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UNITED STATES BANKRUPTCY COURT

NORTHERN DISTRICT OF CALIFORNIA

SAN JOSE DIVISION

In re: **TECHNOLOGY PROPERTIES LIMITED LLC, fake TECHNOLOGY PROPERTIES LIMITED INC., A CALIFORNIA CORPORATION, fake TECHNOLOGY PROPERTIES LIMITED, A CALIFORNIA CORPORATION,** Debtor.	Case No. 13-51589-SLJ-11 Chapter 11 Date: Feb. 11, 2015 Time: 10:00 a.m. Place: United States Bankruptcy Court 280 S. First Street, Room 3099 San Jose, CA 95113 Judge: Honorable Stephen L. Johnson

OBJECTION OF UNSECURED CREDITORS CHESTER A. BROWN, JR. AND MARCIE BROWN TO THE JOINT PLAN OF REORGANIZATION (DATED JANUARY 8, 2015)

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Unsecured Creditors CHESTER A. BROWN and MARCIE BROWN (collectively the "Browns") hereby submit the following Objection to Confirmation of the Joint Plan of Reorganization by Official Committee of Unsecured Creditors and Debtor (dated January 8, 2015) (the "Plan").

I. THE BROWNS' OBJECTIONS TO THE PLAN

The Browns object to the Plan of the following two grounds:

1. The Plan includes an invalid release of third party claims in violation of 11 U.S.C. § 524(e). The proposed release is also inequitable, unfair, and not presented in good faith because it is overly broad (releasing non-debtor, uninvolved parties and entities) and unlimited in scope (releasing all claims between the released parties without relation to the bankruptcy case).

2. The Plan is inequitable, unfair, and presented in bad faith in violation 11 U.S.C. § 1129 (a)(7)(A), (a)(8), (a)(10), (a)(11), and (b), because it substantially reduces the Brown's payment under the Plan if they do not approve or object to the Plan.

II. STATEMENT OF FACTS

A. <u>The Browns' Claim Against the Debtor</u>

The Debtor entered into a Contract with the Browns under which the Browns received a percentage of the gross proceeds generated by the Debtor from its commercialization of various patents. (See, Proof of Claim 22-1.) After the Debtor ceased making payments to the Browns (and others) despite its continued generation of proceeds from the relevant patents, the Browns filed a lawsuit against Debtor in Santa Clara Superior Court. (See, Proof of Claim 22-1.) In response to the complaint, the Debtor filed a cross-complaint asserting numerous claims against the Browns. On April 18, 2012, after a three week jury trial, the jury returned a special verdict in favor of the Browns and against the Debtor in the amount of $8,887,732. (See, Proof of Claim 22-1.) Because equitable issues remained to be tried, judgment could not be entered immediately after the jury verdict. (Plan p. 5.) On March 20, 2013, after the equitable issues were tried and decided, the Debtor filed for bankruptcy – only hours before the superior court judge had notified the parties that he would be signing the judgment. (Docket No. 1.)

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B. The Litigation Between the Browns and the Debtor is Continuing

After the bankruptcy filing, the Browns and the Debtor stipulated to lifting the automatic stay in order to allow the judgment to be entered. (Docket No. 125.) Judgment was entered on June 5, 2013. (Plan, p. 5.) Debtor then appealed the judgment to the Sixth Appellate District and the Browns cross-appealed. (See, Plan p. 5.)

C. The Browns Claim in Bankruptcy and Appointment to the Unsecured Creditors Committee

The Browns timely filed Proof of Claim Number 22-1 in connection with their Judgment in the amount of $10,021,511 plus post-judgment interest. (Plan p. 5.)

The Browns were appointed to the Official Committee of Unsecured Creditors ("Committee") although given one vote. (See, Plan p. 6.) The Committee elected Marcie Brown as the Chairperson. (Plan p. 64.)

