IN THE UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF MISSOURI
EASTERN DIVISION

In re:	) **Case No. 12-40164-659**
	) **Chapter 7**
	)
BURTON DOUGLAS MORRISS,	)
	) **Judge Kathy A. Surratt-States**
	)
Debtor.	) **Hearing Date: March 19, 2012**
	) **Hearing Time: 10:00 a.m.**
	) **Hearing Location: Courtroom 7 North**
	)

OBJECTION OF RECEIVERSHIP ENTITIES TO APPLICATION FOR ORDER PURSUANT TO 11 U.S.C. SECTION 327 OF THE BANKRUPTCY CODE AUTHORIZING EMPLOYMENT AND RETENTION OF THE ASHCROFT LAW FIRM, LLC AS COUNSEL FOR DEBTOR *NUNC PRO TUNC* TO JANUARY 20, 2012 OR, ALTERNATIVELY, A RULING THAT THE RETENTION OF THE ASHCROFT LAW FIRM, LLC IS BEYOND THE SCOPE OF THE DEBTOR'S ESTATE

COME NOW Acartha Group, LLC ("Acartha Group"), Acartha Technology Partners, L.P., MIC VII, LLC, and Gryphon Investments III, LLC (collectively, the "Receivership Entities"), by and through Claire M. Schenk as Receiver ("Receiver"), creditors and parties in interest, and with the assistance of counsel Thompson Coburn LLP, object to the Application for Order Pursuant to 11 U.S.C. Section 327 of the Bankruptcy Code Authorizing Employment and Retention of the Ashcroft Law Firm, LLC as Counsel for Debtor *Nunc Pro Tunc* to January 20, 2012 or, Alternatively, a Ruling That the Retention of the Ashcroft Law Firm, LLC is Beyond the Scope of the Debtor's Estate (the "Application"). In support of this Objection to the Application (this "Objection"), the Receivership Entities state:

Background on Debtor's Case and SEC Case Resulting in Appointment of Receiver

1. On January 9, 2012 (the "Petition Date"), only days before the filing of the SEC Case more particularly described below, Burton Douglas Morriss, debtor in the above captioned case ("Debtor"), filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code with the United States Bankruptcy Court for the Eastern District of Missouri, thereby securing the shelter of this forum.

2. Prior to the relief being granted in the SEC Case as more particularly described below, Debtor served as the chief executive officer and chairman of Acartha Group's board of directors, the

managing member of MIC VII, LLC. Debtor also served as a manager of Gryphon Investments III, LLC, the general partner of Acartha Technology Partners, L.P. Debtor also served as the chairman and controlling member of Morriss Holdings, LLC and a member of its board of directors.

3. On January 17, 2012, the United States Securities and Exchange Commission (the "SEC") filed its *Complaint for Injunctive and Other Relief* (the "Complaint") against Debtor, Acartha Group, LLC, Acartha Technology Partners, L.P., MIC VII, LLC, Gryphon Investments III, LLC and Morriss Holdings, LLC (collectively, the "SEC Defendants") in the United States District Court for the Eastern District of Missouri (the "Missouri District Court"), Case No. 4:12-cv-00080-CEJ (the "SEC Case"). *See* Complaint (SEC Case, Dkt. No. 1).

4. Papers filed by the SEC in the SEC Case allege, among other things, that:

- From 2005 until the present, Debtor, through the Receivership Entities, defrauded investors by transferring more than $9 million in investor funds to himself and a related company, Morriss Holdings, LLC.
- Debtor and the Receivership Entities made these transfers without disclosing to or seeking approval of investors.
- The transfers resulted not only in the misappropriation of investors' money, but the dilution of their shares of the Receivership Entities' investments.
- Approximately 97 investors invested at least $88 million in Acartha Group, a private equity fund management company Debtor controlled, and the funds and other entities it managed, namely MIC VII, Acartha Technology Partners, and Gryphon Investments.
- Those investments are now at risk as both Acartha Group and the investment entities controlled by Debtor are facing a financial shortfall.

5. Relief sought in the SEC Case included the immediate appointment of a receiver for the Receivership Entities to: (a) administer and manage the business affairs, funds, assets, choses in action and other property of the Receivership Entities, (b) act as sole and exclusive managing member or partner of the Receivership Entities, (c) maintain sole authority to administer any and all bankruptcy cases in the manner determined to be in the best interests of the Receivership Entities' estate, (d) marshal and

safeguard all of the assets of the Receivership Entities, and (e) take whatever actions are necessary for the protection of investors.

