IN THE UNITED STATES BANKRUPTCY COURT
FOR THE MIDDLE DISTRICT OF TENNESSEE
NASHVILLE DIVISION

In re:	)	
ORECK CORPORATION, et al.	)	Chapter 11
	)	Case No. 13-04006
565 Marriott Dr., Suite 300	)	Judge Lundin
Nashville, TN 37214	)	
Debtors.	)	(Jointly Administered)

DEBTORS' RESPONSE IN OPPOSITION TO THE MOTION FOR RELIEF FROM THE AUTOMATIC STAY OR, IN THE ALTERNATIVE, FOR CLASS CERTIFICATION FILED BY THE LEAD PLAINTIFFS AND PUTATIVE CLASS

Oreck Corporation; Oreck Direct, LLC; and Oreck Homecare, LLC (collectively the "Debtors") hereby file this response in opposition to the motion for relief from the automatic stay or, in the alternative, for class certification pursuant to Bankruptcy Rule 7023 [Docket No. 795] (the "Motion")[1] filed by certain "Lead Plaintiffs", on behalf of themselves and all others similarly situated, including without limitation, the class of persons and entities defined as the "Putative Class" and represented, or sought to be represented, in the consolidated class action entitled *In re: Oreck Corporation Halo Vacuum and Air Purifiers Marketing and Sales Practices Litigation*, pending in the United States District Court for the Central District of California, MDL Case No. 2:12-ML-02137-CAS-JEM (the "MDL Class Action"). For their response in opposition to the Motion, the Debtors state as follows:

INTRODUCTION

The United States Supreme Court long ago established that the fundamental purpose of the Bankruptcy Code is to provide a prompt and effectual administration and settlement of a debtor's estate within a limited time period. In order to achieve this goal, the Bankruptcy Code

[1] All capitalized terms not otherwise defined herein shall have the meaning ascribed to them in the Motion.

provides a streamlined procedure that centralizes all litigation involving the debtor in one forum to be adjudicated by the bankruptcy court in summary proceedings. These provisions for centralized claims resolution and avoidance of piecemeal litigation have been at the very core of the bankruptcy process since its inception in 1898.

To promote and enforce centralized claims resolution, the Bankruptcy Code provides for an automatic stay as of the filing of the bankruptcy petition, which requires a debtor's creditors to discontinue their actions or proceedings against the debtor and instead pursue their claims through the claims administration process within the bankruptcy forum. Given these fundamental policies and procedures codified within the Bankruptcy Code, bankruptcy courts routinely deny stay relief to creditors seeking to litigate their claims against the debtor in a non-bankruptcy forum. Absent special circumstances where the prejudice to the movant outweighs the prejudice to the debtor, creditors must adhere to the long-established procedures provided by the Bankruptcy Code and Bankruptcy Rules for claims allowance. Most often, these special circumstances are established where the debtor files bankruptcy on the eve of trial – which creates the unique situation where the non-bankruptcy court is actually in a position to provide a resolution more quickly and with less costs than the bankruptcy court.

However, no special circumstances exist so as to justify stay relief in this instance. The Lead Plaintiffs seek stay relief to pursue general unsecured claims in the MDL Class Action pending in the Central District of California, but the costs and burden of pursuing those claims in California decisively outweigh the benefits of handling the claims through the bankruptcy process. Importantly, the MDL Class Action was in its infant stages at the time of the Debtors' bankruptcy filing – a scheduling order had not even been entered or discovery commenced – so

the long process of class-certification and merits discovery has not begun. Accordingly, there the MDL Class Action is procedurally immature to warrant stay relief.

The Lead Plaintiffs' general unsecured claims do not involve the kind of unique circumstances that justify stay relief. Instead of disrupting this bankruptcy, the Lead Plaintiffs should be required to pursue their claims through the claims administration process provided by the Bankruptcy Code just as all of the other creditors are required to do. In any event, the Lead Plaintiffs should not be allowed to impose substantial costs on scarce estate resources by pursuing class certification. Rule 23's class action procedures are too expensive in this liquidation case, and the advantages that Rule 23 can provide in cases outside of bankruptcy disappear in this case, where claims administration makes class certification superfluous.

In that same vein, the Court should deny the alternative relief sought by the Lead Plaintiffs. The Court should not allow the Lead Plaintiffs to pursue a Class Proof of Claim under Bankruptcy Rue 7023 because the costs and burdens of class action procedures make class procedures inferior to using the standard bankruptcy claims process. Litigating class issues under Bankruptcy Rule 7023 would impose an expensive and time-consuming overlay onto the bankruptcy process, as the class claims the Lead Plaintiffs seek to pursue are simply too small to justify the time and expense. Furthermore – and most importantly for present purposes – unless and until the Debtors object to the Class Proof of Claim, any request for class procedures is not ripe. Only after a claim objection can the Lead Plaintiffs request that the Court apply Bankruptcy Rule 7023 through Bankruptcy Rule 9014(c). For this reason alone, Lead Plaintiffs' request for alternative relief is due to be denied.

I. THE LEAD PLAINTIFFS ARE NOT ENTITLED TO STAY RELIEF.

The automatic stay affords "one of the fundamental debtor protections provided by the bankruptcy laws," *Midlantic Nat'l Bank v. New Jersey Dep't of Evntl. Prot.*, 474 U.S. 494, 503

(1986), and is intended to "allow the bankruptcy court to centralize all disputes concerning property of the debtor's estate so that reorganization can proceed efficiently, unimpeded by uncoordinated proceedings in other arenas," *SEC v. Brennan*, 230 F.3d 65, 71 (2d Cir.2000) (internal quotation omitted). *See also In re Curtis*, 40 B.R. 795, 798 (Bankr. Utah 1984) (recognizing that the automatic stay "enables the debtor to avoid the multiplicity of claims against the estate arising in different forums").[2] This "stay is critical to debtors" because it shifts the focus away from litigation and to the productive work of reorganization. *In re Residential Capital, LLC*, 2012 WL 3860586, at *4 (Bankr. S.D.N.Y. August 8, 2012) ("Residential Capital I") (citing *In re Pioneer Commercial Funding Corp.*, 114 B.R. 45, 48 (Bankr. S.D.N.Y. 1990)).

