No.

# In the Supreme Court of the United States

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LISA ANNE HENRY, ET AL., PETITIONERS

*v.*

OFFICIAL COMMITTEE OF UNSECURED CREDITORS
OF WALLDESIGN, INC.

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*ON PETITION FOR A WRIT OF CERTIORARI*
*TO THE UNITED STATES COURT OF APPEALS*
*FOR THE NINTH CIRCUIT*

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**PETITION FOR A WRIT OF CERTIORARI**

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## QUESTION PRESENTED

Whether a person who obtains funds from a debtor and exercises complete control over the funds, but lacks the legal authority to do so, is an "initial transferee" under Section 550(a)(1) of the Bankruptcy Code.

## PARTIES TO THE PROCEEDING

Petitioners are Lisa Anne Henry, Donald F. Buresh, and Sharon J. Phillips. Respondent is the Official Committee of Unsecured Creditors of Walldesign, Inc.

## TABLE OF CONTENTS

Page

Opinions below ... 1

Jurisdiction ... 2

Statutory provisions involved ... 2

Statement ... 3

Reasons for granting the petition ... 9

A. The decision below squarely presents a conflict among the courts of appeals ... 10

B. The decision below is incorrect ... 16

C. The question presented is exceptionally important and warrants review in this case ... 19

Conclusion ... 23

## TABLE OF AUTHORITIES

Cases:

*Antex, Inc., In re,* 397 B.R. 168 (B.A.P. 1st Cir. 2008) ... 15

*Auto-Pak, Inc., In re,* 73 B.R. 52 (D.D.C. 1987) ... 14

*Baker Botts L.L.P.* v. *ASARCO LLC*, 135 S. Ct. 2158 (2015) ... 20

*Bonded Financial Services, Inc.* v. *European American Bank*, 838 F.2d 890 (7th Cir. 1988) ... 8, 18

*Boyer* v. *Belavilas*, 474 F.3d 375 (7th Cir. 2007) ... 15

*Bullock* v. *BankChampaign, N.A.*, 133 S. Ct. 1754 (2013) ... 20

*C.F. Foods, L.P., In re,* 265 B.R. 71 (Bankr. E.D. Pa. 2001) ... 14

*Catco Recycling, LLC, In re,* Civ. No. 15-1012, 2016 WL 556173 (D.N.H. Feb. 10, 2016) ... 19

*Chase & Sanborn Corp., In re,* 848 F.2d 1196 (11th Cir. 1988) ... 18

*Christy* v. *Alexander & Alexander of New York, Inc.*, No. 97-1400, cert. dismissed, 524 U.S. 912 (1998) ... 22

*Clark* v. *Rameker*, 134 S. Ct. 2242 (2014) ... 20

Page

Cases—continued:

*Global Protection USA, Inc.*, *In re,*
546 B.R. 586 (Bankr. D.N.J. 2016)....................................19
*Hall* v. *United States*, 566 U.S. 506 (2012) ..........................20
*Harwell*, *In re,*
628 F.3d 1312 (11th Cir. 2010).......................10, 12, 13, 18
*Husky International Electronics, Inc.* v. *Ritz*,
136 S. Ct. 1581 (2016) ........................................................20
*Incomnet, Inc.*, *In re,* 463 F.3d 1064 (9th Cir. 2006)...........8
*Manhattan Investment Fund Ltd.*, *In re,*
397 B.R. 1 (S.D.N.Y. 2007)..................................................14
*Merit Management Group, LP* v. *FTI Consulting, Inc.*, No. 16-784, slip op. (Feb. 27, 2018).................17, 20
*Nordic Village, Inc.*, *In re,*
915 F.2d 1049 (6th Cir. 1990),
rev'd on other grounds, 503 U.S. 30 (1992) ............11, 12
*Orange County Sanitation, Inc.*, *In re,*
221 B.R. 323 (Bankr. S.D.N.Y. 1997) .............................14
*Pony Express Delivery Services, Inc.*, *In re,*
440 F.3d 1296 (11th Cir. 2006).........................................13
*Railway Labor Executives' Association* v. *Gibbons*,
455 U.S. 457 (1982)...........................................................20
*Regency International Flooring, LLC*, *In re,*
Civ. No. 09-1146, 2010 WL 4053982
(W.D. Mich. Oct. 14, 2010) ...............................................19
*Reves* v. *Ernst & Young*, 507 U.S. 170 (1993).....................17
*Southeast Hotel Properties Limited Partnership*,
*In re*, 99 F.3d 151 (1996) ...........................................14, 15

Constitution and statutes:

U.S. Const. Art. I, § 8, cl. 4 ...................................................20
Bankruptcy Code, 11 U.S.C. 101-1532 .......................*passim*
11 U.S.C. 101(54)(D)..............................................5, 16, 17
11 U.S.C. 544(b)(1).................................................................5
11 U.S.C. 548(a)(1)(B) ........................................................5
11 U.S.C. 550(a)..............................................................3, 5
11 U.S.C. 550(a)(1) ..................................................*passim*
11 U.S.C. 550(b)(1)...................................................*passim*

Page

Statute—continued:

28 U.S.C. 1254(1) ........................................................................2

Miscellaneous:

Craig H. Averch, *Protection of the 'Innocent' Initial Transferee of an Avoidable Transfer: An Application of the Plain Meaning Rule Requiring Use of Judicial Discretion*, 11 Bankr. Dev. J. 595 (1995) .....................................18, 21

Jessica D. Gabel & Paul R. Hage, *Who Is a 'Transferee' Under Section 550(a) of the Bankruptcy Code?: The Divide Over Dominion, Control, and Good Faith in Applying the Mere Conduit Defense*, 21 J. Bankr. L. & Prac. 47 (Jan. 2012) ...........................21

Troy A. McKenzie, *Judicial Independence, Autonomy, and the Bankruptcy Courts*, 62 Stan. L. Rev. 747 (2010) ..............................................21

S. Rep. No. 989, 95th Cong., 2d Sess. (1978) ......................17

Joseph Story, *Commentaries on the Constitution of the United States* (1833) ..............................................20

United States Courts, *Business and Nonbusiness Bankruptcy County Cases Commenced, by Chapter of the Bankruptcy Code*, tbl. F-5A (Dec. 31, 2017) <tinyurl.com/bankruptcycasetable2017> ....................19

United States Courts, *Judicial Facts and Figures 2016*, tbl. 2.3 <tinyurl.com/factsandfigures2016> .......22

Lori V. Vaughan, *Eleventh Circuit: Good Faith Is Required for Mere-Conduit Defense to § 550(a)*, Am. Bankr. Inst. J. 36 (Mar. 2011) .................................21

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**PETITION FOR A WRIT OF CERTIORARI**

Lisa Anne Henry, Donald F. Buresh, and Sharon J. Phillips respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Ninth Circuit in this case.

**OPINIONS BELOW**

The opinion of the court of appeals (App., *infra*, 1a-38a) is reported at 872 F.3d 954. The opinion of the district court (App., *infra*, 39a-53a) and orders of the bankruptcy court (App., *infra*, 54a-59a) are unreported.

## JURISDICTION

The judgment of the court of appeals was entered on October 2, 2017. Petitions for rehearing were denied on November 9, 2017 (App., *infra*, 60a-61a). On January 19, 2018, Justice Kennedy extended the time within which to file a petition for a writ of certiorari to and including February 28, 2018. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

## STATUTORY PROVISIONS INVOLVED

Section 101 of Title 11 of the United States Code provides in relevant part:

(54) The term "transfer" means—

(A) the creation of a lien;

(B) the retention of title as a security interest;

(C) the foreclosure of a debtor's equity of redemption; or

(D) each mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with—

(i) property; or

(ii) an interest in property.

Section 550 of Title 11 of the United States Code provides in relevant part:

(a) Except as otherwise provided in this section, to the extent that a transfer is avoided under sections 544, 545, 547, 548, 549, 553(b), or 724(e) of this title, the trustee may recover for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from—

(1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or

(2) any immediate or mediate transferee of such initial transferee.

(b) The trustee may not recover under section (a)(2) of the section from—

(1) a transferee that takes for value, including satisfaction or securing of a present or antecedent debt, in good faith, and without knowledge of the voidability of the transfer avoided; or

(2) any immediate or mediate good faith transferee of such transferee.

**STATEMENT**

This case presents a recurring question of statutory interpretation under the Bankruptcy Code on which the courts of appeals are in conflict. Where a debtor fraudulently transfers property, the Code empowers a bankruptcy trustee to recover the property or its value from the "initial transferee" or from any subsequent transferee. 11 U.S.C. 550(a). A trustee's right of recovery against the initial transferee is absolute. A subsequent transferee, by contrast, is entitled to a safe harbor: a trustee may not recover from a subsequent transferee who accepted the property "for value, * * * in good faith, and without knowledge of the voidability of the transfer." 11 U.S.C. 550(b)(1).

Whether a transferee is initial or subsequent is thus critical in cases, such as this one, where a trustee seeks to recover from innocent transferees. The question presented here is whether a person who obtains funds from a debtor and exercises complete control over the funds, but does so unlawfully, is an "initial transferee" under Section

550(a)(1), with the result that subsequent transferees are eligible for the safe harbor in Section 550(b)(1).

Petitioners face an action to recover funds they received from Michael Bello in arm's-length transactions for fair value because, unbeknownst to them, Mr. Bello was perpetrating a fraud on his company. Mr. Bello served as the president, sole shareholder, and sole director of debtor Walldesign, Inc. Walldesign maintained a legitimate bank account from which it paid its expenses. But Mr. Bello also created a secret bank account in Walldesign's name to siphon money from the company solely for personal expenses.

Petitioner Lisa Henry is a small business owner whom Mr. Bello paid to provide interior-design services to him and his wife; petitioners Donald Buresh and Sharon Phillips are a husband and wife who sold their property to Mr. Bello to fund their retirement. Mr. Bello made payments to petitioners from the secret account, totaling hundreds of thousands of dollars. Walldesign subsequently petitioned for bankruptcy. Respondent, a committee of Walldesign's unsecured creditors, brought actions to recover the money petitioners received from Mr. Bello in exchange for their services and property.