6. The SEC additionally sought to immediately freeze the assets of the Receivership Entities and for certain other emergency relief.

7. On January 17, 2012, the Missouri District Court granted (a) the SEC's emergency motion for the appointment of a receiver pursuant to its Order Appointing Receiver (the "Receivership Order"); and (b) the SEC's emergency motion to freeze assets, pursuant to a certain Asset Freeze Order and Other Emergency Relief (as modified by the Missouri District Court's supplemental Order entered January 19, 2012, the "Initial Asset Freeze Order").

8. On January 27, 2012, after a hearing, the Missouri District Court entered a final asset freeze order, by which the SEC obtained an order freezing the Receivership Entities' and Morriss Holdings, LLC's assets, an order requiring sworn accountings, and an order prohibiting the destruction of documents (the "Final Asset Freeze Order").

9. Pursuant to the Receivership Order, the Missouri District Court appointed the Receiver as receiver for the Receivership Entities. The Receiver was not appointed a receiver over Debtor under the Receivership Order.

10. Among other things, the Receivership Order authorizes the Receiver to operate and manage the businesses and financial affairs of the Receivership Entities and directs that the Receiver succeeds to all rights and powers of managing member and/or managing partner of the Receivership Entities, with sole and exclusive authority to take all actions necessary in such capacity.

11. As more fully described in the SEC Case, Debtor is alleged to have committed, and may continue to commit, various acts of fraud. As alleged in the SEC Case, between 2005 and 2011, Debtor, using the Receivership Entities, fraudulently transferred approximately $9.1 million of investor funds to himself and his family's holding company, Morriss Holdings, LLC, for his personal use.

12. Among other things alleged, Debtor used the fraudulently obtained investor funds to satisfy personal loans, pay alimony, and take expensive vacations.

13. During the pendency of his Chapter 11 proceeding, Debtor did not perform the responsibilities of a Debtor as required under the Bankruptcy Code and related Rules. Among other things, Debtor (i) did not timely file statements and schedules, (ii) did not appear for the first meeting of creditors as initially scheduled in this case for February 7, 2012, and (iii) has not responded to various requests to provide information to the Office of the U.S Trustee.

14. As a result of Debtor's handling of his Chapter 11 proceeding, on or about February 6, 2012, the Receivership Entities acting through the Receiver filed with this Court an emergency Motion seeking the appointment of a Trustee in Debtor's Chapter 11 case, or alternatively, the conversion of the Debtor's Chapter 11 case to one under Chapter 7 (the "Motion for Trustee").

15. This Court heard the Motion for Trustee on an expedited basis on February 13, 2012. Following appropriate notice and the opportunity to be heard, this Court entered an Order on February 13, 2012 granting the Motion for Trustee with respect to the alternative relief thereby sought, converted Debtor's case to one under Chapter 7, and appointed Charles W. Riske as Chapter 7 Trustee (the "Trustee").

16. Prior to the conversion of Debtor's case, Debtor had not undertaken the appropriate steps to obtain an order from this Court approving counsel.

17. Since the conversion of Debtor's case from one under Chapter 11 to one under Chapter 7, the Trustee moved to employ as counsel the law firm of Summers Compton Wells PC by application filed with this Court on February 22, 2012. The Trustee's application to employ counsel was granted by order of this Court entered on February 24, 2012.

18. Further since the conversion of Debtor's proceeding to a case under Chapter 7, Debtor did not appear at a meeting of creditors scheduled for March 8, 2012.

19. On February 21, 2012, the Ashcroft Law Firm, LLC d/b/a Ashcroft Hanaway ("Ashcroft Hanaway"), filed its Application for Order Pursuant to 11 U.S.C. Section 327 of the Bankruptcy Code Authorizing Employment and Retention of the Ashcroft Law Firm, LLC as Counsel for Debtor Nunc Pro Tunc to January 20, 2012 or, Alternatively, a Ruling that the Retention of the Ashcroft Law Firm, LLC is

Beyond the Scope of the Debtor's Estate ("Application"). In the Application, Ashcroft Hanaway seeks, in addition to its employment, to pay its fees from proceeds of (a) a certain director's and officer's insurance policy issued by Federal Insurance Company ("Federal") numbered 8207-6676 (the "Policy"), and (b) the sale of a membership interest of an entity known as Malinmor Land Company, LLC ("Malinmor"). Ashcroft Hanaway asserts, on its information and belief, that the Burton Douglas Morriss Irrevocable Trust ("Trust") is a member of Malinmor and that such interest is beyond "the scope of these proceedings."

