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UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF CALIFORNIA

LLOYD RAYMOND FREE and  
SYLVIANE FREE,  
  
Debtors.

Case No. 94-57808-JRG  
Chapter 7

COMERICA BANK-CALIFORNIA, a  
California corporation,

Adversary No. 95-5272  
[Consolidated with Adversary  
No. 95-5273]

Plaintiff,

vs.

**ORDER ON MOTION FOR SEPARATE  
PRIOR TRIAL OF ISSUE**

LLOYD RAYMOND FREE and  
SYLVIANE FREE,  
  
Defendants.

L.R. FREE, INC., LLOYD R.  
FREE, SYLVIANE FREE and MITRA  
SOLEYMANI,

Counter-Claimants,

vs.

COMERICA BANK-CALIFORNIA, a  
California corporation,

Counter-Defendants.

AND CONSOLIDATED ACTION.

**I. INTRODUCTION**

The court has before it the motion of debtor-defendants and counter-claimants L.R. Free, Inc., Lloyd Free, Sylviane Free and

1 Mitra Soleymani seeking a separate prior trial of certain issues  
2 set forth in their Third Amended Counterclaim. In essence,  
3 counter-claimants want a jury trial, to be conducted prior to  
4 the non-dischargeability trial on plaintiff's complaint, on the  
5 issues of breach of contract, breach of fiduciary duty, fraud  
6 and intentional infliction of emotional distress. For the  
7 reasons hereafter stated the motion will be granted in part.

8 At the time of the hearing the court considered two issues  
9 orally. The first issue was whether the court should exercise  
10 its discretion and grant the debtors a separate trial of their  
11 counterclaim. The court discussed at some length the factual  
12 allegations underlying both the complaint and the counterclaim  
13 pointing out that the facts in the complaint were totally  
14 unrelated to those in the counterclaim. The facts discussed  
15 orally at the hearing are incorporated in this ruling but will  
16 not be repeated here.

17 The court indicated tentatively that as the operative  
18 incidents were totally unrelated, the witnesses completely  
19 different and the banks with whom the debtors dealt at the time  
20 were even different, it made sense to have separate trials. In  
21 fact, separate trials would serve to avoid confusion on the part  
22 of the trier of fact. The court did, however, disagree with the  
23 debtors with respect to the counterclaim being tried first. The  
24 court indicated that, to the extent that both the complaint and  
25 counterclaim were tried in this court, the complaint of  
26 plaintiff would be tried first. The court now adopts its  
27 tentative ruling regarding these issues.

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1 The second issue dealt with by the court at the hearing  
2 involved the question of whether the debtors had waived their  
3 right to a jury trial. Plaintiff argued that even if the  
4 debtors had a right to a jury trial, it was waived by virtue of  
5 the loan documents they signed with the plaintiff's  
6 predecessors, Plaza Commerce Bank and Pacific Western Bank,  
7 which contained jury waiver provisions. The court indicated  
8 tentatively that the debtors did not waive their right to a jury  
9 trial by virtue of executing the loan documents because the  
10 waivers were not knowing, voluntary and intelligent, and thus  
11 unenforceable. The court now adopts its tentative ruling for  
12 the reason stated on the record.

13 The remainder of the motion dealt with the question of  
14 whether the debtors waived their right to a jury trial by other  
15 actions. The court took the remaining parts of the motion under  
16 submission.

17 **II. DISCUSSION**

18 **A. The Debtors Have a Right to a Jury Trial Absent Any**  
19 **Waiver of That Right.**

20 Where the right to a jury trial is disputed, the court must  
21 initially determine whether the moving party, the counter-  
22 claimants, have a Seventh Amendment right to a jury trial.  
23 Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 41-42, 109 S.Ct.  
24 2782, 2790 (1989); Local Rule 700-7(a); 5 Moore's Federal  
25 Practice ¶ 38.11[1]. The right is determined by a three-part  
26 test. Leslie Salt Company v. Marshland Development, Inc., 129  
27 B.R. 628 (Bankr. N.D. Cal 1991). First, the court must decide  
28 whether there would have been a right to a jury trial in

1 18<sup>th</sup>-century England. Granfinanciera, 109 S.Ct. at 2790.  
2 Second, the court must decide whether the matter should be  
3 characterized as legal rather than equitable. Id. Finally, the  
4 court must decide whether the matter involves private rights, as  
5 opposed to public rights. Id. All three factors must be present  
6 in order for there to be a Seventh Amendment right to a jury  
7 trial. Marshland, 129 B.R. at 628.