The bankruptcy court granted summary judgment to petitioners in relevant part. It held that Mr. Bello was the initial transferee of Walldesign's funds and that petitioners were thus subsequent transferees protected by Section 550(b)(1)'s safe harbor.

The district court reversed, and a divided panel of the Ninth Circuit, over an impassioned dissent from Judge Nguyen, affirmed the district court's decision. The court of appeals recognized that Mr. Bello had complete practical control over the funds in the secret account and put the funds solely to personal use. The court of appeals nevertheless held that Mr. Bello did not qualify as the initial

transferee of the funds because he lacked legal title—precisely because his use of the funds was illicit. As the decision below recognized, the courts of appeals are in conflict as to whether legal authority to spend the funds in any manner is required in order to qualify as an initial transferee under the Code. Because this case is an optimal vehicle for resolving that conflict, the petition for a writ of certiorari should be granted.

1. This case concerns the meaning of the word "transferee" in the Bankruptcy Code. The Code defines a "transfer" as, *inter alia*, "each mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with (i) property; or (ii) an interest in property." 11 U.S.C. 101(54)(D).

Under the Code, a trustee (or debtor in possession) can invalidate fraudulent transfers and thereby enlarge the pool of assets available to a debtor's creditors. See 11 U.S.C. 544(b)(1), 548(a)(1)(B). The Code empowers the trustee to recover the fraudulently transferred property from "(1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or (2) any immediate or mediate transferee of such initial transferee." 11 U.S.C. 550(a). The trustee's ability to recover from the initial transferee is absolute. But the Code provides a safe harbor for a subsequent transferee: a trustee may not recover from a subsequent transferee who accepted the property "for value, * * * in good faith, and without knowledge of the voidability of the transfer." 11 U.S.C. 550(b)(1). A transferee's ability to retain property that he received in good faith and for fair value thus depends on whether he qualifies as an initial or subsequent transferee.

2. Michael Bello served as the president, sole shareholder, and sole director of debtor Walldesign, Inc., a Cal-

ifornia-based construction company. Walldesign maintained a legitimate bank account from which it paid its expenses; that account was disclosed in Walldesign's books and records. App., *infra*, 4a.

In 2002, however, Mr. Bello opened a secret account at a different bank in Walldesign's name. Mr. Bello used his home as the account's address, and later named his wife, who was not a Walldesign employee, as the only other signatory. That account was neither used to pay Walldesign's expenses nor disclosed in its books and records. To the contrary, Mr. Bello "actively concealed" the account from Walldesign's management, employees, and creditors. App., *infra*, 4a-5a, 43a.

Over several years, Mr. Bello deposited millions of dollars in checks written to Walldesign into the secret account. Those checks came from suppliers, which provided rebates on Walldesign's purchases of bulk materials. Mr. Bello used those funds to support a lavish lifestyle, paying for a horseracing stable, vineyards, Las Vegas casino bills, and country-club fees. App., *infra*, 5a.

Petitioner Lisa Henry is a small business owner whom Mr. Bello paid to provide interior-design services to him and his wife; petitioners Donald Buresh and Sharon Phillips are a married couple who sold their land to Mr. Bello to fund their retirement. Mr. Bello paid petitioners a total of approximately $450,000 from the secret account; it is undisputed that all the transactions were at arm's length and for fair value. Apart from those transactions, petitioners had no relationship with Mr. Bello, his family, or his businesses. App., *infra*, 6a.

In 2012, Walldesign petitioned for bankruptcy. Respondent, Walldesign's committee of unsecured creditors, learned of the secret account and brought actions against petitioners to recover the payments Mr. Bello made from the account. Respondent also sought to recover those

amounts directly from Mr. Bello and related individuals in a separate action. App., *infra*, 7a.

3. In the actions against them, petitioners argued that Mr. Bello was the initial transferee of the funds he deposited in the secret account; that they were thus subsequent transferees; and, as a result, that they qualified for the safe harbor in Section 550(b)(1). The bankruptcy court agreed and granted summary judgment to petitioners in relevant part. App., *infra*, 54a-59a.

4. The district court reversed, holding that petitioners should be treated as initial rather than subsequent transferees of the fraudulent payments. App., *infra*, 39a-53a. It identified "two distinct tests" courts had developed to determine whether a party is an initial transferee under Section 550(a)(1): the "dominion" test and the "control" test. *Id.* at 45a-46a. The dominion test focuses on the recipient's "legal authority over the money," whereas the control test "takes a more gestalt view" to determine "who, in reality, controlled the funds in question." *Id.* at 46a (citation omitted). The district court concluded that the Ninth Circuit followed the dominion test. *Ibid.* Applying that test, the court determined that Mr. Bello was not an initial transferee because he lacked legal authority over the funds, which, as a formal matter, remained in Walldesign's name. *Id.* at 49a-50a. Accordingly, the court deemed petitioners to be initial transferees. *Ibid.*

5. A divided panel of the court of appeals affirmed. App., *infra*, 1a-31a.

a. At the outset, the court of appeals recognized the "critical" distinction between initial and subsequent transferees. App., *infra*, 8a (citation omitted). In assessing whether Mr. Bello, rather than petitioners, qualified as the initial transferee of the funds, the court rejected petitioners' reliance on an "over-simplistic syllogism from the meaning of 'transfer'" in the Bankruptcy

Code. *Id.* at 10a. The court of appeals observed that courts construing the phrase "initial transferee" are divided on whether to apply the dominion test, the control test, or some combination of the two. *Id.* at 12a. Following circuit precedent as well as precedent from the Seventh Circuit, the court of appeals applied the dominion test, "reject[ing]" the "more lenient" standard applied by the Eleventh Circuit and several other courts. *Id.* at 11a-12a (citing *In re Incomnet, Inc.*, 463 F.3d 1064 (9th Cir. 2006), and *Bonded Financial Services, Inc.* v. *European American Bank*, 838 F.2d 890 (7th Cir. 1988)); see also *id.* at 23a-24a.