Description of Insurance Policy

20. Acartha Group obtained the Policy to cover claims made during the period of the Policy against insureds (which include Acartha Group, other organizations, and their executives) for a wide variety of wrongful acts, including errors, misstatements, misleading statements, acts, omissions, neglect, or breach of duty. Ashcroft Hanaway does not dispute that the Policy itself is owned by Acartha Group. *See* Application at p. 7, n. 3. The Receiver contends that the Policy is owned by Acartha Group and that the *proceeds thereof* are property of Acartha Group and other Receivership Entity insureds. However, to the extent that Morriss has any rights or interest in proceeds of insurance under the Policy, these constitute assets of the bankruptcy estate pursuant to 11 U.S.C. § 541 and are therefore under the control of the Trustee for the specific benefit of those harmed by the conduct described in the SEC Case.

Bases for Objection

21. With respect to the request made in the Application that the Ashcroft Firm be employed as Debtor's counsel, the Court should deny the requested relief because, among other reasons:

(a) the Chapter 7 Trustee assumed control of the Debtor's estate in mid-February and appropriately employed counsel through papers filed with this Court and that counsel properly represents the interests of the bankruptcy estate, *see* 11 U.S.C. § 327 and Fed. R. Bankr. Proc. 2014, providing that the *trustee* is the appropriate party to pursue employment of counsel and that such employment should be sought by application to the Court alleging, among other things, the necessity for such employment;

(b) the retention of counsel to the Debtor in a Chapter 7 proceeding (particularly for purposes of defending Debtor against criminal allegations and allegations of civil fraud) is unnecessary and affords no benefit to the bankruptcy estate; and

(c) even if a request to hire Debtor's counsel *nunc pro tunc* were appropriate under the circumstances (and the Receivership Entities contend it is not), counsel has not undertaken the proper steps to be retained or shown what benefit such counsel afforded or would afford the estate by such retention, *see* 11 U.S.C. § 329; Fed. R. Bankr. P. 2016.

22. Furthermore, the Application fails to identify what work has been performed by the Aschcroft firm and the law firm of Graves, Bartle, Marcus and Garrett (GBMG) for the benefit of the bankruptcy estate commencing January 20, 2012 and at what cost. The Memorandum filed in Support of the Application vaguely advises that the law firm of Graves, Bartle, Marcus and Garrett (GBMG) has "contracted with Aschcroft Hanaway to provide joint defense in this matter" and that GBMG also will provide "services to the Debtor in the above-described representation." However, GBMG is not seeking to be employed through the Bankruptcy Court nor has it made appropriate disclosures relative to its role and the compensation it has received.

23. With respect to the request in the Application for a determination that certain assets be made available to pay legal fees and costs associated with defending Debtor as to claims asserted against him in the SEC Case and a pending criminal investigation, the Court should deny the requested relief because, among other reasons:

(a) Acartha Group owns the Policy[1] and holds all rights and interests arising thereunder, including the right to insurance proceeds, *see In re Pasquinelli Homebuilding, LLC*, 463 B.R. 468, 472 (Bankr. N.D. Ill. 2012) (as an insured under the policy, a corporation has rights in and to the proceeds of the policy, and "where the policy provides both direct coverage to the directors and officers,

[1] *In re Eastwind Group, Inc.*, 303 B.R. 743, 746 (Bankr. E.D. Pa. 2004) ("corporations pay for and own [D&O] insurance policies"); *In re GB Holdings, Inc.*, No. 05-42736/JHW, 2006 WL 4457350, at *2 (Bankr. D.N.J. Sept. 21, 2006) (as the named entity on the D&O policy, the corporation was the owner of the policy).

