**IN THE UNITED STATES DISTRICT COURT**
**FOR THE DISTRICT OF DELAWARE**

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| In re HECHINGER INVESTMENT COMPANY OF DELAWARE, et al.,<br><br>Debtors. | Chapter 11<br>Case Nos. 99-2261-PJW to 99-2283<br>(Jointly Administered) |
| THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF HECHINGER INVESTMENT COMPANY OF DELAWARE, et al., on behalf of HECHINGER INVESTMENT COMPANY OF DELAWARE, et al.,<br><br>Plaintiffs,<br><br>v.<br><br>FLEET RETAIL FINANCE GROUP, et al.,<br><br>Defendants. | Civil Action No. 00-840-RRM |

**MEMORANDUM IN SUPPORT OF MOTION TO DISMISS**
**OF DEFENDANTS CATHERINE S. ENGLAND,**
**RICHARD ENGLAND, JR., AND LOIS ASSOCIATES L.P.**

## TABLE OF CONTENTS

**Page**


INTRODUCTION . . . . . . . . . . 1

STATEMENT OF FACTS . . . . . . . . . . 2

ARGUMENT . . . . . . . . . . 5

A. Count II Should Be Dismissed Because The England Family Defendants Did Not Owe Anyone Fiduciary Duties. . . . . . . . . . . 6

B. Counts VI and VII Should Be Dismissed Because the Payments to the England Family Defendants Were "Settlement Payments" Within Code Section 546(e) and Thus Are Exempt from the Avoidance Provisions of Section 544. . . . . . . . . . . 8

C. Count III Should Be Dismissed Because It Merely Restates the Failed Fraudulent Transfer Claims and Is In Any Event Preempted by the Bankruptcy Code. . . . . . . . . . . 9

1. Plaintiff's Unjust Enrichment Claim Is Nothing More Than a Section 544 Avoidance Claim Barred by Section 546(e). . . . . . . . . . . 10

2. Plaintiff's Unjust Enrichment Claim Is Preempted by the Bankruptcy Code. . . . . . . . . . . 13

D. The Defendant-Banks' Cross-Claims Should Be Dismissed Because There Is No Right To Contribution Or Indemnification For Allegedly Fraudulent Transfers. . . . . . . . . . . 17

CONCLUSION . . . . . . . . . . 18

## TABLE OF AUTHORITIES

**Page**

**Cases**

*Abercrombie v. Davis*, 130 A.2d 338 (Del. Ch. 1957) . . . . . . . . . . . . . . . . . . . . . . . . . . 14, 15, 16

*Askanase* v. *Fatjo*, 148 F.R.D. 570 (S.D.Tx. 1993) . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . 17

*Bessette* v. *Avco Financial Services, Inc.*, 230 F.3d 439 (1st Cir. 2000) . . . . . . . . . . . . . . . . 14-16

*Caplin* v. *Marine Midland Grace Trust Co. of New York*, 406 U.S. 416 (1972) . . . . . . . . . . . . . 12

*Cipollone* v. *Liggett Group, Inc.*, 505 U.S. 504 (1992) . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . 13

*Cox* v. *Zale Delaware, Inc.*, 239 F.3d 910 (7th Cir. 2001) . . . . . . . . . . . . . . . . . . . . . . . . . 14-16

*Foye* v. *New York University*, 269 A.2d 63 (Del. 1970) . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . 7

*Gilbert* v. *El Paso Co.*, 490 A.2d 1050 (Del. Ch. 1984) . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . 6

*Harris v. Carter*, 582 A.2d 222 (Del. Ch. 1990) . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . 6

*In re Bassett*, 2000 WL 1800213 (9th Cir. B.A.P. Nov. 17, 2000) . . . . . . . . . . . . . . . . . . . . . . 14

*In re Colonial Realty Co.*, 980 F.2d 125 (2d Cir. 1992) . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . 16

*In re John Peterson Motors, Inc.*, 56 B.R. 588 (Bankr. D. Minn. 1986) . . . . . . . . . . . . . . . . . . . 17

*In re Knox*, 237 B.R. 687 (N.D. Ill. 1999) . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . 14, 15

*In re Mortgageamerica Corp.*, 714 F.2d 1266 (5th Cir. 1983) . . . . . . . . . . . . . . . . . . . . . . . . . . 16

*In re Resorts International, Inc.*, 181 F.3d 505 (3d Cir. 1999) . . . . . . . . . . . . . . . . . . . . 9-12, 16

*In re Sea-Land Corp. Shareholders Litig.*, 1987 WL 11283 (Del. Ch. May 22, 1987) . . . . . . . 7, 8

*In re Walker, 51 F.3d 562* (5th Cir. 1995) . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . 17

*International Shoe Co.* v. *Pinkus*, 278 U.S. 261 (1929) . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . 14

*Ivanhoe Partners* v. *Newmont Mining Corp.*, 535 A.2d 1334 (Del. 1987) . . . . . . . . . . . . . . . . . 8

*Kaplan* v. *Centex Corp.*, 123 A.2d 119 (Del. Ch. 1971) . . . . . 8

*Koch Refining* v. *Farmers Union Central Exchange, Inc.*, 831 F.2d 1339 (7th Cir. 1987) . . . . . 12