In conjunction with the protections and centralizing effect afforded by the automatic stay, Congress vested bankruptcy courts with the express power to allow or disallow claims filed against a debtor's estate. As the Supreme Court established long ago in *Katchen v. Landy*, 382 U.S. 323 (1966), "a chief purpose of the bankruptcy laws is to secure a prompt and effectual administration of the estate of all bankrupts within a limited period." 382 U.S. at 329 (internal quotation marks and citations omitted). To that end, the Supreme Court recognized that it is "clear that the expressly granted power to 'allow,' 'disallow' and 'reconsider' claims, which is of basic importance in the administration of the bankruptcy estate, is to be exercised in summary proceedings and not by the slower and more expensive process of a plenary suit." *Id*. (internal

[2] *See also Chao v. Hosp. Staffing Servs., Inc.*, 270 F.3d 374, 382–83 (6th Cir. 2001) (stating that the automatic stay is intended to "preserve what remains of the debtor's insolvent estate and ... provide a systematic equitable liquidation procedure for all creditors, secured as well as unsecured, thereby preventing a chaotic and uncontrolled scramble for the debtor's assets in a variety of uncoordinated proceedings in different courts.") (quoting *Holtkamp v. Littlefield*, 669 F.2d 505, 508 (7th Cir.1982) (omission in original) (internal quotation marks omitted)).

quotation marks and citations omitted). This power to allow or disallow claims "is essential to the performance of the duties" imposed upon a bankruptcy court. *Id.* (citations omitted).[3]

One advantage of the centralized claims process is that one court – i.e., the bankruptcy court – can coordinate all the facets of the bankruptcy to ultimately provide for a timely distribution to a debtor's creditors. *In re Mirant Corp.*, 316 B.R. at 242 ("An important advantage of centralized determination of claims is the bankruptcy court's ability to coordinate the timing of [the distribution process] with other aspects of a debtor's reorganization and ensure expeditious distribution to creditors"). Allowing claimants to liquidate their claims (especially general unsecured claims) against the estate in a piecemeal fashion in other non-bankruptcy forums thwarts this advantage by dividing the administration of the estate and diluting the bankruptcy court's role in reordering the debtor-creditor relationships.[4]

Accordingly, courts are very reluctant to grant stay relief to allow a creditor to litigate its claims in a non-bankruptcy forum, and place the initial burden on the movant to establish a legally sufficient basis, i.e., "cause," for such relief. *In re Curtis*, 40 B.R. at 802; *see also In re Porter*, 2013 WL 3992444, at 2* (Bankr. E.D. Kent. Aug. 2, 2013) (recognizing that a creditor seeking stay relief to litigate in another forum "has the initial burden of proof to make a prima facie showing that there is a factual and legal right to the relief sought"). Thus, Movants must

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[3] *In re Mirant Corp.*, 316 B.R. 234, 239–40 (Bankr. N.D. Tex. 2004) (recognizing that liquidating and allowing (or disallowing) claims "is at the very heart of the bankruptcy court's function and purpose" and allowing for non-bankruptcy claims resolution conflicts with the purposes of the Code by "robbing this [C]ourt of its ability to deal with the adjustment of the debtor-creditor relationship"); *Lesser v. A-Z Assocs. (In re Lion Capital Group)*, 46 B.R. 850, 860 (Bankr. S.D.N.Y. 1985) ("Adjustment of claims against an estate has been and remains central to bankruptcy proceedings").

[4] *See also In re Residential Capital I*, 2012 WL 3860586, at 4* (Bankr. S.D.N.Y. August 8, 2012) ("Claims for damages against the Debtors are the usual grist for the bankruptcy claims allowance process and absent unusual circumstances the bankruptcy court remains the appropriate forum to resolve such claims. Permitting courts around the country to adjudicate claims risks diverting the attention of Debtors' personnel from pressing issues in the chapter 11 case.").

demonstrate special circumstances to establish cause for relief. Generally, courts employ an equitable balancing test to determine if sufficient cause for stay relief exists, and the Lead Plaintiffs have cited 12 nonexclusive factors from *Sonnax Indus., Inc. v. Tri Component Prods. Corp.* (*In re Sonnax Indus. Inc.*), 907 F.2d 1280, 1286 (2d Cir. 1990) to guide this determination.[5] The Debtors agree that the 12 factors in the *Sonnax* opinion (the "Sonnax Factors") are useful for a court's analysis in determining cause for stay relief.

However, it is important to note that the balancing test embodied in the Sonnax Factors does not start with the scales in equipoise. Instead, the scales are tilted in favor of adhering to the claims process. *See In re Curtis*, 40 B.R. 795 at 800 ("[I]n considering the foregoing factors, it must be borne in mind that the process of determining the allowance of claims is of basic importance to the administration of a bankruptcy estate."). Moreover, the scales are tilted against unsecured creditors as they must present "extraordinary circumstances" to obtain stay relief. *In re Residential Capital I*, 2012 WL 3860586, at *4 (quoting *In re Leibowitz*, 147 B.R. 341, 345 (Bankr. S.D.N.Y.1992) ("[T]he general rule is that claims that are not viewed as secured in the context of § 362(d)(1) should not be granted relief from the stay unless extraordinary circumstances are established to justify such relief."); *see also In re Sonnax*, 99 B.R. 591, 595 (Bankr. D. Vt. 1989) ("As an unsecured creditor, Tri Component would not be entitled to relief except in extraordinary circumstances").

[5] This 12-factor analysis adopted by the Second Circuit was originally set out by the Bankruptcy Court for the District of Utah. *See In re Curtis*, 40 B.R. at 799-800. As recently recognized in the Ninth Circuit, "the *Curtis* factors are appropriate, nonexclusive, factors to consider in deciding whether to grant relief from the automatic stay to allow pending litigation to continue in another forum." *In re Kronemyer*, 405 B.R. 915, 921 (9th Cir. BAP 2009). That said, while the *Curtis* factors are often employed by courts to determine the existence of cause, "not all of the factors are relevant in every case, nor is a court required to give each factor equal weight." *In re Landmark Fence Co., Inc.*, 2011 WL 6826235, at *4 (C.D. Cal. 2011) (citing *In re Plumberex Specialty Prods., Inc.*, 311 B.R. 551, 559 (Bankr. C.D. Cal. 2004)). Moreover, "[t]he Sixth Circuit has not adopted a single, clear test to determine whether 'cause' exists…in the context of a motion to modify the automatic stay to allow pending litigation in a nonbankruptcy forum to proceed to finality," but it generally considers the following factors: "judicial economy, trial readiness, the resolution of preliminary bankruptcy issues, the creditor's chance of success on the merits, the cost of defense or other potential burden to the bankruptcy estate, and the impact of the litigation on other creditors." *In re Williams*, 2012 WL 2974914 at *2 (Bankr. W.D. Tenn. July 20, 2012) (citations omitted). These factors generally align with the Sonnax factors.