D. The Initial Plan Filed By the Debtor

On October 29, 2014, the Debtor and Committee filed a Joint Plan of Reorganization. (Docket Nos. 587.) The U.S. Trustee objected to the October 29, 2014 Plan, in part, because it contained an illegal release. (Docket No. 595.) In light of the objections to the plans, the Committee and Debtor were given time by the Court to file another Joint Plan.

E. The Plan Terms

The Debtor and Committee then filed the present Plan. The Plan, however, includes the Release previously objected to.

Marcie Brown signed the Plan as the Committee Chairperson because a majority of Committee members approved it despite the Browns' individual objections to several terms of the Plan, including the Release. (Plan p. 64.) Marcie Brown as Chair of the Creditors' Committee signed the Plan for the Creditors' Committee, solely in that capacity, because she has a fiduciary duty to carry out the vote of the Creditors' Committee. However, the Browns as individual creditors are exercising their rights to object to the Plan. These objections are consistent with objections and concerns that they have raised throughout the process of negotiation.

1. The Classification and Subordination of the Browns' Claims

Although the Browns' claim is based upon a judgment, the Plan classifies the Browns' claim as a contract claim -- "Non-Insider 13% Claims" -- along with three other creditors who had non-litigated but similar contracts with the Debtor. (See, Plan at p. 11.)

Under the terms of the Plan, if the Browns "accept the Plan and do not object to confirmation of the Plan," their claim is defined as "Accepting Non-Insider 13% Claims" (Plan p. 2) and their claim is classified in Class 6A (50%) and Class 6B (25%) and Class 6C (25%). (Plan pp. 16-18, 23-25.)

2. The Reclassification and Further Subordination of the Browns' Claim If the Browns Refuse to Approve or Object to the Plan

The Plan includes a hammer provision, requiring the Browns (but no other creditor) to approve and not object to the Plan. (Plan pp. 16-18, 23-25.) If the Browns refuse to approve or object to the Plan, their claim (and the other Non-Insider 13% Claimants) is reclassified and placed 100% into Class 6C or Class 7, substantially reducing the distribution on their claim (only 20% of the claim will be paid over time versus 100%).[1] (Plan pp. 23-25.) Further, the reclassification causes the Browns' claim (and the other Non-Insider 13% Claims") to lose priority to other claims simply because the Browns exercise their legal right to object to or to vote against the Plan. (Plan p. 16-18, 23-25.)

Compounding the inequitable provisions foisted on the Browns, the Plan also provides that a claim will not be "deemed disputed or subject to any objection" if the claimant has agreed to subordinate its claim and has accepted the Plan. (Plan, p. 46.) Thus, if the Browns object to the Plan, and other creditors do not, the other Claims are deemed allowed even if those claims should be disallowed if challenged.

3. The Plan Requires the Browns to Release Claims against Named and Unnamed Non-Debtor Third Parties

The Plan also improperly requires the Browns to sign a Release. "Class 6C Accepting

[1] The Plan is ambiguous as to the treatment of the Browns' (and the other 13% Claimants). Section I, subsections 6(a), (b), and (c) specific that 100% of the Browns' claim will revert to a 6(c) claim if they do not approve or object to the Plan, while subsection 7 states the Browns claim will revert to a Section 7 claim. (Plan pp. 17-18.)

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Non-Insider 13% Claims who affirmatively vote to accept the plan and do not object to confirmation of the Plan and who provide releases to the Released Parties shall be deemed to be Allowed Claims which are not subject to dispute." (Plan p. 23.)

The Plan defines the "Released Parties" as: "Dwayne Hannah, Mike Davis, Robert Neilson, Susan Anhalt, Daniel ("Mac") McNary Leckrone, Leckrone, Janet Neal, Nick Antonopoulos, Interconnect Portfolio, John Leckrone, Alliacense, Eric Saunders, Michael Montvelishsky, William Martin, and any and all entities wholly-owned or partially owned by Leckrone, the Daniel Leckrone Survivor's Trust U/D/T dated February 14, 2006, including HSM, MCM, VNS Portfolio LLC, and any predecessor or successor thereto but excluding Patriot Scientific." (Plan p. 14.) The Plan does not identify all of the entities that are wholly-owned or partially owned by Leckrone or his family trust. (Plan p. 14 and Exhibit E.)