*LaSalle Nat'l Bank* v. *Perelman*, 82 F. Supp. 2d 279 (D. Del. 2000) . . . . . 6

*Lenior* v. *GE Capital Corp.*, 231 B.R. 662 (N.D. Ill. 1999) . . . . . 14

*MSR Exploration, Ltd.* v. *Meridian Oil, Inc.*, 74 F.3d 910 (9th Cir. 1996) . . . . . 13, 14

*Orson, Inc.* v. *Miramax Film Corp.*, 189 F.3d 377 (3rd Cir. 1999) . . . . . 13, 16

*Penn Terra Ltd.* v. *Dep't of Environmental Resources*, 733 F.2d 267 (3d Cir. 1984) . . . . . 11

*Pension Benefit Guaranty Corp.* v. *White Consolidated Indus.*, 998 F.2d 1192 (3d Cir. 1993) . . . . . 3

*Pereira* v. *Chapman*, 92 B.R. 903 (C.D. Cal. 1988) . . . . . 13-15

*Pertuso* v. *Ford Motor Co.*, 233 F.3d 417 (6th Cir. 2000) . . . . . 14

*United States* v. *Nappi*, 243 F.3d 758 (3d Cir. 2001) . . . . . 11

*Weibolt Stores, Inc.* v. *Schottenstein*, 111 B.R. 162 (N.D. Ill. 1990) . . . . . 17

*Winitz* v. *Kline*, 288 A.2d 456 (Del. Ch. 1971) . . . . . 7


**Statutes**


11 U.S.C. § 524 . . . . . 7

11 U.S.C. § 544 . . . . . 17

11 U.S.C. § 546(a) . . . . . 14-16

11 U.S.C. § 546(e) . . . . . 12

U.S. CONST. art. I, § 8, cl. 4 . . . . . 13

U.S. CONST. art. VI, § 2 . . . . . 14-16

## INTRODUCTION

Catherine S. England, Richard England, Jr. and Lois Associates L.P. collectively the "England Family Defendants"), are defendants by afterthought. In their original complaint (filed in November 2000), plaintiff, the Official Committee of Unsecured Creditors of the Hechinger Investment Company and its affiliated debtors, sued defendants Fleet Retail Finance Group, the Chase Manhattan Bank, and Back Bay Capital Funding, which helped finance the transactions that plaintiff seeks to have avoided. In their amended complaint (filed in April 2001), plaintiff added – along with the England Family Defendants – Leonard Green & Partners and Green Equity Investors, which ultimately acquired Hechinger in the transactions, and defendants John W. Hechinger; John W. Hechinger, Jr.; S. Ross Hechinger; Ann D. Jordan; Robert S. Parker; Melvin A. Wilmore; Alan J. Zakon; Kenneth J. Cort; W. Clark McClelland; June R. Hechinger; Nancy Hechinger Lowe; and Sally Hechinger Rudoy, almost all of whom were either directors of the debtor, or officers, or both.

The England Family Defendants, in contrast, were none of the above. In fact, they were so tangentially involved in the transactions at issue in this lawsuit that they may as well have learned about them from reading the *Washington Post.* Long before the transaction ever took place, the England Family Defendants, though shareholders of Hechinger Company, had relinquished their voting rights in their stock. Because they were neither directors, nor officers, nor controlling – or even voting – shareholders, the England Family Defendants owed no one any fiduciary duties, and plaintiff's claim for breach of fiduciary duties therefore fails as a matter of law. Plaintiff's other claims, for fraudulent transfer and unjust enrichment, are contrary to the terms of the Bankruptcy Code and controlling Third Circuit authority and, accordingly, fail as a matter of law as well. So, finally, do the cross-claims brought by defendants Fleet and Back Bay for indemnification or

contribution. The England Family Defendants should not have been haled into this lawsuit to begin with. This memorandum explains why they should be let out.

## STATEMENT OF FACTS

This case arises from a series of transactions involving the sale of the Hechinger Company, which owned and operated home improvement stores located mostly in the Northeast and mid-Atlantic. According to the allegations in the complaint (which we assume to be true for the purposes of this motion only), competition from other home improvement chains resulted, by the mid-1990s, in a steady decline in the company's performance. Am. Compl. ¶¶ 58-60. In 1997, the company retained the investment firm of Donaldson, Lufkin & Jenrette (DLJ) to shop around for a buyer. *Id.* ¶ 61. Defendant Leonard Green then decided to buy Hechinger and merge it with Builders Square, a competitor. Shareholders in the Hechinger Company, including the England Family Defendants, were ultimately paid $2.375 per share for their holdings. *Id.* ¶ 68. Plaintiff alleges that the payments to Hechinger's shareholders totaled "at least" $127 million. *Id.* ¶¶ 80, 82, 93(G). For their part, the England Family Defendants together received approximately $4.7 million – less than 4% of that total.

