

United States Bankruptcy Court, Northern District of Illinois

Name of Assigned Judge	A. Benjamin Goldgar	Case No.	09 B 32672
DATE	March 8, 2010	ADVERSARY NO.	
CASE TITLE	Life Fund 5.1, LLC, <i>et al.</i>		
TITLE OF ORDER	Order confirming election of Jeffrey Marwil as chapter 11 trustee		

DOCKET ENTRY TEXT

The objections of Patrick Collins, the U.S. Trustee, the Texas State Securities Board, Harry and Adela Parlette, Dr. Charles Giger, and Grace Johnson to the election of Jeffrey Marwil as chapter 11 trustee are overruled. The election of Jeffrey Marwil as trustee is confirmed.

[For further details see text below.]

STATEMENT

These jointly administered chapter 11 cases are before the court for ruling on the disputed election of Jeffrey Marwil as trustee. Marwil's election has drawn several objections, including objections from the U.S. Trustee and the current chapter 11 trustee Patrick Collins. The objections were briefed, and an evidentiary hearing was held on them. The court has carefully considered the briefs, the hearing transcript, and the exhibits admitted into evidence. For the following reasons, the objections to the election will be overruled. Marwil's election as trustee will be confirmed.

1. Background

The dispute over the election is narrow. To understand why, it is necessary to lay out the facts that produced the election and the dispute as well as the legal framework governing the election of chapter 11 trustees.

a. Facts

These bankruptcy cases were filed on September 2, 2009, by seven debtors: Life Fund 5.1 LLC, Life Fund 5.2 LLC, A&O Life Fund LLC, A&O Resource Management LLC, A&O Bonded Life Settlement LLC, A&O Bonded Life Assets LLC, and Houston Tanglewood Partners LLC. Each of the debtors operated in what is known as the "life settlement industry,"

STATEMENT

soliciting funds from individual investors to acquire life insurance policies.

One week after the cases were filed, the U.S. Trustee moved under section 1104(a) of the Bankruptcy Code for the appointment of a trustee. The motion was granted on September 16, and on September 21 the appointment of Collins as chapter 11 trustee was approved. He has served in that capacity ever since.

Collins was appointed over the objection of a number of creditors who for purposes of this case are known simply as the "Group of Investors." These creditors are represented by a Houston law firm, Johnson Trent West & Taylor. On September 17, 2009, Lori Hood, a partner at Johnson Trent, sent a form letter (the "September 17 letter") to investors in the debtor. (Just how many were sent the September 17 letter is unclear, but it appears essentially anyone who could be identified as having a claim in the bankruptcy received a copy.) The letter noted that numerous creditors had retained Johnson Trent (known at the time as Johnson Spalding) to represent them in the bankruptcy case. The letter went on to say: "Should you retain us, we will file your claim. If you have already filed your claim, I would ask that you refrain from giving any other entity your proxy and instead consider providing us your proxy."

Enclosed with the September 17 letter were two other letters, an engagement letter and a conflict of interest waiver. The conflict waiver advised that "John Spalding, an investor, is a lawyer with our firm" but was not an equity partner. The letter did not disclose that Spalding was an officer of Bayou City Escrow, Inc., and Spalding's wife Laura was the owner of Bayou City. Bayou City had a business relationship of some kind with one or more of the debtors, since at least some of the funds invested in the debtors were wired through Bayou City, although how often that occurred is unclear. Bayou City and its registered agent had the same address as the Johnson Trent firm. However, Bayou City was never a client of Johnson Trent. In February 2007, Bayou City stopped doing business with the debtors, and in October 2007, Laura Spalding sold the company.

The Spaldings also owned all or part of an entity called Consolidated Wealth Management LLC, another investor Johnson Trent represents in this case. The nature of Consolidated Wealth Management's business was not explained.

On October 13, the Group of Investors filed a notice through their counsel requesting an election of a trustee at the creditors' meeting. At the meeting, the Group of Investors also made an oral request through counsel for the election of a trustee, naming Marwil as the Group's candidate. Because several creditors objected to a lack of notice of the request, the Group of Investors chose not to press the issue, and the meeting was continued to another date for purposes of holding a trustee election with adequate notice.

On October 20 and 21, the noticing agent for trustee Collins duly mailed a notice for each

STATEMENT

bankruptcy case giving November 13, 2009, as the continued date of the creditors meeting. Each notice made clear that the U.S. Trustee was convening the meeting “for the purpose of electing a disinterested person to serve as trustee in the case.”

On November 11, just before the continued meeting, Johnston Trent filed a “Notification pursuant to Bankruptcy Rule 2006.” The Notification stated, among other things, that Johnson Trent represented the Group of Investors, named each investor represented, stated that Johnson Trent held powers of attorney from the named investors, and described how those powers of attorney were obtained. The Notification was supported with the affidavit of Lori Hood, a partner at Johnson Trent which attached an copy of the September 17 letter sent to investors in the debtors. In the letter, Hood offered to represent the recipients in the bankruptcy cases.

