IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	:	Chapter 11
SCRIPSAMERICA, INC.,[1]	:	Case No. 16-11991 (LSS)
Debtor.	:	
THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS FOR SCRIPSAMERICA, INC.	:	Adv. No. 17-50010 (LSS)
Plaintiff,	:	
v.	:	
SCRIPSAMERICA, INC. and ANDREW R. VARA, in his official capacity as ACTING UNITED STATES TRUSTEE FOR REGION 3	:	
Defendants.	:	

BRIEF OF THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF SCRIPSAMERICA, INC. IN SUPPORT OF THE MOTION FOR SUMMARY JUDGMENT

Dated: January 23, 2017
Wilmington, Delaware

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[1] The last four digits of the Debtor's federal tax identification number are 8594. The location of the Debtor's corporate headquarters is 1094 Main Ave., Suite A, Clifton, NJ 07011.

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The Official Committee of Unsecured Creditors of ScripsAmerica, Inc. (the "**Committee**"), by and through its attorneys, respectfully submits this opening brief in support of its motion for summary judgment seeking a declaratory judgment that the Office of the United States Trustee has no statutory authority to disband a statutory appointed committee of unsecured creditors, and that the Committee continues to exist as a statutory Committee.

STATEMENT OF THE NATURE AND STAGE OF THE PROCEEDING

The Committee commenced this adversary proceeding at the direction of the United States Bankruptcy Court for the District of Delaware (the "**Court**") pursuant to which it is seeking a declaration that Andrew R. Vara, in his official capacity as the Acting United States Trustee for Region 3 ("**U.S. Trustee**") lacks the statutory authority pursuant to chapter 11 of The Bankruptcy Reform Act of 1978, as codified in title 11 of the United States Code, 11 U.S.C. §§ 101-1532 (the "**Bankruptcy Code**") and title 28 of the United States Code, 28 U.S.C. §§ 581-598b (the "**Judicial Code**") to disband a duly-formed, statutory committee of unsecured creditors.

On September 7, 2016 (the "**Petition Date**"), the Debtor filed a voluntary petition for relief (the "**Bankruptcy Case**") under chapter 11 of The Bankruptcy Code in the United States Bankruptcy Court for Delaware (the "**Court**").

On November 3, 2016 the U.S. Trustee appointed the Committee. The Committee consists of two members, Robert Schneiderman and Ironridge Global Partners, LLC.

On November 4, 2016, the Debtor filed its *Motion for Order Pursuant to 11 U.S.C. §[§] 105(a) and 1102 Directing the Disbandment of the Official Committee of Unsecured Creditors or, Alternatively, the Removal of Ironridge Global Partners, LLC and Robert Schneiderman from the Committee* [D.I. 75] (the "**Motion to Disband**").

On November 21, 2016, the U.S. Trustee filed its objection and reservation of rights with respect to the Motion to Disband [D.I. 93] (the "**U.S. Trustee Objection**").

On November 21, 2016, the Committee filed its objection to the Motion to Disband [D.I. 75].

On December 15, 2016, the Court entered orders authorizing the Committee to retain its professionals: (A) Bayard, P.A. and (B) EisnerAmper LLP (together, the "**Committee Professionals**"). Neither the Debtor nor the U.S. Trustee objected to the entry of the orders approving the Committee Professionals' retention.

On January 9, 2017, an *Amended Notice of Motion* [D.I. 132] was filed scheduling the Motion to Disband for hearing on January 25, 2017 at 2:00 p.m. ET.

On January 11, 2017, the U.S. Trustee filed its Notice of Disbandment of The Official Committee of Unsecured Creditors [D.I. 143] (the "**Notice of Disbandment**"). A copy of the Notice of Disbandment is attached as Exhibit "B" to the complaint for declaratory judgment filed in this adversary proceeding [Adv. D.I. 1] (the "**Complaint**").

On January 11, 2017, the Committee filed its Request for Status Conference to bring the Notice of Disbandment to the Court's attention and to raise its concern regarding the U.S. Trustee's lack of authority to disband the Committee. At the related status conference held on January 13, 2017, the Court took no position as to whether the U.S. Trustee has authority to disband the Committee and directed the Committee to commence this adversary proceeding seeking a declaratory judgment in that regard. *See* Transcript, *In re ScripsAmerica, Inc.*, Case No. 16-11991 (LLS) (Bankr. D. Del. Jan. 17, 2017) [hereinafter, the "**Transcript**"] at p. 49:13-21. A copy of the Transcript is attached as Exhibit "A" hereto.

SUMMARY OF ARGUMENT

The issue in this Adversary Proceeding is one of first impression for this Court: whether the U.S. Trustee has the authority to disband a statutory committee of unsecured creditors. There is no disagreement that the Bankruptcy Code is silent regarding the authority to disband a statutory committee. However, in addition to a review of the express statutory language, the

analysis must look to statutory interpretation based on implication of actual authority granted taking into account the legislative purpose behind the statutory provisions.