The court of appeals embraced the dominion test despite acknowledging that it could lead courts to "lose track of the original question proposed by the statute—namely, whether a party is a transferee." App., *infra*, 10a (citation omitted). The court of appeals explained that the dominion test "strongly correlates with legal title, and is akin to legal control." *Id.* at 24a (internal quotation marks, citation, and emphasis omitted). The court proceeded to determine that, regardless of Mr. Bello's "de facto control" over the funds transferred into the secret account, he was not the initial transferee because he lacked "legal title" to, and thus "*legal* control" of, the funds, which formally belonged to Walldesign. *Id.* at 19a-20a.

The court of appeals conceded that, as an equitable matter, the result in this case "seem[ed] harsh," and it further acknowledged that its approach "may elevate form over substance." App., *infra*, 3a, 21a (internal quotation marks, citation, and alteration omitted). Nonetheless, the court deemed the dominion test dispositive and concluded that petitioners "are strictly liable to [respondent] as initial transferees." *Id.* at 31a.

b. Judge Nguyen dissented, stating that she "strongly disagree[d]" with the majority's reasoning and result.

App., *infra*, 31a-38a. She began by observing that, while bankruptcy courts are courts of equity, "[t]here [was] nothing equitable" about the majority's approach, which imposed potentially "ruinous" liability on petitioners even though they knew nothing of Mr. Bello's fraud. *Id.* at 31a-32a.

Judge Nguyen urged the majority to "ditch[] the dominion test" and either adopt the control test "used successfully by other circuits," or return to a "hybrid approach" that would allow it "to step back and evaluate a transaction in its entirety." App., *infra*, 33a (citation omitted). She explained that any test that incorporated "the pragmatic control test used in other circuits" "would have produced the correct result here without fuss and held [Mr.] Bello personally liable for his fraudulent acts as the initial transferee." *Id.* at 32a (internal quotation marks and citation omitted).

In the alternative, Judge Nguyen contended that Mr. Bello would qualify as an initial transferee even under the dominion test because the sham account legally belonged to him, rather than to Walldesign, under state law. App., *infra*, 33a-37a. In so contending, Judge Nguyen noted that applying the dominion test would often be a "difficult" task that could lead to "disagreement[s]" premised on varying interpretations of state law. *Id.* at 33a.

6. The court of appeals subsequently denied petitions for rehearing. App., *infra*, 60a-61a.

**REASONS FOR GRANTING THE PETITION**

The court of appeals' decision in this case presents the Court with the opportunity to resolve an acknowledged conflict among the courts of appeals on an important question of statutory interpretation under the Bankruptcy Code. That conflict creates intolerable discord on an important issue of bankruptcy law, and the conflict plainly

will not be resolved without the Court's intervention. The decision below is incorrect, flouting the Code's text and reaching a deeply unfair result in the name of a judge-made exception designed to do equity. Because this case presents an optimal vehicle for resolving the conflict, the petition for a writ of certiorari should be granted.

### A. The Decision Below Squarely Presents A Conflict Among The Courts Of Appeals

The decision below presents a deeply rooted conflict among the courts of appeals concerning the meaning of the phrase "initial transferee" in Section 550(a)(1). Despite the broad statutory language, lower courts have excluded certain recipients of funds from initial-transferee status. That exception, which was first created in cases in which financial institutions were acting as intermediaries, was intended to "prevent the unjust or inequitable result of holding an innocent transferee liable for fraudulent transfers where the innocent transferee is a mere conduit and had no control over the funds transferred." *In re Harwell*, 628 F.3d 1312, 1324 (11th Cir. 2010).

But the courts of appeals have adopted a variety of different legal standards for determining who qualifies as an initial transferee for purposes of that judge-made exception. As the decision below acknowledged, the tests employed in at least two other circuits would have led to the opposite result in this case. The Sixth and Eleventh Circuits, as well as multiple district and bankruptcy courts, have adopted a "more lenient" control test that views a transaction in its entirety. App., *infra*, 12a. Under that test, courts classify as an initial transferee a person who in fact exercises control over funds, regardless of whether that person has the legal authority to do so. On the other hand, the Fourth, Seventh, and Ninth Circuits, along with the Bankruptcy Appellate Panel of the First Circuit, have

adopted some form of the "more restrictive" dominion test, limiting initial-transferee status to recipients with legal authority over the funds. *Ibid.* (citation omitted). Certiorari is warranted to resolve that entrenched conflict about the meaning of a fundamental concept in the Bankruptcy Code.