and direct entity coverage, 'the general rule is that since the insurance proceeds may be payable to the [corporation] they are property of the [corporate] estate'"); however, to the extent that any rights in insurance proceeds flow to Debtor, the Trustee controls these rights for the benefit of the bankruptcy estate, *see In re Williams*, 222 B.R. 662 (Bankr. S.D. Fla. 1998) (finding that Chapter 7 trustee obtained from debtor, and controlled, debtor's right to determine how insurance proceeds would be distributed), including without limitation, the right to waive use of insurance proceeds to defend against criminal and civil fraud allegations, and to instead permit such proceeds to be used to pay third party indemnity claims, thereby reducing claims assertable against the estate;

(b) Debtor fails to establish that the interest in Malinmor he proposes to liquidate to pay legal fees is not an asset of the estate;

(c) the proper vehicle for establishing whether an interest in property is an asset of the estate is the filing and prosecution of an adversary proceeding, and not the filing of an application or motion;[2]

(d) the Trustee has not had sufficient opportunity to determine the rights in such assets or the scope of the bankruptcy estate due to Debtor's lack of cooperation in this Case and due to the Trustee's recent appointment and retention of counsel to assist in locating assets of the estate; and

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[2] *See* Fed R. Bankr. P. 7001(2); *see also In re Johnson*, 346 B.R. 190, 195-96 (9th Cir. BAP 2006) (Federal Rules of Bankruptcy Procedure require an adversary proceeding to determine interests in property; thus, in a relief from stay motion that is a Rule 9014 contested matter, not a Rule 7001 adversary proceeding, the bankruptcy court is not authorized by the rules of procedure to enter an 'in rem' order that determines interests in property) (citing *In re Loloee*, 241 B.R. 655, 661-62 (9th Cir. BAP 1999)); *In re Indian Nat. Finals Rodeo, Inc.*, No. 11-60113-11, 2011 WL 2470628, at *8 (Bankr. D. Mont. June 20, 2011) (determination of interest in property requires adversary proceeding); *In re Whitehall Jewelers Holdings, Inc.*, No. 08-11261 (KG), 2008 WL 2951974, at *6 (Bankr. D. Del. July 28, 2008) (court cannot determine whether the property is property of the estate through a contested matter; the bankruptcy rules require that an adversary proceeding be commended to determine the 'validity, priority or extent of [an] interest in property.'); *In re McGreevy*, 388 B.R. 917, 922 (Bankr. D.S.D. 2008) ("[t]o the extent treatment covered by the insurance policy is continuing, i.e., if the policy limits have not been reached, the parties will need to estimate the amount of reimbursable post-petition medical claims or ask the Court to do so through an adversary proceeding to determine property of the estate"); *In re First Assured Warranty Corp.*, 383 B.R. 502 (Bankr. D. Colo. 2008) (motion to be excused from having to turn over assets was in reality a request for determination that the debtor did not have an interest in the assets sufficient to bring those assets into property of the estate, such that the request must be brought by way of an adversary proceeding and not by motion).

(e) allowing Morriss to utilize proceeds of insurance to cover legal fees and costs to defend against allegations of criminal misconduct will effect an inequitable result under the circumstances.

24. Notwithstanding assertions to the contrary in the Application and Memorandum in Support thereof, there is little expectation that use of Policy proceeds to pay costs of defense for Debtor will result in the reduction of claims against the estate under the circumstances of this case. Debtor's right under the terms of the Policy to use proceeds of insurance for costs of defense may be limited due to the nature of his alleged misconduct. Accordingly, it is possible that if a defense is pursued for Debtor, the insurance company would be willing to pay for such defense only with reservation of rights and expect reimbursement of costs of defense from Debtor if such costs are determined not covered under the Policy. Further, use of insurance proceeds to cover costs of defense will reduce the recovery for indemnification dollar for dollar, and Debtor is unwilling or unable to secure his likely reimbursement obligation, whether from third-party resources or otherwise. Debtor's use of the proceeds of the Policy to cover costs of defense in this manner is inequitable and defeats the rights and interests of those incurring covered losses. As noted in the Memorandum in Support of the Application, rights and interests in insurance proceeds are determined based on the facts and circumstances of each case. *See* Application at p. 7 and cases cited therein; *see, e.g., In re Beach First Nat'l Bancshares, Inc.*, 451 B.R. 406, 409 (D.S.C. 2011). None of the cases cited in support of the Application involve a company principal as the Debtor-insured. In this instance, the Debtor is seeking to use insurance proceeds for his own benefit and independent of the Trustee of the bankruptcy estate, when, to the extent the Debtor has an interest in policy proceeds, such proceeds are property of the estate and under the Trustee's control for the benefit of those who may have claims against Debtor and other insureds.[3]

