, even assuming the course of dealing does not modify the payment terms, Consulting's purported claim is subject to a bona fide dispute. One of the invoices is not yet due, because under the express terms of the final invoice, payment is not due on that invoice until thirty days after the Involuntary Petition was filed.

[4] The aggregation requirements contained in 11 U.S.C. §§ 303 (b)(1) and (b)(2) are identical. The only difference between the two subparagraphs is their scope: subparagraph (b)(1) applies where there are more than 12 creditors and subparagraph (b)(2) applies where there are fewer than 12 creditors.

claimholders, single petitioning claimholder must be undersecured by at least $13,475) (internal citations omitted).

MOI is oversecured. The assets of VC include the Vaccine and its related, proprietary intellectual property (the "IP"). The Vaccine and the IP are on the verge of paying huge dividends. Recently, VC signed, subject to final approval, a Government Contract that is worth a minimum of $37 million and has the potential to be worth up to $147 million. Adopting a conservative mid-point valuation, the government contract is worth $92 million – a figure well in excess of MOI's claim for $51.5 million.

Additionally, VC is negotiating licensing the Vaccine to foreign governments. Already, the French government has offered an up-front payment of $2 million to license VC's swine flu vaccine, pending final approval of the Government Contract. VC is also negotiating with other prospective licensees for a potential $18 million in up-front payments. Those sums represent only additional payments and VC would also stand to gain millions in recurring license fees.

MOI may argue that the Note is undersecured and that final approval of the Government Contract is unlikely, because VC may be unable to make the requisite showing of financial stability necessary for final approval. The argument follows that without final approval of the Government Contract, the Note is worth far less than VC's assets. However, this argument ignores the fact that VC's financial distress was due to unexpected costs and delays in obtaining FDA approval for the Vaccine, as well as unexpected costs of developing the IP. In addition, this argument ignores the facts that the clinical trials phase of the Vaccine is showing excellent results and is on the verge of final FDA approval. Moreover, VC appears to be on solid financial footing, as evidenced by the fact that numerous investors are willing to invest considerable sums of money in VC. Those investors are willing to pay off the Note in full.

MOI, however, has refused to cooperate with VC and its potential investors because it wants to use this involuntary bankruptcy petition to loot VC of the swine flu vaccine and related IP, two valuable assets. If MOI's real concern was securing full payment on the Note, it never would have filed an involuntary bankruptcy petition. Instead, MOI would have seized the chance to be repaid in full, because full recovery is a dim prospect in most bankruptcy cases.

MOI's claim is fully secured and as a result, MOI cannot meet the aggregation requirements of 11 U.S.C. §§ 303(b)(1) or (b)(2).

C. The "Generally Not Paying Debts" Requirement of 11 U.S.C. § 303(h)(1) is Not Satisfied

Given that VC has timely controverted the Involuntary Petition, the Petitioning Creditors must -- but cannot -- establish that VC "is generally not paying [its] debts as [they] come due." 11 U.S.C. § 303(h)(1); *See In re Caucus Distribs., Inc.*, 106 B.R. 890, 914 (Bankr. E.D. Va. 1989) (holding creditors carry the burden of establishing that the alleged debtor is generally not paying its debts as they come due).

Testing's and Consulting's claims are subject to bona fide disputes, and therefore, are excluded from a determination of whether VC is generally not paying its debts as they come due. *See In re AMC Investors*, 406 B.R. at 483.

There is "no mathematical test" that determines whether an alleged debtor is generally not paying its debts. Bankruptcy courts consider "the totality of the circumstances" and must "balance the interests of the debtor with those of the creditors." *See In re Norris*, 183 B.R. 437, 456 (Bankr. W.D. La. 1995) (*citing In re All Media Properties, Inc.*, 5 B.R. 142 (Bankr. S.D. Tex. 1980)). Factors that the court may consider are both the amount of debt not being paid and the number of creditors not being paid.

Admittedly, VC has been *slow* in paying its many trade creditors. However, the petitioning creditors cannot allege that VC *has not paid* its trade creditors, because the record establishes that Vaccine Corp. has only been *slow* in payment.

The only claim, not subject to a bona fide dispute that VC has not paid is MOI's secured claim. Failure to pay that one debt, without more, is not "general nonpayment." *See In re Smith*, 123 B.R. 423 (Bankr. M.D. Fla. 1990 (*aff'd* 129 B.R. 262 M.D. Fla. 1991). When considered under the "totality of the circumstances," VC's lack of payment on the Note -- even though it is a large debt -- does not establish that VC is generally not paying its debts as they come due.

Among the circumstances that should be considered are that: (i) MOI is the impediment to VC paying off its outstanding obligation under the Note; (ii) multiple investors are interested in VC; (iii) these investors are willing to pay off the Note in full as part of their investment in VC; and (iv) MOI's refusal to cooperate with those investors has frustrated VC's repayment of the Note. As a matter of equity, MOI's bad faith and ulterior motives should not be permitted to establish that VC is generally not making payments as they come do. Under the totality of the circumstances test, bankruptcy courts have considered whether the motives of the petitioning creditor are "something other than a self-centered desire to get paid." *See In re Harmsen*, 320 B.R. 188, 197 (10th Cir. BAP 2005). Given MOI's actions, the "totality of the circumstances" does not warrant a finding that VC is generally paying its debts as they come due.

II. BALANCING THE INTERESTS OF VACCINE CORP. AND ITS CREDITORS WEIGHS IN FAVOR OF DISMISSAL OR ABSTENTION UNDER 11 U.S.C. § 305(A)(1)

"[C]ourts that have construed Section 305(a)(1) are in general agreement that abstention in a properly filed bankruptcy case is an extraordinary remedy, and that dismissal is appropriate under Section 305(a)(1) only in the situation where the court finds that both 'creditors and the debtor'

would be 'better served' by a dismissal." *In re AMC Investors, LLC*, 406 B.R. at 487-88 (*citing In re Eastman*, 188 B.R. 621, 624 (9th Cir. BAP 1995)). Granting a dismissal "pursuant to § 305(a)(1) requires more than a simple balancing of harm to the debtor and creditors; rather, the interests of both the debtor and its creditors must be served by granting the requested relief." *In re AMC Investors, LLC*, 406 B.R. at 488; *see also In re Monitor Single Lift I, Ltd.*, 381 B.R. 455, 462 (Bankr. S.D.N.Y. 2008). The moving party "bears the burden to demonstrate that the interests of the debtors and creditors would benefit from dismissal." *See In re Globo Comunicacoes e Participacoes S.A.*, 317 B.R. 235, 255 (S.D.N.Y. 2004). Although dismissal under Section 305(a)(1) may be rare, MOI's bad faith motives in pursuing an involuntary petition establish that this case is the exceptional case where abstention is necessary.

