

THIS OPINION IS NOT INTENDED
FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

FILED
02 JUL 25 PM 3:40

U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
CLEVELAND

In re:) Case No. 00-10145
)
THE V COMPANIES and) Chapter 7
V-S ARCHITECTS, INC.,) Jointly Administered
)
Debtors.) Judge Pat E. Morgenstern-Clarren
)
) **MEMORANDUM OF OPINION**

Virgil E. Brown, Jr., the Chapter 7 Trustee in these jointly administered cases, seeks authority to: (1) assume and assign executory contracts to Mayfield Engineering and Construction Management, Inc. ("Mayfield"); (2) sell assets to Mayfield free and clear of liens and encumbrances; and (3) enter into a compromise with Independence Bank. (Docket 485, 492). MWH Americas, Inc. ("MWH") objects to part of that request. (Docket 493). For the reasons stated below, the Trustee's motion is granted.¹

JURISDICTION

The Court has jurisdiction to hear this matter under 28 U.S.C. § 1334 and General Order No. 84 entered by the United States District Court for the Northern District of Ohio. This is a core proceeding under 28 U.S.C. § 157(b)(2).

FACTS

The Court held an evidentiary hearing on this matter on June 18, 2002. The Trustee supported his motion with the testimony of V. Michael Raig, who is the president and sole

¹ Initially, the Trustee also sought to assume and assign a contract with Specialty Restaurants Corporation. When that entity objected, the Trustee withdrew the contract from this motion, making the objection moot. (Docket 494). Gannett Fleming Engineers & Architects PC also objected to the Trustee's motion, but the parties resolved that by an agreement that was read into the record. (Docket 481).

THIS OPINION IS NOT INTENDED
FOR PUBLICATION

shareholder of Mayfield, and exhibits. MWH offered the testimony of Robert Frutchee, its vice president, in support of its objection. Additionally, the Court notified the parties at that time that it would take judicial notice of the case file in deciding this matter. FED. R. EVID. 201(c) and (e).

The Motion to Assume and Assign

Debtors The V Companies (“V Co.”) and V-S Architects, Inc. filed Chapter 11 cases on January 7, 2000 and continued to operate their architectural and engineering business until March 8, 2002, when the cases were converted to Chapter 7 on motion of the United States Trustee and the Board of County Commissioners of Jefferson County, Ohio.

The Chapter 7 Trustee initially filed a motion for authority to assume and assign certain executory contracts (including the MWH contract) and to sell certain assets to Mayfield free and clear of liens and encumbrances. (Docket 454). That motion presupposed that secured lender Independence Bank (the “Bank”) would consent to the transaction and provide a release of its lien rights. (Docket 454 at 9). MWH and the Bank, however, both objected to the motion. (Docket 470, 471).

The evidentiary hearing scheduled for April 26, 2002 to consider the motion and objections did not go forward because Mayfield did not yet have the required financing commitment or insurance. Instead, the Trustee, MWH, and the Bank engaged in discussions at that time which resulted in settlement proposals. The hearing was concluded to allow the Trustee to file a new motion that would incorporate these anticipated agreements. The agreements, however, fell through.

The Trustee then took a slightly different approach. On May 31, 2002, he filed the motion currently under consideration in which he requests authority to assume and assign six executory contracts and to sell certain assets to Mayfield. The six contracts involve these

THIS OPINION IS NOT INTENDED
FOR PUBLICATION

projects: the Cleveland PEP 6053 project (with MWH); the Joy Park Homes project (with Akron Metropolitan Housing Authority); the Berea Underpass project (with Gannett Fleming Engineers and Architects, P.C.); the Mayfield Heights City Hall project (with City of Mayfield Heights); the Euclid Family House project (with Gateway Health Care Centres Limited Partnership); and the Bingham Building (with Case Western Reserve University). The sale assets include the Debtors' intellectual property and goodwill (including all prospective work which they had been pursuing), as well as their customer and client lists, telephone, fax, and cell phone numbers. The Trustee also moves to compromise his claims against the Bank as part of the proposed assignment and sale transaction, with the Bank then consenting to the transaction. At this point, MWH is the only objecting party.

The Contract Between MWH and V Co.

