Minutes of Proceedings

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

Date: February 16, 2006	:	
In re	:	
ENRON CORP., *et al*.,	:	
Debtors,	:	Case No. 01-16034 (AJG)
ENRON CORP. and ENRON ENERGY SERVICES NORTH AMERICA, INC.	:	Proceeding No. 03-93353
Plaintiffs,	:	
v.	:	
BROOK ENERGY SERVICES, INC.	:	
Defendant.	:	

Present: Hon. Arthur J. Gonzalez, Bankruptcy Judge; Jacqueline De Pierola, Courtroom Deputy; _____, Court Reporter

Plaintiffs: Enron Corp. and Enron Energy Services North America, Inc.

Counsel: Togut, Segal & Segal LLP
By: Neil Berger, Esq.
Jonathan Hook, Esq.

Defendant: Brook Energy Services, Inc.

Counsel: Riker, Danzig, Scherer, Hyland & Peretti LLP
By: Jeffrey M. Sponder, Esq.

Proceeding: Defendant's Motion to Vacate Entry of Default

Order: For the reasons set forth in the decision attached hereto as Exhibit A, the relief sought is

X Granted Denied

FOR THE COURT: Kathleen Farrell, Clerk of the Court

BY THE COURT:

s/Arthur J. Gonzalez
United States Bankruptcy Judge

2/16/2006
Date

Jacqueline De Pierola
Courtroom Deputy

EXHIBIT A

Before the Court is a motion to vacate an entry of default pursuant to Federal Rule of Civil Procedure 55(c), made applicable to adversary proceedings by Federal Rule of Bankruptcy Procedure 7055. Defendant Brook Energy Services, Inc., ("Brook" or "Defendant") seeks to set aside entry of default by the Clerk of the Court in an adversary proceeding initiated by Enron Corporation and Enron Energy Services North America, Inc., (collectively "Enron," "Plaintiffs" or "Debtors"). Brook also requests leave to file a responsive pleading to Enron's complaint. Brook's motion is granted. The entry of default is vacated and Brook is permitted to file a responsive pleading to Enron's complaint.

The facts that led to the present matter are as follows. Starting in September 1999, Brook, as a subcontractor of general contractor Enron, replaced lighting fixtures for the Archdiocese of Chicago. In the summer of 2001, as Brook had almost finished the work requested by Enron, Enron asked Brook for some modifications. At the time, Enron owed Brook about $9,000. Enron and Brook agreed that Enron would immediately pay these $9,000 and prepay the modifications to be done. According to this agreement, in late August 2001, Enron sent Brook a check dated August 27, 2001 for the total sum.

On November 18, 2003, Enron, as debtor-in-possession, filed a complaint against Brook to avoid and recover $144,142.20, which is most of the amount paid by the check dated August 27, 2001. In application of sections 547, 548 and 550 of the Bankruptcy Code, the complaint alleged that most of the amount paid with that check was a voidable preference or, in the alternative, a fraudulent transfer. Enron served the summons and complaint upon Brook by mail sent on February 4, 2004 and addressed to "Brook Energy Services, Inc., 645 Heathrow Dr, Lincolnshire, IL 60069, Attn: Chief

Executive Officer, Managing or General Agent." Plaintiffs' Affidavit of Service of (i) Summons in an Adversary Proceeding; (ii) Order Establishing Streamlined Procedures Governing Adversary Proceedings Commenced by the Debtors Pursuant to 11 U.S.C. §§ 544, 547, 548 and 550; and (iii) Complaint to Avoid and Recover Transfers Pursuant to 11 U.S.C. §§ 547, 548 and 550 ("Pls.' Aff. of Service of Summons and Complaint."). Brook did not file any responsive pleading.

Enron gave notice to Brook that Enron sought default judgment by mail sent on July 23, 2004. Plaintiffs' Affidavit of Service of (i) Notice of Proposed Order Granting Default Judgment; and (ii) Affidavit in Support for Entry of Default Judgment. The Clerk of the Court entered default against Brook six days later.