1. As the Ninth Circuit expressly recognized, see App., *infra*, 17a-18a, 23a-24a, its decision in this case conflicts with the decisions of at least two other courts of appeals. While the Ninth Circuit deemed dominion dispositive and held that Mr. Bello was not the initial transferee despite his actual control of the funds, the Sixth and Eleventh Circuits do not require dominion to establish initial-transferee status. Instead, those courts interpret "initial transferee" in Section 550(a)(1) more expansively to encompass recipients who exercise actual control over the funds, even without formal ownership.

a. In *In re Nordic Village, Inc.*, 915 F.2d 1049 (6th Cir. 1990), rev'd on other grounds, 503 U.S. 30 (1992), a corporate officer used the funds of a debtor corporation to obtain cashier's checks, which he then used to pay the Internal Revenue Service for personal tax liabilities. See *id.* at 1050-1051. The Sixth Circuit observed that, "when a corporate officer takes checks drawn from corporate funds to pay personal debts, the corporate officer[] and not the payee on the check is the initial transferee." *Id.* at 1055 n.3. Accordingly, it explained that, if the corporate officer "t[ook] money illegally from [the company]," he, rather than the IRS, would be the "initial transferee." *Id.* at 1055. The court ultimately concluded that the IRS had failed to establish that it would otherwise qualify for the Section 550(b)(1) safe harbor. See *id.* at 1055-1056 & n.3.

The Sixth Circuit's reasoning in *Nordic Village* cannot be reconciled with the Ninth Circuit's in the decision below: Mr. Bello, who took checks drawn from corporate

funds and deposited them into an account he used solely for personal expenses, would plainly be an initial transferee in the Sixth Circuit. Recognizing the conflict, the Ninth Circuit expressly "rejected" *Nordic Village*: it described it as following the "minority approach" and emphasized that the Ninth Circuit has moved "even further away from the equitable concerns" that drove the Sixth Circuit's decision in favor of "the pure dominion test and its focus on legal control." App., *infra*, 17a-18a (internal quotation marks and citation omitted).

b. For its part, the Eleventh Circuit has recognized that treating all initial recipients of funds as initial transferees can lead to unfair results. See *Harwell*, 628 F.3d at 1320-1321. Accordingly, like the Ninth Circuit in the decision below, it has "eschewed the literal statutory language" in favor of a judicially crafted "exception." *Ibid.* (internal quotation marks and citation omitted). But the exception it adopted is diametrically different from the Ninth Circuit's. Under the Eleventh Circuit's test, initial recipients of funds are presumptively initial transferees unless they can show *both* "(1) that they did not have control over the assets received[] * * * *and* (2) that they acted in good faith as an innocent participant in the fraudulent transfer." *Id.* at 1323. In other words, a person who *either* had actual control over the funds *or* acted in bad faith qualifies as an initial transferee, even if he lacked the legal authority to use the funds for his own purposes.

The Eleventh Circuit applied that framework to a lawyer for a debtor; the lawyer, who did not have legal authority to use the funds as he pleased, deposited the debtor's funds in a trust account, then transferred the funds to the debtor and to third parties according to the debtor's instructions. See 628 F.3d at 1323. The Eleventh Circuit first observed that, as the initial recipient of the funds, the lawyer was "the 'initial transferee' under the

language of [Section] 550(a)(1)." *Id.* at 1323-1324. The court then addressed whether the lawyer "may equitably escape his 'initial transferee' status." *Id.* at 1324. The court ultimately held that summary judgment in the lawyer's favor was inappropriate because there was evidence the lawyer may have participated in the fraud and "the equitable mere conduit defense requires a showing of good faith." *Ibid.*

Under the Eleventh Circuit's reasoning, Mr. Bello, who undisputedly carried out the fraud here, would plainly qualify as an initial transferee, thus rendering petitioners subsequent transferees entitled to invoke the Section 550(b)(1) safe harbor. Indeed, Mr. Bello would fail *both* of the Eleventh Circuit's requirements for the exception from initial-transferee status: he not only had control over the funds, but also lacked the requisite good faith. See *Harwell*, 628 F.3d at 1323; see also *In re Pony Express Delivery Services, Inc.*, 440 F.3d 1296, 1302 (11th Cir. 2006) (noting that the Eleventh Circuit's test is "very flexible" and "pragmatic," requiring courts to "look beyond the particular transfers in question to the entire circumstance of the transactions" to ensure that "their conclusions are logical and equitable" (citation omitted)).