MWH has a consulting contract with the City of Cleveland, Ohio to provide engineering and construction program management services to rehabilitate and upgrade the city's water plants. That contract is not in evidence. On July 1, 1997, MWH entered into its own contract with V Co., under which V Co. agreed to act as a subconsultant for MWH on the Cleveland PEP 6053 project (the "Contract"). (Trustee Exh. 9).

V Co. performed under its Contract with MWH until the Chapter 11 cases were converted. Since the conversion, MWH has taken over V Co.'s role and will not consent to the assignment of the Contract because it wants to continue to serve in that role. MWH has offered to purchase the Contract from the Trustee for \$125,000.00, with \$50,000.00 to be paid immediately and the balance on January 3, 2003.

As of the hearing date, MWH was performing V Co.'s part of the Contract using the services of Jay Harris, a former V Co. employee familiar with the project, and other individuals

THIS OPINION IS NOT INTENDED
FOR PUBLICATION

who had worked on the project for V Co. as independent contractors. Mr. Frutchey of MWH expressed general concern regarding Mayfield's ability to perform the services required under the Contract if the Contract is assigned to Mayfield, based on its lack of staff. However, he expressed faith and confidence in the former V Co. people who are working on the Contract currently. He also testified that MWH's contract with the City was awarded under a competitive procurement process requiring approval of the City and the Board of Control.

The Contract (between the Debtor and MWH) includes this provision:

SECTION VII. NON-TRANSFERABILITY

Subconsultant [V Co.] may not assign, sublet or transfer any part or all of its obligations under, or interest in and to, this Agreement except by approval of the Board of Control, the Director and [MWH]; if any such approval be given, the terms and conditions of this Agreement shall apply to and bind the party or parties to whom the Agreement is assigned, sublet, or transferred, as fully and completely as Subconsultant [V Co.] is hereunder bound.

The Contract also states:

SECTION VI. SPECIAL PROVISIONS

1. All subconsultants for the Program must be or have been authorized by the Board of Control prior to the execution of this Agreement to assist [MWH] in the completion of the Program.

* * *

3. Except as provided above, [MWH] or its subconsultant [V Co.] shall not sublet or subcontract nor shall any new or replacement Subconsultant commence performance of any part of the work or services included in this Agreement without prior written approval of the Division expressed by resolution of the Board of Control.

The Proposed Assignment and Sale to Mayfield

The Trustee seeks to assign the six contracts and sell the assets to Mayfield for a maximum purchase price of \$146,000.00 under these terms:

THIS OPINION IS NOT INTENDED
FOR PUBLICATION

Purchase Price. [Mayfield] agrees to pay the Trustee \$86,000 upon the entry of the Order approving the assumption and assignment of the Assigned Contracts and the transfer of the Sale Assets. In addition to the initial \$86,000 payment, the Buyer will pay to the Trustee on a weekly basis the following: (a) an amount equal to three percent of the first \$1,000,000 of gross receipts paid to the Buyer . . . under the Assigned Contracts . . . ; (b) an amount equal to 2 percent of the second \$1,000,000 of gross receipts paid to the Buyer . . . under the Assigned Contracts . . . ; and (c) an amount equal to one percent of the third \$1,000,000 of gross receipts paid to the Buyer . . . under the Assigned Contracts[.]

Mayfield would only proceed with the proposed agreement if the Trustee requested the assignment of all six contracts.

Mayfield is a construction management service company which was incorporated in March 2002 after the Debtors' Chapter 11 cases were converted to Chapter 7. V. Michael Raig, a vice president of V Co. and the individual formerly responsible for its daily operations, is the sole shareholder and president of Mayfield. (Docket 492).

As a start-up company, Mayfield does not have paid employees, work in progress, or assets. It has, however, arranged a \$200,000.00 line of credit with the Bank and carries general liability, automobile liability, and professional liability insurance in amounts which equal or exceed the limits required by the six contracts.

Raig is familiar with the six contracts because he helped negotiate them for the Debtors and hired the individuals who worked on them. V Co. performed its Contract services using a small group of individuals and Raig anticipates that Mayfield will be able to perform under the Contract by using those same people. Several of those individuals are currently working on the Contract for MWH as independent contractors and he believes their services will become available to Mayfield in the event it is authorized to assume the Contract. Alternatively, Raig

THIS OPINION IS NOT INTENDED
FOR PUBLICATION

believes he can staff the project by drawing from a pool of individuals with whom he has dealt in the past.