With the scales properly set in favor of bankruptcy and against granting stay relief for prosecuting unsecured claims, the relevant Sonnax Factors demonstrate that the Lead Plaintiffs are not entitled to the stay relief they request.

A. Stay Relief Will Not Result in Partial or Complete Resolution (Factor No. 1).

The first Sonnax Factor – whether relief would result in partial or complete resolution of the issues – weighs in favor of denying stay relief.

While relief might ultimately allow for partial or complete resolution of the underlying merits of Lead Plaintiffs' claims, Lead Plaintiffs would have to return to this Court to pursue satisfaction of any liability established in the Central District of California. Returning to this Court for satisfaction, in turn, raises issues related to claim allowance, administration and enforcement – issues that will have to be handled by this Court. *See e.g., In re Landmark Fence Co., Inc.*, 2011 WL 6826253 at *5 (upholding bankruptcy court's conclusion that because there would be the necessity for further evaluation of the claims in bankruptcy, continuing litigation in state court would not result in a complete resolution).

Moreover, the possibility of resolution in the non-bankruptcy forum does not justify stay relief if the proceeding is still in the beginning stages, as the MDL Class Action is here. *See, e.g., In re Residential Capital, LLC*, 2012 WL 3860586 at *4 ("Discovery, trial preparation and, absent a settlement, trial all remain to be done. Therefore, since the [litigation] is in its early stages, the first Sonnax Factor weighs against lifting the stay."). Accordingly, the first Sonnax Factor weighs against granting the requested stay relief.

B. The MDL Class Action Will Interfere with the Debtors' Bankruptcy (Factor No. 2).

The second Sonnax Factor – lack of any connection or interference with the bankruptcy case – also favors denying the requested stay relief. As the *Curtis* court noted: "The most important factor in determining whether to grant relief from automatic stay is the effect of such

litigation on the administration of the estate." 40 B.R. at 800. The *Curtis* court concluded: "Even slight interference with the administration may be enough to preclude relief in the absence of a commensurate benefit." *Id.* As explained herein, granting stay relief in this case will undoubtedly interfere with the administration of the Debtors' estate without a commensurate benefit. Thus, stay relief should be denied.

First, the Debtors will have to litigate the MDL Class Action in California. Instead of using scarce time and resources formulating a plan and overseeing distributions, the Debtors will have to spend additional time and resources defending class litigation in a distant forum, which will be infinitely more expensive when compared to the claims allowance procedures provided by the Bankruptcy Code.[6] As discussed further in Subsection G below, Debtors will have to incur the additional costs and expenses of special litigation/local counsel, which will necessarily reduce the distribution pool available for other creditors. The Debtors will not incur these costs if the Lead Plaintiffs are required to pursue their general unsecured claims through the same claims administration process as all the other creditors are using.

Moreover, as also discussed in Subsection G, litigating in a separate forum will delay the claims liquidation process, which could interfere with the timing of distributions to other creditors. *See e.g., Residential Capital I,* 2012 WL 3860586 at *4; *see also In re Ephedra Products Liability Litigation*, 329 B.R. 1, 5 (S.D.N.Y. 2005) (recognizing that "class litigation is inherently more time-consuming than the expedited bankruptcy procedure for resolving contested matters"). Bankruptcy is a collective proceeding which "can proceed no faster than its

[6] Describing the cost-intensive and timely procedures associated with a class action lawsuit, the Seventh Circuit has stated: "And what suits! Each starts off with complex problems about commonality of claims and adequate representation, followed by notice, opt-out, and other procedural issues unique to class actions, on top of which the substance of the case may be very difficult. Class actions consume judicial time, putting off adjudication for other deserving litigants; they impose steep costs on defendants, even those in the right. The systemic costs of class litigation should not be borne lightly." *In re American Reserve Corp.*, 840 F.2d 487 (7th Cir. 1988).

slowest matter." *In re Woodward & Lothrop Holdings, Inc.*, 205 B.R. 365, 376 (Bankr. S.D.N.Y. 1997) (citing *In re American Reserve Corp.*, 840 F.2d at 491). Because creditors with undisputed claims cannot recover until all disputes have been resolved, granting stay relief to allow the Lead Plaintiffs to proceed with their class action may "gum up the works" as the entitlement of other creditors cannot be determined until the litigation is complete. *In re American Reserve Corp.*, 840 F.2d at 491. Accordingly, granting the Lead Plaintiffs stay relief would initiate protracted litigation that will likely delay distribution of the estate for years. Thus, the second Sonnax Factor weighs in favor of denying the requested stay relief.

C. The MDL Class Action Does Not Involve the Debtors as Fiduciaries (Factor No. 3).

The third Sonnax Factor – whether the proceeding involves the debtor as a fiduciary – decisively favors denying stay relief. If the proceeding involves the debtor as a fiduciary, then stay relief is generally allowed. *In re Curtis*, 40 B.R. at 799 ("Generally, proceedings in which the debtor is a fiduciary…need not be stayed because they bear no relationship to the purpose of the automatic stay, which is debtor protection from his creditors."). The Lead Plaintiffs fail to address this factor given that the MDL Class Action does not involve the Debtors in a fiduciary capacity, but instead seeks direct liability as to the Debtors. Therefore, the third Sonnax Factor weights against lifting the stay as the Debtors are not fiduciaries in the MDL Class Action. *See Residential Capital I*, 2012 WL 3860586 at *7 (whether or not the proceeding involves the debtor as a fiduciary bears a significant relationship to the automatic stay).