In *In re AMC Investors, LLC*, the Court articulated seven factors to be considered in determining the best interests of the creditors and debtor, including:

> (1) the economy and efficiency of administration;
>
> (2) whether another forum is available to protect the interests of both parties or there is already a pending proceeding in state court;
>
> (3) whether federal proceedings are necessary to reach a just and equitable solution;
>
> (4) whether there is an alternative means of achieving an equitable distribution of assets;
>
> (5) whether the debtor and the creditors are able to work out a less expensive out-of-court arrangement which better serves all interests in the case;
>
> (6) whether a non-federal insolvency has proceeded so far in these proceedings that it would be costly and time consuming to start afresh with the federal bankruptcy process; and
>
> (7) the purpose for which bankruptcy jurisdiction has been sought.

In re AMC Investors, LLC, 406 B.R. at 488 (citations omitted).

In determining whether dismissal is proper, all of the seven factors are considered, but the court is not required to give them equal weight or conduct a strict balancing. *In re AMC Investors, LLC*, 406 B.R. at 488 (*citing Monitor Single Lift I*, 381 B.R. 455, 465 (Bankr. S.D.N.Y. 2008)).

In *AMC Investors*, the Court denied the alleged debtors' motion to abstain because: 1) an independent trustee was needed to investigate the directors and officers; 2) geographic issues that made centralized administration more efficient; and 3) a bankruptcy would not be harmful to the alleged debtors' business because they were no longer operating. *In re AMC Investors, LLC*, 406 B.R. at 488-89. None of these factors are implicated with respect to VC.

First, there is no need of an independent trustee to "investigate the financial affairs of the debtor." MOI is already pursuing direct claims against VC's officers in state court with its allegations of fraudulently obtaining shareholder disproval. There are no allegations of financial mismanagement or insider payments, as MOI must concede. Moreover, the Note is in default. Thus, MOI could pursue a state court receivership, if it wanted. To date, it has chosen to interfere with repayment of the Note rather than file such an action.

Second, centralized administration is a non-issue. There is no evidence that the geographic scope of the parties to this case is expansive. Moreover, as noted above, MOI has not sought a judgment lien against VC. Thus, unlike *AMC Investors*, there is no suggestion that an attempt to liquidate VC would be cumbersome or inefficient.

Last, bankruptcy would be harmful to VC's business as it is fully operational and on the brink of prosperity. The Petitioning Creditors are seeking to liquidate VC. However, this would clearly be harmful, indeed detrimental, to VC *and its creditors*. Already, an independent financial report indicates that VC is worth substantially more as a going concern as opposed to if its assets were liquidated. Moreover, after two years of delay in obtaining FDA approval, the Vaccine is

currently in the clinical trials phase and showing excellent results. On that basis, VC entered into the Government Contract. It remains in negotiations with several countries to license its technology. Without dismissal of the Involuntary Petition, it is unlikely that the Government Contract will take effect or that the negotiations will be fruitful.

CONCLUSION

For the foregoing reasons, the Involuntary Petition should be dismissed with VC's costs and reasonable attorneys' fees being borne by the Petitioning Creditors. *See* 11 U.S.C. § 303(i)(1). Moreover, the Court should grant a judgment in favor of VC for punitive and consequential damages based on MOI's bad faith. *See* 11 U.S.C. § 303(i)(2).

Dated: January 13, 2010

CHEHI, HERRMANN &
IBRAHIMI, LP

_____

Mark S. Chehi, Esquire
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Yosef Ibrahimi, Esquire
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IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	:	
	:	Involuntary Chapter 7
Vaccine Corporation,	:	
	:	Case No. 10-12345 (RG)
Alleged Debtor.	:	
	:	

Petitioning Creditors' Pretrial Brief

Argument

A. MOI is an Eligible Petitioner and Bankruptcy Relief is Appropriate Pursuant to 11 U.S.C § 303

Section 303 of the Bankruptcy Code sets out a three part test for a contested involuntary petition commenced by three or more creditors: (i) the petitioning creditors must each hold a claim that is not contingent as to liability or the subject of a *bona fide* dispute as to liability or amount, (ii) the petitioning creditors are undersecured by at least $13,475 in the aggregate, and (iii) the debtor is generally not paying such debtors' debts as they come due unless such debts are the subject of a *bona fide* dispute as to liability or amount. *See* 11 U.S.C. §§ 303(b)(1), (b)(2) and (h)(1).

1. The Petitioning Creditors' Claims Are Not Subject to a *Bona Fide* Dispute.

Although the Bankruptcy Code does not define a "bona fide dispute," the Third Circuit has held that a bona fide dispute exists

> "if there is a genuine issue of material fact that bears upon the debtor's liability, or a meritorious contention as to the application of law to undisputed facts. Under this standard, the bankruptcy court must determine whether there is an objective basis for either a factual or a legal dispute as to the validity of debt."

In re AMC Investors, LLC, 406 B.R. 478, 484 (Bankr. D. Del. 2009) (citing *B.D.W. Assoc. v. Busy Beaver Bldg. Ctrs.*, 865 F.2d 65, 66 (3d Cir. 1989)). In applying this standard, "the court's objective is to ascertain the existence of a dispute, not to actually resolve the dispute." *Id*. at 484.

A bona fide dispute as to the amount of a claim exists only where a claim for offset "arises out of the same transaction and is directly related to the creditor's underlying claim." *In re Euro-American Lodging Corp.*, 357 B.R. 700, 712 n.8 (Bankr. S.D.N.Y. 2007) (quoting *Key Mech. Inc. v. BDC 56 LLC*, 330 F.3d 111, 120 (2d Cir. 2003)). A debtor's assertion of a counterclaim against a petitioning creditor, even "assert[ing] that the petitioning creditor owes it money in the aggregate," generally does not create a bona fide dispute within the meaning of section 303(b)(1) or (h)(1) of the Bankruptcy Code. *Chi Title Ins. Co. v. Seko Inv., Inc.*, 156 F.3d 1005, 1008-09 (9th Cir. 1998).