Although the Plan states the consideration from the Released Parties in exchange for the Release is their subordination and liens under the Plan (Plan p. 55), not all of the Released Parties (e.g. unidentified entities and the Debtor's insurers) subordinated their claims or even have claims against the Debtor.

III. LEGAL ARGUMENT

A. The Proposed Release Violates 11 U.S.C. § 524

The Plan cannot be confirmed because it includes the release of third parties. A discharge "operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect, recover or offset any such debt as a personal liability of the debtor, whether or not discharge of such debt is waived." 11 U.S.C. § 524(a)(2). In other words, section 524(a) provides for the discharge of liability on certain debts of the debtor. Section 524 does not, however, provide for the release of personal liability for a third party non-debtor. To the contrary, 11 U.S.C. § 524(e) provides that a "discharge of a debt of the debtor does not affect the liability of any other entity on, or the property of any other entity for, such debt." 11 U.S.C. § 524(e). Thus, the bankruptcy court does not have the authority to release the liability of non-debtors, and a plan which contains such a provision may not be confirmed. *In re Lowenschuss*, 67 F.3d 1394 (9th Cir. 1995); *In re American Hardwoods, Inc.*, 885 F.3d 621, 626

(9th Cir. 1989); *Underhill v. Royal*, 769 F.2d 1426, 1433 (9th Cir. 1985).

The Ninth Circuit has repeatedly reiterated this principal when a debtor seeks to affect the liability of a non-debtor in its bankruptcy. *See In re American Hardwoods, Inc*., *supra*, 885 F.2d at 626 (§ 105(a)'s grant of equitable powers does not permit a court to issue an injunction against creditors that would prevent creditors from enforcing the obligations of non-debtors); *In re Sun Valley Newspapers, Inc*., 171 B.R. 71, 77 (9th Cir. BAP 1994) (holding reorganization plans which proposed to release non-debtor guarantors violated § 524(e) and were therefore unconfirmable). "[T]he mechanics of administering the federal bankruptcy laws, no matter how suggestive, do not operate as a private contract to relieve co-debtors of the bankrupt of their liabilities." *Seaport Automotive Warehouse, Inc. v. Rohnert Park Auto Parts, Inc. (In re Rohnert Park Auto Parts, Inc.*), 113 B.R. 610, 616 (9th Cir. BAP 1990) citing *Union Carbide Corp. v. Newboles*, 686 F.2d 593, 595 (7th Cir. 1982).

Here, there is no question that third parties are released under the Plan. (*See*, *e.g.*, Plan at page 14 (defining "Released Parties" to include at least 19 named individuals and companies, and additionally "any and all entities wholly-owned or partially owned by [Daniel E.] Leckrone, The Daniel Leckrone Survivor's Trust U/D/T dated February 14, 2006, . . . and any predecessor or successor thereto but excluding Patriot Scientific.") (Plan at page 14.) Thus, the Plan violates 11 U.S.C. § 524(e) and confirmation must be denied.

The Browns anticipate Debtor will argue the bankruptcy court is not discharging the third parties but merely approving a Plan in which individual parties or entities mutually agree to release each other. If the parties wish to release each other separately from the Plan and separately from the bankruptcy court, they can do so. But this Plan requires the Browns to release third parties as a condition to receiving benefits and privileges under the Plan. ("Claims of holders of Class 6A Accepting Non-Insider 13% Claims who do not provide releases shall not be deemed to be Allowed Claims, but instead shall be deemed Disputed Claims, subject to the outcome of the Brown Appeal." Plan p. 23.) Thus, the Release is not consensual or voluntary. In essence, the parties are attempting to use the Court's power over the process to force the Browns into providing a release to third parties of claims that are not even related to the bankruptcy estate.