Despite the fact that DLJ rendered a fairness opinion to the Hechinger board of directors, advising the board that the Leonard Green offer was fair to Hechinger Company and its stockholders (*id.*), plaintiff now alleges that the transaction was a fraud. According to plaintiff, Hechinger Company was insolvent, *id.* ¶ 69-71 – and the transactions increased the company's secured debt, supposedly harming the company's unsecured creditors. *Id.* ¶ 82. After the deal finally closed, in September 1997, the fortunes of the combined Hechinger and Builders Square declined. On June 11, 1999, nearly two years after the transactions at issue, Hechinger Company and various affiliates

filed a petition for bankruptcy under Chapter 11 of the Bankruptcy Code. Plaintiff filed this lawsuit in November 2000, seeking to have the grant of various liens to the bank defendants in connection with the transactions avoided. Plaintiff amended its complaint in April 2001, for the first time asserting claims against the England Family Defendants (claims that were lumped together with claims against the other individual defendants): a claim for breach of fiduciary duty (*id.* ¶¶ 103-11); two claims for fraudulent transfer (*id.* ¶¶ 136-45); and a claim for unjust enrichment (*id.* ¶¶ 112-15).

All of the allegations summarized above are set out in detail in plaintiff's amended complaint. Not set out as precisely, however, are pivotal facts concerning the role – lack of role, that is – in the transaction of the England Family Defendants. To begin with, plaintiff refers repeatedly to the "Hechinger Family Defendants" (*e.g.*, *id.* ¶ 2), but no such collective entity exists. It is true that the three England siblings – Catherine, Richard, and Joan England Akman, the general partners of Lois Associates – are related to members of the Hechinger family. But, as the complaint discloses (albeit inadvertently), the England Family Defendants – almost alone among the putative "Hechinger Family Defendants" – were neither directors nor officers of the company. See Form 14-A Proxy Statement, Sep. 5, 1997 at 63 (listing officers and directors) (relevant portions of which are attached hereto as Exhibit A).[1] And while the England Family Defendants did own stock in the Hechinger Company, they did not, either alone or collectively, own even close to a *majority* of voting stock in the Company: at the time of the vote approving the transactions, the England Family Defendants collectively owned less than one percent of the Class A stock and 14.7% of the Class B stock. See Exhibit A at 61-62.

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[1] In addressing a motion to dismiss, a court may rely both on documents cited in a complaint and on documents that are publicly filed. See, *e.g.*, *Pension Benefit Guaranty Corp.* v. *White Consolidated Indus.*, 998 F.2d 1192, 1196 (3d Cir. 1993).

Faced with these facts, the amended complaint suggests that the England Family Defendants should be treated similarly to the other individual defendants because, according to plaintiff, the monolithic "Hechinger Family Defendants" "controlled the voting stock of certain of the Debtors prior to September 27, 1997" (when the transaction finally closed), *id.* Specifically, plaintiff alleges that the "Hechinger Family Defendants," "by and through a Stockholders Agreement, controlled the voting on all matters to which Hechinger's shareholders voted prior to the Transaction"; and each of the "Hechinger Family Defendants" "agreed to vote their shares in one block in all significant matters, including, without limitation, the vote with respect to the Transaction." Am. Compl. ¶ 107.

But, as to the England Family Defendants, that conclusory allegation is flatly contrary to the terms of the Stockholders Agreement. That agreement, which plaintiff itself cites, was entered into pursuant to a voting trust created in 1989 and still in effect in September 1997. See Exhibit A at C-1, C-7; Form 14-A Proxy Statement, Oct. 20, 1989 at C-1 (attached hereto as Exhibit B). Rather than giving the England Family Defendants actual control over the Hechinger Company, the voting trust *deprived the England Family Defendants of any possible control over Hechinger.*

Under the voting trust, the England Family Defendants (as well as other members of the Hechinger family) gave three individuals, John W. Hechinger, John W. Hechinger, Jr., and S. Ross Hechinger (called the "Voters") – an irrevocable right, for ten years, to vote the England Family Defendants' shares in the Voters' "sole discretion," subject to an exception not relevant here (concerning the election of England family designees to the Board of Directors).[2] As a consequence

[2] The voting trust states, in relevant part: "Each member of the England Family Group * * * grants to the Voters an irrevocable proxy * * * coupled with an interest, to vote such person's Subject Shares as the Voters shall in their sole discretion determine, subject only to [certain limitations relating to the election of England family designees to the Board of Directors], for the election of directors and all other matters which may be presented at any meeting or require the

of this voting trust, John W. Hechinger, John W. Hechinger, Jr., and S. Ross Hechinger exercised *total discretion* over the decision how to cast the England Family Defendants' votes. The Voters had no obligation to consult with the England Family Defendants before voting their shares, or to follow the England Family Defendants' direction or advice – should they have given any, which plaintiff do not allege they ever did. By entering into the voting trust, then, the England Family Defendants relinquished any and all control over management of the Hechinger company – including any decision whether to approve or reject the transactions challenged in this lawsuit. The England Family Defendants, in sum, were not officers, were not directors, and were not controlling shareholders of the Hechinger Company, and they should not be defendants in this lawsuit. As we explain, governing law requires that the claims against them be dismissed.

