Civil Action No. 3:12-cv-00367-F (O)

IN THE UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF TEXAS

JEFF BARON,

Appellant,

v.

CHAPTER 11 TRUSTEE DANIEL J. SHERMAN

Appellee

Appeal from the United States Bankruptcy Court
For the Northern District of Texas, Dallas Division
Bankruptcy Petition No. 09-34784-sgj11

BRIEF FOR THE APPELLANT

Respectfully submitted,

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The undersigned counsel of record certifies that the following listed persons and entities have an interest in the outcome of this case. These representations are made in order that the judge of this Court may evaluate possible disqualification or recusal.

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STATEMENT OF JURISDICTION

28 U.S.C. §158 vests jurisdiction in this Court to hear this appeal from an order of the bankruptcy court, ordering the sale of property and possessing a definitive operative finality. *See Forgay v. Conrad*, 47 U.S. 201, 204 (1848); *Matter of Greene County Hosp*., 835 F.2d 589, 593 (5th Cir. 1988).

ISSUES PRESENTED

ISSUE 1. Is the Bankruptcy Court authorized and empowered to determine the ownership of Servers.com through a 11 U.S.C. §363 motion, and can a Bankruptcy Court authorize the sale of property not owned by the bankruptcy estate under §363(b) ?

ISSUE 2. Were all of the Bankruptcy Court's fact findings clearly erroneous ?

ISSUE 3. Did the Bankruptcy Court err in granting the motion to sell the domain name servers.com, including erring in refusing to allow Jeff Baron's counsel to argue and present evidence on his behalf ?

ISSUE 4. Does the Bankruptcy Court have Subject Matter Jurisdiction, or Constitutional Authority to enter an order Authorizing the Sale of property not owned by the bankruptcy estate ?

STATEMENT OF THE CASE

This is an appeal from an order granting authority to sell property that was not owned by the bankruptcy estate and for which no adversary proceeding was held to determine ownership. R. 8-10.

STATEMENT OF FACTS

The Ondova Bankruptcy Court Judge entered an order placing Servers, Inc. into receivership because Servers, Inc. was in default of its obligations regarding the domain name Servers.com. R. 255. Accordingly, because of Servers, Inc.'s default, as a matter of Texas and Nevada state law, pursuant to the agreement between the parties the domain name servers.com reverted to Baron and Emke and they became 50/50 owners of the domain name. The Ondova bankruptcy estate retains its 50% ownership interest in Servers, Inc., however, as a matter of Texas and Nevada state law, Servers, Inc. no longer owners "servers.com".

ARGUMENT SUMMARY

The Bankruptcy Court is not authorized nor empowered to determine the ownership of property through a 11 U.S.C. §363 motion, and a Bankruptcy Court cannot authorize the sale of property not owned by the bankruptcy estate under 11 U.S.C. §363(b). Moreover, allowing the bankruptcy judge such power would violate the US Constitution.

ARGUMENT AND AUTHORITIES

ISSUE 1. Is the Bankruptcy Court authorized and empowered to determine the ownership of Servers.com through a 11 U.S.C. §363 motion, and can a Bankruptcy Court authorize the sale of property not owned by the bankruptcy estate under §363(b) ?

A) Applicable Standard of Appellate Review

De novo review extends to all legal issues, application of law to fact, and mixed questions of fact and law. *E.g., Southmark Corp. v. Coopers & Lybrand*, 163 F.3d 925, 929 (5th Cir.1999); *Southmark Corp. v. Marley*, 62 F.3d 104, 106 (5th Cir.1995). The bankruptcy court's legal conclusions are always subject to de novo review. *Nichols v. Petroleum Helicopters, Inc.*, 17 F.3d 119, 122 (5th Cir. 1994) *De novo* review requires the Court "to make a judgment independent of the bankruptcy court's without deference to that court's analysis and conclusions." *Lawler v. Guild, Hagen & Clark, Ltd. (In re Lawler)*, 106 B.R. 943, 952 (N.D.Tex. 1989) (Fish, J.).

B) Federal Rule of Bankruptcy Procedure 7001(2)

Federal Rule of Bankruptcy Procedure 7001(2) provides that a proceeding to determine the Estate's "interest in property" be an "adversary proceeding" and "governed by the rules of this Part VII." Fed.R.Bankr.P. 7001. By contrast, a Section 363 motion to sell an asset of the Estate is merely a "contested matter" governed by Rule 9014. Fed.R.Bankr.P. 9014. Accordingly, a bankruptcy court is not empowered or authorized to determine ownership of an asset in deciding a motion under Section 363. *E.g.*, *In re Hearthside Baking*

Co., Inc., 397 BR 899, 902 (Bkrtcy. N.D. Ill. 2008); *In re Whitehall Jewelers Holdings, Inc.*, 2008 WL 2951974 *6 (Bankr.D.Del. 2008), holding:

> "The Court cannot determine whether the [property is] property of the estate through a contested matter, such as a sale motion under Section 363. Federal Rule of Bankruptcy Procedure 7001(2) requires that an adversary proceeding be commenced to determine the 'validity, priority or extent of [an] interest in property.'"