Prior to BAPCPA, the law was clear that an undisputed portion of a claim was sufficient to support an involuntary petition so long as the undisputed portion was greater than the statutory minimum. *See In re Focus Media, Inc.*, 378 F.3d 916, 926 (9th Cir. 2004) (noting the "widely accepted proposition regarding involuntary bankruptcy petitions: If at least a portion of the debt that is the subject of the petition is undisputed, the undisputed portion is sufficient to create a debt under section 303(b)(1) not subject to a *bona fide* dispute"); *IBM Credit Corp. v. Compuhouse Sys.*, 179 B.R. 474, 479 (W.D. Pa 1995), *aff'd*, 85 F.3d 612 (3d Cir. 1996) (same); *In re F.R.P. Indus., Inc.*, 73 B.R. 309, 321 (Bankr. M.D. Fla. 1987) (finding that even though a portion of a claim was subject to a *bona fide* dispute, the undisputed part was greater than the statutory floor and was sufficient to support an involuntary petition).

BAPCPA's addition of the words "as to liability or amount" in section 303(b)(1) did not change the well-settled law regarding the meaning of a *bona fide* dispute. *See In re Demirco Holdings, Inc.*, 2006 WL 1663237, at *3 (Bankr. C.D. Ill. June 9, 2006) ("With a dearth of committee comments and legislative history available to interpret BAPCPA, this Court cannot presume that Congress added the phrase 'as to liability and amount' with the intent that the claims of involuntary petitioners must now be fully liquidated either by agreement or judgment so that no dispute exists as to any portion of such claims. Without clear legislative intent, this Court cannot presume such a change in the law and

declines to do so."); *see also In re Mylotte*, 2007 Bankr. LEXIS 2375, at *18 (Bankr. E.D. Pa. Aug. 10, 2007) (finding that petitioning creditor met its burden by showing that a sufficient portion of its claim was not subject to a *bona fide* dispute); *In re Knight*, 380 B.R. 67, 74 (Bankr. M.D. Fla. 2007) (holding that where a debtor conceded that he owed a debt to the creditor that "his disagreement as to the amount owed does not constitute a *bona fide* dispute").

Here, the claims of MOI, Testing and Consulting are not subject to a *bona fide* dispute and meet the threshold amount required under the Bankruptcy Code for a successful involuntary petition. MOI provided VC with a loan of $50 million, which is evidenced by the Note.[1] VC defaulted on the Note and currently owes MOI $51.5 million. Testing is owed $1.2 million from VC for clinical testing performed on the Vaccine in preparation for its development. VC disputes only $20,000 of the amount owed to Testing for the clinical testing report, which has yet to be delivered to VC. Consulting is owed $300,000 from VC for consulting services performed in connection with the proposed asset sale to MOI. The facts indicate that, other than the $20,000 owed to Testing for the clinical testing report, VC does not dispute the remaining claim amounts.

2. The Petitioning Creditors Meet the Undersecured Requirements Set Forth in Section 303(b).

The aggregate and undisputed amounts owed by VC to the petitioning creditors far exceeds the statutory floor of $13,475 imposed by section 303(b)(1) of the Bankruptcy Code. Furthermore, section 303(b)(1) does not require that each of the three required creditors hold unsecured claims, but rather that such creditors hold $13,475 in unsecured claims in the aggregate. *In Paradise Hotel Corp. v. Bank of Nova Scotia*, 842 F.2d 47 (3rd Cir. 1988), the court stated:

> Read literally, [section 303(b)] requires only that a petitioner be an entity which holds a non-contingent, undisputed claim against the debtor. Its description of the qualification of

1 Whether or not MOI is a fully or partially secured creditor, MOI is eligible to serve as a petitioning creditor. See *Key Mechanical Inc. v. BDC 56 LLC*, 330 F.3d 111 (2d Cir. 2003).

> a petitioner is, therefore, broad enough to include a fully secured holder of a non-contingent, undisputed claim. Moreover, the last clause of the section makes it clear that at least some creditors holding security may be included in the group of three petitioners so long as the unsecured portion of the petitioners' claims totals in the aggregate at least [the statutory minimum]. Since that clause does not distinguish between fully secured and under secured creditors, § 303(b)(1) on its face purports to authorize the filing of an involuntary petition where, as here, a fully secured creditor is joined by two unsecured creditors whose claims exceed [the statutory minimum] in the aggregate.

Id. at 49-50. Accordingly, regardless of whether MOI is partially or fully secured, the fact that the entirety of the petitioning creditor body holds at least $13,475 in unsecured claims in the aggregate is sufficient to meet the statutory requirements.

3. VC is Not Paying Debts as They Come Due.

Although there is no exact formula for determining whether a debtor is "generally not paying its debts," courts will "compare the number of debts unpaid each month to those paid, the amount of the delinquency, the materiality of the non-payment and the nature of the debtors' conduct of its financial affairs." *Mylotte*, 2007 Bankr. LEXIS 2375, at *15. In making this comparison, the courts have a great deal of flexibility, but it seems reasonable to consider both the amount of the debt not being paid and the number of creditors not being paid in determining the answer. *See In re All Media Properties, Inc.*, 5 B.R. 126, 142 (Bankr. S.D. Tex. 1980), *aff'd*, 646 F.2d 193 (5th Cir. 1981) (noting that generally not paying debts includes regularly missing a significant number of payments to creditors or regularly missing payments which are significant in amount in relation to the size of the debtor's operations).

VC is not paying its debts as they come due. The facts indicate that VC has been slow paying many of its trade creditors. Additionally, the impetus for the proposed asset sale to MOI was due to VC's inability to satisfy its debts. The sale was not approved by VC's shareholders. In the aggregate, VC owes approximately $53 million to the petitioning creditors. Although VC signed a contract with the U.S. government for development of the vaccine, the base value of that contract of $37 million is

insufficient to satisfy VC's current liabilities. Further, the Government Contract is contingent upon a showing of financial stability by VC, a requirement that VC will undoubtedly be unable to meet.