Notably, in ruling against petitioners, the Ninth Circuit expressly "declined [petitioners'] invitation[]" to adopt the Eleventh Circuit's "flexible, equitable approach," noting that it could not do so "without intervening Supreme Court (or en banc) precedent." App., *infra*, 23a-24a. But as Judge Nguyen observed in dissent, that test, like other "control"-based tests, "would have produced the correct result here without fuss and held [Mr.] Bello personally liable for his fraudulent acts as the initial transferee." *Id.* at 32a (internal quotation marks and citation omitted).

c. The Ninth Circuit's decision also conflicts with the decisions of numerous district and bankruptcy courts in other circuits. See, *e.g.*, *In re Manhattan Investment Fund Ltd.*, 397 B.R. 1, 15-16, 21 (S.D.N.Y. 2007) (holding that a broker with control but not legal authority was an "initial transferee" while expressly rejecting the Ninth Circuit's "narrower test"); *In re Auto-Pak, Inc.*, 73 B.R. 52, 54 (D.D.C. 1987) (deeming an "initial transferee" a corporate officer who unlawfully used one company's account to pay another entity's tax liability on the ground that he "essentially took control of the [company's] funds"); *In re C.F. Foods, L.P.*, 265 B.R. 71, 81 (Bankr. E.D. Pa. 2001) (deeming an "initial transferee" a general partner of the debtor because the general partner, while acting unlawfully, "took control of the debtor's funds" and used them for his own benefit); *In re Orange County Sanitation, Inc.*, 221 B.R. 323, 327 (Bankr. S.D.N.Y. 1997) (requiring dominion *or* control and concluding that, "[w]hen a corporate officer receives a check drawn on a corporate account and uses it to pay personal debts, the corporate officer, and not the payee on the check, is the initial transferee").

2. On the other hand, two courts of appeals and a bankruptcy appellate panel of a third follow the Ninth Circuit's approach for determining initial-transferee status.

a. Like the Ninth Circuit, the Fourth Circuit has applied a test that requires "legal dominion and control." In *In re Southeast Hotel Properties Limited Partnership*, 99 F.3d 151 (1996), the Fourth Circuit considered whether a manager that exercised actual control over a debtor corporation's funds by directing the funds to a third party constituted an initial transferee under the Code. See *id.* at 153-154. The Fourth Circuit acknowledged that "courts have disagreed about the type of dominion and control that must be asserted," with some requiring "*legal*

dominion and control" and others requiring merely "*physical* dominion and control." *Id.* at 155-156. Siding with the former courts, the Fourth Circuit determined that the manager was not an initial transferee because it lacked the legal authority to put the funds to its own use. See *id.* at 156-157.

b. Similarly, the Seventh Circuit has limited initial-transferee status to those persons who have both legal title and actual control of the funds. In *Boyer* v. *Belavilas*, 474 F.3d 375 (7th Cir. 2007), a company owned by a married couple deposited company funds into custodial accounts for their children, who held legal title to the funds. See *id.* at 376-377. The children's mother exercised control over the funds and used them to make an unlawful transfer for her own benefit. See *id.* at 377. After the children's father filed for bankruptcy, the bankruptcy trustee sought to recover from the mother under Section 550(a)(1). See *ibid.* The Seventh Circuit determined that the mother did not qualify as an initial transferee; it reasoned that, although the mother exercised control over the money, "treating the funds as her own," she lacked legal title to the custodial accounts. *Ibid.*

c. The Bankruptcy Appellate Panel of the First Circuit has reached a materially identical result. In *In re Antex, Inc.*, 397 B.R. 168 (B.A.P. 1st Cir. 2008), the court considered a corporate principal who used corporate funds to satisfy his personal obligations. See *id.* at 173. In determining whether the principal was an initial transferee under the Code, the court acknowledged that "courts are split" on the legal standard for initial-transferee status. *Ibid.* The court proceeded to hold that the principal was not the initial transferee because he never obtained "legal dominion and control" over the funds. *Ibid.*

As the Ninth Circuit recognized in its opinion, see App., *infra*, 17a-18a, 23a-24a, the courts of appeals are in

conflict on this basic question of interpretation under the Bankruptcy Code. Under the current state of affairs, whether a recipient of funds qualifies as an initial transferee turns on the accident of geography. This Court's intervention is badly needed to resolve the conflict.

**B. The Decision Below Is Incorrect**

The Ninth Circuit's interpretation of the phrase "initial transferee" in Section 550(a)(1) is indefensible. By mechanically applying a judicially created rule, the Ninth Circuit reached a starkly inequitable result that—by the court's own admission—lacks any grounding in the Code's text. This Court should grant certiorari to review and correct the Ninth Circuit's deeply flawed decision.

1. The Ninth Circuit acknowledged that Mr. Bello, who transferred Walldesign funds into a secret account used only by him and his wife, had complete control over the funds in that account, spending millions on lavish personal expenses. App, *infra*, 4a-5a, 19a-20a. Applying the dominion test, the court nevertheless concluded that Mr. Bello was not a transferee (and thus not the "initial transferee" under the Code) precisely because he lacked the legal authority to spend the funds in the manner he did. *Id.* at 19a-20a.

That conclusion has no basis in the Code's text. The Code defines "transfer" in the broadest possible terms to cover "each mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing or parting with * * * an interest in property." 11 U.S.C. 101(54)(D). That language plainly encompasses what took place here: Mr. Bello obtained the funds from Walldesign and placed them in the secret account, where he had unfettered control over them. As the first person to receive a "transfer" of Walldesign's funds, Mr. Bello was plainly the "initial transferee of such transfer." See 11 U.S.C.

550(a)(1); cf. *Reves* v. *Ernst & Young*, 507 U.S. 170, 177-178 (1993) (giving two instances of the same word in a statutory phrase a similar construction where the word was used once as a verb and once as a noun).