Given that the Court's involvement is required in overseeing this process, this type of release is invalid.

1. The Releases Causes the Plan to Violate the "Best Interests of Creditors" Test

11 U.S.C. § 1129(a)(7)(ii) requires a plan proponent to prove that every dissenting creditor in a plan of reorganization will receive at least as much from the reorganization as it would from a liquidation. *In re American Family Enterprises*, 256 B.R. 377, 403 (D.N.J. 2000). In a corporate liquidation, there is no discharge. 11 U.S.C. § 727(a)(1). All creditors remain free to pursue discharged debts of a liquidating corporate debtor from third parties which are jointly liable on such debts. Moreover, and crucially, "[i]n a case where claims are being released under the chapter 11 plan but would be available for recovery in a chapter 7 case, the released claims must be considered as part of the analysis in deciding whether creditors fare at least as well under the chapter 11 plan as they would in a chapter 7 liquidation." *In re Washington Mut., Inc.*, 442 B.R. 314, 359-60 (Bankr. D. Del. 2011). The Release requires the Browns to give up potentially valuable claims against third parties for no consideration. Accordingly, the Browns would receive less from the plan of reorganization that they would from a liquidation.

2. The Release is Uncertain and Unfair Because it Requires the Browns to Release all Claims Against Unspecified Persons and Entities

Even if this Court adopts the approach taken in other jurisdictions, which allow releases in limited circumstances, those limited circumstances are not present here. In *In re South Canaan Cellular Investments, Inc.*, the bankruptcy court held that the following elements must be satisfied for a third-party release to pass even the "most flexible" test for granting such releases:

> (1) whether the third party who will be protected by the injunction or release has made an important contribution to the reorganization; (2) whether the requested injunctive relief or release is "essential" to the confirmation of the plan; (3) whether a large majority of the creditors in the case have approved the plan; (4) whether there is a close connection between the case against the third party and the case against the debtor; and (5) whether the plan provides for payment of substantially all of the claims affected by the injunction or release.

427 B.R. 44, 72 (Bankr. E.D. Pa. 2010).

None of those requirements have been met here. Further, even where the minimal requirements for the granting of a non-debtor release are satisfied, the court must also separately find that the releases are equitably justified as an "extraordinary judicial act." *In re Saxby's Coffee Worldwide, LLC*, 436 B.R. 331, 337 (Bankr. E.D. Pa. 2010); *see also In re Genesis Health Ventures, Inc.*, 266 B.R. 591, 608 (Bankr. D. Del. 2001). The broad and unlimited Releases do not satisfy the minimal requirements. In *Airadigm Communs, Inc. v. FCC (In re Airadigm) Communs, Inc.*, 519 F.3d 640 (7th Cir. 2008), the Seventh Circuit found that releasing claims against the plan's primary funder for its role in promulgating the plan was "necessary" because the funder would not proceed without those releases. 519 F.3d at 657. The court, however, took care to note that the release was only appropriate because it was "appropriately tailored" and did not constitute "blanket immunity for all times, all transgressions, and all omissions." *Id.* By contrast, in *Gillman v. Continental Airlines (In re Continental Airlines)*, 203 F.3d 203 (3rd Cir. 2000), the release was not necessary, because there was no evidence that the non-debtor releasees had made any significant financial contribution to the reorganization. 203 F.3d at 215; *see also, Deutsche Bank AG, London Branch v. Metromedia Fiber Network, Inc. (In re Metromedia Fiber Network, Inc.)*, 416 F.3d 136, 143 (2nd Cir. 2005) (noting that even though one releasee had made a financial contribution to the estate, the release covered numerous other parties, and there was no inquiry made as to why the release needed to be so broad).