Raig expects that Mayfield will also win other contracts that the Debtors were pursuing during the Chapter 11 phase of these cases. He has prepared relatively simple cash flow projections for Mayfield's proposed performance under the six contracts at issue, which projections anticipate a positive cash flow. (Trustee Exh. 4). MWH questioned Raig's credentials for preparing such projections, but did not establish any significant way in which they were unreliable or incorrect.

Raig has spoken with the Cleveland Water Commissioner regarding the proposed assignment to Mayfield and he feels the city supports it, although he has not requested city approval of the assignment. The city was served with the motion at issue and has not objected to it.

The Proposed Compromise with the Bank

The Bank filed a proof of claim in the amount of "not less than \$907,568.76" which is secured by a lien or security interest in substantially all of both Debtors' personal property, including the executory contracts and assets which the Trustee seeks to assign and sell at this time. (Docket 471, Exh. A). The Final Cash Collateral Order entered on March 20, 2000 (in connection with the Debtors' use of the Bank's cash collateral) grants the Bank a lien or security interest in certain postpetition collateral and provides for the immediate termination of the automatic stay in the event of a default. (Docket 75). The conversion to Chapter 7 constituted a default under that Order.

The Trustee cannot move forward with this motion unless the Bank waives its lien and security interest related to the contracts and assets which the Trustee seeks to transfer to

THIS OPINION IS NOT INTENDED
FOR PUBLICATION

Mayfield. In recognition of this, the Trustee has reached a settlement which the Bank which provides for this waiver and resolves any potential claims the Trustee may have against the Bank, including avoidance claims and subordination. The proposed settlement includes these terms:

- (1) the Bank is to retain all funds which the Debtors have on deposit with it (\$54,526.18 as of 5/31/02);
- (2) the Trustee and the Bank are to split certain proceeds from the Debtors' accounts receivables with the Trustee;
- (3) the Trustee will pay the Bank 75% of all funds which he hold or receives that are defined as the Bank's prepetition or postpetition collateral under the Final Cash Collateral Order;
- (4) the Debtors' tax refunds which are attributable to periods before March 8, 2002 are to be split, with the Trustee receiving 25% and the Bank receiving 75%;
- (5) the Trustee will release the Bank from any and all claims relating to the Debtors and their estates; and
- (6) the Trustee will waive any right to seek to surcharge the Bank for the costs and expenses of administration.

DISCUSSION

The Trustee's motion asks for several kinds of relief: (1) authority to assume and assign the executory contracts to Mayfield; (2) authority to sell assets to Mayfield; and (3) approval of the Bank compromise. MWH filed a written objection to the initial motion. (Docket 470). By the time that the evidentiary hearing went forward on the motion now under consideration, MWH had changed counsel and new counsel adopted the previously-filed objection. (Docket 493). That objection challenges Mayfield's competency and financial ability to perform under the Contract and also asks whether the business judgment standard supports the Trustee's decision. At the evidentiary hearing, MWH questioned whether the Contract could be assigned without

THIS OPINION IS NOT INTENDED
FOR PUBLICATION

consent and also raised vague concerns about the process by which the Trustee reached his compromise with the Bank. MWH did not provide case law in support of these additional grounds.

Assumption and Assignment of the Contracts

Bankruptcy Code § 365 governs the assumption and assignment of executory contracts. 11 U.S.C. § 365. That section states that a trustee may assume an executory contract subject to court approval. 11 U.S.C. § 365(a). A trustee's decision to assume such a contract is reviewed by asking whether the trustee used appropriate business judgment in deciding whether it would be beneficial or burdensome to the Chapter 7 estate to assume it. *Orion Pictures Corp. v. Showtime Networks, Inc. (In re Orion Pictures Corp.)*, 4 F.3d 1095, 1099 (2d Cir. 1993). Section 365(f)(2) provides that a trustee may assign an assumed contract if adequate assurance of the assignee's future performance is provided. 11 U.S.C. § 365(f)(2).