The continued creditors meeting went ahead as scheduled on November 13. At the meeting, the U.S. Trustee asked whether there was still a request for an election. Counsel for the Group of Investors, this time Deborah Fritsche, requested an election. Fritsche noted that she and Ms. Hood had powers of attorney from the statutorily required number of qualified creditors, and that on behalf of those creditors she was requesting the election. Ms. Hood, she said, would cast the votes.

The U.S. Trustee asked whether there any objections to the Group of Investors’ request. Collins objected that the Johnson Trent firm’s solicitation of proxies violated the Bankruptcy Rules for several reasons. Collins also objected that the Johnson Trent firm had failed adequately to disclose a conflict of interest it had in representing the investors and casting their votes. A creditor, Dr. Charles Giger, joined Collins’s objection. The U.S. Trustee objected to the election for essentially the same reasons as Collins: problems with the solicitation of the proxies and the failure to disclose the claimed conflict of interest.

Finally, the U.S. Trustee called for nominations. The Group of Investors again nominated Marwil.

With the record on these preliminaries established, the U.S. Trustee conducted the election itself. The details of the voting are irrelevant, at least for the moment, since no one disputes that as a purely numerical matter Marwil won the election – and pretty handily, too.

Within days, Collins filed a more detailed, written objection to the election of Marwil. Creditors Harry and Adela Parlette and Dr. Giger joined Collins’s objection. The U.S. Trustee also filed a more detailed, written objection, and another creditor, Grace Johnson, joined the objections of both the U.S. Trustee and Collins.

On November 19, the U.S. Trustee filed with the court the Report of Disputed Election required under Rule 2007.1(b)(3)(B), and the next day the Group of Investors moved to have the

STATEMENT

court resolve the dispute. The Group of Investors later submitted a combined response to the objections, and on January 14 and 15, 2010, the court held an evidentiary hearing to determine the validity of the election.

b. Legal Framework

The Bankruptcy Code promotes the participation of creditors in the administration of bankruptcy cases. *See In re Ben Franklin Retail Stores, Inc.*, 214 B.R. 852, 861 (Bankr. N.D. Ill. 1997); *In re Brent Indus., Inc.*, 96 B.R. 193, 195 (Bankr. N.D. Iowa 1989). To that end, the Code permits unsecured creditors in chapter 7 cases and in chapter 11 cases where the debtor is not a debtor-in-possession to elect the trustee.

The procedures for trustee elections in chapter 7 and chapter 11 cases are virtually identical because the Code provision for the election of chapter 11 trustees piggy-backs the provision for the election of chapter 7 trustees. *See generally Uzzi O. Raanan, Understanding Chapter 11 Trustee Elections*, 29 Cal. Bankr. J. 15, 19 (2007). On a timely request from a party in interest, section 1104(b)(1) requires the U.S. Trustee to convene a creditors meeting for the purpose of electing a trustee and declares that the election must be conducted “in the manner provided in subsections (a), (b), and (c) of section 702 of this title.” 11 U.S.C. § 1104(b)(1).

Section 702(a), in turn, spells out which creditors may vote in a trustee election. The creditor (1) must hold an allowable, undisputed, fixed, liquidated, unsecured claim of a kind entitled to distribution under certain Code provisions; (2) must not have “an interest materially adverse” to the interest of creditors entitled to such distributions; and (3) must not be “an insider.” 11 U.S.C. § 702(a). Sections 702(b) and (c) describes how many creditors it takes to request an election and how many votes it takes to win. *See* 11 U.S.C. §§ 702(b), (c).

Rule 2007.1 is the Bankruptcy Rule on the election of chapter 11 trustees. Just as section 1104(b)(1) piggy-backs section 702, Rule 2007.1(b)(2) piggy-backs the rules for the election of chapter 7 trustees, specifically Rules 2003(b)(3) and 2006.

Rule 2003(b)(3) explains that a creditor can vote if the creditor has filed a proof of claim or writing setting forth facts showing a right to vote under section 702(a). *See* Fed. R. Bankr. P. 2003(b)(3). The Rule also explains how the U.S. Trustee tabulates votes if there is an objection to a claim for purpose of voting. *See id.*

Rule 2006 concerns the solicitation and voting of proxies in connection with a trustee election. Rule 2006(b)(1) defines a “proxy” as “a written power of attorney authorizing any entity to vote the claim or otherwise act as the owner’s attorney in fact in connection with the administration of the estate.” *See* Fed. R. Bankr. P. 2006(b)(1). Rule 2006(b)(2) defines the “solicitation of a proxy” as “any communication . . . by which a creditor is asked, directly or