D. No Specialized Tribunal Has Been Established (Factor No. 4).

The fourth Sonnax Factor – whether a specialized tribunal with necessary experience has been established to hear the cause of action – also supports denying stay relief. This factor

examines the experience of the non-bankruptcy forum with the stayed litigation or its expertise regarding the particular legal issues involved.

In support of their request for stay relief, the Lead Plaintiffs argue that the consolidation order in MDL Class Action provides that Judge Snyder "has issued a lengthy ruling on Oreck's motions to strike and motion to dismiss, indicating that the judge has already gained significant familiarity with at least some of the involved allegations." (Exhibit B to the Motion). However, in the consolidation order, the Panel first states that the Central District of California was chosen for consolidation given that "[t]he *Edge* action, which is the only action involving all four products (i.e., the Halo and the three air purifiers) is pending in that district, and a majority of plaintiffs favor centralization there." *Id*. Though the Lead Plaintiffs fail to acknowledge this important fact, this was the primary reason the Central District of California was chosen. The Lead Plaintiffs also do not mention that Roxy Edge has since voluntarily dismissed her claims, eliminating one of the primary connections to the Central District of California.

The Lead Plaintiffs further argue that since the entry of the consolidation order, Judge Snyder has issued decisions relating to consolidation, a contested appointment of interim class counsel, motions to dismiss, and status conferences. But ruling on these initial procedural rulings does not make the Central District a specialized tribunal as contemplated by the fourth Sonnax Factor. The MDL Class Action has just barely begun, and the Court's involvement has not been extensive or germane to the issues that will guide the case going forward. Moreover, Judge Snyder's order on the motions to dismiss related almost entirely to issues regarding standing, pleading standards under *Twombly*/*Iqbal* and Federal Rule of Civil Procedure 9, and personal jurisdiction as to David Oreck. By definition, Judge Snyder could not have considered

evidence on the claims in ruling on Rule 12(b) defenses. Accordingly, the Central District of California has not meaningfully delved into the substance of the Lead Plaintiffs' claims.

Before the bankruptcy filing, the parties had filed a Rule 26(f) report in MDL Class Action, and the parties had not reached agreement on many important issues that would govern class discovery, class certification, merits discovery, and trial. To begin to resolve these differences, the Court set a scheduling conference for May 13, 2013. However, the Debtors filed this bankruptcy before that hearing and before the Court entered a scheduling order. Accordingly, the parties had just begun to scratch the surface of the litigation at the time of the petition. Notably, the only discovery which had occurred involved jurisdiction. There had been no other discovery regarding class certification, nor briefing on class certification, which would have to be determined before beginning discovery and briefing on the merits, and then trial (if necessary). (*See* Footnote Five, above).

The cases which Lead Plaintiffs cite in support of their argument on this factor are distinguishable as all of the cases were much closer to trial. In the *SCO Group* opinion, the bankruptcy was filed on the eve of trial and the litigation had been pending before the non-bankruptcy court for four years.[7] *In re SCO Group, Inc.*, 141 B.R. 854, 858–60 (Bankr. D. Del. 2007). Timing was likewise significant in the *Projection Orange* opinion: the debtor filed bankruptcy on the eve of summary judgment in one non-bankruptcy action and on the day before the judge intended to enter a summary judgment order in the other. *In re Project Orange Assocs., LLC*, 432 B.R. 89, 109–110 (Bankr. S.D.N.Y. 2010). In comparison, the MDL Class Action had barely passed the pleadings phase at the time of the bankruptcy filing and had not even begun the first phase of discovery related to class certification.

[7] Trial was set to begin on Monday, September 17, 2007, and the bankruptcy was filed on Friday, September 14, 2007.

Similarly, the cases which Lead Plaintiffs cite in support of their argument that the Central District somehow has an "expertise" in the subject matter of the claims are also distinguishable. In *Bison Resources*, the bankruptcy court deferred to West Virginia state court for ruling on issues which potentially reversed a century of existing state law relating to oil and gas rights.[8] *In re Bison Res., Inc.*, 230 B.R. 611, 617 (Bankr. D. Ok. 1999). In *Taub*, the bankruptcy court deferred to a New York matrimonial court for experience in connection with a related divorce proceeding, recognizing the state court's "significant expertise in domestic relations matters."[9] *In re Taub*, 413 B.R. 55, 63–64 (Bankr. E.D.N.Y. 2009). These cases differ from this case because the Lead Plaintiffs' general unsecured claims do not involve unsettled questions of state law, nor do they require adjudication before a specialized tribunal. The MDL Class Action seeks to be nationwide and does not draw on – much less require – the particular geographical or topic expertise of a particular court.

Because the Central District of California has not made any substantive determinations in the MDL Class Action, this Court may interpret and apply state law in liquidating the claims through the streamlined bankruptcy claims administration process provided for by the Bankruptcy Code and Bankruptcy Rules. *See In re UAL Corp.*, 310 B.R. 373, 377 (Bankr. N.D.

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[8] "Although the State Court is a court of general civil jurisdiction, it is better equipped than this Court to deal with issues pertaining to West Virginia oil and gas law. Indeed, some of the litigants in the State Court Action have argued that the pretrial rulings of the State Court 'established a new rule of law in West Virginia and reversed a century of existing landowner and industry practice.' (*See* Movants' Exhibit 9 at 3). This Court sees no reason to interject itself into a dispute on the cutting edge of the law of the state of West Virginia relating to oil and gas rights. Such issues are best left to the State Court." *In re Bison Res., Inc.*, 230 B.R. 611, 617 (Bankr. D. Ok. 1999).

[9] "In New York, matrimonial courts have long been empowered, in connection with divorce actions, to determine the issues of title to property and to make directions pertaining to the possession of property...Federal courts, including bankruptcy courts, ordinarily defer to the state courts in matrimonial matters to promote judicial economy and out of respect for the state courts' expertise in domestic relations issues.... New York's state courts are more familiar with the concepts of marital property and how to apply the statutory and discretionary factors that govern equitable distribution. Bankruptcy courts, on the other hand, rarely interpret or apply the equitable distribution statute." *In re Taub*, 413 B.R. 55, 63-64 (Bankr. E.D.N.Y. 2009) (quoting *In re Cole*, 202 B.R. 356, 359–61 (Bankr. S.D.N.Y. 1996) (citations omitted)).