B. Dismissal or Abstention Under Section 305(a)(1) Is Improper in this Case Under *In re AMC Investors LLC*

As a general matter, abstention is only warranted if "the interests of creditors and the debtor would be better served by dismissal or suspension." 11 U.S.C. § 305. This Court laid out the framework for dismissal or abstention recently in *AMC Investors*: "The courts that have construed § 305(a)(1) are in general agreement that abstention in a properly filed bankruptcy case is an extraordinary remedy, and that dismissal is appropriate under § 305(a)(1) only in the situation where the court finds that both 'creditors and the debtor' would be 'better served' by a dismissal." *AMC Investors*, 406 B.R. at 487-88 (Bankr. D. Del. 2009) (citing *In re Eastman*, 188 B.R. 621, 624 (B.A.P. 9th Cir. 1995). "Granting an abstention motion pursuant to § 305(a)(1) requires more than a simple balancing of harm to the debtor and creditors; rather, the interests of both the debtor and its creditors must be served by granting the requested relief." *AMC Investors*, 406 B.R. at 488 (citing *In re Monitor Single Lift I, Ltd.*, 381 B.R. 455, 462 (Bankr. S.D.N.Y. 2008) (citing *In re Globo Comunicacoes e Participacoes S.A.*, 317 B.R. 235, 255 (S.D.N.Y. 2004))). "The movant bears the burden to demonstrate that the interests of the debtors and creditors would benefit from dismissal." *Id.*

In *AMC Investors*, the Court described the factors often considered in making a determination as to the best interests of the creditors and debtor, including:

> (1) the economy and efficiency of administration;
>
> (2) whether another forum is available to protect the interests of both parties or there is already a pending proceeding in state court;
>
> (3) whether federal proceedings are necessary to reach a just and equitable solution;
>
> (4) whether there is an alternative means of achieving an equitable distribution of assets;

(5) whether the debtor and the creditors are able to work out a less expensive out-of-court arrangement which better serves all interests in the case;

(6) whether a non-federal insolvency has proceeded so far in these proceedings that it would be costly and time consuming to start afresh with the federal bankruptcy process; and

(7) the purpose for which bankruptcy jurisdiction has been sought.

AMC Investors, 406 B.R. at 488 (citing *In re Paper Partners, L.P.*, 238 B.R. 661, 679 (Bankr. S.D.N.Y. 2002) (citing *In re 801 South Wells Street, L.P.*, 192 B.R. 718, 723 (Bankr. N.D. Ill. 1996)). "While all factors are considered, they are not given equal weight in each case, nor should the Court conduct a strict balancing." *AMC Investors*, 406 B.R. at 488 (citing *Monitor Single Lift*, 381 B.R. at 465).

AMC Investors differed from this case because it involved a single creditor seeking collection from two related holding company debtors on a guarantee of their operating subsidiary's debt. Even with those less favorable facts, this Court denied the alleged debtors' motion to abstain. The Court's reasons are set forth below in full because of their particular relevance to this case. First, this Court noted the need for an independent trustee to investigate the directors and officers:

> Here, Eugenia's primary, and perhaps only reason for filing the involuntary petition is to seek the appointment of a chapter 7 trustee, who will possess the authority to investigate and, if appropriate, to pursue claims against the officers and directors of the Alleged Debtors relating to alleged fraud perpetrated against Eugenia by AMC Computer. While such a purpose for seeking bankruptcy jurisdiction may not be proper in every case, under these facts, Eugenia has a valid bankruptcy purpose. It is highly unlikely that Eugenia could pursue claims against the Alleged Debtors' officers and directors in either a direct or derivative suit. Thus, either a bankruptcy trustee or state court receiver is necessary to pursue these potential assets, if appropriate. While receivership is certainly an option in this case, no such action has been instituted.

AMC Investors, 406 B.R. at 488-89 (footnote omitted).

Second, this Court noted geographic issues that made centralized administration more efficient:

> Furthermore, the geographic scope of the parties to this case spans state and national boundaries. The Alleged Debtors are Delaware LLC's managed from Florida. The involuntary petition for Eugenia reflects a mailing address in London. AMC Computer operated out of New York. The state court judgment was obtained in New York and filed as a judgment lien in Florida. While a state court receiver may certainly attempt to liquidate the Alleged Debtors, it would certainly be a more cumbersome and less efficient

> process for the receiver to obtain recognition in various jurisdictions, rather than permitting the use of federal bankruptcy jurisdiction.

AMC Investors, 406 B.R. at 489.

Finally, this Court recognized that a bankruptcy would not be harmful to the alleged debtors' business because they were no longer operating:

> Moreover, since the Alleged Debtors are insolvent, non-operating limited liability companies that hold stock in a defunct computer company, it is not clear how a bankruptcy petition is harmful. In fact, the only entities that may be harmed by entering an order for relief in this case are the officers and directors of the Alleged Debtors. While these individuals may desire to avoid the threat of lawsuits pursued by a chapter 7 trustee, their interests are not relevant in a decision to abstain under section 305(a)(1).

Id.

Here, as in *AMC Investors*, the circumstances do not warrant abstention.

1. There is a Need for an Independent Trustee in Bankruptcy.

The principal need for an investigation here centers on VC's payments to insiders during the two years before bankruptcy. First, although there is nothing in the record either to show or to rule out director or officer misconduct that an independent trustee should investigate (as was also the case in *AMC Investors*), the principal need for an investigation centers on VC's payments to insiders during the two years before bankruptcy. Although the record does not yet reveal director or officer misconduct, VC's conduct to date in this case in making significant pre-petition transfers further supports the need for an independent investigation and equal treatment of creditors. Additionally, as in *AMC Investors*, a receivership action has not been instituted. Even if such an action could be instituted, a receiver for VC only would have limited rights to pursue fraudulent transfer claims and would not have the same rights as a bankruptcy trustee to investigate or pursue preferences. Thus, as in *AMC Investors*, there is a clear need for an independent trustee to "investigate the financial affairs of the debtor". 11 U.S.C. § 704(3).

2. Geographic Dispersion Makes Centralized Administration More Efficient.

The parties' geographic dispersion provides another reason for the centralized administration that only a bankruptcy case can provide. VC is based in Delaware and the petitioning creditors are based in New York, Illinois and California. Under these circumstances, economy and efficiency are served by addressing the numerous claims of creditors in a centralized proceeding where, for example, "creditors need not go around the country or the world to obtain relief, and where assets can be distributed in a pari passu manner, without races to obtain judgments". *In re Paper I Partners, L.P.*, 283 B.R. 661, 679 (Bankr. S.D.N.Y. 2002).

