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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re: **DEWEY & LEBOEUF LLP,** **Debtor.**	**Case No. 12-12321 (MG)** **Chapter 11**
ALAN M. JACOBS, as Liquidating Trustee of the Dewey & LeBoeuf Liquidation Trust, **Plaintiff,** **v.** **STEPHEN H. DiCARMINE and JOEL I. SANDERS,** **Defendants.**	**Adv. Pro. No. 13-01765 (MG)**

LIQUIDATING TRUSTEE'S OPPOSITION
TO DEFENDANTS' MOTION TO STRIKE

(This pleading responds to Adv. Dkt. 23)

Alan M. Jacobs, as Liquidating Trustee ("Trustee") of the Dewey & LeBoeuf Liquidation Trust ("Trust"), files this opposition to the Supplemental Motion to Dismiss Plaintiff's First Amended Complaint and to Strike All Conduct-Related Claims and Allegations ("Motion to Strike") [Adv. Dkt. 23, 24] filed by Stephen DiCarmine ("DiCarmine") and Joel Sanders ("Sanders," and, together with DiCarmine, "Defendants").

PROCEDURAL NOTE

For the Court's convenience, the Liquidating Trustee files this separate response to the Defendants' Motion to Strike [Adv. Dkt. 24]. The Defendants previously filed a Motion to Dismiss [Adv. Dkt. 15], which they incorporated by reference into the Motion to Strike. The two motions cover different ground. The Motion to Dismiss challenges the sufficiency of the Trustee's complaint. The Motion to Strike argues that certain of the Trustee's claims are barred by an insurance settlement. The Trustee's response to the Motion to Dismiss is filed separately.

SUMMARY

The Defendants cannot meet the high bar required to win a motion to strike. The Defendants assert that the Trustee's chapter 5 avoidance actions in the First Amended Complaint ("FAC") are barred by the XL Settlement, which the Defendants themselves actively opposed and refused to participate in, and therefore must be stricken from the FAC. Even if the Defendants had standing to enforce a settlement to which they are, at most, incidental beneficiaries, their arguments fail because the XL Settlement expressly carves out chapter 5 avoidance actions.

The Defendants attempt to avoid the chapter 5 carve out by manufacturing, out of whole cloth, the concept of "Conduct Claims," a term that appears nowhere in the settlement documents. The Defendants suggest that the XL Settlement somehow blesses and immunizes the Defendants'

past actions because it releases *some* of the claims that might have arisen from those actions. Their argument contradicts the plain terms of the XL Settlement because the expressly excepted chapter 5 avoidance actions necessarily rely upon the Defendants' past actions (such as the receipt of transfers or entry into contracts outside the ordinary course of the Debtor's business).

The Defendants' argument also fails because it conflates "claims" with "facts." The Defendants suggest that when a specific cause of action is released, all facts that would support that cause of action are inadmissible for any purpose, even in support of other non-released claims. The Defendants go so far as to suggest that facts that might support a released claim should be stricken from a pleading. The XL Settlement released *claims*, it did not release *facts*, and it certainly does not bar the Trustee from marshalling evidence in support of non-released claims.

Finally, the Motion to Strike fails because Defendants' interpretation is at odds not only with the plain language of the settlement, but also with its purpose. The parties to the XL Settlement were not concerned about the Defendants' past conduct as such. They were negotiating over insurance coverage for certain causes of action. That is why the XL Settlement expressly carved out, in addition to chapter 5 claims, "claims . . . not covered by the Policy." And it is why the XL Settlement carefully noted that "the Liquidating Trustee reserves all his rights with respect to [the Defendants'] liability or wrongdoing with respect to the claims being settled under the Settlement Agreement." (XL Settlement Order ¶ G.) These carve outs show that the Defendants are flat wrong when they argue that the settlement immunizes their past conduct.

BACKGROUND

On April 22, 2013, the Trustee signed the XL Settlement with XL Specialty Insurance Company ("XL") and the Debtor's former chairman, Steven Davis ("Davis"). The XL Settlement is attached hereto at **Exhibit A**. The Defendants were not parties to the settlement. After extensive negotiations, the Defendants refused to participate in the settlement. In fact, they filed objections to Court approval of the settlement. (*See, e.g.*, Main Dkt. 1395.) On May 30, 2013, the Court approved the XL Settlement under Bankruptcy Rule 9019 over the objections of the Defendants. The XL Settlement Order is attached hereto at **Exhibit B**.

The XL Settlement contemplates a partial release of claims against "Insureds" under a policy written by XL for the benefit of the Debtor. The Defendants qualify as Insureds. The structure of the XL Settlement is a general release of claims paired with a carve out of specific categories of claims. The effect is a partial release. The general release provides, among other things, that:

> "[T]he Liquidation Trust . . . shall and hereby does . . . release . . . all Insureds . . . from any and all claims, obligations, demands, actions, causes of action, and liabilities of whatever kind and nature or character and description, and whether in law or equity, whether sounding in tort, contract or other applicable law, whether known or unknown, whether fixed or contingent, whether held directly or derivatively, and whether anticipated or unanticipated, that have been or could be asserted against the Insureds . . . .