C) Conclusion

Thus, the Bankruptcy Court erred and exceeded its authority in ordering the sale of Servers.com without first establishing the Bankruptcy Estate's interest, if any, in the asset in an adversary proceeding pursuant to Rule 7001(2). *Id*. Notably, the public policy served by this rule is substantial– before businesses outside of bankruptcy proceedings can be stripped of their assets, the bankruptcy court must conduct a full adversarial proceeding including service of process on the interested parties and the full disclosures required by Fed.R.Civ.P. 26(a). *See* Fed.R.Bankr.P. 9014(c) (mandatory disclosure requirements of 'adversary proceedings' do not apply in 'contested matters'). Accordingly, because a mandatory element required for authorization pursuant to Section 363(b) is that the property be owned by the bankruptcy estate, the Bankruptcy Court's order to sell an asset not owned by the bankruptcy estate was not an authorization under the grant of authority provided by Section 363(b).

ISSUE 2. Were all of the Bankruptcy Court's fact findings clearly erroneous ?

A) Applicable Standard of Appellate Review

The bankruptcy court's findings of fact are reviewed under the clearly erroneous standard. *See* Bankr.R.P. 8013; *Richmond Leasing Co. v. Capital Bank, N.A.*, 762 F.2d 1303, 1308 (5th Cir.1985). *De novo* review extends to all legal issues, application of law to fact, and mixed questions of fact and law. *E.g., Southmark Corp,* 163 F.3d at 929.

B) Uncontroverted Evidence

Pursuant to Bankruptcy Rule of Procedure 363(p), the entity asserting an interest in property has the burden of proof on the issue of the extent of such interest. Bankr.R.P. 363(p); 11 U.S.C. §101 (15) ("entity" includes the estate). However, the uncontroverted evidence established Jeff Baron and not the bankruptcy estate of Ondova owned a half interest in the domain name "servers.com".

C) <u>As a Matter of Law</u>, Jeff Baron and not the Ondova bankruptcy estate owns half of the domain name "Servers.com"

i. The Emke Settlement

The Emke settlement transferred most of the rights to "servers.com" to a new entity (Servers, Inc., a Nevada corporation). R. 246-9. The new corporation's stock was owned 50/50 by Ondova and Emke. *Id.* No one disputes Ondova's right to ownership of the Servers, Inc. stock. However, the Emke settlement expressly reserved an interest in the domain name for Emke and Baron personally. *Id.* Pursuant to the agreement, **<u>Baron and Emke reserved a security and reverter interest</u>** in the domain name, reverting ownership on the condition that the corporation was ever placed into receivership. *Id.* Specifically the Emke settlement agreement provides:

> "In the event of insolvency, receivership and/or other default of the jointly owned company, the domain name <servers.com> shall revert to Jeff Baron and Mike Emke, to be owned jointly and equally. To this degree, these two principals shall maintain a first lien and security interest in the domain name superior to any other investor, equity holder or creditor."
>
> R. 247.

On October 18, 2011, the Ondova Bankruptcy Court Judge entered an order placing Servers, Inc. into receivership because Servers, Inc. was in default of its obligations regarding the domain name Servers.com. R. 255. Accordingly, because of Servers, Inc.'s default, as a matter of Texas and Nevada state law, pursuant to the agreement between the parties, the domain name servers.com reverted to Baron and Emke and they became 50/50 owners of the domain name. The Ondova bankruptcy estate retains its 50% ownership interest in Servers, Inc., however, as a matter of Texas and Nevada state law, Servers, Inc. no longer owns "servers.com"

