

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

In re:	)	Chapter 11
	)	
CD LIQUIDATION CO., LLC, <i>et al.</i> ,	)	Case No. 09-13038 (KG)
	)	
Debtors.	)	Substantively Consolidated
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CHARLES M. MOORE, as trustee of	)	
the CD LIQUIDATION TRUST,	)	Adv. Proc. No. 11-51636 (KG)
	)	
Plaintiff,	)	
	)	
vs.	)	
	)	
JOHN MARTILLO,	)	
	)	
Defendant.	)	<b>Re: Docket No. 51</b>
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**MEMORANDUM ORDER**

The Court has before it Defendant John Martillo’s (the “Defendant” or “Martillo”) Motion for Summary Judgment on Certain Counts and to Dismiss Certain Counts of the Amended Complaint (the “Second Dismissal and Summary Judgment Motion”) (D.I. 51) and the Trustee’s Brief in Response to John Martillo’s Motion for Summary Judgment on Certain Counts and to Dismiss Certain Counts of the Amended Complaint (the “Trustee’s Response”) (D.I. 57). A hearing on the Second Dismissal and Summary Judgment Motion was held on March 12, 2012 (the “Hearing”). At the beginning of the Hearing, counsel for the Trustee informed the Court that on Friday, March 9, 2012, after the close of business, he filed a Motion for Leave to Amend First Amended Complaint and to file a Second Amended Complaint (the “Motion to Amend”) (D.I. 84). The Trustee did not show the courtesy to notify the Court of its filing until argument and thereby allowed the Court to prepare for an argument without knowledge of the Trustee’s allegations.

Because of the Trustee's inaction with regard to discovery, and the Second Amended Complaint which the Court has not yet authorized, the Court is not in a position to issue a ruling on the Second Dismissal and Summary Judgment Motion. As a result, as set forth in more detail herein, the Court is allowing the Trustee to conduct limited discovery described herein. At the conclusion of the discovery and supplemental briefing, the court will decide the Second Dismissal and Summary Judgment Motion.

### **JURISDICTION**

The Court has jurisdiction over this adversary proceeding pursuant to 28 U.S.C. §§ 157 and 1334. This is a core proceeding under 28 U.S.C. § 157(b)(2). Venue is proper pursuant to 28 U.S.C. §§ 1408 and 1409.

### **BACKGROUND**

The Court finds it necessary to recite at length the timeline of docket entries to illustrate the procedural morass the Trustee's inaction and belated action have created. This litigation gamesmanship has placed this Court, and the parties, in an unusual and awkward procedural posture in relation to the Second Dismissal and Summary Judgment Motion.

- The Trustee filed his original Complaint on March 28, 2011 (D.I. 1).
- On July 29, 2011, Martillo filed his Motion for Summary Judgment on Redemption Claims and to Dismiss the Remaining Claims (the "Original Summary Judgment Motion"), seeking dismissal of all eight counts of the Trustee's original Complaint. In the Original Summary Judgment Motion, Martillo asserted that the prepetition redemption transactions that liquidated his interest in the Debtors were exempted from avoidance under 11 U.S.C. § 546(e) (the "Bankruptcy Code") as settlement

payments that were made by or to a financial institution.

- In response, the Trustee filed an amended complaint against Martillo amending some counts and asserting ten additional counts (the “First Amended Complaint”) (D.I. 35). The Trustee omitted reference to Bankruptcy Code § 544 in an effort to argue that the claims were brought separately under state law, not § 544, and therefore were not barred by § 546(e).
- In response to the Amended Complaint, on October 12, 2011, Martillo filed the Second Dismissal and Summary Judgment Motion.
- On November 23, 2011, the Trustee filed The Trustee’s Response.
- On December 23, 2011, Martillo filed his Reply Brief in Support of his Second Dismissal and Summary Judgment Motion (“Martillo’s Reply Brief”) (D.I. 59).
- On December 30, 2011, Martillo filed a Notice of Completion of Briefing on the Second Dismissal and Summary Judgment Motion (the “Notice of Completion of Briefing”) (D.I. 62).
- After briefing was completed, on January 19, 2012, the Trustee filed a Motion for Leave to File Surreply Brief to Reply Brief in Support of Martillo’s Motion for Summary Judgment on Certain Counts and to Dismiss Certain Counts of the Amended Complaint (the “Surreply Motion”) (D.I. 64). In conjunction with the Surreply Motion, the Trustee filed a Declaration in Support of the Surreply Motion (the “Surreply Declaration”) (D.I. 65).
- On February 2, 2012, Martillo filed an Objection to Liquidation Trustee’s Motion for Leave to File a Sur-Reply (the “Surreply Objection”) (D.I. 67).