## ARGUMENT

Even assuming the truth of the allegations in the amended complaint, plaintiff has failed to state any claims against the England Family Defendants as to which relief can be granted. *First*, the England Family Defendants owed no pertinent fiduciary duties and thus could not have breached any such duties (Count II). *Second*, controlling Third Circuit precedent makes clear that the payments to the England Family Defendants (and other individuals) were "settlement payments" within the meaning of Section 546(e) of the Bankruptcy Code and thus exempted from the Code provision that might otherwise allow an allegedly "fraudulent" transaction to be avoided (Counts VI and VII). *Third*, plaintiff's state-law claim for unjust enrichment is simply a repackaging of their fraudulent transfer claims is thus similarly barred by controlling law and, in any event, is preempted by the Bankruptcy Code (Count III).

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consent of stockholders of the Company." Exhibit B at C-4.

**A. Count II Should Be Dismissed Because The England Family Defendants Did Not Owe Anyone Fiduciary Duties.**

In Count II of their amended complaint, plaintiff alleges that the England Family Defendants breached fiduciary duties supposedly owed to both the corporation itself and to its creditors. Plaintiff's claim fails as a matter of law. With respect to the Hechinger Company, none of the England Family Defendants owed fiduciary duties to anyone.

Under Delaware law, which governs plaintiff's claim (*e.g.*, *LaSalle Nat'l Bank* v. *Perelman*, 82 F. Supp. 2d 279, 289 (D. Del. 2000) (law of state of incorporation governs action "concern[ing] conduct of officers, directors and controlling shareholders")), fiduciary duties are owed *only* by directors, officers, or controlling shareholders. See *Harris v. Carter*, 582 A.2d 222, 234 (Del. Ch. 1990). Plaintiff does not allege that any of the England Family Defendants was a director or officer of Hechinger at the time of the transaction, and none was. See Exhibit A at 63 (listing officers and directors). Nor does plaintiff allege that any of the England Family Defendants owned a majority of the company stock or controlled a majority of votes, and none did. See Exhibit A at 61-62 (showing percentage of stock owned by the England Family Defendants). "Generally, a shareholder who owns less than 50% of a corporation's outstanding stock does not, without more, become a controlling shareholder of that corporation, with a concomitant fiduciary status." *Gilbert* v. *El Paso Co.*, 490 A.2d 1050, 1055 (Del. Ch. 1984).

Plaintiff does assert that a voting bloc they call the "Hechinger Family Shareholders" controlled the Hechinger Company. As we have explained, however, no such monolith existed. Rather, the England Family Defendants, through a voting trust, gave up any and all control that they had over the direction of the Company's affairs. As is the case with all voting trusts established

under Delaware law, this voting trust divorced the England Family Defendants' ability to control the direction of the corporation – through the exercise of their voting rights – from their beneficial ownership of Hechinger stock. "A 'beneficiary' of a voting trust * * * is the stockholder concerned with, and *relieved of, the vote and control of the corporation* for purposes that seemed good and sufficient to him when he entered into the voting trust agreement." *Foye* v. *New York University*, 269 A.2d 63, 69 (Del. 1970) (emphasis added); see also *Winitz* v. *Kline*, 288 A.2d 456, 459 (Del. Ch. 1971) ("A stockholder who deposits his stock in a voting trust parts with his voting rights but retains 'beneficial' ownership."); *Abercrombie v. Davis*, 130 A.2d 338, 344 (Del. Ch. 1957) ("[O]ne essential feature that characterizes a voting trust is the separation of voting rights of the stock from other attributes of the stock."). When a voting trust is created, then, the control of a corporation is transferred from the stockholders to those who exercise the power conferred by the trust – here, from the England Family Defendants and the Voters under the trust.

Because the England Family Defendants irrevocably ceded their ability to influence (not to mention control) the Hechinger Company, they were not controlling shareholders with any concomitant fiduciary obligations. It is no answer to say that, by entering into the voting trust a full eight years prior to the transactions at issue, the England Family Defendants helped ensure that a majority of shares were voted together. Rather, the dispositive question is *whether, in 1997, at the time of the relevant events, the England Family Defendants exercised actual control* over the corporation. "A stockholder is not deemed controlling unless it owns a majority of the stock, or has exercised actual domination and control in directing the corporation's business affairs." *In re Sea-Land Corp. Shareholders Litig.*, 1987 WL 11283, at *4 (Del. Ch. May 22, 1987) (citations omitted) (holding that entity owning 40% of corporation's stock was not a controlling shareholder); see also

*Ivanhoe Partners* v. *Newmont Mining Corp.*, 535 A.2d 1334, 1344 (Del. 1987) ("Under Delaware law a shareholder owes a fiduciary duty only if it owns a majority interest in or exercises control over the business affairs of the corporation."). In *Sea Land*, for example, plaintiffs argued that the defendant, who owned 40% of the subject corporation's stock and had the right to name three of its directors, was for those reasons a controlling shareholder. Granting defendant's motion to dismiss, the court held that the complaint "does not establish actual domination or control." 1987 WL 11283, at *4; see also *Kaplan* v. *Centex Corp.*, 123 A.2d 119, 123 (Del. Ch. 1971) (fact that two defendant corporations had representatives on the subject corporation's board did not demonstrate that defendant corporations "dominated or controlled" the subject corporation). The simple fact is that the England Family Defendants gave away what ability they may have once had to influence the affairs of Hechinger *eight years before* the transaction being challenged here. The England Family Defendants were not controlling shareholders, and they owed no one fiduciary duties.[3] Plaintiff's claim for breach of fiduciary duty should therefore be dismissed.