[3]Ashcroft Hanaway has also asserted Debtor's entitlement to Policy proceeds in pleadings filed in the SEC Case. In response, the Receiver has asserted that any use of the proceeds by Debtor for costs of defense would violate the asset freeze in place in that Case, otherwise violate the terms and conditions of the Policy and effect an inequitable result. Thus, the status of the Policy and the proceeds thereof is the subject of debate in multiple forums. The Trustee is only now becoming familiar with Morriss' efforts in the SEC case to obtain the use of insurance proceeds and to the extent Morriss is determined in the SEC Case as having any rights in the Policy proceeds, the Trustee

25. Even assuming the Application and a hearing thereon constitute the proper means to assert and determine Debtor's rights, if any, in the Policy (and the Receivership Entities contend it is not and that an adversary proceeding is the proper proceeding in which to determine such matters), the Application fails to demonstrate that: (i) Debtor has any rights or interests in the Policy or the proceeds thereof (or why any rights that Debtor may have held are not property of the estate), or (ii) allowing use of proceeds to cover the costs of Morriss' legal defense affords any benefit to the bankruptcy estate or is otherwise an equitable allocation of rights under the Policy. Use of insurance proceeds to pay legal fees and costs to defend Debtor against allegations of criminal misconduct and fraud offers no benefit to the estate given the terms and limitations of the Policy. Debtor has asserted that he is entitled to use Policy proceeds to cover costs of defense. However, Debtor has not established that the Policy covers Debtor's use of proceeds for mounting a defense against criminal conduct or fraud. Nor has Debtor explained why, given the terms of Section 541 of the Bankruptcy Code, any rights Debtor may have under the Policy are not now assets of the bankruptcy estate under the control of the Chapter 7 Trustee. Further, given that Debtor is asserting a Fifth Amendment privilege in actions as to which the automatic stay is inapplicable, and the automatic stay currently shields Debtor from being sued as to other claims that might be asserted against him, Debtor has protections available to him beyond those of other insureds. The Policy (which has a single limit and is eroded by payment of costs of defense) covers losses other than those of Debtor and the Court must balance these competing interests in an equitable manner. Even assuming Debtor has any rights under the Policy, and regardless of who may hold those rights, allocating Policy proceeds to Debtor for the uses requested under the circumstances by Ashcroft Hanaway unduly burdens other insureds and would work greater harm than good relative to the resources of the Policy.

26. In conclusion, the Application should be denied because Morriss is not entitled to have counsel employed as a Chapter 7 debtor, and even if he was, he has not followed the appropriate rules in order to have counsel properly engaged through this Court. Additionally, Morris has failed to properly

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ought to control those rights.

evidence that he has any rights or interests in the proceeds of the Policy, or that to the extent he has any such rights and interests, such are not assets of the bankruptcy estate subject to the control of the Chapter 7 Trustee. The Policy is an asset of Acartha Group – even Morriss does not dispute this - and the Receivership Entities contend that the proceeds of the Policy are assets of the Receivership Entities. Furthermore, proceeds of the Policy, even if the Debtor or the Chapter 7 Trustee has any rights or interests in the same, are subject to the asset freeze order in place in the SEC case. Finally, even assuming Morriss or the Trustee hold any rights or interests in the proceeds of the Policy, access to such proceeds should be limited on an equitable basis for the benefit of the Receivership Entities to cover investor losses. Under the facts and circumstances of this case, allowing access to insurance proceeds for the purposes of defending Morriss against allegations of criminal misconduct and fraud would work an injustice.

WHEREFORE, the Receivership Entities respectfully request the Court enter an Order:

A. Denying the relief sought by the Application; and

B. Providing for such other and further relief as the Court deems just and proper.

Respectfully submitted,

THOMPSON COBURN LLP

By *__/s/ Cheryl A. Kelly__*

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CERTIFICATE OF SERVICE

In addition to those parties served with this document by the Court's CM/ECF system, the undersigned certifies that she served a true and complete copy of this document by first class mail, postage prepaid, upon each of the parties listed below this the 12th day of March, 2012:

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