Ill. 2004) ("It has long been recognized that one of the essential, 'core' functions of bankruptcy is the allowance or disallowance of claims against the debtor's estate, without regard to the source of the claim."); *In re Bally Total Fitness of Greater N.Y., Inc.*, 402 B.R. 616, 624 (Bankr. S.D.N.Y. 2009)("This Court has significant experience in applying state law…"). Accordingly, the fourth Sonnax Factor weighs in favor of denying the requested stay relief.

E. No Insurer Has Assumed Responsibility For The MDL Class Action (Factor 5).

The fifth Sonnax Factor – whether the debtor's insurer has assumed full responsibility for defending the non-bankruptcy action – also weighs against lifting the automatic stay. While it is true that the Debtors settled a declaratory judgment action with its insurer prior to the petition date, no insurer has assumed financial responsibility for defense of the MDL Class Action. All costs and expenses of litigating the MDL Class Action would be borne from the limited funds from the bankruptcy estate. Thus the fifth Sonnax Factor weighs in favor of denying the requested stay relief. *See e.g., Residential Capital I*, 2012 WL 3860586, at *7; *In re Curtis*, 40 B.R. at 806.

F. The MDL Class Action Does Not Primarily Involve Third Parties (Factor No. 6).

The Lead Plaintiffs fail to address the sixth Sonnax Factor – whether non-bankruptcy action primarily involves third parties – and this factor weighs against granting stay relief. Three of the four identified defendants in the MDL Class Action – Oreck Corporation, Oreck Direct, LLC, and Oreck Homecare, LLC – are debtors in this bankruptcy case; David Oreck is the only identified non-Debtor defendant. The MDL Class Action primarily involves these Debtors, and the presence of a single, individual third party does not justify lifting the stay. Thus, the sixth Sonnax Factor weights in favor of denying stay relief given that the Debtors are primary parties to the non-bankruptcy litigation. *See Residential Capital I*, 2012 WL 3860586 at *7 (Bankr.

S.D.N.Y. Aug. 8, 2012) (denying stay relief where two of the three defendants were debtors) (citing *City Ins. Co. v. Mego Int'l Inc.* (*In re Mego Int'l Inc.*), 28 B.R. 324, 326 (Bankr. S.D.N.Y. 1983)).

G. Litigation In Another Forum Will Prejudice Other Creditors (Factor No. 7).

The seventh Sonnax Factor – whether litigation in another forum would prejudice the interests of other creditors – weighs heavily against granting the requested stay relief because litigating the MDL Class Action in California will be particularly expensive and time-consuming and will diminish the available distributions from the estate.

In support of their Motion, the Lead Plaintiffs argue that stay relief will not prejudice other creditors in that no plan of liquidation has been submitted, no distributions have been made, and the Lead Plaintiffs are merely seeking general unsecured claims.[10] Lead Plaintiffs further assert that the failure to liquidate their claims in the Central District of California would actually prejudice the Debtors' other creditors, insinuating that the non-bankruptcy forum would proceed more expeditiously. The Lead Plaintiffs' argument is wrong for three reasons.

First, requiring Debtors to defend litigation in another forum would frustrate the "strong bankruptcy code policy that favors centralized and efficient administration of all claims in the bankruptcy court." *Pub. Indus. Inc. v. United States (In re Cuyahoga Equip. Corp.)*, 980 F.2d 110, 117 (2d Cir. 1992). As established by the Supreme Court, the chief purpose of bankruptcy is to secure a prompt and effectual administration of the estate within a limited period of time, and the provision for summary disposition, without regard to usual modes of trial, is one of the

[10] Lead Plaintiffs cite *In re New York Medical Group, P.C.*, 265 B.R. 408, 413–414 (Bankr. S.D.N.Y. 2001) in support of their argument, but this case is distinguishable because the movants there sought stay relief to pursue a claim for personal injury. Special rules apply to personal injury claims as a bankruptcy court lacks jurisdiction to liquidate a personal injury claim. *See* 28 U.S.C. § 157(b)(2)(B); *United States Liners, Inc.*, 1998 WL 382023, at *4 (S.D.N.Y. July 9, 1998), *aff'd*, 216 F. 3d 228 (2d. Cir. 2000). Thus, the state court was the only court able to liquidate the claim. The Lead Plaintiffs bring no personal injury claim, so this case is inapposite.

means chosen by Congress to effectuate that purpose. *Katchen*, 382 U.S. at 329. The Supreme Court continued by recognizing the express power of Bankruptcy Courts to allow and disallow claims is to be "exercised in summary proceedings and not by slower and more expensive processes of a plenary suit." *Id.*

If the stay remains in place, the Bankruptcy Court will hear the claims (if objection is presented) through the streamlined claims adjudication procedures that are integral to the bankruptcy process – including the streamlined procedures for contested matters under Bankruptcy Rule 9014, which are faster and less expensive than litigating in a non-bankruptcy forum. *See In re Shumate*, 42 B.R. 462, 467 (Bankr. Tenn. 1984) (recognizing that objections to a proof of claim pursuant to Section 502 of the Bankruptcy Code and Bankruptcy Rule 3007 become a contested matter governed by the streamline procedure under Bankruptcy Rule 9014). Requiring the Debtors' to defend the class claims in another forum "would be unfair to other creditors who must bring their claims in [the bankruptcy court]." *In re Residential Capital, LLC*, 2012 WL 3556912, at *4 (Bankr. S.D.N.Y. Aug. 16, 2012) ("Residential Capital II").

If the litigation is allowed to proceed in the Central District of California, Debtors will be forced to incur the additional costs and expenses associated with litigating a plenary proceeding (involving general unsecured claims) in another forum located on the other side of the country. In addition to the additional time and expenses incurred by Debtors' bankruptcy counsel, the Debtors will have the additional costs and expenses of special litigation/local counsel, which will not be necessary should the stay remain. Fortunately, the costs and expenses of special litigation/local counsel have been almost non-existent since the petition date, and will remain that way so long as the stay remains in place. Should the Court grant the stay relief, the

additional costs and expenses of special litigation/local counsel will only serve to diminish the limited estate funds available for distribution to the other creditors.