STATEMENT

indirectly, to give a proxy after or in contemplation of the filing of a petition by or against the debtor.” *See* Fed. R. Bankr. P. 2006(b)(2). The solicitation of a proxy, however, does not include a request “from an attorney to a regular client who owns a claim,” nor does it include a request “from an attorney to the owner of a claim who has requested the attorney to represent the owner.” *Id.*

The rules also specify who can and cannot solicit proxies. Rule 2007.1(b)(2) says that a proxy may be solicited only by a creditors committee appointed under section 1102 or by a party entitled to solicit a proxy under Rule 2006. *See* Fed. R. Bankr. P. 2007.1(b)(2). Rule 2006(c), in turn, permits certain creditors and committees as well as bona fide trade and credit associations to solicit proxies. *See* Fed. R. Bankr. P. 2006(c). More important, Rule 2006(d) specifies who cannot solicit proxies. *See* Fed. R. Bankr. P. 2006(d). In particular, Rule 2006(d)(3) prohibits the solicitation of a proxy “by or on behalf of any entity not qualified to vote under section 702(a).” *See* Fed. R. Bankr. P. 2006(d)(3). And Rule 2006(d)(4) prohibits the solicitation of a proxy “by or on behalf of an attorney at law.” *See* Fed. R. Bankr. P. 2006(d)(4).

If proxies will be voted at an election, Rule 2006(e) requires anyone holding two or more proxies to file and transmit to the U.S. Trustee a verified list of the proxies to be voted and a verified statement of the pertinent facts and circumstances in connection with the execution and delivery of each proxy. *See* Fed. R. Bankr. P. 2006(e). Subparts (1) through (6) of Rule 2006(e) describe the specific information that the Rule 2006(e) statement must include. *See* Fed. R. Bankr. P. 2006(e)(1)-(6).

If the outcome of an election is disputed, Rule 2007.1(b)(3)(B) says the U.S. Trustee must file a report notifying the court of the dispute and its nature, *see* Fed. R. Bankr. P. 2007.1(b)(3)(B), and section 1104(b)(2)(C) of the Code requires the court to resolve the dispute, *see* 11 U.S.C. § 1104(b)(2)(C). In so doing, Rule 2006(f) permits the court, on motion of any party in interest or on its own motion, to “determine whether there has been a failure to comply” with Rule 2006 or “any other impropriety in connection with the solicitation or voting of a proxy.” Fed. R. Bankr. P. 2006(f).

2. Discussion

The objections to Marwil’s election focus solely on the role of the Johnson Trent firm, in particular the firm’s solicitation of proxies. All told, the objecting parties assert five grounds for rejecting the proxies and overturning the election: (1) the proxies were improperly solicited by an attorney in violation of Rule 2006(d)(4); (2) the proxies were improperly solicited by someone with an interest materially adverse to other creditors in violation of Rule 2006(d)(3) and section 702(a)(2); (3) the proxies were improperly solicited by an insider in violation of Rule 2006(d)(3) and section 702(a)(3); (4) Johnson Trent substantially failed to comply with the disclosure requirements of Rule 2006(e); and (5) Johnson Trent is guilty of improprieties that

STATEMENT

warrant relief under Rule 2006(f).

a. Burden of Proof

The objecting parties bore the burden of proving these objections – meaning not only the burden of production but also of persuasion.

The Code and Rules say nothing about evidentiary burdens in the resolution of disputed trustee elections, and no case addresses the question directly. Several cases, however, take as a given that a party objecting to the outcome of a trustee election has the burden of proving the facts necessary for the objection to be sustained. *See, e.g., In re Amherst Techs., LLC*, 335 B.R. 502, 509 (Bankr. D.N.H. 2006); *In re New York Produce Am. & Korean Auction Corp.*, 106 B.R. 42, 47 (Bankr. S.D.N.Y. 1989); *In re Poage*, 92 B.R. 659, 666 (Bankr. N.D. Tex. 1988); *In re Metro Shippers, Inc.*, 63 B.R. 593, 599 (Bankr. E.D. Pa. 1986); *In re Blesi*, 43 B.R. 45, 47 (Bankr. D. Minn. 1984); *see also* 4 William L. Norton, Jr. & William L. Norton III, *Norton Bankruptcy Law & Practice* § 77:4 at 77-14 (3d ed. 2009).

Placing the burden on the objecting parties also fits with basic concepts of allocating burdens of proof. When a proceeding arises under a statute silent on the burden of proof, the default rule is that the party seeking relief has the burden. *See Schaffer v. Weast*, 546 U.S. 49, 51 (2005); *see also* 2 Kenneth S. Broun, *McCormick on Evidence* § 337 at 474 (6th ed. 2006) (noting that the burden of proof generally falls, and should fall, on the party seeking to “change the present state of affairs”); 1 Christopher B. Mueller & Laird C. Kirkpatrick, *Federal Evidence* § 3:3 at 430 (3d ed. 2007) (noting that the “broadest and most accepted idea” concerning trial burdens “is that the person who seeks court action should justify the request”).