(Ex. B. ¶ 2 (hereinafter, "General Release").)

The carve out provides that the release "shall not include any claims, obligations, demands, actions, causes of action, and liabilities that are not covered by the XL Policy, including without limitation, claims arising under Chapter 5 of the Bankruptcy Code."

These provisions are echoed in the XL Settlement Order, which provides that "[t]he Released Claims . . . shall not include . . . claims arising under Chapter 5 of the Bankruptcy

Code . . . (whether or not they are covered by the [XL] Policy) and ***all of the Liquidating Trustee's rights to prosecute such claims are fully reserved***." (Ex. B ¶ 9 (emphasis added).) The Order separately clarifies that, despite the release of liability of the insureds, "the Liquidating Trustee reserves all his rights with respect to such liability or wrongdoing with respect to the claims being settled under the Settlement Agreement." (Ex. B ¶ G.

The Court emphasized the scope of the carve out on the record during the hearing held on approval of the XL Settlement: "THE COURT: I don't know how to state it anymore clearly, [approval of the Settlement] is without prejudice to [the Trust's] ability to assert Clawback and Chapter 5 claims against [Defendants]." (Hr'g Tr., May 15, 2013, Main Dkt. 1450, at 58:6-14.)

On June 9, 2014, the Trustee filed his First Amended Complaint ("FAC"). The FAC contains nine separate counts. Counts I, III, IV and V state claims under Bankruptcy Code § 548. Counts II and VI states claims under § 544 and 550. Count VIII states claims under § 547. Counts VIII and IX do not seek affirmative recovery, but instead relate to the Trustee's objections to the Defendants' proofs of claim.

ARGUMENT

The Motion to Strike should be denied on three separate, independent grounds.

I. The Defendants Lack Standing To Invoke A Settlement They Did Not Join.

Neither Defendant was a party to the Settlement Agreement. In fact, they actively opposed the Court's approval of the settlement.

Under New York law, non-parties to a contract lack standing to invoke its benefits. *Mendel v. Henry Phillps Plaza West, Inc.*, 6 N.Y.3d 783, 786 (2006). To establish standing as third-party beneficiaries, a non-party must establish (1) a valid contract; "(2) that the contract was intended for their benefit," and "(3) that the benefit to them is sufficiently immediate, rather

than incidental, to indicate the assumption by the contracting parties of a duty to compensation them if the benefit is lost." *Id.*; *see also Consol. Edison, Inc. v. Ne. Utils.*, 426 F.3d 524, 528 (2d Cir. 2005) ("To create a third party right to enforce a contract, the language of the contract must clearly evidence an intent to permit enforcement by the third party.").

Nothing in the XL Settlement indicates the intention of the settling parties to benefit to the Defendants directly, or to create a right to relief. With respect to the Trust and XL, the purpose of the settlement was to resolve claims for which XL might be liable to the Trust under an insurance policy. That is clear from the release terms of the settlement, which expressly carve out not only chapter 5 claims, but also "any claims, obligations, demands, actions, causes of action, and liability that are not covered by the XL Policy." (Ex. A ¶ 2.)

Davis's participation proves the point. Davis, who was also an Insured under the policy, sought personal benefit from the Trust's releases, and he paid for it by entering into the settlement and giving consideration. (*See, e.g.*, Ex. A ¶ 7 (the Davis Note payable to the Trust). The XL Settlement provides releases for Davis that are wholly separate from the more general releases applying to other "Insureds." (*Compare* Ex. A ¶ 3 ("Release of Davis") *with* ¶ 2 ("Release of all Insureds").) Neither DiCarmine nor Sanders elected to participate in the settlement. They gave no consideration. The XL Settlement was not intended to benefit them.

The Defendants are, at best, incidental beneficiaries of the XL Settlement. Their inclusion is incidental to their status as "Insureds" under the policy the settlement is based on. The Defendants are not even identified by name in the settlement. The purpose of the release for the benefit of the "Insureds" is to relieve XL's liability on the insurance policy. It is incidental that individual insureds themselves might also benefit from that release. Accordingly, as

incidental beneficiaries, the Defendants lack standing to enforcement the settlement agreement to which they were not parties. *Mendel*, 6 N.Y.3d at 786.

II. The Motion to Strike Fails To Satisfy the Requirements of Rule 12(f).

Defendants ask the Court to strike allegations under Rule 12(f). That rule allows courts to strike from a pleading allegations that are "redundant, immaterial, impertinent, or scandalous." Fed. R. Civ. P. 12(f). "Motions to strike are generally disfavored, and should be granted only when there is a strong reason for doing so." *In re Dewey & LeBoeuf LLP*, 507 B.R. 522, 530 (Bankr. S.D.N.Y. 2014) (internal quotation marks and citation omitted). The Second Circuit admonishes that "courts should not tamper with the pleadings unless there is a strong reason for doing so.'" *In re Lehman Bros. Holdings Inc.*, 474 B.R. 441, 446 (Bankr. S.D.N.Y. 2012) (quoting *Lipsky v. Commonwealth United Corp.*, 551 F.2d 887, 893 (2d Cir. 1976)).