Second, as previously discussed in Subsection B, regardless of the ultimate determination as to the movants' claims and the effect on the overall pro rata distributions to unsecured creditors, the additional time and energy expended in liquidating general unsecured claims through a plenary suit in a distant forum will, at the very least, delay distributions to the other creditors. *See In re Mirant Corp.*, 316 B.R. at 239–40 ("An important advantage of centralized determination of claims is the bankruptcy court's ability to coordinate the timing of that process with the other aspects of a debtor's reorganization and ensure expeditious distribution to creditors."); *In re Woodward & Lothrop Holdings, Inc.*, 205 B.R. at 376 ("[A] bankruptcy case can proceed no faster than its slowest matter, and a class action may 'gum up the works' because until complete, the bankruptcy court cannot determine the entitlement to the other creditors").

Third, the MDL Class Action may have no reason to proceed if the assets remaining for general unsecured creditors are depleted, which becomes increasing likely with the additional costs which would be associated with protracted class action litigation in another forum. *See e.g.*, *In re Landmark Fence Co., Inc.*, 2011 WL 6826253 at *5 (upholding bankruptcy court's finding that the high cost of litigating a class action in state court might overwhelm the estate, resulting in a class of creditors that probably would have little or no chance of recovery); *In re Johnson*, 2006 WL 6593254, *2 (Bankr. N.D. Ga. Oct. 11, 2006).

Ultimately, as stated in the *Residential Capital I* opinion: "The [movants] must be treated as any other unsecured creditors and litigate their claims in this Court along with the Debtors'

other similarly situated creditors." 2012 WL 3860586 at *7.[11] Accordingly, the seventh Sonnax Factor weighs in favor of denying the requested stay relief.

H. The Interests of Judicial Economy and the Expeditious and Economical Resolution of the Claims Are Best Served by Maintaining the Automatic Stay (Factor No. 10).

The tenth Sonnax Factor – the interests of judicial economy and the expeditious and economical resolution of litigation – also weighs in favor of denying stay relief.

The Lead Plaintiffs argue that stay relief is necessary to avoid duplicative litigation, but the fundamental policies and purposes of bankruptcy sometimes require creditors to litigate in multiple forums. The Sixth Circuit has recognized that a necessary by-product of bankruptcy is duplicative litigation, and emphasized that such duplication exists by Congressional mandate. *Lynch v. Johns-Manville Sales Corp*., 710 F. 2d 1194, 1199 (6th Cir. 1983) ("[I]t is initially observed that any duplicative or multiple litigation which may occur is a direct by-product of bankruptcy law. As such, the duplication, to the extent that it may exist, is congressionally created and sanctioned."). Thus, while Lead Plaintiffs may suffer the inconvenience of having to pursue similar claims in different forums, such is a necessary by-product of bankruptcy that does not ordinarily justify the requested stay relief.[12]

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[11] *See also In re Motors Liquidation Co.*, 2010 WL 4966018, at *4 (S.D.N.Y. 2010) (quoting *In re Leibowitz*, 147 B.R. 341, 345 (Bankr. S.D.N.Y. 1992)) (affirming the bankruptcy court's denial of a class plaintiff's motion for stay relief, the Southern District of New York noted: "Far from an abuse of discretion, [the reasoning of the bankruptcy court] accorded with the general rule that, 'generally, unsecured claims should be granted relief from stay because to do so would result in a violation of one of the fundamental concepts of bankruptcy law[:] that there should be an equality of distribution among creditors. An unsecured claimant should not be entitled to obtain a distributive advantage over other unsecured claimants who are similarly enjoined from seeking distribution by any method other than in accordance with the distributive scheme under the Bankruptcy Code.")

[12] Consider the alternative: If a bankruptcy court were required to grant stay relief every time a creditor sued a non-debtor third-party in a separate forum, litigation involving third parties would be effectively carved out of the bankruptcy court's jurisdiction and control. This carve out would be bad policy standing alone, but it becomes even worse if (like in this case) the third-party defendant is an individual who served as spokesperson/agent for the Debtors. As discussed in Subsection F, the relief sought in the MDL Class Action comes primarily from the Debtors, and the conduct at issue is primarily conduct of the Debtors.

Notably, each of the cases which the Lead Plaintiffs cite in support of their argument (that duplicative litigation is grounds for stay relief) featured non-bankruptcy litigation that was ready for trial. *See In re Rexene Prods. Co.*, 141 B.R. 574, 577 (Bankr. D. Del. 1992) ("Discovery is nearly complete…both sides are represented by local Texas counsel who were ready to go to trial in Texas District Court last August."); *Smith v. Tricare Rehab. Sys., Inc.* (*In re Tricare Rehab. Sys. Inc.*), 181 B.R. 569, 575 (Bankr. N.D. Ala. 1994) ("[Movant's] case is almost certain to be tried in state court in less than three months. The parties stipulated that significant preparation has already occurred. Both camps are firmly entrenched, fully armored, well provisioned, and set for the fight."); *In re Anton*, 145 B.R. 767, (Bankr. E.D.N.Y. 1992) (where movant sought relief from stay to add debtor, who was the principal of the non-debtor defendant, as a co-defendant to the non-bankruptcy litigation, the Court noted: "If he is not made a party, this Court, in order to evaluate the claim of [movant] in this proceeding, will have to plow the same ground, lacking the advantages and headstart now enjoyed by the District Court in which the action against [non-debtor] has been pending since 1989 and in which discovery has been taken of most of the major parties and in which a complete resolution of the issues should be forthcoming."). Given that these cases were ready for trial, it made sense for the bankruptcy court to defer to the non-bankruptcy forum for a more expeditious and economical resolution. This case, by contrast, is not remotely trial ready.

Contrary to Lead Plaintiffs' assertions, the interests of judicial economy and expeditious and economical resolution of litigation weigh in favor of denying stay relief and requiring the Lead Plaintiffs, who are asserting general unsecured claims, to abide by the claims administration process established by the Bankruptcy Code and "designed to centralize and expedite claims against a debtor's estate." *In re SMEC, Inc.*, 161 B.R. 953 (M.D. Tenn. 1993);

see also In re Atlas Concrete Pipe, Inc., 668 F. 2d 905, 910 (6th Cir. 1982) (recognizing that proceedings in bankruptcy are summary, rather than plenary, in nature and that "a bankruptcy proceeding is less formal and more expeditious than a full trial in a district court"); *see also In re Ephedra Prods. Liab. Litig.*, 329 B.R. 1, 10 (S.D.N.Y. 2005) ("The only real beneficiaries of applying Rule 23 would be the lawyers representing the class."). Thus, the tenth Sonnax Factor weighs in favor of denying the requested stay relief.