Placing the burden on the objecting parties is also consistent with the allocation of burdens in disputes over other kinds of elections. Union representation elections, for example, are presumed valid, and the objecting party has the “formidable burden” of showing the election was invalid. *See, e.g., N.L.R.B. v. Erie Brush & Mfg. Co.*, 406 F.3d 795, 801 (7th Cir. 2005). Elections of political candidates in most states are likewise presumed valid, with the burden of showing otherwise falling squarely on the challenger. *See, e.g., Fuller v. Thomas*, 284 Ga. 397, 397, 667 S.E.2d 587, 588 (2008); *In re Contested Election of Schoessler*, 140 Wash. 2d 368, 392, 998 P.2d 818, 831 (2000); *In re Appeal of Ramseur*, 120 N.C. App. 521, 525, 463 S.E.2d 254, 256-57 (1995).

A similar presumption of validity attends Marwil’s election as trustee here. Not only are trustee elections part of the “creditor democracy” the Code encourages, *see In re Michelelex Ltd.*, 195 B.R. 993, 1003 (Bankr. W.D. Mich. 1996), but Marwil unquestionably prevailed in the election and in the absence of some objection would have been certified as trustee without any action from the court. *See* 11 U.S.C. § 1104(b)(2)(A); Fed. R. Bankr. P. 2007.1(b)(3)(A). Court

STATEMENT

action became necessary only because Collins, the U.S. Trustee, and others did object. Since these parties “seek to change the present state of affairs,” 2 Broun, *supra*, § 337 at 474, by having the court overturn the result of the election, they had the burden of coming forward with facts sufficient to “justify the request,” 1 Mueller & Kirkpatrick, *supra*, § 3:3 at 430. It was not Marwil’s burden, or the burden of the creditors who voted for him, to demonstrate the election’s validity.

b. Objections to the Election

The scant evidence adduced at the January hearing did not begin to meet the objecting parties’ burden of proving their objections to Marwil’s election. The evidence offers no reason at all to change the election result and dislodge Marwil as the creditors’ choice for trustee.

i. Solicitation of Proxies by an Attorney

The objecting parties first contend that Marwil’s election cannot stand because all of the proxies Hood voted were solicited by an attorney (Hood herself) in violation of Rule 2006(d)(4). The objecting parties point to Hood’s September 17 letter as the offending solicitation. The Group of Investors respond that under Rule 2006(b)(2) no proxies were solicited by an attorney (or anyone else) because all of the proxies voted at the November 14 election were voted on behalf of Johnson Trent’s existing clients.

Both sides are mistaken. The Group of Investors is wrong to contend that all of the proxies were valid because they were voted on behalf of clients. The relevant question under Rule 2006(b)(2) is not whether an attorney *voted* the proxy on behalf of a “regular client” or a claimant who had asked the attorney to represent him in the case but whether the attorney *solicited* the proxy from one of those two. *See* Fed. R. Bankr. P. 2006(d) advisory committee’s note (1993) (noting that “[s]olicitation by an attorney of a proxy from a creditor who was not a client prior to the solicitation is objectionable . . .”). The September 17 letter was plainly a solicitation of proxies expressly directed to people who were neither “regular clients” of Johnson Trent nor claimants who had previously sought Johnson Trent’s representation. That the solicitation was successful, resulting in proxies Hood voted at the election, in no way legitimates their solicitation.

But the objecting parties are equally mistaken in contending that the September 17 letter invalidated all of the proxies Hood voted. The September 17 letter only solicited proxies from a limited class of people. The relevant sentence on page 2 said: “If you have already filed your claim, I would ask that you refrain from giving any other entity your proxy and instead consider providing us your proxy.” In other words, Hood solicited proxies only from non-client creditors who had *already filed claims*, no one else. If, as it appears, Hood later requested proxies from people who had not filed claims and who responded to the letter only by becoming Johnson

STATEMENT

Trent clients, those later proxy requests fell under the exception in Rule 2006(b)(2) for communications between an attorney and a claimant who had sought representation from the attorney in the bankruptcy case. They were not “solicitations” subject to the Rule.

Recognizing this, apparently, Collins notes that the Rule defines “solicitation” as a communication that asks a creditor “directly or indirectly” to give a proxy. Collins argues that despite the limited scope of the relevant sentence, the rest of the September 17 letter should be considered an “indirect” solicitation from an attorney.

The problem with this argument is that it finds no support in the letter itself. The word “proxy” appears only on page two and only in the sentence quoted earlier. The rest of the letter is a solicitation of clients, not a solicitation of proxies. It addresses reasons to hire Johnson Trent and asks the recipients to sign and return the enclosed engagement letter and conflict waiver. Nothing besides the sentence on page two can be read as soliciting a proxies from the recipients, and Collins points to nothing. The word “indirectly” in Rule 2006(b)(2) cannot be stretched to turn any communication using the word “proxy” into a blanket solicitation of proxies regardless of the communication’s actual content.