The text itself is dispositive here; indeed, just this Term, the Court reiterated the supremacy of statutory language in interpreting the Code. See *Merit Management Group, LP* v. *FTI Consulting, Inc.*, No. 16-784, slip op. 11, 14, 18 (Feb. 27, 2018). But the Code's legislative history confirms that Congress intended the term "transfer" to be "as broad as possible." S. Rep. No. 989, 95th Cong., 2d Sess. 27 (1978). Congress sought to encompass "any transfer of an interest in property * * * , including a transfer of possession, custody, *or control even if there is no transfer of title*." *Ibid.* (emphasis added). As is clear from the statutory language, the Ninth Circuit's requirement that there be a transfer of legal title, regardless of the control exercised by the recipient of the funds, is patently erroneous.

Unable to root its crabbed reading in the text or history of the Code, the Ninth Circuit did not even try. To the contrary, it candidly acknowledged that applying the dominion test could lead courts to "lose track of the original question proposed by the statute—namely, whether a party is a transferee." App., *infra*, 10a (citation omitted). But in light of prior circuit precedent adopting the dominion test, the Ninth Circuit refused to come to grips with the statutory language, going so far as to reject as "misplaced" any "reliance on the meaning of 'transfer' in [Section] 101(54)(D)." *Ibid.* The court viewed itself bound to follow the dominion test in the absence of "Supreme Court (or en banc) precedent." *Id.* at 24a.

2. Not only was the Ninth Circuit's test wholly unmoored from the statutory language; it lacked any valid

justification in policy (or common sense). Courts originally excluded certain initial recipients of funds from the definition of "transferee" as a functional means of avoiding the inequitable results that would occur if innocent financial intermediaries were deemed initial transferees. See, *e.g., Bonded Financial Services*, 838 F.2d at 893-895; *Harwell*, 628 F.3d at 1322-1324 (citing *In re Chase & Sanborn Corp.*, 848 F.2d 1196, 1199-1202 (11th Cir. 1988)). As one commentator observed, "[d]espite the clear, plain, and unambiguous language of the statute, courts have purposefully ignored its plain language to refrain from imposing liability on initial transferees that are considered 'mere conduits' of transferred property." Craig H. Averch, *Protection of the 'Innocent' Initial Transferee of an Avoidable Transfer: An Application of the Plain Meaning Rule Requiring Use of Judicial Discretion*, 11 Bankr. Dev. J. 595, 596 (1995) (Averch).

Whatever the propriety of that exception as an original matter, extending it to these facts does not serve, and in fact disserves, the exception's purpose. It would be the height of inequity to apply the exception to protect a corporate fraudster from initial-transferee status while subjecting innocent individuals to potentially ruinous liability as initial transferees. Yet that is exactly what the decision below does. The Ninth Circuit acknowledged that its approach elevated "form over substance." App., *infra*, 21a. It would be one thing if, by "form," the Ninth Circuit meant that it was simply applying the language of a statute. But it defies all sense to apply a judge-made exception, born of practical, equitable considerations, to reach inequitable results in the name of "formality." The Ninth Circuit's reasoning is deeply flawed; its outcome is profoundly unfair; and its decision demands this Court's review.

**C. The Question Presented Is Exceptionally Important And Warrants Review In This Case**

The question presented in this case is of exceptional legal and practical importance, yet it rarely reaches the courts of appeals. This case, which cleanly presents the question, is an optimal vehicle for the Court's review.

1. As an initial matter, the existence of disparate rules for who qualifies as an initial transferee under the Bankruptcy Code is of enormous practical importance. Resolution of the question presented could affect millions of Americans and vast sums of money.

More than 750,000 individuals or entities file for bankruptcy every year. United States Courts, *Business and Nonbusiness Bankruptcy County Cases Commenced, by Chapter of the Bankruptcy Code*, tbl. F-5A (Dec. 31, 2017) <tinyurl.com/bankruptcycasetable2017>. A typical bankruptcy proceeding implicates a number of third parties who may be "transferees" of fraudulent or otherwise avoided transfers. And it is not unusual for a corporate bankruptcy to present the very fact pattern presented here, where innocent recipients of funds misappropriated by corporate insiders seek to avail themselves of Section 550(b)(1)'s safe harbor but cannot do so unless the insiders are deemed initial transferees. See, *e.g.*, *In re Catco Recycling, LLC*, Civ. No. 15-1012, 2016 WL 556173, at *11 (D.N.H. Feb. 10, 2016); *In re Regency International Flooring, LLC*, Civ. No. 09-1146, 2010 WL 4053982, at *5-*6 (W.D. Mich. Oct. 14, 2010); *In re Global Protection USA, Inc.*, 546 B.R. 586, 620-622 (Bankr. D.N.J. 2016).

2. In addition, the conflict in the lower courts on this important question contravenes the necessary uniformity in the interpretation and application of the bankruptcy laws. By virtue of the conflict, parties in different jurisdictions face divergent rules as to whether they constitute initial transferees.