After learning of the entry of default in early August 2004, Brook contacted Enron and requested that the default be set aside and that Brook be allowed to file an answer. Enron did not consent to have the default be set aside, but agreed to adjourn an August 6 hearing on the motion for default judgment. Settlement negotiations did not succeed and a hearing was held regarding the matter on June 9, 2005.

Rule 55(c) provides that the Court may vacate an entry of default for "good cause." Fed. R. Civ. P. 55(c). Although courts include the grounds for relief from default judgments provided in Rule 60(b) in the concept of "good cause," they note that this concept is broader and more liberal than any of the Rule 60(b) grounds, and that, therefore, not as much is demanded to vacate a default entry as what would be required to set aside a default judgment. *Lutwin v. City of New York*, 106 F.R.D. 502, 504 (S.D.N.Y. 1985), *aff'd*, 795 F.2d 1004 (2d Cir. 1986) (affirmance without opinion); *Broder v. Pfizer & Co.*, 54 F.R.D. 583, 583 (S.D.N.Y. 1971); *SEC v. Vogel*, 49 F.R.D. 297, 299 n.2

(S.D.N.Y. 1969). Even inexcusable neglect under Rule 60(b) will not necessarily preclude good cause under Rule 55(c). *Rasmussen v. W.E. Hutton & Co.*, 68 F.R.D. 231, 235 (N.D. Ga. 1975); *Finch v. Big Chief Drilling Co.*, 56 F.R.D. 456, 458 (E.D. Tex. 1972); *Teal v. King Farms Co.*, 18 F.R.D. 447, 447-448 (E.D. Pa. 1955).

A decision under 55(c) is within the Court's discretion, but the Court should resolve any doubt regarding vacatur of the default entry in favor of the moving party so that the matter can be decided on the merits. *Lutwin*, 106 F.R.D. at 504; *Vogel*, 49 F.R.D. at 299; *In re Sem*, 40 B.R. 959, 960 (Bankr. S.D.N.Y. 1984). The Court must consider three factors: (i) whether Defendant's conduct was willful, (ii) whether Plaintiffs would be prejudiced, and (iii) whether Defendant has a meritorious defense. *In re Men's Sportswear, Inc.*, 834 F.2d 1134, 1138 (2d Cir. 1987); *Lutwin*, 106 F.R.D. at 504; *Fleet Factors Corp. v. Roth (In re Roth)*, 172 B.R. 777, 780 (Bankr. S.D.N.Y. 1994). Additionally, the Court may take into consideration the promptness with which the defaulting party has moved for relief. *Dow Chem. Pac. Ltd. V. Rascator Maritime, S.A.*, 782 F.2d 329, 336 (2d Cir. 1986); *Broder*, 54 F.R.D. at 584.

Defendant Brook argues that consideration of the three factors should convince the Court to find good cause to vacate the entry of default.

First, Brook asserts that its default was not willful. Although it admits having an office at 645 Heathrow Dr., Lincolnshire, IL 60069, Defendant contends that it "does not have any record of having received the Summons and the Complaint that was purportedly served by the Plaintiffs" at this address. Defendant's (i) Verified Objection to Plaintiffs' Presentment of an Order Granting Default Judgment and (ii) Request for Leave to File a Responsive Pleading 4 ("Def.'s Objection"). Defendant explains

that if it had known of the proceeding earlier it would not have allowed an entry of default. Brook also notes that upon learning of the default it acted in good faith and immediately retained counsel.

Second, Brook submits that Plaintiffs will not be prejudiced if the default is vacated. According to Brook, no evidence has been lost, no collusion occurred, and Plaintiffs could not have relied on the default, especially because of the settlement negotiations between Plaintiffs and Defendant. Furthermore, Brook argues that all of Plaintiffs' records pertinent to this adversary proceeding "presumably have been and continue to be stored and safeguarded" by Plaintiffs "in light of the fact that the Plaintiffs are simultaneously prosecuting hundreds of avoidance actions." Def.'s Objection 7-8. Brook notes as well that the stay on discovery in this proceeding has only been recently lifted.