An investigation and, if appropriate, avoidance of preferences and fraudulent transfers cannot reasonably be pursued outside of bankruptcy. There is no comparable preference statute that would apply outside of bankruptcy. Non-bankruptcy fraudulent transfer laws would permit pursuit of the payments made within up to four years before bankruptcy, but each creditor would have to pursue them separately and possibly in different courts, depending on where jurisdiction and venue would lie. Furthermore, recovery would benefit all creditors, not just those who have the financial wherewithal to pursue claims independently, and would be distributed equitably in accordance with the Bankruptcy Code's priority scheme. *See Moore v. Bay*, 284 U.S. 4 (1931).

3. This Case is not a "Two-Party Dispute" or Collection Action.

Finally, this case is manifestly not "a two-party dispute between the debtor and a single creditor … where relief is available in a non-bankruptcy forum [and that] has the potential to transform the bankruptcy process into a collections device, which it is not." *AMC Investors* at 488 (quoting 2 COLLIER ON BANKRUPTCY ¶ 305.02[2]) (internal quotation mark omitted). The phrase "two-party dispute" has consistently referred to a creditor's collection action against the debtor. A bankruptcy case does not become a two-party dispute because the debtor faces a group of creditors with common

interests in opposing the debtor. Although some of the legal issues facing the petitioning creditors and their economic interests may be aligned, they do not comprise a single creditor constituency. For example, in *In re Paper I Partners*, where the debtor engaged in an intentional and systematic effort to avoid paying a particular group of creditors of "at least 29 parties" holding a majority of the debt, the court concluded that the dispute was not between the debtor and one or two other parties. *In re Paper I Partners*, 283 B.R. at 680. Therefore, this case is neither a two-party dispute nor a collection device.

Conclusion

In sum, the petitioning creditors have satisfied the elements of section 303 of the Bankruptcy Code. Additionally, the seven factors that this Court listed in *AMC Investors* all weigh heavily in favor of prompt entry of an order for relief, as does the more general statement of law in *AMC Investors*: "abstention in a properly filed bankruptcy case is an extraordinary remedy … appropriate … only … where … the interests of both 'creditors and the debtor' would be 'better served' by a dismissal". The collective remedy of a federal bankruptcy is both necessary and appropriate. The factors discussed above support the need for this Court to maintain jurisdiction in this case and show that abstention under section 305 of the Bankruptcy Code would not serve the interest of creditors. Accordingly, the petitioning creditors respectfully request that this Court grant the order for relief.

Dated: January 13, 2010

COHEN, COLLINS & HAUPT, P.A.

_____

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	:	Case No. 10-12345 (RG)
Alleged Debtor.	:	
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OPINION

Before the Court is an involuntary bankruptcy case commenced by Medical Organization Incorporated ("MOI"), Clinical Testing, Inc., ("Testing") and Consulting Services, LP ("Consulting") against Vaccine Corporation ("VC"), the alleged debtor, pursuant to section 303 of title 11 of the United States Code, §§ 101-1532 (the "Bankruptcy Code"). The alleged debtor filed a motion to dismiss (the "Motion to Dismiss") the involuntary bankruptcy petition based on two grounds: (1) failure to state a claim upon which relief can be granted because the requirements under 11 U.S.C. § 303 have not been met, specifically that (a) section 303(b) was not satisfied, because each of the three claims asserted by the petitioning creditors is either subject to bona fide dispute or is a secured claim and (b) section 303(h)(1) was not satisfied because the involuntary petition does not establish that the alleged debtor is generally not paying its debts; and (2) that this court should abstain from making a determination in this case and dismiss it pursuant to section 305. For the forgoing reasons, this court will not dismiss under section 303 but will abstain pursuant to section 305.

Jurisdiction

This Court has jurisdiction over this matter pursuant to 28 U.S.C. § 1334. Venue of this proceeding is proper in this district pursuant to 28 U.S.C. §§ 1408 and 1409. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A).

Procedural and Factual Background

VC is a privately held company that develops and manufactures vaccines. It has two lines of business: (i) the development and manufacture of vaccines and (ii) the development of new technology which permits production of new vaccines at an accelerated rate (the "IP").

One of VC's main products currently under development is a promising new swine flu vaccine, which is in the clinical trials phase and showing excellent results. Despite the potential in this and other products, VC began to experience financial difficulties approximately two years ago due to unexpected costs and delays in obtaining FDA approval for its swine flu vaccine as well as expected costs associated with developing the IP. VC has attempted to move forward with both the swine flu vaccine and other areas of its business in the hopes that it will soon begin to see a return on these investments, but it has been unable to pay certain recent debts as they became due.

Attempting to rectify its financial situation, VC entered into negotiations and signed a letter of intent, subject to shareholder approval, to sell all of its assets to MOI. In anticipation of the potential sale and in order to aid cash flow, MOI loaned VC $50 million evidenced by a promissory note (the "Note") secured by a lien on substantially all of VC's assets.

The CEO and COO of VC did not believe that the agreement between MOI and VC (the "MOI APA") was in the best interest of the VC shareholders. Both the CEO and COO hold a 10% interest in VC. The VC Board approved the MOI APA over the CEO and COO objections, although some board members felt pressured to approve the deal due to VC's financial condition despite believing that MOI was receiving far more in the deal. The shareholders did not approve the MOI APA due primarily to the belief that VC has significantly more value than the MOI deal was attributing to it.

MOI brought a cause of action against VC in state court, alleging that the CEO and COO had fraudulently obtained shareholder disapproval. VC countered that MOI had disavowed critical portions of its LOI. As a result of this litigation, VC decided not to repay the Note when it became due, lining up investors willing to purchase MOI's debt at full price, but MOI refused to cooperate with any of the potential investors.

During the pendency of that action, VC signed a multi-million dollar contract with the U.S. government for the development of the swine flu vaccine (the "Government Contract"). The Government Contract has a base value of $37 million, and may be worth a total of $147 million to VC. Final approval of the Government Contract, however, is contingent upon a showing of financial stability by VC. The award of the Government Contract has dramatically increased the likelihood that VC will be able to obtain similar contracts from other governmental entities around the world, thereby bringing in significant revenues to VC. Such contacts have already been made with offers from or negotiations with various countries, including France, with the potential of $20 million in up-front payments. Any extended offers, however, like the one for $20 million from France, are contingent upon final approval of the Government Contract.

