

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
GREENSBORO DIVISION

ENTERED

MAR 30 2004

U.S. BANKRUPTCY COURT
MDNC - RMB

IN RE:)
)
Inter-Act Electronics, Inc.,) Case No. 02-11557C-7G
)
Debtor.)
_____)
)
Charles M. Ivey, III, Trustee)
for the Bankruptcy Estate of)
Inter-Act Electronics, Inc.,)
)
Plaintiff,)
)
v.) Case No. 03-2035
)
Albertson's, Inc.,)
)
Defendant.)
)

ORDER

This adversary proceeding came before the court on January 13, 2004, for hearing upon the Defendant's motion to compel arbitration and to stay proceedings. Edwin R. Gatton and Charles M. Ivey, III appeared on behalf of the Plaintiff and Jeffrey E. Oleynik and Clinton R. Pinyan appeared on behalf of the Defendant.

BACKGROUND

The following background facts are reflected in the Plaintiff's complaint. The Plaintiff is the Chapter 7 trustee for Inter-Act Electronics, Inc. (the "Debtor"). At various times between 1994 and 1997, the Debtor entered into agreements with three different grocery store chains: Lucky Stores, Inc. ("Lucky");

ACME Markets, Inc. ("ACME"); and Jewel Food Stores, Inc. ("Jewel"). Under these agreements, the Debtor installed computer terminals in grocery stores of Lucky, ACME and Jewel that provided customized coupons to shoppers, based upon identification of the customers through their shopping loyalty cards. The Debtor was paid by manufacturers and distributors of groceries for distribution of the coupons, and the Debtor in turn agreed to pay Lucky, ACME and Jewel a portion of each coupon redeemed by customers. After a number of terminals had been installed in the Lucky, ACME and Jewel stores, the Plaintiff alleges that the agreements were breached and wrongfully terminated by the Defendant (who had acquired Lucky, ACME and Jewel). The agreements provided that the terminals and equipment installed by the Debtor remained the property of the Debtor and that upon termination could be removed by the Debtor. Notwithstanding such provisions, the Plaintiff alleges that the Debtor was not permitted to reclaim the terminals and equipment.

The Plaintiff's complaint contains claims for breach of contract, fraud, conversion, failure to act in good faith, unfair and deceptive trade practices and bailment. The claims for failure to act in good faith and for unfair and deceptive trade practices have been voluntarily dismissed. The claims for breach of contract and fraud involve only the Lucky stores and the agreements between the Debtor and Lucky. The conversion and bailment claims, on the

other hand, involve the ACME and Jewel stores, as well as the Lucky stores. In the conversion claim, the Plaintiff alleges that the Defendant "damaged, disposed of and converted to its own use equipment owned by Inter-Act" and thereby converted such equipment and seeks to recover the value of the property allegedly converted. In the bailment claim, Plaintiff alleges that when the Debtor placed its terminals and equipment in the Lucky, ACME and Jewel stores, a bailment was created for the mutual benefit of the parties and that the Defendant is liable for the terminals and equipment which were not returned by the Defendant after the agreements were terminated.

MATTER BEFORE THE COURT

Defendant's motion to compel arbitration is based upon a provision contained in the Jewel agreement which provides:

Arbitration. In the event a problem or dispute shall arise with respect to the performance or interpretation of the Agreement which cannot be informally settled by the parties, the matter shall be submitted to a single arbitrator selected by the parties, unless they are unable to agree on an arbitrator in which case the American Arbitration Association shall choose the arbitrator. If the matter is submitted to arbitration, it shall be conducted in accordance with the commercial arbitration rules of the American Arbitration Association and shall be held in the metropolitan area of Chicago. Both parties expressly covenant to be bound by the decision of the arbitrator as final determination of the matter in dispute. Each party shall assume its own costs, but

shall share the cost of the resolution entity equally. Judgment upon the award rendered by the dispute resolution entity may be entered in any court having jurisdiction.

Based upon this provision, the Defendant prays that the court compel arbitration of all claims "related to Debtor's relationship with Jewel" and that the court "stay all proceedings in this Court on those matters pending completion of the arbitration." Since the only claims involving Jewel are the conversion and bailment claims the motion amounts to a request that the conversion and bailment claims against Jewel be referred to arbitration. Since the Lucky and ACME agreements do not contain arbitration clauses, the Defendant has not sought to compel arbitration of the conversion and bailment claims against Lucky and ACME.