Because Hood, a lawyer, solicited proxies from non-clients who had already filed claims, the solicitation of those proxies violated Rule 2006(d)(4), and the votes of those creditors cannot be counted. Since the remaining proxies were apparently voted on behalf of creditors who were already in the Johnson Trent fold when their proxies were obtained – and no evidence showed otherwise – those proxies by definition were not “solicited” under Rule 2006(b)(2), and the votes of those creditors must be counted.

The question, then, is whether subtracting the disqualified votes changes the outcome of the election. The answer to that question in turn depends on the answers to two more questions: (1) which creditors had already filed claims before they received the September 17 letter, and (2) whether Hood sought to vote the proxies of those creditors at the election. Only those votes are invalid; the rest are valid.

A review of the court’s claims register (of which the court can take judicial notice) and the transcript of the election (a document in evidence) shows (1) that only a few investors had already filed claims by the time they received the September 17 letter (even assuming several days for delivery), and (2) Hood voted few of those claims at the election. Subtracting the disqualified votes has no effect on the outcome, because even without them Marwil still received enough votes under section 702(c)(2) to be elected trustee.

Specifically:

- *Life Fund 5.1*. In the *Life Fund 5.1* case, creditors holding claims totaling

STATEMENT

\$3,337,357.48 voted for Marwil, and creditors holding claims totaling \$1,520,156.25 voted against him, including Dr. Giger. Of the votes for Marwil, only the vote of Piche (holding a claim of \$100,000) is disqualified. Marwil won by a substantial majority, and subtracting \$100,000 makes no difference.

• ***Life Fund 5.2.*** In the *Life Fund 5.2* case, creditors holding claims totaling \$1,829,945.40 voted for Marwil, and creditors holding claims totaling \$399,717.06 voted against him. No votes are disqualified. Marwil won by a substantial majority.

• ***Houston Tanglewood Partners.*** In the *Houston Tanglewood Partners* case, creditors holding claims totaling \$4,597,720.91 voted for Marwil, and creditors holding claims totaling \$897,798 voted against him (including the Parlettes and Dr. Giger). Of the creditors who voted for Marwil, the vote of Hodel (holding a claim of \$100,000) is disqualified. At the election, the U.S. Trustee also objected to the votes of John and Laura Spalding and Consolidated Wealth Management, creditors holding claims totaling \$1,250,708.85, on the ground that those creditors are insiders. Even if the insider objection is assumed to be valid and the votes of the Spaldings and Consolidated Wealth Management as well as Hodel are disqualified, Marwil still won by a substantial majority.

• ***A&O Resource Management.*** In the *A&O Resource Management* case, creditors holding claims totaling \$6,270,557.18 voted for Marwil, and creditors holding claims totaling \$315,000 voted against him. Of the votes for Marwil, the votes of the Coopers, the Kesslers, McDowell, Nordby, and Shelton are disqualified. Those creditors hold claims totaling \$721,011.15. Subtracting that figure from the nearly \$6.3 million in claims voted for Marwil makes no difference to the outcome.

• ***A&O Life Fund.*** In the *A&O Life Fund* case, creditors holding claims totaling \$1,962,092.55 voted for Marwil, and creditors holding claims totaling \$298,624.990 voted against him. Of the votes for Marwil, only the vote of Dunlap (holding a claim of \$68,768.77) is disqualified. Marwil won by a substantial majority.

• ***A&O Life Fund.*** In the *A&O Bonded Life Assets* case, creditors holding claims totaling \$902,752.82 voted for Marwil, no creditors voted against him, and no votes for him are disqualified. Marwil won the election.

• ***A&O Bonded Life Settlement.*** In the *A&O Bonded Life Settlement* case, finally, creditors holding claims totaling \$1,952,861.95 voted for Marwil, and creditors holding claims totaling \$743,009.74 voted against him. Of the votes for Marwil, the votes of Monkres, Hennessy, and Moore are disqualified. Those creditors hold claims totaling \$157,000, not enough to change the outcome of the election.

STATEMENT

Because the improper solicitation of proxies by an attorney in this case has no effect on Marwil's election, the objection based on Rule 2006(d)(4) will be overruled.

ii. "Materially Adverse Interest" and "Insider"

The next two objections can be overruled for the same reason. The objecting parties complain that the September 17 letter was a solicitation by "an entity not qualified to vote under § 702(a)," and Rule 2006(d)(3) bars proxy solicitations by such an entity. *See* Fed. R. Bankr. P. 2006(d)(3). Section 702(a) only entitles a creditor to vote if the creditor has no interest materially adverse to other creditors and is not an insider. *See* 11 U.S.C. § 702(a). The objecting parties contend that Spalding's involvement with Bayou City and Bayou City's involvement with the debtors gave the Johnson Trent firm a materially adverse interest, made Johnson Trent an insider, and so barred Johnson Trent from soliciting proxies.