The day after VC signed the Government Contract, MOI, Testing and Consulting filed an involuntary petition (the "Involuntary Petition") under chapter 7 of the Bankruptcy Code naming VC as the alleged debtor. MOI alleges that it is owed $51.1 million based on the Note. Testing alleges that it is owed $1,200,000 in connection with some clinical testing services it provided to VC, and Consulting alleges that it is owed $300,000 in connection with consulting services it provided to VC in connection with the potential sale to MOI.

The $300,000 owed to Consulting is based upon three monthly invoices of $100,000 with one due thirty days from the date of the Involuntary Petition, one currently due and one thirty days

past due. Although the Consulting invoices are due thirty days from receipt, VC has in the past paid some Consulting invoices between thirty and sixty days from receipt with no late charges ever assessed by Consulting. With respect to the Testing debt, the alleged debtor believes, and has argued before this Court, that approximately $20,000 of the $1,200,000 claim can validly be disputed because VC never received a clinical testing report from Testing which the parties have stipulated is worth $20,000. Additionally, VC has been slow paying many of its trade creditors.

VC responded by filing the Motion to Dismiss the involuntary petition, arguing that MOI orchestrated the Involuntary Petition as a litigation tactic to either (i) put pressure on VC shareholders to approve the MOI APA or (ii) take control of VC through the chapter 7 proceeding. It is this Motion to Dismiss that is before this Court at this time.

Discussion

The motion before the Court is brought under Rule 1011(b) of the Federal Rules of Bankruptcy Procedures (the "Bankruptcy Rules"). This Rule provides that defenses and objections to involuntary petitions shall be presented in the matter prescribed by Rule 12 of the Federal Rules of Civil Procedure. VC moves for dismissal of the Involuntary Petition under Rule 12(b)(6).

Motion to Dismiss for Failure to State a Claim

The alleged debtor has moved to dismiss the Involuntary Petition under Rule 12(b)(6) for failure to state a claim upon which relief can be granted under section 303. Specifically, VC claims that the requirements of section 303(b) have not been met because each claim asserted by the petitioning creditors either is subject to bona fide dispute or is a secured claim. Additionally, it has argued that the standard set out under section 303(h)(1) is similarly not met because the petitioning creditors have not demonstrated that VC is generally not paying its debts as they come due.

The Requirements of 11 U.S.C. § 303(b) are Satisfied

With respect to Consulting, the alleged debtor asks this court to consider the course of dealing between the parties, specifically the fact that Consulting has previously allowed VC to tender payment between thirty and sixty days from receipt of an invoice without assessing a late fee when evaluating this debt. In doing so, the alleged debtor asks this Court to make a determination that because none of the invoices upon which Consulting has based its claim are more than thirty days past due, the debt owed to Consulting is subject to bona fide dispute and therefore Consulting is not a qualified petitioning creditor. Similarly, the alleged debtor asks this Court to hold that Testing's claim is also subject to a bona fide dispute because a portion of it, $20,000 of $1,200,000 is contested. They ask, therefore, that Testing be disqualified as a petitioning creditor. Neither Consulting nor Testing have advanced arguments with respect to the Motion to Dismiss.

Finally, VC argues that while it does not dispute the validity and amount of MOI's claim, the claim is nevertheless secured and therefore does not qualify MOI as a petitioning creditor in light of the fact that both Testing and Consulting's claims are subject to a *bona fide* dispute. To support this argument, they cite the language of the code itself which states in 11 U.S.C. § 303(b)(1) that the qualifying entities must hold "undisputed claims which aggregate at least $13,475 more than the value of any lien on property of the debtor securing such claims held by the holders of such claims." MOI responded on behalf of all three creditors, arguing that the claims of Testing and Consulting are not subject to a bona fide dispute, and that their claims in conjunction with MOI's claim aggregate to at least $13,475 more than the aggregate value of all liens held by the petitioning claimants because the claims of Testing and Consulting are for $1.5 million unsecured.

In order to resolve this issue, the Court must first look to the definition of "bona fide dispute." This term is not defined in the Bankruptcy Code, but the Third Circuit has made a determination regarding this term, holding that a bona fide dispute exists:

> if there is a genuine issue of material fact that bears upon the debtor's liability, or a meritorious contention as to the application of law to undisputed facts. Under this standard, the bankruptcy court must determine whether there is an objective basis for either a factual or a legal dispute as to the validity of debt.

In re AMC Investors, LLC, 406 B.R. 478, 484 (Bankr. D. Del. 2009) (citing *B.D.W. Assoc. v. Busy Beaver Bldg. Ctrs.*, 865 F.2d 65, 66 (3d Cir. 1989)). When applying this standard, "the court's objective is to ascertain the existence of a dispute, not to actually resolve the dispute." *Id.* at 484. Accordingly, for the foregoing reasons, this Court has determined that no bona fide dispute exists with respect to the Testing and Consulting claims, and therefore the aggregate amount of those unsecured claims combined with MOI's claim are sufficient to satisfy section 303(b)(1).

As an initial matter, the burden is on the petitioning creditor to establish a prima facie case that no *bona fide* dispute exists. Once it has done so, the burden shifts to the alleged debtor to demonstrate that such a dispute does exist. *See Key Mechanical Inc. v. BDC 56 LLC (In re BDC 56 LLC)*, 330 F.3d 111, 118 (2d Cir. 2003).

Here, the three creditors have made a prima facie showing of the absence of a *bona fide* dispute by presenting the Note and invoices. Therefore, the burden has shifted to the alleged debtor which has made two discrete arguments: that a *bona fide* dispute exists when, through the course of dealing of the parties and not withstanding a due date on an invoice, a debt has not yet come due, and when part of a debt is in dispute, the entire debt is subject to a *bona fide* dispute.