MWH objects to the assignment of its Contract based on a lack of information about Mayfield's ability to perform the requisite services and its financial wherewithal. The Trustee has, however, provided adequate assurance of Mayfield's future performance under the Contract. Although Mayfield is a start-up company, Raig (its president) is familiar with the Contract and his testimony established that Mayfield has obtained the requisite insurance and has adequate financial means. With respect to staffing and performance, it appears that the workers with knowledge of the Contract are taking a pragmatic approach and are likely to work for and with whichever entity ends up with the Contract. If not, Raig's testimony that an alternative pool of skilled workers is available was not effectively challenged.

MWH also argues that the Trustee's decision to assign the Contract to Mayfield is not a proper exercise of business judgment because MWH has offered to purchase the Contract for

THIS OPINION IS NOT INTENDED
FOR PUBLICATION

\$125,000.00 and that offer is the highest and best offer. This argument fails. A review of the file and the history of this motion shows that the Bank has a lien on this Contract, among other assets. The Bank and the Trustee have had a number of disagreements on various issues. The Trustee cannot assign the Contract without the Bank's consent and the Bank has consented in the context of an overall settlement of the disputes between the parties. There is, therefore, a sufficient showing by the Trustee that he properly exercised his business judgment in choosing a buyer whose purchase offer also meshed with the Trustee's desire to settle all claims with the Bank. There is logic behind this decision and the Court will not second-guess the Trustee's judgment in this regard.

Finally, MWH argues that its Contract is a public contract and the Trustee may not assign it to Mayfield without consent. This argument was first raised at the hearing and MWH did not provide briefing or legal authority in support. In any case, the argument is unavailing. Sections 365(f)(1) and (c)(1) establish a trustee's ability to assign a contract. Under § 365(f):

(f)(1) Except as provided in subsection (c) of this section, notwithstanding a provision in an executory contract . . . or in applicable law, that prohibits, restricts, or conditions the assignment of such contract . . . , the trustee may assign such contract . . . under paragraph (2) of this subsection[.]

11 U.S.C. § 365(f)(1). Under § 365(f)(1) "a general prohibition against the assignment of executory contracts, *i.e.*, by contract or 'applicable law,' is ineffective against the trustee."

Rieser v. Dayton Country Club Co. (In re Magness), 972 F.2d 689, 695 (6th Cir. 1992). There are, however, certain circumstances in which a trustee may not assign an executory contract:

- (c) The trustee may not assume or assign any executory contract . . . of the debtor, whether or not such contract . . . prohibits or restricts assignment of rights or delegation of duties, if –

THIS OPINION IS NOT INTENDED
FOR PUBLICATION

(1)(A) applicable law excuses a party, other than the debtor, to such contract . . . from accepting performance from or rendering performance to an entity other than the debtor or the debtor in possession, whether or not such contract . . . prohibits or restricts assignment of rights or delegation of duties; and

(B) such party does not consent to such assumption or assignment[.]

11 U.S.C. § 365(c)(1). Therefore, “if the attempted assignment . . . will impact upon the rights of a non-debtor third party, then any applicable law protecting the right of such party to refuse to accept from or render performance to an assignee will prohibit assignment by the trustee.” *In re Magness*, 972 F.2d at 695. The issue is whether applicable law (other than law generally prohibiting assignments) excuses MWH from accepting the performance of Mayfield under the Contract.

MWH argues that the assignment is not appropriate because the Contract is a public contract. This characterization does not, however, preclude its assignment. First, while the City of Cleveland may be interested in the Contract based on its agreement with MWH, it is not a party to the Contract. Second, there is no general prohibition against the assignment of public contracts under Ohio law. *See Ernst v. Kunkle*, 5 Ohio St. 520 (Ohio S.Ct. 1856). To the contrary, Ohio law generally provides that contracts are assignable. *See Bricker v. Am. Ins. Union*, 16 Ohio Law Abs. 469 (Ohio App. Ct. 1933). The exception is “personal contracts, or contracts in which the personality of one of the parties is material, [which contracts] are not assignable.” *Starchroom Publ’g Co. v. Threlkeld Engraving Co.*, 13 Ohio App. 281 (Ohio App. Ct. 1920). Whether a contract is personal depends on the intention of the parties as indicated by the language used in the contract and the nature of the contract. *Id.* Even if the kind of contract at issue might potentially come within the description of a personal contract (which MWH did

THIS OPINION IS NOT INTENDED
FOR PUBLICATION

not prove and the Court is not finding), MWH did not present sufficient evidence to support a finding that this particular Contract falls within this category. Ohio law does not, therefore, prohibit the assignment of the Contract.