- On February 22, 2012, the Trustee filed a Declaration Pursuant to Fed. R. Civ. P. 56(d) (the “Rule 56(d) Declaration”) (D.I. 71).
- On February 23, 2012, Martillo filed his Objection to and Motion to Strike the Trustee’s Declaration Pursuant to Fed. R. Civ. P. 56(d) and Cross Motion for Leave to File Declaration (the “Motion to Strike”) (D.I. 72).
- On March 6, 2012, the Trustee filed a Brief in Opposition to the Motion to Strike (D.I. 77).
- On March 7, 2012, Martillo filed a Reply in Support of his Motion to Strike (D.I. 78).
- On March 9, 2012, this Court entered an order granting Martillo’s Motion to Strike (D.I. 83).
- On March 9, 2012, the Trustee filed the Motion to Amend.
- On March 12, 2012, the Hearing went forward.

### **DISCUSSION**

On March 12, 2012, the Court had scheduled and was prepared to hear oral argument on Martillo’s Second Dismissal and Summary Judgment Motion and those matters that were properly noticed and presented in the Notice of Completion of Briefing. Notwithstanding these parameters and the Court’s preparation and reasonable expectations, at the Hearing the Trustee’s counsel informed the Court that on the eve of the Hearing, he filed a Motion for Leave to File Second Amended Complaint and Incorporated Memorandum of Law (D.I. 84). Subsequently, the Trustee’s oral argument on the Second Dismissal and Summary Judgment Motion referenced facts and evidence that were not before the Court. Specifically, at the Hearing the Trustee argued (as set forth in his Rule 56(d) Declaration) that the redemption transactions that cashed out Martillo’s interest in

the Debtors were not shielded by the 11 U.S.C. § 546(e) settlement payments exception because § 546(e) does not apply to settlement payments that were made with actual intent to hinder, delay, or defraud creditors under 11 U.S.C. § 548(a)(1)(A).<sup>1</sup> Additionally, at the Hearing, the Trustee's counsel alleged and relied on factual statements contained within the Trustee's previously stricken Rule 56(d) Declaration, specifically that the Debtors fraudulently inflated their EBITDA figures to various lenders to obtain the funds needed to cash out Martillo's shares. Moreover, at the Hearing, the Trustee attempted to present the Court with information contained in the untimely filed Surreply which the Court had stricken. This included an October 24, 2007, Memorandum (the "Memorandum")<sup>2</sup> that purportedly details the steps that would be taken to effectuate a reorganization

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<sup>1</sup> After completion of briefing, the Trustee raised the § 548(a)(1)(A) defense to the § 546(e) settlement payments exception. The Court finds it necessary to note that Count I of the First Amended Complaint, which is at issue in the Second Dismissal and Summary Judgement Motion, does not specify whether the Trustee is bringing that Count under § 548(a)(1)(A) (actual fraud), which would be an exception to the settlement payments doctrine, or under § 548(a)(1)(B) (constructive fraud) to which the exception does not apply. At the hearing the Trustee's counsel admitted as much, and that the First Amended Complaint is not clear which subsection of § 548 the Trustee was pursuing. Although the Court does not believe that the Trustee was required to use the magic words of § 548(a)(1)(A) "made such transfer . . . with actual intent to hinder, delay, or defraud any entity . . .", the Court does believe that at the very least, the Trustee is required to adequately plead whether he is pursuing a theory of actual fraud or constructive fraud against Defendant and at the very least should have specified which subsection of § 548 the Trustee is raising. The reason, of course, is that depending on which avenue the Trustee pleads determines which defenses are available to the Defendant, including, in this case, the § 546(e) settlement payments doctrine. Fundamental fairness requires that a Defendant be put on notice of the claims being asserted against him or her and based on those claims, what potential defenses are available to the Defendant. By proceeding in this manner, and ambiguously pleading a claim under § 548 (without specifying actual or constructive fraud) in Count I, the Trustee is playing "Alphonse and Gaston," to the clear and unfair disadvantage of the Defendant. The Court recognizes that a Trustee is often at an informational disadvantage when bringing claims on behalf of the estate and that some flexibility may be warranted in certain situations; however, here, where discovery was available but not utilized, this disadvantage does not give the Trustee the flexibility to force the Defendant to litigate against a moving target.