As for the first argument, this Court looks to other jurisdictions for guidance. The Ninth Circuit has given considerable additional guidance as to what constitutes a *bona fide* dispute beyond

that given by courts within this Circuit. For example, in *In re Vortex Fishing Systems, Inc.*, the court held that the mere existence of pending litigation or the filing of an answer by the debtor to the creditor's claim is insufficient to establish a *bona fide* dispute. 262 F.3d 985 (9th Cir. 2001). In fact, that court seemed to suggest that a limited circumstance under which a claim may be subject to a *bona fide* dispute is when the debtor has an affirmative defense to the claim. *Id.* In another Ninth Circuit case, *In re Seko Inv., Inc.*, the court held that a claim is contingent as to liability when the debtor's duty to pay arises only upon occurrence of a future event that was contemplated by the parties at the time of the contract's execution. 156 F.3d 1005 (9th Cir. 1998).

These cases compel this court to determine that past due and currently due invoices, notwithstanding the fact that the course of dealing of the parties suggests that the alleged debtor may have additional time to pay the invoices, are not subject to a *bona fide* dispute. The alleged debtor has not asserted any basis under which the claims may not be valid, nothing amounting to an affirmative defense to the claim. Further, VC's payment is not contingent on a future event. Consulting has already rendered the services for which it invoiced VC. The only remaining action is for VC to make payment. No argument has been made as to the existence of a meritorious, existing conflict as to the creditor's right to payment as required under the standard that exists within the Third Circuit. Therefore, the alleged debtor's argument as to the *bona fide* nature of Consulting's claim must fail.

As to VC's second argument, that if a portion of a claim is in dispute, the entire claim is subject to a *bona fide* dispute, this Court has evaluated case law rendered both prior to and following the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA") and determined that this argument similarly must fail. Prior to BAPCPA, case law demonstrated that an undisputed portion of a claim was sufficient to support an involuntary petition so long as the

undisputed portion was greater than the statutory minimum. *See In re Focus Media, Inc.*, 378 F.3d 916, 926 (9th Cir. 2004) (noting "widely accepted proposition regarding involuntary bankruptcy petitions: If at least a portion of the debt that is the subject of the petition is undisputed, the undisputed portion is sufficient to create a debt under 303(b)(1) not subject to a *bona fide* disputes"); *IBM Credit Corp. v. Compuhouse Sys.*, 179 B.R. 474, 479 (W.D. Pa. 1995), *aff'd*, 85 F.3d 612 (3d Cir. 1996) (same); *In re F.R.P. Indus., Inc.*, 73 B.R. 309, 321 (Bankr. M.D. Fla. 1987) (finding that even though portion of claim was subject to *bona fide* dispute, undisputed part was greater than statutory floor and sufficient to support involuntary petition).

BAPCPA, however, amended section 303(b)(1) to include the words "as to liability or amount." This amendment did not change the well-settled law regarding the meaning of a *bona fide* dispute. *See In re Demirco Holdings, Inc.*, 2006 WL 1663237, at *3 (Bankr. C.D. Ill. June 9, 2006) ("With a dearth of committee comments and legislative history available to interpret BAPCPA, this Court cannot presume that Congress added the phrase 'as to liability and amount' with the intent that the claims of involuntary petitioners must not be fully liquidated either by agreement or judgment so that no dispute exists as to any portion of such claims. Without clear legislative intent, this Court cannot presume such a change in the law and declines to do so."); *see also In re Mylotte*, 2007 Bankr. LEXIS 2375, at *18 (Bankr. E.D. Pa. Aug. 10, 2007) (finding that petitioning creditor met its burden by showing that a sufficient portion of its claim was not subject to a *bona fide* dispute); *In re Knight*, 380 B.R. 67, 74 (Bankr. M.D. Fla. 2007) (holding that where debtor conceded that he owed debt to creditor that "his disagreement as to the amount owed does not constitute a *bona fide* dispute").

Analyzing this case under the attendant law, this Court holds that even if there is a *bona fide* dispute as to the $20,000 of Testing's claim, Testing still holds a claim for $1,180,000 which is not

subject to a *bona fide* dispute, and therefore still qualifies to bring an involuntary petition against the alleged debtor. Because the Court so holds, it will not address whether the argument with respect to the remaining $20,000 is subject to a *bona fide* dispute.

Because the court has determined that no *bona fide* dispute exists with respect to Consulting and Testing's claims and the undisputed portions of those unsecured claims totals $1,580,000, VC's argument with respect to the secured nature of MOI's claim is moot. The aggregate amount of the three claims exceeding the liens held by the claimants is greater than the statutory floor of $13,475 set out by section 303(b)(1) of the Bankruptcy Code. Therefore, the Court will not dismiss the Involuntary Petition based on failure to state a claim under section 303(b)(1).

VC is Not Paying Debts as they Come Due

VC also contends in its Motion to Dismiss that the section 303(h)(1), the "generally not paying" debts requirement of an involuntary petition has not been met. Supporting this argument, the alleged debtor contended that the record does not support a finding that VC is generally not paying its debts, and that it is in the best interest of VC and its creditors that VC continue its ongoing operations outside of bankruptcy and to grow its business.

MOI, in its response, asserted various factual allegations that in addition to the non-payment of the $51.5 million owed to MOI when it came due, the debtors have been slow paying many of its trade creditors.

Section 303(h)(1) requires that a "court shall order relief against the debtor in an involuntary case under the chapter under which the petition was filed only if. . . the debtor is generally not paying such debtor's debts as such debts become due unless such debts are the subject of a bona fide dispute as to liability or amount." 11 U.S.C. § 303(h)(1).

MOI, as the petitioning creditor has the burden on demonstrating that the debtor is generally not paying its debts as they become due. *See In re The Food Gallery at Valleybrook,* 222 B.R. 480, 486 (Bankr. W.D. Pa. 1998). Several courts have engaged in a mechanical analysis of this requirement, reviewing numerous factors. *See In re Knoth*, 168 B.R. 311, 317 (Bankr. D.S.C. 1994) (factors to consider are "(1) timeliness of payments on past due obligations; (2) the amount of debts long overdue; (3) the length of time during which the debtor has been unable to meet large debtors; (4) any reduction in the debtor's assets; and (5) the debtor's deficit situation"); *In re H.I.J.R. Properties Denver*, 115 B.R. 275, 277 (D. Colo. 1990) (listing as factors number of debts, amount of delinquencies on said debts, materiality of nonpayment, and nature of the debtor's conduct with respect to his financial affairs). However, courts generally do not limit themselves to such factors, nor do they give any weight to any one factor over another. *See In re The Food Gallery*, 222 B.R. at 487.

In this case, the Court is convinced that MOI has demonstrated the timeliness of the payments of Consulting and other trade creditors is slow enough to constitute not paying debts as they come due.