The disposition of the attorney solicitation objection under Rule 2006(d)(4) takes care of these objections as well. Again, most of the proxies were not obtained through "solicitations" as defined under Rule 2006(b)(2) because the September 17 letter sought proxies from a limited group; as far as we can tell, the remaining proxies were obtained through communications Hood had with creditors who had already retained Johnson Trent as counsel. If the votes of the few improperly solicited proxies are disqualified, the election result is the same. If there were not enough solicitations improper under Rule 2006(d)(4) to change the election's outcome, there were not enough solicitations improper under Rule 2006(d)(3) to change the outcome, either.

It may be worth noting that if the September 17 letter had solicited proxies from every recipient rather than just a few, the election would indeed be objectionable under Rule 2006(d)(3) – not because there was evidence making Johnson Trent out to be an insider or showing that it held any interest materially adverse to the creditors (there was no evidence), but for a more fundamental reason. The only "entity . . . qualified to vote under section 702(a)" is, according to the words that begin section 702(a), "a creditor." 11 U.S.C. § 702(a). Rule 2006(d)(3) thus prohibits non-creditors from soliciting proxies. *See* 9 *Collier on Bankruptcy* ¶ 2006.05 at 2006-8 (Alan N. Resnick & Henry J. Sommer eds., 15th ed. rev. 2009). There is no reason to believe either Johnson Trent or Hood is a creditor in this case (and neither is a bona fide trade or credit association). So Rule 2006(d)(3) prohibited them from soliciting proxies just as Rule 2006(d)(4) did, whether or not they were insiders and whether or not they had an interest materially adverse to other creditors.

But the problem is not fatal because, again, the September 17 letter was not the broad "solicitation" the objecting parties maintain. The limited violation of Rule 2006(d)(3) has no more effect on the election of Marwil than the limited violation of Rule 2006(d)(4). The objections based on Rule 2006(d)(3) will be overruled.

STATEMENT

iii. Disclosure

The objecting parties next contend, or appear to contend, that Johnson Trent's "Notification pursuant to Bankruptcy Rule 2006" failed to disclose the information required by Rule 2006(e). The only response appears in the Notification itself, where Johnson Trent takes the position that Johnson Trent had no obligation to comply with Rule 2006(e). This is so, the Johnson Trent maintains, because the firm solicited no proxies.

Johnson Trent is mistaken. For starters, the firm did solicit proxies, though not many. But even if Johnson Trent had solicited no proxies, the disclosure statement would have been necessary. Rule 2006(e) "sets forth an elaborate set of reporting requirements for anyone holding two or more proxies." 9 *Collier on Bankruptcy, supra*, ¶ 2006.06 at 2006-9. The critical word is "holding." The Rule requires information from any "holder of two or more proxies," not just a holder of proxies who obtained them through solicitations. *See* Fed. R. Bankr. P. 2006(e). Johnson Trent undeniably held two or more proxies, no matter how obtained, and so the firm was obligated to provide the information called for in Rule 2006(e).

That said, the Rule 2006(e) objection is deficient for two reasons. The first is that it is not clear the objection was ever made, let alone explained. The U.S. Trustee's Report of Disputed Election states somewhat confusingly: "Collins contested the validity of the proxies of the Group of Investors, because their attorneys' solicitation was unauthorized under Fed. R. Bankr. P. 2006(d)(4), and because they failed to substantially comply with Fed. R. Bankr. P. 2006(e)" If this is meant to suggest Collins objected on the ground that Johnson Trent failed to comply with Rule 2006(e), the Report is incorrect. Collins never made that objection – not at the election itself, and not in the written objection he filed afterward. The U.S. Trustee never made the objection, either. Rule 2006(e) is mentioned only in the Report of Disputed Election, and how Johnson Trent failed to comply with the Rule is nowhere described. The Rule 2006(e) objection therefore is waived. *See In re Commercial Loan Corp.*, 316 B.R. 690, 699 (Bankr. N.D. Ill. 2004) (holding that "[a]rguments a party fails to raise in a timely fashion, or raises but then fails to press responsibly throughout the litigation, are waived").

Second, the objection had little going for it anyway because the Notification Johnson Trent filed substantially complied with Rule 2006(e). Rule 2006(e) requires a holder of two or more proxies to file and transmit to the U.S. Trustee a "verified list of the proxies to be voted and a verified statement of the pertinent facts and circumstances in connection with the execution and delivery of each proxy." Fed. R. Bankr. P. 2006(e). The Rule goes on to list six items that the "statement of pertinent facts" must include. *Id.*

Here, Johnson Trent's Notification supplied a verified list of the proxies to be voted. The Notification also contained four of the six items that Rule 2006(e) insists must be included in the statement of pertinent facts (and the other two do not apply in this case).