**B. Counts VI and VII Should Be Dismissed Because the Payments to the England Family Defendants Were "Settlement Payments" Within Code Section 546(e) and Thus Are Exempt from the Avoidance Provisions of Section 544.**

In Counts VI and VII of their amended complaint, plaintiff seek to avoid the transaction – in particular, the payments to the England Family Defendants for their Hechinger shares – as a fraudulent transfer. As explained more fully in the memorandum in support of the Memorandum of Law in Support of Motion to Dismiss Plaintiff's First, Second, Third, Sixth and Seventh Claims

[3] In the event that the court rejects this argument, and concludes that the England Family Defendants should be treated as controlling shareholders, we adopt the arguments set forth in the Memorandum of Law in Support of Motion to Dismiss Plaintiff's First, Second, Third, Sixth and Seventh Claims for Relief Against Certain Former Directors and Shareholders at Section II.

for Relief Against Certain Former Directors and Shareholders ("Memorandum of Certain Former Directors, et al.") at Section I, which we adopt and incorporate by reference, plaintiff have failed to state claims as a matter of law. In brief: Section 544 of the Code, 11 U.S.C. § 544, allows a trustee in bankruptcy to avoid certain transfers of property. (Here, plaintiff are acting in the trustee's stead.) At the same time, however, Section 546(e) of the Code, 11 U.S.C. § 546(e), exempts from Section 544 any "settlement payment * * * made by or to a commodity broker, forward contract merchant, stockbroker, financial institution, or securities clearing agency, that is made before the commencement of the case." In *In re Resorts International, Inc.*, 181 F.3d 505 (3d Cir. 1999), the Third Circuit held that a payment of precisely the type made to the England Family Defendants was a "settlement payment" within the meaning of Section 546(e). Plaintiff thus cannot avoid the payment, and its claims for fraudulent transfer should be dismissed.

**C. Count III Should Be Dismissed Because It Merely Restates the Failed Fraudulent Transfer Claims and Is In Any Event Preempted by the Bankruptcy Code.**

In Count III of the amended complaint, plaintiff contends that the England Family Defendants were unjustly enriched. This claim fails for two independent reasons. First, the claim should be viewed for what it really is – an avoidance claim under Section 544 that, just like the fraudulent transfer claims under that same section, is precluded by Section 546(e) and controlling precedent. Second, as numerous courts have held, the Bankruptcy Code preempts the state law of unjust enrichment where, as here, the Code addresses the very conduct at issue and, indeed, bars the very relief plaintiff seeks.

### 1. Plaintiff's Unjust Enrichment Claim Is Nothing More Than a Section 544 Avoidance Claim Barred by Section 546(e).

As discussed above, plaintiff's efforts to avoid and recover the settlement payments to the England Family Defendants as a fraudulent transfer fails as a matter of law. See 11 U.S.C. § 546(e); *In re Resorts International, Inc.*, 181 F.3d at 514-16. In an attempt to avoid dismissal, plaintiff tries to recast its claims of fraudulent transfer as an action for unjust enrichment under state law. Notwithstanding the change in terminology, however, the claims are the same.

Plaintiff itself asserts that all of their "causes of action arise out of an integrated financial transaction." Am. Compl. ¶ 2. It premises Count III on assertions that the England Family Defendants were unjustly enriched "[t]hrough the wrongful receipt of the proceeds of the Hechinger LBO." Am. Compl. ¶ 113. Although plaintiff never clarifies why the payments were supposedly unjust, the only grounds in the amended complaint that conceivably support the averment are plaintiff's allegations that Hechinger Company was (or was rendered) insolvent and that the transaction enriched shareholders at the creditors' expense. See, *e.g.*, *id*. ¶¶ 2, 4-5, 81-83, 94. And they seek the return of "the payments [defendants] received in connection with the Hechinger LBO." Id. ¶ 115.

These allegations and the relief sought are indistinguishable from the allegations and relief sought in plaintiff's fraudulent transfer claims. See Am. Compl. ¶¶ 137-140, 142-45. In the fraudulent transfer claims, plaintiff again allege that Hechinger was insolvent and that the Transaction defrauded creditors. *Id.* 1¶¶ 136-39, 141-44. And plaintiff seeks exactly the same relief: the "Shareholder Payments," which they assert they are entitled to "avoid and recover." *Id.* ¶¶ 140,

145. In fact, plaintiff incorporates the very same allegations of unjust enrichment into its fraudulent transfer claims. *Id.* ¶¶ 136, 141.