The relevant statutory provisions are found in section 307 and section 1102 of the Bankruptcy Code and section 586 of the Judicial Code. Analysis of the relevant statutes produces a clear theme – that the U.S. Trustee's administrative tasks were separated from the Court's judicial tasks. The Committee maintains that the proper statutory interpretation confers no authority on the U.S. Trustee to disband the Committee. This interpretation is premised on this overarching separation of judicial and administrative tasks, and the express statutory authority granted to the Court to determine matters relating to the membership of committees adequately representing their intended constituencies.

STATEMENT OF THE FACTS

The material facts relevant to the declaratory relief sought herein are uncontested and set forth above in the section pertaining to the nature and stage of the proceeding. In the way of background, the Committee notes the following additional facts.

On January 10, 2017, the U.S. Trustee requested a letter from counsel to the Committee as to why the U.S. Trustee should not disband the Committee, but without stating the basis or reason for the request. As set forth more fully in the Letter to Richard L. Schepacarter, Esquire from Scott D. Cousins dated January 11, 2017 (the "**January 11 Letter**"), counsel to the Committee was given a deadline of January 11, 2017 at 4:00 p.m. to respond to the U.S. Trustee's request. A copy of the January 11 Letter is attached to the Complaint as Exhibit "A."

Two and one-half hours *before* that deadline, the U.S. Trustee filed its Notice of Disbandment.

The January 11 Letter sets forth a very unusual set of circumstances where the Committee was placed into a position of justifying its existence *two months* after its formation based on a written request by the Debtor to the U.S. Trustee to "remove the Committee members

without further delay." Among the remarkable aspects of that request, however, is the fact that neither the Debtor nor the U.S. Trustee was willing to provide the Debtor's written request to the Committee or even to summarize the concerns, allegations or alleged bases or cause for disbandment to aid in the Committee's response. The Committee noted the unfairness and prejudicial effect of such in the January 11 Letter:

> While we respect the fact that "Debtor's bankruptcy counsel are former employees of your office, with more than two decades of service," Letter from Jeffrey B. Crockett to Andy R. Vara, *et. al* (Exh. A), the fact that the Committee cannot address the Debtor's allegations in its request puts the Committee at a severe disadvantage particularly given some of the accusations that the Debtor and its professionals have made against the Committee and its professionals.

See Exhibit A (January 11 Letter at p 2).

ARGUMENT

A. Summary Judgment

"The court shall grant summary judgment if the movant shows that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." FED. R. CIV. P. 56(a). *See also Celotex Corp. v. Catrett*, 477 U.S. 317, 322-23 (1986). "An issue is genuine only if there is a sufficient evidentiary basis on which a reasonable jury could find for the non-moving party, and a factual dispute is material only if it might affect the outcome of the suit under governing law." *Kaucher v. Cty. of Bucks*, 455 F.3d 418, 423 (3d Cir. 2006). In determining whether summary judgment is appropriate, the Court must "view the facts and draw inferences in the light most favorable to the nonmoving party." *Ray v. Twp. of Warren*, 626 F.3d 170, 173 (3d Cir. 2010). The Committee contends that summary judgment is appropriate in this circumstance in which the material facts relevant to the declaratory relief sought herein are uncontested.

B. The U.S. Trustee Lacks Authority to Disband the Committee

1. *The U.S. Trustee's Authority is Limited to Administrative Tasks*

The limitations and restrictions imposed on the U.S. Trustee's authority is an intentional consequence of legislative amendments over time to ensure satisfaction of the primary legislative objective to separate administrative tasks from judicial tasks. Prior to the Bankruptcy Reform Act of 1978, all administrative tasks (which included ensuring payment of withholding and other taxes by bankrupt debtors, organizing and scheduling meetings of creditors, organizing creditors' committees, appointing private trustees in Chapter 7 liquidation and Chapter 13 wage-earner cases, monitoring the filing of reports and schedules required by the Bankruptcy Code, and monitoring cases for signs of fraud or abuse) as well as judicial functions were handled by the bankruptcy courts. *See* H.R. REP. NO. 99-764, 99th Cong., 2d Sess. 17 (1986), *reprinted in* 1986 U.S.C.C.A.N. 5227, 5229.

The handling of both administrative and judicial functions by the bankruptcy courts created an appearance of favoritism, cronyism, and bias, which eroded the public confidence in the bankruptcy system. H.R. REP. NO. 99-764 at 17. In response, the Bankruptcy Reform Act of 1978 sought to separate administrative duties from judicial functions and, in so doing, leaving the bankruptcy judges free to resolve disputes untainted by knowledge of administrative matters unnecessary and perhaps prejudicial to an impartial judicial determination. *Id*. *See also* U.S. Trustee Objection at ¶ 24 (acknowledging "Congress's desire to separate the judicial and administrative functions and to screen courts from administrative functions, like appointing committees, that could raise conflict of interest issues."). It was these fundamental principles that established the U.S Trustee Pilot Program, which is now a permanent program. H.R. REP. NO. 99-764 at 32.