STATEMENT

- Rule 2006(e)(1) requires a copy of the solicitation of any proxy. Fed. R. Bankr. P. 2006(e)(1). A copy of the September 17 letter was attached to the Notification.
- Rule 2006(e)(2) requires an identification of the solicitor and the proxyholder. Fed. R. Bankr. P. 2006(e)(2). The Notification identified both.
- Rules 2006(e)(3) and (4) requires a statement that no consideration had been paid or promised by the proxyholder for the proxy, and a statement whether there was an agreement between the proxyholder and any other entity for the payment of any consideration in connection with voting the proxy or for the sharing of compensation with any entity. Fed. R. Bankr. P. 2006(e)(3), (4). The Notification contained the required statements.

The Notification was arguably insufficient only in that it failed to describe the pertinent facts and circumstances “in connection with the execution and delivery of *each* proxy.” Johnson Trent attached the September 17 letter, explained that the firm held two conference calls to respond to inquiries it received about the bankruptcy cases, and stated that the proxies for its clients were signed after the clients retained Johnson Trent as counsel. But the Notification did not set out for each proxy the facts and circumstances relating to its execution and delivery.

Although it would have been better if Johnson Trent had supplied this detail, its absence provides no cause for concern in this case. The methods Johnson Trent used to contact creditors have been disclosed. It is clear – or clear enough, at least – which creditors had proxies “solicited” and which did not. Those that did not were clients of Johnson Trent when the proxies were obtained. Whether each proxy was sought by mail, by phone, or by fax, and whether each was signed in the creditor’s office, at his kitchen table, or elsewhere, is information that makes no real difference here. And if it does make a difference, no objecting party has said why.

Bankruptcy courts have wide discretion in handling proxy disputes, and harmless deviations from Rule 2006 will not invalidate an election. *See Metro Shippers*, 63 B.R. at 599; *see also Ben Franklin Retail Stores*, 214 B.R. at 861. Since the deviation here appears harmless, the objection under Rule 2006(b)(3), if there was an objection, will be overruled.

iv. Improprieties

Finally, the objecting parties invoke Rule 2006(f), which permits the court on the motion of any party in interest or on its own motion to determine where there as been any “impropriety in connection with the solicitation or voting of a proxy.” Fed. R. Bankr. P. 2006(f). The objecting parties assert that two improprieties infected the voting here: first, that John Spalding’s connection to Bayou City meant Johnson Trent had a conflict of interest, and the conflict was not adequately disclosed; and second, that Hood and Fritsche obtained proxies by telling creditors they could not expect Collins or the court to protect their interests because both Collins and the

STATEMENT

court are corrupt.

The sparse record fails to substantiate the conflict of interest argument. The evidence showed only that Spalding is “of counsel” at Johnson Trent, that he was formerly a partner in the firm, that he was also an officer of Bayou City, that his wife was the owner of Bayou City, and that at some point more than two years before the bankruptcies were filed Bayou City was doing business of some kind with some of the debtors (it is unclear how many of the debtors, what kind of business, or how much). According to Fritsche, the business relationship between John Spalding and Bayou City was disclosed to creditors. The Spaldings themselves are creditors in these cases, and Johnson Trent represents them, just as Johnson Trent represents Consolidated Wealth Management, another entity in which the Spaldings have an interest.

None of this demonstrates a conflict. Collins’s counsel suggested obliquely at the hearing that as a result of the Bayou City connection, the trustee might have some sort of claim against John Spalding on behalf of the estate. (The word “target” was used.) But the suggestion was never more than oblique. Neither Collins nor his counsel chose to elaborate, and no evidence was introduced – no set of facts offered, no legal theory proposed – that would support a claim. The mere possibility that the Spaldings’ relationship with the debtors might be investigated, or that the trustee might one day file an action of some kind against John Spalding, is not enough to warrant throwing out Marwil’s election. *Cf. Amherst Techs.*, 335 B.R. at 502 (holding that an objection to a creditor’s vote on “materially adverse interest” grounds must be based on more than the “mere suspicion” that the trustee might sue the creditor); *New York Produce*, 106 B.R. at 47 (same).

The same evidentiary shortfall afflicts the objecting parties’ claim that Fritsche and Hood secured proxies through fearmongering. Collins asserted in his written objection that during one of the conference calls, either Fritsche or Hood told creditors that Collins had filed a motion to deprive investors of notice, that the bankruptcy case was a “Chicago conspiracy,” and that the court was not following the rules. But the evidence did not bear out Collins’s assertions. No witness testified that Fritsche or Hood said any of these things, and Fritsche herself specifically denied telling anyone that Collins was appointed without notice, the case was a “Chicago conspiracy, or the court was not following the rules. Fritsche was a difficult and uncooperative witness – exceptionally so – but these denials were credible.