It is obvious, then, that these supposedly distinct claims are really the same; indeed, plaintiff effectively admits as much at the very outset of the amended complaint, Am. Compl. ¶ 1 (stating that "[t]his is an action to recover fraudulent transfers," and nowhere mentioning any supposedly separate claim for unjust enrichment). And, in summarizing the relief it seeks, plaintiff candidly admits that their unjust enrichment and fraudulent transfer claims seek the same remedy, *id.* ¶ 5 (to "avoid and recover for the benefit of the estates the amounts paid to the Hechinger Family Defendants * * * in connection with the Hechinger LBO.").

Plaintiff cannot circumvent Section 546(e) merely by relabeling its fraudulent transfer claims as a claim for unjust enrichment. As the Third Circuit noted with respect to another section of the Bankruptcy Code, "the legislative intent behind subsection 362(b)(5) should not be defeated by artful pleading that depends on form rather than substance." *Penn Terra Ltd.* v. *Dep't of Environmental Resources*, 733 F.2d 267, 275 (3d Cir. 1984); see also *United States* v. *Nappi*, 243 F.3d 758, 767 (3d Cir. 2001) (declining "to elevate form over substance").

Moreover, the only conceivable statutory basis for plaintiff's standing to assert its purported unjust enrichment claim is Section 544 – the very same section of the Code plaintiff rely on for their fraudulent transfer claims. Yet, Section 546(e) and *Resorts International* provide the England Family Defendants with a complete defense to a claim under Section 544. In bankruptcy, normally the debtor-in-possession or the trustee, not a creditor's committee, has standing to bring suit on behalf of the estate. Plaintiff states that it is bringing this action "pursuant to the authority granted to it" under a stipulation and bankruptcy court order entered in March 2001. Am. Compl. ¶ 9. But,

by its terms and in accordance with applicable law, that stipulation and order authorized plaintiff to bring only claims relating to the Transaction "which could have been brought by the Debtors themselves."[4] Thus, plaintiff may bring only claims that the Debtors, in the first instance, could have brought. As a general rule, debtors (or trustees) in bankruptcy proceedings lack standing to assert claims on behalf of their creditors. See, *e.g.*, *Caplin* v. *Marine Midland Grace Trust Co. of New York*, 406 U.S. 416 (1972). To be sure, Congress has created an exception to this general rule in Section 544, permitting a debtor-in-possession (or trustee), under certain circumstances, to avoid some transfers that a creditor could avoid outside of bankruptcy. 11 U.S.C. § 544; see also *Koch Refining* v. *Farmers Union Central Exchange, Inc.*, 831 F.2d 1339, 1348 (7th Cir. 1987) (a trustee or debtor-in-possession "has creditor status *under section 544* to bring suits for the benefit of the estate and ultimately of the creditors") (emphasis added). But Congress has also expressly decided that Section 544 may *not* be used "to avoid an transfer that is * * * a settlement payment." 11 U.S.C. § 546(e).

Thus, either the unjust enrichment claim is a Section 544 avoidance action in disguise, in which case it is barred by Section 546(e) and *Resorts International*, or it is not a Section 544 avoidance action (notwithstanding all of the similarities between it and plaintiff's fraudulent transfer claims), in which case plaintiff lacks standing to bring it. In either event, the claim fails as a matter of law.

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[4] See Stipulation, Agreement and Order Between the Debtors and the Committee Authorizing the Committee to Investigate, Commence and Prosecute Claims, ¶ 1 ((Mar. 30, 2001), *In re Hechinger Investment Co. of Delaware, Inc.*, Bankr. Case No. 99-2261 (PJW). Plaintiff also cites a separate stipulation and order entered by the bankruptcy court in 1999, but that stipulation and order addressed plaintiff's authority to investigate potential claims only against Hechinger's lenders, not against the England Family Defendants.

### 2. Plaintiff's Unjust Enrichment Claim Is Preempted by the Bankruptcy Code.

Under the Supremacy Clause of the United States Constitution, U.S. CONST. art. VI, § 2, state laws that interfere with or are contrary to federal law are "preempted" and "without effect." *Cipollone* v. *Liggett Group, Inc.*, 505 U.S. 504, 516 (1992). Federal law may preempt state law either expressly or impliedly – the latter, either by occupying the field, or because state and federal law conflict. See, *e.g.*, *Orson, Inc.* v. *Miramax Film Corp.*, 189 F.3d 377, 381-82 (3rd Cir. 1999). Under "field preemption," federal law displaces state law when "'federal law so thoroughly occupies a legislative field as to make reasonable the inference that Congress left no room for the States to supplement it.'" *Id.* at 381 (quoting *Cipollone*, 505 U.S. at 516). Under "conflict preemption," federal law displaces state law when "it is impossible to comply with both the state and federal law * * * or when the state law 'stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.'" *Id.* at 381-82 (citations omitted). Here, both field and conflict preemption bar plaintiff's claim for unjust enrichment.