To be clear, the reversion interest was triggered not because Ondova or Servers, Inc., went into bankruptcy. Servers, Inc. was not placed into bankruptcy. The event triggering the reversion interest was the **default of the jointly owned company** (Servers, Inc.) in carrying out its purpose as agreed in the original Emke settlement and being forced into receivership. Notably, it is Servers, Inc. that lost ownership of servers.com, not Ondova. Similarly, Servers, Inc.'s loss of servers.com had nothing to do with the fact that Ondova happened to file for bankruptcy. The Ondova estate owned stock in Servers, Inc. and it did not lose that stock. Just as if Ondova had owned stock in Microsoft, Inc. and Microsoft defaulted on some contract and lost rights thereby, Ondova's stock in Microsoft, Inc., would be decreased in value accordingly. Nothing in the bankruptcy law prevents Microsoft, Inc., from losing assets pursuant to pre-existing legal rights and agreements because Ondova owned Microsoft stock and then went bankrupt. Similarly, nothing in the bankruptcy law creates any special rights relating to Servers, Inc., because Ondova happened to own Servers, Inc. stock and Ondova went into bankruptcy. The statutory protections afforded to an entity in bankruptcy do not extend to corporations the bankrupt entity happens to own stock in.

ISSUE 3. Did the Bankruptcy Court err in granting the motion to sell the domain name servers.com, including erring in refusing to allow Jeff Baron's counsel to argue and present evidence on his behalf ?

A) Applicable Standard of Appellate Review

The bankruptcy court's findings of fact are reviewed under the clearly erroneous standard. *See* Bankr.R.P. 8013; *Richmond Leasing,* 762 F.2d at 1308. *De novo* review extends to all legal issues, application of law to fact, and mixed questions of fact and law. *E.g., Southmark Corp,* 163 F.3d at 929.

B) Failure of Due Process

The Bankruptcy Court refused to allow Jeff Baron to be heard on the sale motion. ASR. 98. That refusal is a fundamental failure of Due Process. *E.g.*, *Armstrong v. Manzo,* 380 U.S. 545, 552 (1965)(A fundamental requirement of due process is "the opportunity to be heard); *Goldberg v. Kelly*, 397 U.S. 254, 267 (1970) ("The fundamental requisite of due process of law is the opportunity to be heard."); *Goss v. Lopez*, 419 U.S. 565, 579 (1975) (same); *Logan v. Zimmerman Brush Co.*, 455 U.S. 422, 429-430 (1982). Accordingly, the Bankruptcy Court's order should be found to be void. *Bass v. Hoagland*, 172 F.2d 205, 209 (5th Cir. 1949) ("We believe that a judgment, whether in a civil or criminal case, reached without due process of law is without jurisdiction and void"). The Bankruptcy Court appears to have erroneously found that the District Court could strip Baron of his Constitutional right to Due Process by its receivership order. Notably, the purported receiver did not claim any ownership interest in the domain name servers.com.

ISSUE 4. Does the Bankruptcy Court have Subject Matter Jurisdiction, or Constitutional Authority to enter an order Authorizing the Sale of property not owned by the bankruptcy estate ?

A) Applicable Standard of Appellate Review

The bankruptcy court's findings of fact are reviewed under the clearly erroneous standard. *See* Bankr.R.P. 8013; *Richmond Leasing,* 762 F.2d at 1308. *De novo* review extends to all legal issues, application of law to fact, and mixed questions of fact and law. *E.g., Southmark Corp,* 163 F.3d at 929.

B) Unconstitutional Delegation of Judicial Authority

Authorizing a bankruptcy judge to finally adjudicate and transfer ownership interest in non-estate property, the statute would be an unconstitutional delegation of federal judicial authority to non-Article III judges. *See Northern Pipeline Constr. Co. v. Marathon Pipe Line Co*., 458 U.S. 50, 71-72 (1982); *Stern v. Marshall*, 131 S.Ct. 2594, 2615 (2011). Allowing a bankruptcy judge to finally adjudicate state law ownership rights would unconstitutionally grant such judges unbridled and unchecked judicial authority over the property of the entire community. *See Id.* The constitutional violation is illustrated by the example of an individual who retires and purchases a multi-family dwelling with their life savings. By mistake or through the deception of an unscrupulous debtor, while our retiree sleeps one night, the bankruptcy court might sell that property to an investor for a fraction of the property's value. In the morning, without notice, our retiree would find themselves homeless and penniless—without any hearing before an Article III judge and without any order issuing from an Article III court.

CONCLUSION

The Bankruptcy Court's order should be reversed.

PRAYER

Appellants pray that the Court reverse the bankruptcy court's Order. In the alternative, Appellants pray that this appeal be considered as an application for writ of mandamus to order the Bankruptcy Court to vacate its order, which exceeded the Bankruptcy Court's statutory grant of authority. In the alternative Appellants pray for remand to determine ownership of the asset, and to compensate Appellants for their ownership interest.

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CERTIFICATE OF SERVICE

This is to certify that this brief was served this day on all parties who receive notification through the Court's electronic filing system.

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