Not credible, on the other hand, was Fritsche’s insistence that she did not know the meaning of “the Chicago way,” a phrase she conceded using more than once in her conversations with creditors. The phrase comes from the 1987 movie “The Untouchables,” in which Sean Connery used it to describe the vengeful tendencies of 1920’s Chicago mobs. *See* Mark Jacob, “‘The Chicago Way’ (and Other Wayward Words),” *Chi. Trib.* Sept. 13, 2009, *available at* <http://archives.chicagotribune.com/2009/sep/13/opinion/chi-perspec0913chicagosep13>. More recently, journalists such as Chicago Tribune columnist John Kass have taken to using “the

STATEMENT

Chicago way” as shorthand for the ruthless and occasionally corrupt quality of local Chicago politics. See, e.g., John Kass, *An 11th Ward Nightmare*, Chi. Trib., Feb. 26, 2010, § 1 at 2 (asserting that “the muscled-up Chicago Way crushes regular folks who play by the rules”); John Kass, *Obama to Deliver Healthcare the Chicago Way*, Chi. Trib., Feb. 25, 2010, § 1 at 2 ; John Kass, *The No. 1 Rule for Client 10: Embrace the Chicago Way*, Chi. Trib., March 13, 2008, § 1 at 2. In using the phrase “the Chicago way,” Fritsche could have been trying to convey to creditors that Collins and this court are ruthless and corrupt – a good reason for creditors to retain Johnson Trent as counsel and have that firm’s protection.

But the record is insufficient to conclude that Fritsche was trying to convey any such thing. The only evidence of how Fritsche used the phrase consists of a single e-mail Fritsche sent to Janet Chafin, counsel for the Parlettes, on September 17, 2009. In the e-mail, Fritsche wrote: “I will ask local counsel about the [C]hic[a]go way (as they say) to lift stay and would motion now be handled [*sic*].” Fritsche’s statement referred only to local practice in the Chicago bankruptcy court (since court practices do differ from place to place), and her reference to “the Chicago way” was merely flippant. Chafin, moreover, read Fritsche’s reference in that vein, responding an hour later: “Please let me know what you decide about ‘the Chicago way’ of proceeding with a motion”

No creditor in this case has the slightest reason – or has ever had the slightest reason – to be concerned about the honesty and integrity of the Chicago bankruptcy court (a federal court) or of Collins (a former Assistant U.S. Attorney who made his reputation prosecuting corrupt politicians). Fritsche surely knows this – just as she knows that recklessly calling into question the honesty and integrity of another lawyer or a judge with false accusations of corruption is not only defamation but a basis for professional discipline. See, e.g., *In re Phelps*, 55 Ill. 2d 319, 303 N.E.2d 13 (1973); *In re Maloney*, 949 S.W.2d 385 (Tex. Ct. App. 1997) (per curiam).

In short, Fritsche could have chosen her words more carefully, but the thin record here does not demonstrate an impropriety justifying relief under Rule 2006(f). The Rule 2006(f) objection will be overruled, as well.

c. A Final Point

One final point. The court’s decision to overrule the objections and confirm Marwil’s election should not be taken as an indication that Collins has been a poor trustee and creditors have some reason to be dissatisfied with his performance. On the contrary, it appears that over the last few months Collins and his able counsel have done an exceptional job in a difficult case. They should be commended. By the same token, Marwil is an experienced and capable bankruptcy lawyer. Perhaps he will do as well. Perhaps not. Perhaps he will do better.

The point, simply, is that who would make the better trustee, Collins or Marwil, is not a

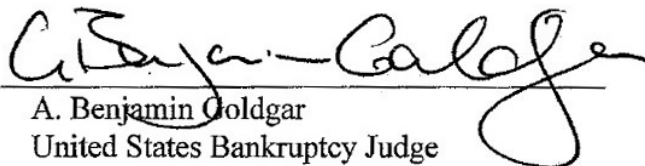
STATEMENT

question for the court to decide (assuming each man is qualified, and each is). Creditors are entitled to elect a new trustee for any reason or none at all. *See Uzzi O. Raanan, supra*, at 35-36. Although the paramount consideration in deciding an election challenge is “the welfare of the estate itself,” *Poage*, 92 B.R. at 666, the estate’s welfare in a creditor democracy is best judged by the creditors, provided the election was fair and legal. In a dispute over a trustee election, then, the court is called upon only to determine the fairness and legality of the *process*. *See In re Nanvarok Seven, Inc.*, 148 B.R.86, 87 (Bankr. D.D.C. 1992) (noting that “[a]s a general rule, the choice of the unsecured creditors should be recognized and upheld” unless their selection was contrary to law). The creditors here have made their choice, and the objecting parties have not shown that the process by which they made it was unfair or contrary to law.

3. Conclusion

For these reasons, the objections of Patrick Collins, the U.S. Trustee, the Texas State Securities Board, Harry and Adela Parlette, Dr. Charles Giger, and Grace Johnson to the election are overruled. The election of Jeffrey Marwil as chapter 11 trustee is confirmed.

Dated: March 8, 2010


A. Benjamin Goldgar
United States Bankruptcy Judge