Uniform interpretation, however, is fundamental to the proper administration of the Code. The Constitution itself acknowledges the importance of uniformity in bankruptcy law, granting Congress the power "[t]o establish * * * uniform Laws on the subject of Bankruptcies throughout the United States." U.S. Const. Art. I, § 8, cl. 4; see *Railway Labor Executives' Association* v. *Gibbons*, 455 U.S. 457, 471-472 (1982). The power to create a uniform system was considered necessary, *inter alia*, to "secur[e] equality of rights and remedies among the citizens of all the states." 3 Joseph Story, *Commentaries on the Constitution of the United States* § 1102, at 6 (1833). This Court therefore routinely grants certiorari to resolve conflicts among the courts of appeals, even shallow ones, concerning the correct interpretation or application of provisions of the Code. See, *e.g.*, *Merit Management Group*, No. 16-784, slip op. 9; *Husky International Electronics, Inc.* v. *Ritz*, 136 S. Ct. 1581, 1585 (2016); *Baker Botts L.L.P.* v. *ASARCO LLC*, 135 S. Ct. 2158, 2162-2163 (2015); *Clark* v. *Rameker*, 134 S. Ct. 2242, 2244 (2014); *Bullock* v. *BankChampaign, N.A.*, 133 S. Ct. 1754, 1758 (2013); *Hall* v. *United States*, 566 U.S. 506, 508, 511 & n.1 (2012).

The discord on the question presented is especially acute given several courts' adoption of the dominion test. As the opinions below illustrate, see App., *infra*, 26a-29a; *id.* at 34a-37a (Nguyen, J., dissenting), applying the dominion test often requires courts to parse the intricacies of state law to determine whether a recipient had sufficient legal authority over the funds at issue. As Judge Nguyen noted in her dissent, that task is often "difficult" and can lead to "disagreement[s]" premised on varying interpretations of state law. *Id.* at 33a. The reliance on state law can lead to divergent results for transferees

even within a circuit that applies the dominion test, amplifying the disuniformity caused by the circuit conflict as to which test to use in the first place.

3. This case is an optimal vehicle for resolving the circuit conflict. It readily satisfies the standard criteria for certiorari: the relevant facts are undisputed and the question presented was raised and passed upon below. Indeed, the court of appeals examined the question in depth, expressly recognizing the circuit conflict on the question, and the arguments on both sides of the question are thoroughly developed in the majority and dissenting opinions. Nothing impedes the Court's resolution of the question presented in this case.

There is no legitimate reason to wait before resolving the widely recognized and well-developed conflict.[*] Although the question presented arises often in bankruptcy cases, see p. 19, *supra*, it reaches the courts of appeals relatively rarely. That is unsurprising. As one commentator has explained, "[t]he nature of bankruptcy cases tends to discourage further appellate review in the Article III courts because of the twin concerns of delay and cost associated with prolonged litigation." Troy A. McKenzie, *Judicial Independence, Autonomy, and the Bankruptcy*

[*] Numerous commentators have noted the existence of the conflict. See, *e.g.*, Jessica D. Gabel & Paul R. Hage, *Who Is a 'Transferee' Under Section 550(a) of the Bankruptcy Code?: The Divide Over Dominion, Control, and Good Faith in Applying the Mere Conduit Defense*, 21 J. Bankr. L. & Prac. 47, 51 (Jan. 2012) (describing the "various tests" that "courts have adopted * * * to determine whether a recipient of a transfer should be deemed an initial transferee"); Lori V. Vaughan, *Eleventh Circuit: Good Faith Is Required for Mere-Conduit Defense to § 550(a)*, Am. Bankr. Inst. J. 36, 77 (Mar. 2011) (discussing the "split among the circuits" as to the proper interpretation of "initial transferee"); Averch 605-615 (identifying the various approaches courts have taken to interpret the phrase "initial transferee").

*Courts*, 62 Stan. L. Rev. 747, 782 (2010). Over an eight-year period, for example, only one out of every 1,580 bankruptcy cases reached the courts of appeals, compared to one in every 12 non-prisoner civil suits. *Id.* at 783-784. And despite the many bankruptcy filings each year, bankruptcy appeals represent only 1.25% of all appeals filed in the regional circuits; including business bankruptcies, there are now fewer than 800 bankruptcy appeals per year, on any issue, in the entire country. See United States Courts, *Judicial Facts and Figures 2016*, tbl. 2.3 <tinyurl.com/factsandfigures2016>.

Accordingly, although the circuit conflict on the question presented has existed for some time, that question reaches the court of appeals level only rarely, and it reaches this Court even less often: our research indicates that the last petition for certiorari on the meaning of "initial transferee" was filed more than twenty years ago. See *Christy* v. *Alexander & Alexander of New York, Inc.*, No. 97-1400, cert. dismissed, 524 U.S. 912 (1998). There is thus considerable uncertainty about when the Court would have another opportunity to resolve the question, if at all, if it denies review here.

* * * * *

In sum, the Ninth Circuit's erroneous decision reinforces an entrenched and widely recognized conflict on the question whether a person who obtains funds from a debtor must have legal authority over the funds to qualify as an "initial transferee" within the meaning of Section 550(a)(1) of the Bankruptcy Code. That is an important and recurring question, and this case is the ideal vehicle for resolving it. Further review is plainly warranted.

**CONCLUSION**

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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