Dismissal is Appropriate Under Section 305

VC also contends in its Motion to Dismiss, that the Involuntary Petition should be dismissed under section 305(a) which governs abstention. Citing the recent decision issued in this jurisdiction, *In re AMC Investors, LLC*, the alleged debtor argues that abstention is warranted in this case as "both creditors and the debtor would be better served by a dismissal." 406 B.R. 478, 487-88 (Bankr. D. Del. 2009) (quoting *In re Eastman*, 188 B.R. 621, 624 (9th Cir. BAP 1995) (internal quotation marks omitted)). MOI, for their part, argues that the distinctions between *In re AMC* in this case only serve to forward the proposition that abstention is not warranted under the

circumstances. For the forgoing reasons, this Court has determined that abstention is warranted in this case and will dismiss the Involuntary Petition accordingly.

Section 305(a) provides, in relevant part, that:

> (a) The court, after notice and a hearing, may dismiss a case under this title, or may suspend all proceedings in a case under this title, at any time if- (1) the interests of creditors and the debtor would be better served by such dismissal or suspension;

The Court in *In re AMC* described the current case law centering on this controversy in detail, setting out a detailed list "of factors to gauge the overall best interests of the creditors and debtor," including:

> (1) the economy and efficiency of administration;
>
> (2) whether another forum is available to protect the interests of both parties or there is already a pending proceeding in state court;
>
> (3) whether federal proceedings are necessary to reach a just and equitable solution;
>
> (4) whether there is an alternative means of achieving an equitable distribution of assets;
>
> (5) whether the debtor and the creditors are able to work out a less expensive out-of-court arrangement which better serves all interests in the case;
>
> (6) whether a non-federal insolvency has proceeded so far in those proceedings that it would be costly and time consuming to start afresh with the federal bankruptcy process; and
>
> (7) the purpose for which bankruptcy jurisdiction has been sought.

Id. at 488 (citing *In re Paper I Partners, L.P.*, 283 B.R. 661, 679 (Bankr. S.D.N.Y. 2002) (citing *In re 801 South Wells Street, L.P.*, 192 B.R. 718, 723 (Bankr. N.D. Ill. 1996))).

Of these seven factors, only two support this Court retaining jurisdiction over this case. It is unlikely that the alleged debtor and MOI will be able to work out a less expensive out-of-court arrangement than an in-court determination, given the extensive ill will harbored against one another. However, notwithstanding this fact, there is no evidence leading this Court to conclude

that such an in-court proceeding necessarily must be heard in the Bankruptcy Court. Similarly, factor six cuts in favor of retaining this case because there is not non-federal insolvency commenced in this case. Indeed, the alleged debtors are striving to carry on as a going concern, and may possibly be able to do so. Therefore, initiating a federal bankruptcy proceeding would not necessarily be duplicative of previous efforts, but this factor, alone, cannot support retention of this cause of action.

The remaining five factors all support this Court abstaining from this cause of action. First, another forum is available to protect the interests of both parties. There is, in fact, a state court proceeding currently pending. As the primary dispute is between the alleged debtor and MOI, and that dispute is already in progress in state court, this Court thinks it would be prudent to allow that proceeding to run its course. *See In re Mountain Dairies, Inc.*, 372 B.R. 623, 636 (Bankr. S.D.N.Y. 2007)(dismissal appropriate where involuntary was used essentially a two party dispute with remedies available in State Court). This leads to the second factor favoring abstention, a federal proceeding is not necessary to reach a just and equitable solution. The state court is well-equipped to resolve this issue which relates directly to a contract dispute. Having such a dispute heard by a federal bankruptcy court is not necessary.

Further, there is an alternative means of achieving an equitable distribution of assets. Because VC is endeavoring to remain a going concern through the acquisition of the Government Contract and other potential deals, allowing it to continue in that process (which is conditioned on a showing of financial health) likely will lead to a much greater result for VC and its creditors than the continuation of a bankruptcy proceeding. *See e.g. GMAM Investment Funds Trust I v. Globo Comunicacoes e Participacoes S.A.*, 317 B.R. 235, 255 (S.D.N.Y. 2004)(applying a test of whether section 305 abstention is beneficial to both the creditors and the debtor). Under this analysis, the

Court also finds that allowing VC to attempt to survive through acquisition of the Government Contract and other such deals would be a far more economic and efficient administration of this entity than an involuntary bankruptcy proceeding.

Finally, this Court finds that the purpose for which bankruptcy jurisdiction has been sought is not appropriate to support continuation of this proceeding. This proceeding was brought by MOI as a litigation tactic to either put pressure on VC shareholders to approve the MOI APA or to take control of VC, thereby gaining the benefit of the Government Contract. Such motivations are not a proper basis to give this Court jurisdiction over this case. *See In re Pac Rollforming, LLC,* 415 B.R. 750, 755 (Bankr. N.D. Cal. 2009). Because the majority of the factors support a holding of abstention, the Court will dismiss this case.

Conclusion

For the foregoing reasons, VC's Motion to Dismiss is GRANTED and the Court shall enter an ORDER FOR RELIEF dismissing the Involuntary Petition.

/s/Law clerk. Uh, I mean, Judge

The Critics are raving . . .

"Involuntary is Fabulous" The Real Deal

Debtor's Financial Analyst gives it "Eleven Stars out of Ten"

"Two Thumbs Up!" Shannon and Gross

The Broken Piggy Bank Theater Company and Empty Pocket Productions proudly present

INVOLUNTARY

ACT I.....A Plan Is Hatched

Setting: The Boardroom of Medical Organization Incorporated

The CEO of Medical Organization Incorporated meets with Bankruptcy and Litigation Counsel to discuss the possibility of filing an Involuntary against Vaccine Corporation.

ACT II.....What Now?

Setting: The Boardroom of Vaccine Corporation

The CEO of Vaccine Corporation meets with Bankruptcy Counsel to discuss options now that Medical Organization Incorporated has filed an Involuntary naming Vaccine Corporation as the alleged debtor.

ACT III.....The Courtroom Drama

Setting: United States Bankruptcy Court

The Courtroom drama unfolds after Medical Organization Incorporated files its Brief in Support of the Involuntary and Vaccine Corporation files its Motion to Dismiss the Involuntary.

WRITTEN MATERIALS