I. The MDL Class Action Is Nowhere Near Ready For Trial (Factor No. 11).

The eleventh Sonnax Factor – whether the parties are ready for trial in the other proceeding – weighs in favor of denying the requested stay relief. Following the consolidation order of the MDL Class Action, the Lead Plaintiffs' filed an amended consolidated complaint on September 7, 2012. The Court (*i.e.*, Central District of California) ruled on the Defendants' motions to dismiss on December 3, 2012, after which the Defendants filed their answers on December 19, 2012. The parties filed a Rule 26(f) report on January 24, 2013, and the Court set a scheduling conference for May 13, 2013. However, the Debtors filed Chapter 11 bankruptcy on May 6, 2013, before the Court issued a scheduling order. The MDL Class Action is nowhere near ready for an initial ruling on class certification, much less a full trial. As of the petition date, the case was not even ready to *begin* discovery. Other than limited jurisdictional discovery, there had been no other discovery regarding class certification, nor briefing on class certification, which would have to be determined before beginning discovery and briefing on the merits, and then trial (if necessary). (See Footnote Five, *supra*). As proposed by the Defendants in the Rule 26(f) report, the parties would not have been ready for trial until April 2015 (which is no longer possible given the stay delaying the case even further). Accordingly, the eleventh Sonnax Factor weights in favor of denying stay relief.

J. The Balance of Harms Favors Maintaining the Automatic Stay (Factor No. 12).

The twelfth and final Sonnax Factor – the impact of stay on the parties and the balance of harms – also weighs in favor of denying stay relief.

Lead Plaintiffs first argue that there will be neither prejudice to this Court nor interference with the instant bankruptcy case given that this Court has already approved the sale of substantially all of the Debtors' assets. But, in fact, the Lead Plaintiffs seek to have the Debtors litigate their general unsecured claims in a forum on the other side of the country, before a court which is not overseeing the range of proceedings and related scheduling involving the instant bankruptcy before this Court, and with the assistance of special litigation/local counsel whose services will not be necessary should the stay remain in place. Despite these salient burdens on the Debtors' bankruptcy, the Lead Plaintiffs erroneously assert that there will be no interference with the bankruptcy.

As set forth above, the very purpose of the automatic stay is to centralize all claims so that the debtor can "proceed efficiently, unimpeded by uncoordinated proceedings in other arenas." *SEC*, 230 F.3d at 71. The subject claims implicate issues central to the claims administration and confirmation processes before this Court (effectively setting up a shadow debt adjustment process in a forum court), and the bifurcation of these issues between this Court and the Central District of California will unduly prejudice the Debtors and the Debtors' creditors (as discussed above). Debtors need the opportunity to formulate and propose a plan without the substantial cost, delay, and other burdens associated with defending a subset of general unsecured claims in a distant jurisdiction. Thus, stay relief should be denied.

The Lead Plaintiffs next argue that there will be no prejudice to the bankruptcy given that the Debtors have employed separate litigation counsel in MDL Class Action. Lead Plaintiffs thus argue that the Debtors' undersigned bankruptcy counsel will not have to litigate class action

certification and claims liquidation. Lead Plaintiffs also argue that if stay relief is not granted, the Debtors will incur the same amount of costs and expenses in the bankruptcy claim allowance and objection process as would be incurred in litigating the MDL Class Action in the Central District of California. These arguments miss the mark.

As previously stated (see Subsection G, *supra*), the Debtors will not have to incur the costs and expenses of special litigation/local counsel should stay relief be denied. Moreover, despite the presence of special litigation/local counsel (who had been retained in the MDL Class Action to replace previous local counsel prior to the bankruptcy filing), undersigned bankruptcy counsel will be heavily involved in overseeing the litigation should it take place in the Central District of California.

Finally, the costs associated with litigating a class action in a plenary proceeding across the country will far exceed the costs incurred in the streamlined claims allowance process established under the Bankruptcy Code. *See Katchen*, 382 U.S. at 329 (establishing that the claims allowance processes provided for in bankruptcy are "to be exercised in summary proceedings and not by the slower and more expensive processes of a plenary suit."); *In re Atlas Concrete Pipe, Inc.*, 668 F. 2d at 910 (recognizing that "a bankruptcy proceeding is less formal and more expeditious than a full trial in a district court"). Bankruptcy achieves the procedural advantages of class actions better than Rule 23: "The bankruptcy forum, as a mandatory collective proceeding, serves this [procedural] purpose without the overlay of the class action." *In re American Reserve Corp.*, 840 F.2d 487, 489 (7th Cir. 1988). Likewise, bankruptcy is superior to class actions for handling claims for relatively small amounts (such as the claims here), both in terms of efficiency and fairness. *See In re Ephedra*, 329 B.R. at 9 (summarizing advantages of bankruptcy over class action procedures). The scales in bankruptcy tilt strongly

against class actions: "Since superiority of the class actions is lost in bankruptcy, only ***compelling*** reasons for allowing a particular opt-out class claim can justify applying Rule 23." *Id*. (emphasis added).

In support of their Motion, Lead Plaintiffs also posit that the Putative Class members will suffer considerable harm in the absence of stay relief, stating that these potential claimants may be unable or unwilling to submit a claim. However, the bankruptcy claims administration process is specifically designed so that a claimant may file a proof of claim without an attorney and without paying a filing fee. The Official Form B 10 is designed to facilitate the process, and creditors are even granted a *prima facie* claim by completing this official and without the burden of actually "proving" their claim.[13] Additionally, although class actions may facilitate the collective litigation of many small claims in non-bankruptcy contexts, the "superiority of the class action vanishes when the other available method is bankruptcy, which consolidates all claims in one forum and allows claimants to file proofs of claim without counsel and at virtually no cost." *In re Ephedra*, 329 B.R. at 9; *see also In re Blockbuster Inc.*, 441 B.R. 239, 240 (Bankr. S.D.N.Y. 2011) ("[C]lass certification is often less desirable in bankruptcy than in ordinary civil litigation, as class-based claims have the potential to adversely affect the administration of a case by adding layers of procedural and factual complexity siphoning the Debtors' resources and interfering with the orderly progression of the reorganization") (citations, quotation marks, and other textual markings omitted).