Third, Brook claims it has meritorious defenses. Brook says that Plaintiffs have stopped pursuing their preference claim, thus tacitly admitting that Brook has a meritorious defense to it. As for Plaintiffs' fraudulent transfer claim, Brook says it fails because Plaintiffs have not shown that Debtors were insolvent at the time they made the payment with the August 27, 2001 check and because Debtors paid Brook in exchange for reasonably equivalent value.

In response, Plaintiffs assert that Defendant does not show good cause to vacate entry of default. Plaintiffs emphasize that they served Defendant at the correct address and that Defendant does not offer any explanation why service of process was never received. They claim that Defendant's lack of explanation amounts to willful conduct.

Plaintiffs claim that vacating the default will increase their discovery costs. They are also concerned about the precedential effect of a vacatur in this proceeding on other proceedings involving default judgments. Plaintiffs finally say that they made clear during the settlement negotiations that the

fraudulent transfer claim, not the preference one, was the main cause of action in this proceeding. They argue that Defendant has failed to assert a meritorious defense to this fraudulent transfer claim.

Under the circumstances of the present matter, the Court makes the following determinations concerning the relevant factors. As to willful conduct, Plaintiffs argue that Defendant's flat assertion that Defendant does not have any record of having received the summons and complaint, despite Defendant's admission that the summons and complaint were sent to the correct address, amounts to willful conduct. A rebuttable presumption that an addressee received a mailed notice arises when the mailing party submits sufficient evidence to demonstrate the notice was addressed and mailed. *Hagner v. United States*, 285 U.S. 427, 430 (1932); *Meckel v. Continental Resources Co.*, 758 F2d 811, 817 (2d Cir. 1985); *Capital Data Corp. v. Capital Nat'l Bank*, 778 F. Supp. 669, 675 (S.D.N.Y. 1991). Evidence of actual mailing, in the form of an affidavit submitted by an individual who supervised the mailing is sufficient to allow the presumption to arise. *In re Adler, Coleman Clearing Corp.*, 204 B.R. 99, 104-105 (Bankr. S.D.N.Y. 1997). Additional evidence, other than an addressee's mere denial of receipt, is required to rebut the presumption that the addressee received a properly addressed notice. *Meckel*, 758 F.2d at 817 (*citing Engel v. Lichterman*, 95 A.D.2d 536, 544 (N.Y. App. Div. 1983)).

Plaintiffs submitted an affidavit of service of the summons and complaint, which is sufficient evidence for the presumption of receipt to arise. *See* Pls.' Aff. of Service of Summons and Complaint. Defendant's blank denial of receipt cannot rebut the presumption. Therefore, the Court presumes that Defendant received the notice of summons and complaint.

The Court must then assess whether Defendant's behavior amounts to willful conduct that warrants denying the motion to vacate the default entry. Courts rarely make a finding of willful conduct. In *Titus v. Smith*, 51 F.R.D. 224, 226 (E.D. Pa. 1970), the court noted defendant's "wilful and deliberate failure to act over a period of approximately one year and ten months in spite of the numerous and repeated efforts of plaintiff's counsel" to apprise the defendant of the ongoing process. The court found that "[t]his failure to act with any semblance of reasonable promptness or due diligence over such an extensive period of time can only be condemned as gross and inexcusable neglect." *Id.* Therefore, the court denied vacatur of the default entry. *Id.* at 227.

The parties have argued over the relevance of this Court's "International Paper" opinion regarding the issue of willful conduct. *See In re Enron, Inc.*, 325 B.R. 114 (Bankr. S.D.N.Y. 2005). That opinion applied Rule 60(b) to make a decision on a motion for reconsideration of an order expunging a creditor's proof of claim. As stated before, although standards under Rules 60(b) and 55(c) overlap, vacating an entry of default does not call for an analysis exactly identical to the one required to vacate a decision under 60(b). The Court therefore does not find the "International Paper" analysis controlling in the instant matter.