DISCUSSION

The property of a bankruptcy estate under § 541 of the Bankruptcy Code includes the pre-petition causes of actions and contracts of the debtor. This entitles the bankruptcy trustee to make claims under the non-executory contracts of the debtor and to sue on the pre-petition causes of action of the debtor. When the trustee does so under § 541, the trustee is the successor to the debtor's interest and stands in the shoes of the debtor. In that posture, the trustee has the rights possessed by the debtor and, conversely, is subject to the same defenses that could have been asserted against the debtor had the action been filed by the debtor. See generally 3 COLLIER ON BANKRUPTCY ¶ 323.03 [2] (15th ed.

rev. 2003). If a cause of action asserted by a bankruptcy trustee is covered by an agreement by the debtor to arbitrate, the same rule is controlling and the agreement to arbitrate may be invoked against the trustee just as it could have been against the debtor. See Hays and Co. v. Merrill Lynch, Pierce, & Smith, Inc., 885 F.2d 1149, 1153-54 (3d Cir. 1989); Fallick v. Kehr, 369 F.2d 899, 904 (2d Cir. 1966); In re Ostrom-Martin, 188 B.R. 245, 251 (Bankr. C.D. Ill. 1995). Hence, if the conversion and bailment claims asserted in this proceeding are encompassed by the arbitration clause contained in the Jewel Agreement, then the Plaintiff, as the successor to the Debtor's rights, is subject to a contractual obligation to arbitrate those claims. Defendant's motion to compel arbitration of those claims necessitates a determination of whether those claims are covered by the arbitration clause.

In deciding whether the arbitration clause is applicable to the conversion and bailment claims, this court must remain cognizant of the rules of construction that are applicable to arbitration agreements. Because of the strong federal policy favoring arbitration, "any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration." Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24-25, 103 S.Ct. 927, 941, 74 L.Ed.2d 765 (1983). This "heavy presumption of arbitrability requires that when the scope of the arbitration clause is open to question, a court must decide the

question in favor of arbitration. . . ." Long v. Silver, 248 F.3d 309, 316 (4th Cir. 2001). Consequently, an arbitration agreement must be enforced "unless it may be said with positive assurance that the arbitration clause is not susceptible of an interpretation that covers the asserted dispute." Id. The arbitration clause in the Jewel Agreement provides for the arbitration of any "problem or dispute . . . with respect to the performance or interpretation of the Agreement." Giving effect to the foregoing rules of construction, the court concludes that this language is broad enough to encompass any dispute or claim having a significant relationship with the Jewel Agreement, including tort claims related to the Agreement. See Long, 248 F.3d at 316; J.J. Ryan & Sons v. Rhone Poulenc Textile, S.A., 863 F.2d 315, 321 (4th Cir. 1988).

The court is satisfied that both the conversion and bailment claims are related to the Jewel Agreement to a significant degree. The equipment and property in question came into the possession of Jewel pursuant to the Jewel Agreement. The Jewel Agreement specifically addresses the return of the equipment upon the termination of the Agreement, providing:

Upon the termination of this Agreement, Retailer shall grant I-A reasonable access to Retailer's stores and other locations where Program equipment is installed so that I-A may pick up all elements and components of the Program . . . including, without limitation the equipment"

The conversion and bailment claims involve a "dispute" regarding the "performance" of these duties by the Defendant or its predecessor. In proving the claims, the Plaintiff will need to show that the Defendant treated the equipment in a manner that was "unauthorized" by the terms of the contract. See In re Rosin, 620 N.E.2d 368, 370 (Ill. 1993) (conversion involves unauthorized or wrongful possession of another's property); Liddle v. Salem Sch. Dist. No. 600, 619 N.E.2d 530, 531-32 (Ill. App. Ct. 1993) (in bailment claim, plaintiff must establish existence of contractual bailment and failure to deal with property in accordance with the terms of contract). Because of the significant relationship between the Jewel Agreement and the conversion and bailment claims, both claims are subject to the arbitration clause in the Jewel Agreement.

Based upon the contention that the conversion and bailment claims against the Defendant are core matters, the Plaintiff argues that this court therefore has the discretion to deny the motion to compel arbitration even if the arbitration agreement does apply to the claims. The conversion and bailment claims are non-bankruptcy, state-law claims being asserted by the Plaintiff pursuant to § 541 and ordinarily would be non-core matters. See Hays, 885 F.2d at 1156 n.9. However, because the Defendant filed a proof of claim in this case, the Plaintiff contends that the claims are compulsory