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[13] *See In re Davis*, 2011 WL 1302222 at *9 (Bankr. E.D. Tex. Mar. 31, 2011) ("The information required by Bankruptcy Rule 3001 and Official Form 10 is designed to streamline the litigation by facilitating the administration of claims."); *In re Batiste*, 2009 WL 2849077 at *3 (Bankr. E.D. La. 2009) ("The claims process helps streamline the administration of a bankruptcy by allowing creditors a prima facie claims if they comply with the requirements of Bankruptcy Rule 3001. This policy serves two important functions: first it relieves the creditor from the burden of initially 'proving' its claim, eliminating unnecessary expense and time; and second, it provides debtors, interested parties, and the Court with a clear and simple method for determining what claims exist against a bankruptcy estate.").

Finally, the Lead Plaintiffs argue that if stay relief is not granted, the Court will jeopardize the Lead Plaintiffs' constitutionally protected interest in a right to jury trial. This argument first ignores that the Bankruptcy Code provides bankruptcy courts with the express power to govern the claims allowance process. *Katchen*, 382 U.S. at 329.[14] Additionally, this argument ignores that there is no Seventh Amendment right to a jury trial for the allowance and disallowance of claims under 11 U.S.C. § 502. *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33, 57–59 (1989) (resolving debtor-creditor relations is an equity function that does not bring the right to a jury trial). Further, the Lead Plaintiffs have filed proofs of claim against three of the Debtors and accordingly the claims administration process should be used to determine their claims. Thus, the final Sonnax Factor weighs in favor of Debtors.

II. THE COURT SHOULD NOT CERTIFY A CLASS UNDER BANKR. RULE 9023.

Debtors assert that Lead Plaintiffs' alternative motion for class certification pursuant to Bankruptcy Rule 7023 is premature and is not appropriate with a motion for relief from stay. Under certain circumstances, a bankruptcy court has discretion under Bankruptcy Rule 9014(c) to apply Bankruptcy Rule 7023 to proofs of claim. FED. R. BANKR. P. 9014(c) ("The court may at any stage in a particular matter direct that one or more of the other rules in Part VII shall apply"); *Reid v. White Motor Corp.*, 886 F.2d 1462, 1469-70 (6th Cir. 1989) ("Rule 9014 authorizes bankruptcy judges, within their discretion, to invoke Rule 7023, and thereby Fed. R. Civ. P. 23, the class action rule, to 'any stage' in contested matters, including, class proofs of claim"). However, the circumstances that justify applying Bankruptcy Rule 7023 are not

[14] *See also In re UAL Corp.*, 310 B.R. 373, 377 (Bankr.N.D.Ill.2004) ("It has long been recognized that one of the essential, 'core' functions of bankruptcy is the allowance or disallowance of claims against the debtor's estate, without regard to the source of the claim."); *U.S. v. Rhodey (In re R & W Enters.)*, 181 B.R. 624, 643 (Bankr. N.D. Fla. 1994) ("The process of claim determination and payment is within the exclusive province of the bankruptcy court."); *In re Chateaugay Corp.*, 111 B.R. 67, 71 (Bankr. S.D.N.Y. 1990) (recognizing that restructuring of debtor-creditor relations is at the core of bankruptcy court power).

present here because the Lead Plaintiffs' filing of the Class Proof of Claim does not give rise to a contested matter, their motion to apply Bankruptcy Rule 7023 is procedurally premature.[15]

A. The Court Cannot Certify A Class Because There Is No Adversary Proceeding Or Contested Matter.

At this procedural posture, Bankruptcy Rule 7023 cannot apply because there is no adversary proceeding or contested matter in which a class may be certified. The pending Motion applies only to stay relief and not to the merit of the MDL Class Action. When the Debtors object to the claims filed by the Lead Plaintiffs, the alternative relief requested by the Lead Plaintiffs will be ripe for determination. See *In re Charter Co.*, 876 F.2d 866, 876 (11th Cir. 1989) ("[A]bsent an adversary proceeding, the first opportunity a claimant has to move under Bankruptcy Rule 9014, to request application of Bankruptcy Rule 7023, occurs when an objection is made to a proof of claim"; *Reid*, 886 F.2d at 1469 (citing *Charter* with approval); *Gentry v. Siegel*, 668 F.3d 83, 92 (4th Cir 2012) (applying *Charter* rule). Accordingly, Bankruptcy Rule 9014(c) does not authorize the application of Bankruptcy Rule 7023 at this point in the case – the "invocation of Rule 23 procedures" is "not ripe, because there is neither an adversary proceeding nor a contested matter." *Charter*, 876 F.2d at 874.

For this reason, the Court can deny the Motion without consideration of the relevant factors under Bankruptcy Rule 9014(c). Unless and until the Debtors object to the Class Proof of Claim, any request for class procedures is not ripe. Only after a claim objection can the Lead Plaintiffs request that the Court apply Bankruptcy Rule 7023 through Bankruptcy Rule 9014(c).

[15] The Debtors' response is limited to this procedural issue for purposes of responding to the Motion, but the Debtors reserve all rights to raise such other arguments as may be appropriate, including, without limitation, that the facts and posture of the Lead Plaintiffs' claims make class action procedures both substantively and procedurally inferior to the standard bankruptcy claims process and that the Lead Plaintiffs have not presently presented facts and legal arguments sufficient to meet their heavy burden of certifying a class under Bankruptcy Rule 7023.

CONCLUSION

For the reasons set forth herein, the Court should deny the Motion.

Respectfully Submitted:

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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was filed electronically. Notice of this filing will be sent by operation of the Court's electronic filing system to those parties indicated on the electronic filing receipt. The following parties will also be served via first-class, U.S. Mail, postage prepaid to:

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on this the 1st day of October, 2013

The parties may access this filing through the Court's electronic filing system.

/s/ Thor Y. Urness
Thor Y. Urness