Here, the release is not limited in scope in any manner and requires the Browns to release unidentified third parties. The Release itself (Exhibit E) provides for a release of additional unnamed parties, as it provides for a release of "TPL Insiders" -- defined as "any and all entities wholly-owned or partially owned by Leckrone, the Leckrone Family Trust and [other specific entity names to be inserted]" but also including "their successors in interest, beneficiaries, heirs, assigns, attorneys, agents, representatives, and insurers" for "any claim or pending or threatened action or legal proceeding which any Non-Insider 13%er [the Browns] may assert or possess against or involving the Debtor or any TPL Insider." (Exhibit E to Plan, section 2.1.) The Release in Exhibit E to the Plan specifically recognizes that the entities are not yet named and defers to another day the identification with the language "[other specific entity names to be inserted].”

3. The Inclusion of the Overly Broad Release was not in Good Faith

The release, as crafted, is unnecessarily broad and, thus, the Plan is also not made in good faith as required by law. Good faith is an inherent requirement which runs throughout the entire Bankruptcy Code. Section 1129(a)(3). “Good faith” means honesty in purpose, faithfulness to one's duty or obligation, observance of concepts of fair dealing, and the absence of intent to defraud or to seek unconscionable advantage. BLACK’S LAW DICTIONARY (9th ed. 2009). In order to determine good faith, a court must inquire into the totality of circumstances surrounding the plan, the application of the principals of fundamental fairness in dealing with creditors, and then decide whether the plan will fairly achieve a result consistent with the objectives and purposes of the Code. *In re Sylmar Plaza, L.P.*, 314 F.3d 1070, 1074 (9th Cir. 2002); *Ryan v. Loui (In re Corey)*, 8902 F.2d 829, 835 (9th Cir. 1989); *In re Stolrow’s, Inc.*, 84 B.R. 167, 172 (9th Cir. 1988); *In re Jorgensen*, 66 B.R. 104, 109 (9th Cir. 1986); *see also In re Kemp*, 134 B.R. 413, 414-15 (Bankr. E.D. Cal. 1991); *In re Jasik*, 727 F.2d 1379, 1383 (5th Cir. 1984). Here, the overly broad and unlimited Release fails to meet those standards.

One of the goals of bankruptcy is to create an ordered system with finality, transparency, and fairness. See, *In re Coastal Plains, Inc.*, 179 F.3d 197, 208 (5th Cir. 1999) (Debtors must divulge all relevant facts in order to receive the full benefits and protections of the Bankruptcy Code, with the broad policy and goals of the Code “favor[ing] transparency and disclosure whenever possible.”). Here, requiring parties to release unknown entities is not fair, transparent, or final. For example, under the terms of the proposed release, if Dan Leckrone or the Leckrone Trust owns one share of Apple, the Browns are required to release Apple and also Apple’s unidentified “successors in interest, beneficiaries, heirs, assigns, attorneys, agents, representatives, and insurers” in order to gain the benefits of the Plan and to be treated on parity with other creditors.

Compounding the unfairness and lack of good faith, the release not only extends to unnamed and unnecessary third parties, it is also unlimited in scope and requires the Browns to release “any claim or pending or threatened action or legal proceeding which any Non-Insider

13%er [the Browns] may assert or possess," including the release of unknown claims. (Plan at Exhibit E (section 2.1).) The scope of the release is so broad that no creditor can realistically assess what he or she or it is releasing. That is not good faith.

B. The Plan Unfairly, Inequitably, and in Bad Faith Discriminates against the Browns

In order for a plan to be confirmable, it must not discriminate unfairly and must be fair and equitable. *In re Bonner Mall Partnership*, 2 F.3d 899, 906 (9th Cir. 1993) ("[T]he Code provides that where all requirements for confirmation but section 1129(a)(8) are met, the bankruptcy court *shall* confirm a chapter 11 reorganization plan over the objection of an impaired class or classes "if the plan does not discriminate unfairly, and is *fair and equitable*, with respect to each class of claims or interests that is impaired under, and has not accepted the plan.")