Sale of the Debtors' Assets

Bankruptcy Code § 363(b)(1) provides that a trustee may sell estate property after notice and a hearing. 11 U.S.C. § 363(b)(1). The primary issue is whether there is a business justification for the transaction. *See In re Bakalis*, 220 B.R. 525, 532 (Bankr. E.D.N.Y. 1998). *See also Stephens Indus., Inc. v. McClung*, 789 F.2d 386 (6th Cir. 1986) (discussing § 363(b) sales in the context of Chapter 11). A Chapter 7 trustee's business judgment must be exercised in connection with his duty to maximize value for the estate. *In re Bakalis*, 220 B.R. at 532.

The Trustee has a sound business justification for the proposed sale of assets to Mayfield and the transaction will maximize value for the estate. Authority to sell the assets is, therefore, granted.

Compromise with the Bank

A trustee who wishes to compromise a dispute must obtain court approval, again after notice and a hearing. FED. R. BANKR. P. 9019(a). The basic inquiry is whether the proposed compromise is fair and equitable. *Reynolds v. Comm'r of Internal Revenue*, 861 F.2d 469, 473 (6th Cir. 1988). "In considering a proposed compromise, the bankruptcy court is charged with an affirmative obligation to apprise itself of the underlying facts and to make an independent judgment as to whether the compromise is fair and equitable. The court is not permitted to act as a mere rubber stamp or to rely on the trustee's word that the compromise is 'reasonable'." *Reynolds*, 861 F.2d at 473 (citing *In re American Reserve Corp.*, 841 F.2d 159, 162-63 (7th Cir.

THIS OPINION IS NOT INTENDED
FOR PUBLICATION

1987)). “Basic to this process in every instance, of course, is the need to compare the terms of the compromise with the likely rewards of litigation.” *Protective Comm. for Indep. Stockholders of TMT Trailer Ferry, Inc. v. Anderson*, 390 U.S. 414, 424-425 (1968).

In making this determination, courts consider “the complexity, expense, and likely duration of such litigation, the possible difficulties of collecting any judgment which might be obtained, and all other factors relevant to a full and fair assessment of the wisdom of the proposed compromise.” *Anderson*, 390 U.S. at 424. The factors to be examined include: (1) the probability of success in the litigation; (2) the difficulty of collection; (3) the complexity of the litigation, including any attendant expense, inconvenience, and delay; and (4) the paramount interest of creditors. *Fishell v. Soltow (In re Fishell)*, 47 F.3d 1168 (6th Cir. 1995) (unpublished table decision) (citation omitted); *Myers v. Martin (In re Martin)*, 91 F.3d 389 (3d Cir. 1996).

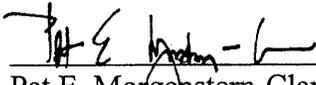
No party filed an objection to the compromise. MWH did make a statement at the hearing to the effect that “We don’t know if they’re trying to sneak something by the Court,” but no explanation was offered and the reference was not clear enough to allow the Court to evaluate it further. Having independently reviewed the proposed compromise, the Court finds that it is fair and equitable, particularly because it benefits the estate, resolves sticky factual and legal issues without the necessity of prolonged litigation, and does so on terms that have not been substantively challenged.

THIS OPINION IS NOT INTENDED
FOR PUBLICATION

CONCLUSION

For the reasons stated, the Trustee's motion is granted. A separate Order will be entered reflecting this decision.

Date: 15 July 2002



Pat E. Morgenstern-Clarren
United States Bankruptcy Judge

Served by mail on: Alan Lepene, Esq.
Alexander Jurczenko, Esq.
Harry Wright, IV, Esq.
Harry Greenfield, Esq.
Bruce Rinker, Esq.
Lenore Kleinman, Esq.

By: Joyce L. Gordon, Secretary

Date: 7/25/02