To prevail on a motion to strike, a party must show that: "(1) no evidence in support of the allegations would be admissible; (2) the allegations have no bearing on the relevant issues; and (3) permitting the allegations to stand would result in prejudice to the movant." *Schoolcraft v. City of New York*, 2014 WL 1870839, at *1 (S.D.N.Y. May 8, 2014).

The Defendants' Motion to Strike fails to establish any of these elements. The Defendants argue that "the Conduct Claims are inadmissible and have no bearing on the subject matter of the action because . . . they have been released, barred, and enjoined by the Settlement Order." The Defendants conflate "claims" with "evidence." Regardless of what claims the XL Settlement released, the XL Settlement says nothing about the admissibility of evidence of the Defendants' conduct. The Defendants do not, and could not, explain why evidence of their past actions and wrongdoing would be inadmissible in support of the Trustee's claims under chapter 5, which claims were expressly carved out of the settlement.

The evidence of past conduct is plainly relevant, as alleged at length in the FAC. To the extent the Defendants want to strike factual allegations on relevancy grounds, the motion is premature. *See Lipsky*, 551 F.2d at 893 ("Usually the questions of relevancy and admissibility in general require the context of an ongoing and unfolding trial in which to be properly decided."). Trial is a long way off, and "courts are very reluctant to determine disputed or substantial issues of law on a motion to strike; these questions quite properly are viewed as determinable only after discovery and a hearing on the merits." *Lehman Bros.*, 474 B.R. at 447.

Finally, the Defendants are not "prejudiced" by allegations in the FAC as that term is understood in the Rule 12(f) context. "The granting of a motion to strike scandalous matter is aimed, in part, at avoiding prejudice to a party by preventing a jury from seeing the offensive matter or giving the allegations any other unnecessary notoriety inasmuch as, once filed, pleadings generally are public documents and become generally available." *Lynch*, 278 F.R.D. at 67. Here, there is nothing "new" about the allegations in the FAC—the world is already familiar with Defendants' mismanagement of the Debtor. *See id.* (denying motion to strike because allegations were "already public and generally available"). Indeed, the press regularly report on this matter, and the Defendants' own lawyers comment for reporters.

The Defendants have not demonstrated an entitlement to relief under Rule 12(f).

III. The XL Settlement Did Not Release Chapter 5 Claims.

To the extent the Defendants also seek relief under Rule 12(b), their arguments fail because they misread the XL Settlement, which expressly does not prejudice, in any way, the Trustee's right to pursue chapter 5 avoidance actions against them.

First, the language of the XL Settlement is clear. "The Released Claims . . . shall not include . . . claims arising under Chapter 5 of the Bankruptcy Code . . . (whether or not they are

covered by the [XL] Policy) and ***all of the Liquidating Trustee's rights to prosecute such claims are fully reserved***." (Ex. A ¶ 9 (emphasis added).) The XL Settlement Order further emphasizes that "the Liquidating Trustee reserves all his rights with respect to [the Insureds'] liability or wrongdoing with respect to the claims being settled under the Settlement Agreement." (Ex. B ¶ G.) And, if agreement and the order were not clear enough, in approving the settlement, the Court ruled "I don't know how to state it anymore clearly, [approval of the Settlement] is without prejudice to [the Trust's] ability to assert Clawback and Chapter 5 claims against [Defendants].". (Hr'g Tr., May 15, 2013, Main Dkt. 1450, at 58:6-14.)

Second, the Defendants' efforts to read into the XL Settlement an implied release of "Conduct Claims" fails because there is simply no support for such an interpretation of the settlement documents. None of the settlement documents refer to the "conduct" of any of the Insureds, let alone the specific wrongdoing of these Defendants. The XL Settlement instead releases *claims* that might lead to liability of the insurance carrier. The settlement says nothing about the use in future proceedings of the *evidence* that might have supported the released claims. On the contrary, by carving out classes of claims (including non-covered claims and chapter 5 actions), the XL Settlement plainly contemplates future litigation against the Insureds. It would be absurd to interpret the XL Settlement as simultaneously reserving for the Trustee the right to pursue claims while barring him from marshalling evidence in support of those claims.

Third, the Defendants' interpretation would have the anomalous result of turning a shield into a sword. For example, the Trustee has alleged constructive fraudulent transfer, and the Defendants argue that their work provided value to support the transfers to them.[1] If the

[1] These arguments appear in the Motion to Dismiss, and are addressed at length in the Trustee's separately filed response to the Motion to Dismiss.

Defendants are right about the XL Settlement, the Defendants would be entitled to introduce evidence to support their claim that their prior conduct provided value to the Debtor, but the Trustee would be barred from admitting any evidence to the contrary. Whatever else the parties to the XL Settlement intended, this outcome was surely not one of them.

CONCLUSION

For the reasons stated herein, the Trustee respectfully requests that this Court deny Defendants' Motion to Strike.

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