Further, pursuant to 11 U.S.C. § 1129(a)(3), the party seeking confirmation must show that "[t]he plan has been proposed in good faith and not by any means forbidden by law." Section 1129(a)(3) "speaks more to the process of plan development than to the content of the plan." *In re Bush Industries, Inc.*, 315 B.R. 292, 304 (Bankr. W.D.N.Y. 2004). Among other things, good faith provides "a check on the debtor's intentional impairment of claims." *Combustion Eng'g*, 391 F.3d at 246; *accord In re Greate Bay Hotel & Casino, Inc.*, 251 B.R. 213, 240 (Bankr. D.N.J. 2000) ("Of course, the classification and treatment of classes of claims is always subject to the good faith requirements under § 1129(a)(3)."); *In re Sandy Ridge Dev. Corp.*, 881 F.2d 1346, 1353 (5th Cir. 1989) (remanding to determine whether the separate classification and impairment of two creditors for the apparent purpose of procuring acceptance of the plan violated the requirement of good faith).

Here, the Plan does not treat the Browns in good faith, fair, or equitably because (in addition to the improper release), it also requires the Browns – and the Browns alone – to accept the Plan and not object to it, or else suffer significant adverse treatment of their claim. If the Browns approve the Plan and do not object to it, the Browns' claim is impaired and divided into three subclasses (6(a), 6(b), and 6(c)), placing a majority of their claim behind other unsecured creditors. Although potentially objectionable, the Browns do not object to the classification of their claim in this manner, but the Browns do object to the punitive provisions which reclassifies 100% of their claim to class 6(c) or 7 simply because they chose to exercise their right to vote against, or object to, the Plan. Further, in addition to reclassifying the Browns' claim, if the Browns vote against or object to the Plan, their legitimate Claim will be challenged by the Debtor while the claims of similar creditors who vote to approve the Plan will be deemed allowed, effectively precluding from the Browns from challenging potentially invalid claims (e.g. the alleged contracts with the Leckrone children that are implausible on their face and barred by the statute of limitations; and the validity of the Alliacence in light of the Debtor's unilateral forgiveness of millions of dollars in debt that was owed to the Debtor immediately prior to the bankruptcy filing.)

Confirmation of a plan should be denied or stayed if the plan provides disparate treatment to creditors depending on how they voted on the plan. *See*, *In re Adelphia Communications Corp*., 361 B.R. 337, 362 (S.D.N.Y. 2007). In finding that the plan likely violated section 1123(a)(4), the *In re Adelphia* Court held:

> Section 1123(a)(4) guarantees that each class member will be treated equally, regardless of how it votes on a proposed plan. Where the receipt of valuable benefits in a plan is conditioned on a vote to accept that plan, there is a very real possibility of dissuading or silencing opposition to the plan. In this context, the Bankruptcy Court's semantic distinction between the treatment of claims and claimants goes against the spirit of section 1123(a)(4) and what it seeks to protect.

Id. at 363-64.

This punitive treatment violates the intent and spirit of section 1123(a)(4) and what it seeks to protect, especially where, as here, the Browns have valid and legitimate grounds for objecting to the Plan.

IV. CONCLUSION

The Browns objections to the Plan should be sustained. The Plan includes an improper release of third parties that is prohibited by the Ninth Circuit. Further, even if a release were to be allowed in this jurisdiction, it would need to be narrowly tailored to the bankruptcy case. It is not.

The overly broad and unlimited release (of named and unidentified third parties) contained in the Plan is not limited or tailored in any way.

Further, because the Plan seeks to punish the Browns by significantly reducing their distribution if they merely exercise their right to vote against or object to the Plan, it violates Section 1123(a)(4) and, therefore, cannot be "crammed down" the Browns.

Respectfully submitted,

Dated: February 4, 2015

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By: /s/ Randy Michelson
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