At issue in this case is plaintiff's effort to supplement the claims and remedies provided by the Bankruptcy Code for the possible avoidance of payments and other transfers with state law claims and remedies. But "a mere browse through the complex, detailed, and comprehensive provisions of the lengthy Bankruptcy Code * * * demonstrates Congress's intent to create a whole system under federal control which is designed to bring together and adjust all of the rights and duties of creditors and embarrassed debtors alike." *MSR Exploration, Ltd.* v. *Meridian Oil, Inc.*, 74 F.3d 910, 914 (9th Cir. 1996) (citations omitted). The Code "reflects a balance, completeness and structural integrity that suggests remedial exclusivity," *Pereira* v. *Chapman*, 92 B.R. 903, 908 (C.D. Cal. 1988) (internal quotation marks omitted), and indeed, the "adjustment of rights and duties"

within it are "uniquely and exclusively federal," *MSR Exploration*, 74 F.3d at 914. Not surprisingly, therefore, the Supreme Court concluded long ago that "[s]tates may not pass or enforce laws to interfere with or complement the Bankruptcy Act or to provide additional or auxiliary regulations." *International Shoe Co.* v. *Pinkus*, 278 U.S. 261, 265 (1929); see also U.S. CONST. art. I, § 8, cl. 4 ("The Congress shall have Power * * * to establish * * * Laws on the subject of Bankruptcies throughout the United States.").

For these reasons, the courts – including three federal courts of appeal in the last year alone – have repeatedly concluded that Congress intended to preempt state law claims of unjust enrichment when such claims are interjected into the bankruptcy context. See *Cox* v. *Zale Delaware, Inc.*, 239 F.3d 910 (7th Cir. 2001); *Pertuso* v. *Ford Motor Co.*, 233 F.3d 417 (6th Cir. 2000); *Bessette* v. *Avco Financial Services, Inc.*, 230 F.3d 439 (1st Cir. 2000); see also *In re Bassett*, 2000 WL 1800213 at ** 10-11 ((9th Cir. B.A.P. Nov. 17, 2000); *In re Knox*, 237 B.R. 687 (N.D. Ill. 1999); *Lenior* v. *GE Capital Corp.*, 231 B.R. 662, 675 (N.D. Ill. 1999); *Pereira* v. *First North American Nat'l Bank*, 223 B.R. 28 (N.D. Ga. 1998). Significantly, in each of these cases the plaintiffs alleged misconduct that violated the Code itself; in *Cox*, *Pertuso*, and *Bessette*, for example, the plaintiffs were former debtors in bankruptcy who claimed that the defendant-creditors had failed to file with the applicable bankruptcy court so-called reaffirmation agreements (agreements under which a debtor reaffirms his or her liability on an otherwise discharged debt) and had nonetheless sought to collect the debts that were the subject of those unenforceable agreements, in direct contravention of Section 524 of the Code, 11 U.S.C. § 524. See *Cox*, 239 F.3d at 912; *Pertuso*, 233 F.3d at 428; *Bessette*, 230 F.3d at 442-43. There was thus no basis to suggest conflict preemption; state law was not seeking to prohibit actions that federal law permitted. On the contrary, the state law of unjust enrichment would

have simply supplemented the remedies provided under the Code itself for conduct that Congress had agreed was improper. See *Bessette*, 230 F.3d at 447; *Pertuso*, 233 F.3d at 426.

Nonetheless, relying only on grounds of field preemption, the courts held that "Congress's intent in enacting the remedial provisions of the Bankruptcy Code leaves no room for the state cause of action." *Bessette*, 230 F.3d at 447 (citations and quotation marks omitted) (citing cases); see also *Pertuso*, 233 F.3d at 426 ("Congress has preempted the field."); *Cox*, 239 F.3d at 913 (the remedies for such conduct "are a matter exclusively of federal bankruptcy law"). Indeed, it was Congress's provision for, or circumscription of, a remedy in the Code to address the allegedly wrongful conduct that led the courts to conclude that Congress intended to preempt the state law of unjust enrichment. See, *e.g.*, *Bessette*, 230 F.3d at 447-48; *Pereira*, 223 B.R. at 31-32; see also *In re Knox*, 237 B.R. at 702 (the preempted unjust enrichment claim sought a remedy "for which the Code itself * * * provide[s] other remedies").

In this case, too, Congress has occupied the field. Plaintiff claims that the England Family Defendants were unjustly enriched when they received cash for their stock in Hechinger and they seek, through their unjust enrichment claim, to recover those payments. The Bankruptcy Code addresses such allegations and provides a remedy, just as it addresses the requirements for an enforceable reaffirmation agreement and the consequences of a creditor's failure to satisfy those requirements. In Section 544, it allows a debtor to avoid, under certain circumstances, payments that would be avoidable outside of bankruptcy by a creditor under state law. But the Code explicitly limits and displaces state law in several ways. First, it specifies its own statute of limitations for the assertion of any such claim. 11 U.S.C. § 546(a). Second, the Code provides that only a debtor-in-possession or trustee (or a creditors committee granted authority by order) may bring such