The emphasis on separation between administrative and judicial functions did not stop at the identification and separation of tasks but went so far as to ensure complete separation of

administrative and judicial functions by placing the Office of the U.S. Trustee within the Department of Justice, and not under the supervision of the Administrative Office for U.S. Courts. *See* H.R. REP. NO. 95–595, 95th Cong., 2d Sess. 115 (1978); *see also* 1978 U.S.C.C.A.N. at 5229.

There is no specific statutory authority for disbanding a creditors' committee. *See In re JNL Funding Corp.*, 438 B.R. 356, 361 (Bankr. E.D.N.Y. 2010) ("Section 1102 is silent as to this Court having power to order a committee to be disbanded. . . ."); *In re Texaco, Inc.*, 79 B.R. 560, 565 (Bankr. S.D.N.Y. 1987) ("The Bankruptcy Code is silent as to the elimination or merger of creditors' committees that were previously appointed by the United States Trustee"); 1 Robert E. Ginsberg & Robert D. Martin, *Ginsberg & Martin on Bankruptcy* § 4.02[B][1] at 4–46 to 47 (Susan V. Kelley, ed. 2013–1 Supp.) ("There is no statutory authority to disband a committee. . . ."). Accordingly, the Committee submits the U.S. Trustee has no express authority to do so. In addition, distinctions between administrative and judicial functions demonstrate that the U.S. Trustee has no implied authority to disband a committee. In other words, a U.S. Trustee is not implicitly authorized to disband a committee pursuant to its authority to appoint and monitor a committee, or otherwise, if the act of disbanding a committee involves judicial functions, which come under the exclusive authority of the Court.

2. *Section 1102(a)(1) Limits the U.S. Trustee's Authority to Committee Appointment*

In understanding the U.S. Trustee's limited authority in connection with statutory committees, it is important to begin with the express statutory language which authorizes the U.S. Trustee to act. Pursuant to section 1102(a) of the Bankruptcy Code, "as soon as practicable after the order for relief under chapter 11 of this title, the United States trustee ***shall*** appoint a committee of creditors holding unsecured claims and may appoint additional committees of creditors or of equity security holders as the United States trustee deems appropriate." 11 U.S.C.

§ 1102 (emphasis added). Bankruptcy Code section 1102(b) provides the U.S. Trustee guidance regarding the composition of the committee. Thus, "Congress directed that the UST shall appoint a creditors committee as early in the case as is practical, and . . . [the] UST is also given both statutory direction and discretion as to who should populate the committee." *JNL Funding*, 438 B.R. at 360–61.

The underlying rationale behind the evolution of Bankruptcy Code section 1102 was "to transfer the authority to appoint the chapter 11 committee of unsecured creditors from the court to the United States trustee as it is an administrative task." H.R. REP. NO. 99-764, at 28; U.S.C.C.A.N. at 5241; *see also JNL Funding*, 438 B.R. at 360 (citing *In re Barney's Inc.*, 197 B.R. 431, 438 (Bankr. S.D.N.Y. 1996) (some internal citations omitted)). In accordance with its limited administrative role in appointing a committee, the U.S. Trustee is involved in identifying who may hold significant unsecured claims, and should not engage in fact finding missions, nor independently decide who holds an allowable claim against the debtor; each of which is a purely judicial function. *JNL Funding*, 438 B.R. at 362.

3. *The Court's Judicial Authority Pursuant to Bankruptcy Code Section 1102 is Consistent with Authority Required to Disband Committee*

Consistent with the policy of separating administrative and judicial functions, following the enactment of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("**BAPCPA**"), section 1102(a)(4) of the Bankruptcy Code granted the Court the express authority to review a committee's membership and order its modification upon the "request of a party in interest and after notice and a hearing." 11 U.S.C. § 1102(a)(4). Bankruptcy courts were granted this express authority because the issue of committee membership and possible modification is a judicial function requiring a legal determination as to whether there is adequate representation. *See In re ShoreBank Corp.*, 467 B.R. 156, 161 (Bankr. N.D. Ill. 2012). This judicial authority to review "adequate representation" issues under section 1102(a)(4) includes

the ability to remedy problems of "improper representation" which may include actual and substantiated conflicts of interest. *See Id*; *see also* U.S. Trustee Objection at ¶ 42.