counterclaims against the Defendant which were converted to core matters as a result of Defendant having filed the proof of claim. See In re Thermal Systems, Inc., 294 B.R. 784, 789 (Bankr. N.D. Okla. 2003) ("the adjudication of counterclaims in the context of claim allowance constitutes the adjudication of public rights by the bankruptcy court. . . . Both the claim and the Complaint are core proceedings"); In re Carrington Gardens Assoc., 248 B.R. 753, 767 (Bankr. E.D. Va. 2000) ("By filing its proof of claim, HUD in essence converted Carrington's adversary proceeding from a breach of contract 'related to' its bankruptcy to a proceeding to adjudicate a counter claim 'arising under' title 11 as part of the Court's claim adjudication capacity."). However, even if the conversion and bailment claims are treated as core matters, it does not follow automatically that the court may decline to enforce the arbitration agreement that binds these parties. Instead, the same process and standard used with respect non-core matters in deciding whether an arbitration agreement must be enforced also should be used with core matters, i.e., whether enforcement of the arbitration clause would seriously jeopardize the objectives of the Bankruptcy Code or would adversely affect the underlying purpose of the Bankruptcy Code. See United States Lines, Inc. v. American S.S. Owners Mut. Prot. and Indem. Ass'n, Inc., 197 F.3d 631, 640 (2d Cir. 1999), cert. den., 529 U.S. 1038 (2000); Matter of

National Gypsum Co., 118 F.3d 1056, 1067 (5th Cir. 1997).

In National Gypsum the court rejected the argument that a bright line test should be adopted under which all core proceedings would be deemed inherently irreconcilable with the Bankruptcy Code and hence never subject to arbitration, noting that "not all core bankruptcy proceedings are premised on provisions of the Code that 'inherently conflict' with the Federal Arbitration Act; nor would arbitration of such proceedings necessarily jeopardize the objectives of the Bankruptcy Code." 118 F.3d at 1067. Rather, the court held that nonenforcement of an arbitration agreement involving a core matter should turn "on the underlying nature of the proceeding, i.e., whether the proceeding derives exclusively from the provisions of the Bankruptcy Code and, if so, whether arbitration of the proceeding would conflict with the purposes of the Code." Id. The court provided further guidance by observing that with respect to core matters, "a bankruptcy court retains significant discretion to assess whether arbitration would be consistent with purpose of the Code, including the goal of centralized resolution of purely bankruptcy issues, the need to protect creditors and reorganizing debtors from piecemeal litigation and the undisputed power of a bankruptcy court to enforce its own orders." Id. at 1069.

The party resisting the enforcement of an arbitration agreement has the burden of showing the requisite conflict between arbitration and the purposes or policies of the Bankruptcy Code. See Shearson/American Express, Inc. v. McMahon, 482 U.S. 220, 227, 107 S.Ct. 2332, 2337, 96 L.Ed.2d 185 (1987). No such showing has been made in the present case. The conversion and bailment claims involve and arise from pre-petition conduct, rights and obligations and were not created by bankruptcy law nor did they arise during the bankruptcy case. The claims involve only issues of state law. If such claims are core matters, it is only because they, in effect, are counterclaims to the proof of claim that the Defendant filed in the underlying bankruptcy case. As Defendant points out, it is doubtful that the arbitration of these claims would be preclusive as to any of the issues involved in its proof of claim which seeks solely to recover money allegedly owed by the Debtor under the terms of the Lucky, ACME and Jewel agreements. There has been no showing that referring such claims to arbitration will unduly interfere with the claims allowance process or alter or effect the allocation of assets among creditors or otherwise jeopardize the objectives of the Bankruptcy Code. See generally In re The Singer Co. N.V., 2001 WL 984678 (S.D.N.Y.); In re Transport Assoc., Inc., 263 B.R. 531 (Bankr. W.D. Ky. 2001).


Plaintiff argues that referring the conversion and bailment claims to arbitration could create duplication and inefficiency by having related claims litigated in two different forums. Actually, the bailment and conversion claims probably are severable in that they arise out of three different contracts and involve three separate groups of stores that were operated by three different entities at the time of the alleged wrongful conduct. However, even if Plaintiff is correct in his prediction of inefficiency, such inefficiency is not a ground for declining to enforce the arbitration clause because the Supreme Court has expressly rejected such arguments as a grounds for denying enforcement of an arbitration agreement. See Dean Witter Reynolds Inc. v. Byrd, 470 U.S. 213, 217, 105 S.Ct. 1238, 1241, 84 L.Ed.2d 158 (1985) ("[T]he Arbitration Act requires district courts to compel arbitration of pendent arbitrable claims when one of the parties files a motion to compel, even where the result would be the possibly inefficient maintenance of separate proceedings in different forums.").

There having been no showing that the arbitration of the conversion and bailment claims related to the Jewel Agreement would seriously jeopardize the objectives of the Bankruptcy Code or adversely affect the underlying purpose of the Bankruptcy Code, this court lacks the discretion to deny Defendant's motion to compel arbitration of the Jewel conversion and bailment claims.

Accordingly, the court will grant the motion to compel arbitration of those claims and stay further proceedings in the bankruptcy court involving those claims pending the conclusion of the arbitration.

IT IS SO ORDERED.

This 29th day of March, 2004.

A handwritten signature in cursive script, reading "William L. Stocks".

WILLIAM L. STOCKS
United States Bankruptcy Judge