a claim in bankruptcy, stripping individual creditors of the right to file suit as they could outside bankruptcy under state law. *E.g., In re Mortgageamerica Corp.*, 714 F.2d 1266 (5th Cir. 1983); *In re Colonial Realty Co.*, 980 F.2d 125 (2d Cir. 1992). Finally, and critically for present purposes, the Code sets specific federal limits on the use of state law avoidance powers under Section 544, expressly providing (among other limitations) that a settlement payment may not be avoided in bankruptcy. 11 U.S.C. § 546(e). In short, by occupying the field and providing – and circumscribing – the remedies for the conduct alleged, Congress necessarily intended to displace inconsistent state law claims and remedies. Indeed, the grounds for preemption of the state law of unjust enrichment are stronger here than they were in the *Cox/Pertuso/Bessette* line of cases. In this case, unlike the others, "state law is in *direct conflict* with the federal law to an extent that the [laws] cannot coexist." *Bessette*, 230 F.3d at 447 (citations and quotation marks omitted). In Section 546(e), Congress expressly excepted the transfers at issue in this case – settlement payments – from avoidance. See *In re Resorts Int'l*, 181 F.3d at 516.

Plaintiff's state law claim of unjust enrichment would directly undermine Section 546(e). It would allow plaintiff to do exactly what Congress enacted Section 546(e) to prevent: the avoidance and recovery of a settlement payment made more than one year before the debtor filed for bankruptcy. This state law may not do. Plaintiff's state law claim of unjust enrichment "'stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.'" *Orson*, 189 F.3d at 381-82 (citations omitted). It is, accordingly, preempted. Plaintiff's unjust enrichment claim must be dismissed.[5]

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[5] Plaintiff's unjust enrichment claim should also be dismissed for the reasons set forth in the Memorandum of Certain Directors, et al., Section III.

**D. The Defendant-Banks' Cross-Claims Should Be Dismissed Because There Is No Right To Contribution Or Indemnification For Allegedly Fraudulent Transfers.**

In its amended complaint, plaintiff asserted claims against Back Bay Capital Funding LLC and Fleet Retail Finance Inc. for allegedly fraudulent transfers. Both banks deny any liability but in identical cross-claims purport to assert causes of action for contribution and indemnification against the England Family Defendants "in the unlikely event that [the Banks have] any liability." Back Bay Cross-Claims at ¶¶ 4, 6; Fleet Cross-Claims at ¶¶ 4, 6. Neither of the Banks provides any factual allegations or legal basis to support its cross-claims. In fact, the grounds for the claims are so indiscernible that they fail to satisfy even the liberal pleading requirements of the Federal Rules of Civil Procedure and should be dismissed for that reason alone. See *Askanase* v. *Fatjo*, 148 F.R.D. 570, 574 (S.D.Tx. 1993) ("the cross-claims contain no indication of the exact theory of indemnity or contribution or of the controlling state law upon which cross-claimants rely") (citing cases).

The Banks' cross-claims also fail as a matter of substantive law. It is well established that the Bankruptcy Code provides no right to contribution or indemnity. See, *e.g.*, *In re Walker*, 51 F.3d 562, 565-67 (5th Cir. 1995) (no express or implied right to contribution under the Bankruptcy Code); *In re John Peterson Motors, Inc.*, 56 B.R. 588, 591 n.5 (Bankr. D. Minn. 1986) ("There is simply nothing in Title 11 to suggest that Congress expressly or implicitly intended to create a right to contribution or indemnity"). Moreover, the courts have refused to infer such causes of action under federal common law. See *In re Walker*, 51 F.3d at 567; *In re John Peterson Motors*, 56 B.R. at 591 n.5.

The Bankruptcy Code aside, there is no basis for the cross-claims under state law either. See, *e.g.*, *Weibolt Stores, Inc.* v. *Schottenstein*, 111 B.R. 162, 173 (N.D. Ill. 1990) ("neither federal nor

state law provides a basis for the third-party plaintiffs' contribution claims"). In fact, our research has not turned up a single case in California, Delaware, Maryland, Michigan or Texas, which the Committee asserts govern its fraudulent transfer claims (see Am. Compl. ¶¶ 176, 186), that granted contribution or indemnification with respect to an alleged fraudulent transfer.

In sum: the Banks' cross-claims are procedurally deficient and should be dismissed for failing to provide even the barest notice of the factual or legal grounds supporting them. The Banks have also failed to state a claim under any conceivably applicable legal theory. Accordingly, the cross-claims should be dismissed.

## CONCLUSION

The claims and cross-claims against the England Family Defendants should be dismissed with prejudice.

Dated: July 16, 2001

Respectfully submitted,

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Lawrence S. Robbins
Arnon D. Siegel
Kathryn S. Zecca
ROBBINS, RUSSELL, ENGLERT,
ORSECK & UNTEREINER LLP
1801 K Street, N.W.
Suite 411
Washington, D.C. 20006
(202) 775-4500

Philip D. Anker
Joshua R. Stebbins
WILMER, CUTLER & PICKERING
2445 M Street, N.W.
Washington, D.C. 20037
(202) 663-6000

Martin S. Lessner
Brendan Shannon
YOUNG, CONAWAY, STARGATT &
TAYLOR LLP
Wilmington Trust Center
1100 North Market Street – 11th Floor
Wilmington, DE 19899
(302) 571-6600