It is these very same issues of conflict requiring legal analysis that arise in the context of disbanding a committee. *See* U.S. Trustee Objection at ¶ 44, n.10 ("if U.S. Trustee discovers facts [to confirm the alleged conflict of interest]…the U.S. Trustee reserves any and all of his rights, duties and obligations to . . . disband the committee entirely."). The U.S. Trustee has no authority to perform such judicial tasks to determine adequate representation. Whether the context involves reconstituting a committee or disbanding a committee, the function remains one reserved exclusively for the judiciary as requiring legal analysis. The U.S. Trustee's role in this regard remains an administrative one in monitoring creditor committees and raising issues requiring judicial action, such as potential committee member conflicts, with the Court. *See, e.g., In re Enron Corp.*, 279 B.R. 671, 684 (Bankr. S.D.N.Y. 2002).[2]

4. *Judicial Code Section 586(A)(3)(E) Limits the U.S. Trustee to Monitoring*

The U.S. Trustee cites to sections 586(a)(3) and 586(a)(3)(E) of the Judicial Code in support of its position that it has statutory authority to disband the Committee. *See* Exhibit B to the Complaint. Those provisions of the Judicial Code, however, limit the U.S. Trustee's statutory authority to the supervision of the "administration of cases and trustees in cases under chapter 7, 11, 12, 13, or 15 by, whenever the United States trustee considers it to be appropriate—*monitoring* creditors' committees appointed under title 11. . . ." 28 U.S.C. § 586(a)(3)(E) (emphasis added). The concept of "monitoring" is consistent with the U.S. Trustee's role in performing administrative tasks. The legislative history supports this conclusion by noting that should the U.S. Trustee become aware of issues through its monitoring

[2] The interpretive doctrine *ex pressio unius est exclusio alterius*—the expression of one thing is the exclusion of another—seems most appropriate in the interpretation of Bankruptcy Code section 1102(a)(1) which expressly grants the U.S. Trustee authority to appoint a committee, yet is completely silent on any authority the U.S. Trustee has to disband a committee. *Cf.* U.S Trustee Objection at ¶ 29.

function that need to be addressed, the U.S. Trustee may comment to the court through pleadings, motions, and other appropriate filings on any of the matters listed in 28 U.S.C. §586(a). *See* H.R. REP. NO. 99-764 at 24-25, 1986 U.S.C.C.A.N. 5227, 5237. There is no support for the proposition that "monitoring" provides authority for the U.S Trustee to perform judicial functions, including that of disbandment.

Therefore, in this Bankruptcy Case the U.S. Trustee's role in "monitoring creditors' committees" limits the U.S. Trustee's action in connection with possible disbandment to presenting the Court with any information it deems appropriate in such regard. This approach is in keeping with the U.S. Trustee's role as an officer of the Department of Justice who protects the public interest by aiding bankruptcy judges in monitoring certain aspects of bankruptcy proceedings, and has the right, pursuant to Bankruptcy Code section 307, to be heard on any issue in any case or proceeding under the Bankruptcy Code. *See In re United Artists Theatre Co.*, 315 F.3d 217, 225 (3d Cir.2003); *see also In re Zarnel*, 619 F.3d 156, 162 (2d Cir. 2010); *see also In re Columbia Gas Sys.*, 33 F.3d 294, 296 (3d Cir.1994) ("[i]t is difficult to conceive of a statute that more clearly signifies Congress's intent to confer standing").

CONCLUSION

The Committee agrees with the U.S. Trustee in that there is "no authority to contravene the specific and carefully crafted [Bankruptcy] Code provisions governing the formation, modification, and oversight of official committees." U.S. Trustee Objection at ¶ 1. The Committee also agrees with the U.S. Trustee concerning the importance evidenced by the legislative history in maintaining the separation between judicial functions and administrative functions performed by the U.S. Trustee. It is against this backdrop that the Committee maintains that only the Court may have the power to disband a committee as it involves judicial functions pertaining to the legal analysis of adequate representation and/or improper representation, analogous to those judicial functions provided to the Court pursuant to

Bankruptcy Code section 1102(4). Consequently, the U.S. Trustee is clearly not authorized to disband a committee. This is not to suggest that the U.S. Trustee's role is secondary or less meaningful, but rather that its role is a critical one intended to provide *aid* to bankruptcy judges in carrying out judicial functions. In this role as watchdog and facilitator, the U.S. Trustee is not authorized to circumvent the Court and unilaterally disband the Committee. This is precisely the separation of administrative and judicial tasks intended by the legislature. Plaintiff, therefore, respectfully maintains that it is appropriate for this Court to enter judgment against the above-captioned defendants declaring the rights and legal relations of the parties, including declaring that the U.S. Trustee violated its limited power and authority by purporting to disband the Committee, that the filing of the Notice of Disbandment was not effective to disband the Committee and is null and void, and declaring that the Committee continues to exist as a statutory committee.

Dated: January 23, 2017
Wilmington, Delaware

BAYARD, P.A.

/s/ Scott D. Cousins

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