<sup>2</sup> The Memorandum is attached as Exhibit A to the Trustee's Surreply.

of the Debtors while also cashing out Martillo's interest in the Debtors. The Trustee attempted to proffer the Memorandum as evidence that the liquidation of Martillo's interest was part of an orchestrated plan on the part of the Debtors, their principals and Martillo. In his reply argument, Martillo argued that the Memorandum simply details the steps that the Debtors' lenders required to accomplish the restructuring in order to retain the Debtors' tax beneficial status. Moreover, Martillo's counsel noted that Martillo was not involved in the Memorandum's creation nor was it sent to him.

In his untimely filed Surreply, his stricken Rule 56(d) Declaration<sup>3</sup> and at the Hearing, the Trustee's counsel argued that the Court should either deny the Second Dismissal and Summary Judgment Motion, or defer ruling on it until after discovery occurs because the case is still in its "infancy" and the Trustee should be given an opportunity to find and develop further facts that support his claims. The Trustee also urged the Court to grant the Motion to Amend at this time. As a preliminary matter, Fed. R. Civ. P. 56(b), made applicable through Fed. R. Bankr. Proc. 7056, provides that "a party may file a motion for summary judgment at any time until 30 days after the close of all discovery." The Court notes that the Trustee availed himself of Rule 2004 discovery in this adversary proceeding. Additionally, the Second Dismissal and Summary Judgment Motion has been fully briefed and argued and the Trustee had from July 29, 2011, the date Martillo filed the Original Summary Judgment Motion, to seek and take discovery. Notwithstanding the seven months since Martillo filed his Original Summary Judgment Motion, and the Trustee filed an Answering Brief, the Trustee sought discovery only a few weeks ago. It appears that the Trustee prefers to

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<sup>3</sup> The Court struck the Declaration because of its late filing and because it was, in reality, a brief rather than a declaration.

litigate by amendment whenever his case is threatened by his own lethargy.<sup>4</sup> Courts endeavor to adjudicate the issues before them based on the merits. There comes a time, however, when parties have an obligation to diligently assist the Court in this respect, which includes actively pursuing discovery when appropriate, and adhering to the rules for timely filing pleadings in this Court as set forth in the Federal Rules of Civil Procedure and this Court's Local Rules.

In an attempt to strike an appropriate balance between the Defendant's procedural rights and the Trustee's assertions that he requires discovery, the Court will permit the Trustee within 30 days of this Order to take and complete limited discovery relating to matters he alleged at the Hearing.

The limited discovery will consist of depositions of the senders and recipients of the Memorandum, and Martillo, limited strictly to the facts and circumstances giving rise to the Memorandum, i.e., Martillo's involvement in its preparation, the purpose and the like. Thereafter, the parties will file simultaneous briefs addressing the discovery results on or before May 7, 2012 and the Court will determine whether or not to hold additional argument. If the Trustee presents evidence sufficient to warrant the Court to deny the Second Dismissal and Summary Judgment Motion, the Court will then consider the Trustee's request to amend the First Amended Complaint. Martillo is first entitled to a ruling on the Second Dismissal and Summary Judgment Motion.

SO ORDERED.

Dated: March 23, 2012

  
KEVIN GROSS, U.S.B.J.

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<sup>4</sup> Trustee's counsel took offense at the Court's reference to the "murderer of parents/orphan" addage. It is appropriate. The Trustee is requesting the Court's "mercy" for difficulties caused by his actions and inaction.