In the present proceeding, assuming that Defendant received the notice of summons and complaint, there is not enough evidence to demonstrate that Defendant willfully ignored the notice. Defendant could have been negligent in handling the service of process it received. Moreover, Defendant requested Plaintiffs to set aside the default a week after it was entered, thus giving credibility to its assertion that had it known of the proceeding earlier it would not have allowed an entry of default.

Therefore, the Court finds that Defendant's conduct was not willful because of the lack of evidence of willful conduct and Defendant's prompt request to Plaintiffs after entry of the default.

Consideration of the second factor, prejudice to the Plaintiffs, does not warrant a denial of the motion either. To preclude vacatur of a default entry, delay by itself is not sufficient; delay must result in loss of evidence, create increased difficulties of discovery, or provide greater opportunity for fraud and collusion. *Argus Research Group, Inc. v. Argus Securities, Inc.*, 204 F. Supp 2d 529, 532 (E.D.N.Y 2002). There is no evidence of fraud or collusion and no allegation that evidence has been lost. Plaintiffs presumably still have now the evidence they needed to decide to pursue an avoidance action against Defendant. Further, setting aside the default will not make discovery more difficult because discovery between Plaintiffs and Defendant has barely started. According to the Avoidance Action Discovery Procedures, approved by the Court's November 18, 2004 order, discovery in the adversary proceeding between Enron and Brook started on December 6, 2005. Notice of Commencement of Sixth Wave Pursuant to Avoidance Action Discovery Procedures (October 7, 2005). The parties have just made their document requests. Notice of Brook Energy Services, Inc.'s Service of Document Requests Pursuant to Avoidance Action Discovery Procedures (February 6, 2006); Affidavit of Service of Plaintiffs' Demand for Production of Documents to Defendant Pursuant to the Federal Rules of Civil Procedure, the Bankruptcy Rules, the Local Civil and Bankruptcy Rules for the Southern District of New York and the Avoidance Action Discovery Procedures (February 6, 2006).

Thus, the Court finds that vacating the default will not prejudice Plaintiffs enough to justify denying the motion.

The Court must finally determine whether Defendant asserts a meritorious defense. Plaintiffs have not significantly litigated their preference action in this Court, focusing instead on their fraudulent transfer action. Plaintiffs' Reply Memorandum in Opposition to Defendant's Motion to Vacate Entry of Default Pursuant to Rule 7055(c) ¶ 44. The Court will therefore only decide whether Defendant has a meritorious defense to the fraudulent transfer action.

To avoid a transaction as a fraudulent conveyance, Plaintiffs must show that (i) they transferred an interest in property; (ii) the transfer occurred within one year prior to the filing of the bankruptcy case; (iii) they were insolvent on the date of transfer or became insolvent as a result of the transfer; and (iv) they received less than reasonably equivalent value in exchange for the transfer. *In re GWI PCS 1, Inc.*, 230 F.3d 788, 805 (5th Cir. 2000), *cert. denied*, 533 U.S. 964 (2001). Defendant asserts that Plaintiffs have not shown that Plaintiffs were insolvent at the time they made the payment with the August 27, 2001 check. Defendant also contends that Plaintiffs paid Defendant in exchange for reasonably equivalent value, namely the value represented by a payment from the Archdiocese of Chicago for the work performed by Defendant.

The defaulting party must set forth supporting facts and cannot only make conclusory statements that a meritorious defense exists. *Robinson v. Bantam Books, Inc.*, 49 F.R.D. 139, 140-141 (S.D.N.Y. 1970); *Vogel*, 49 F.R.D. at 299. Plaintiffs arguably received a payment from the Archdiocese of Chicago for the work performed by Defendant, which may amount to reasonably equivalent value for the payment made by Plaintiffs to Defendant with the August 27, 2001 check. If Plaintiffs received such a payment, their fraudulent transfer claim would fail. Thus, at this stage of the

proceeding, as discovery is just starting, Defendant has set forth a meritorious defense to Plaintiffs' fraudulent transfer claim.

In sum, Brook has shown good cause to set aside the default. Therefore, the entry of default by the Clerk of this Court is vacated and Brook is permitted to file a responsive pleading to Enron's complaint.