8 The counterclaim lists the following claims for relief:  
9 breach of contract, breach of fiduciary duty, fraud, and  
10 intentional infliction of emotional distress. First, the court  
11 finds that there was a right to a jury trial in 18<sup>th</sup>-century  
12 England on the causes of action pled by the plaintiff.<sup>1</sup> There  
13 was a right to a jury trial on the breach of contract, breach of  
14 fiduciary duty, and fraud claims. In 18<sup>th</sup>-century England a  
15 claim for intentional infliction of emotional distress probably  
16 did not exist. Second, the court concludes that this matter is  
17 legal rather than equitable, as money damages are the sole  
18 remedy requested by the debtors. Finally, the court concludes  
19 the matter involves private rights not public rights.

20 Thus, the debtors have a Seventh Amendment right to a jury  
21 trial. The existence of the initial right to a jury trial has  
22 not been seriously disputed by the plaintiff. The issue has  
23 been that of waiver of this right.

24 **B. Have the Debtors Waived Their Right to a Jury Trial?**

25 Plaintiff originally contended that the debtors waived

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27 <sup>1</sup> See generally 8 Moore's Federal Practice ¶ 38.11[5], pp.38-80-38-83  
28 (2d.ed. 1991) for a comprehensive list of actions that historically would have  
been considered triable by a jury.

1 their right to a jury through the execution of the loan  
2 documents as referenced above. The court has disposed of that  
3 issue through the adoption of the tentative ruling set forth  
4 orally at the time of the hearing. Plaintiff asserts that the  
5 debtors have waived a jury trial on three additional grounds:  
6 (1) by filing a voluntary petition in bankruptcy, the debtors  
7 have submitted to the equitable power of the court and have  
8 waived their right to a jury trial; (2) by filing their  
9 counterclaim in the bankruptcy court, the debtors have submitted  
10 to the equitable claims-allowance process of the court and have  
11 waived their right to a jury trial; and (3) the debtors' claim  
12 is a compulsory counterclaim and no jury trial is permitted by  
13 virtue of the nature of the claims.

14 **1. The Debtors Have Not Waived Their Right to a Jury**  
15 **Trial by Virtue of Filing a Bankruptcy Petition.**

16 A debtor does not subject its pre-petition claims to the  
17 bankruptcy court's equitable jurisdiction when he files a  
18 bankruptcy petition. In re Jensen, 946 F.2d 369, 373 (5<sup>th</sup> Cir.  
19 1991). Nor does the petition somehow waive the debtor's right  
20 to a jury trial. Id. at 374. See also 1 Norton Bankruptcy  
21 Practice 2d § 4:44, p. 4-296 (1997); Germain v. Connecticut  
22 Nat'l Bank, 988 F.2d 1323, 1329-30 (2<sup>nd</sup> Cir. 1993). Thus, the  
23 court finds that the debtors have not waived their right to a  
24 jury trial by virtue of filing their bankruptcy petition.

25 **2. The Debtors Have Not Waived Their Right to a Jury**  
26 **Trial by Virtue of Asserting Their Claims in This**  
27 **Court.**

28 By asserting their claims in this court, plaintiff contends  
that counter-claimants have submitted their lender liability

1 causes of action to this court's equitable powers to allow,  
2 disallow, or offset mutual debts, even though the claims are  
3 legal in nature. See In re Romar International Georgia, Inc.  
4 198 B.R. 407 (Bankr. M.D.Ga. 1996). In Romar, the debtor filed  
5 an adversary proceeding asserting state law lender liability  
6 claims against a bank. The bank filed a proof of claim in the  
7 bankruptcy court and asserted a counterclaim against the debtor.  
8 The Romar court held that because the parties asserted  
9 substantial pre-petition claims against each other and the court  
10 may have to resolve set-off issues, the lender liability action  
11 is part of the claims-allowance process and no right to a jury  
12 trial exists for such claims.

13 However, in Germain v. Connecticut National Bank, 988 F.2d  
14 1323 (2d Cir. 1993) the Court of Appeals explains that such  
15 lender liability claims are really not part of the claims-  
16 allowance process. In Germain, the chapter 7 trustee brought an  
17 action against the bank and state court for tortious  
18 interference with debtor's business, coercion and duress, breach  
19 of contractual duty of good faith, unfair or deceptive business  
20 practices, and misrepresentation. The Court of Appeals held  
21 that the right to a jury trial was not waived because the  
22 trustee's claims had nothing to do with the essence of  
23 bankruptcy regulatory scheme of allowing or reordering claims.

24 The court stated that the very phrase "claims-allowance  
25 process" suggests that the resolution of the dispute in which a  
26 jury trial is sought must affect the allowance of the creditor's  
27 claim in order to be part of that process. Germain, 988 F.2d at  
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1 1327. A preference action does so; lender liability actions  
2 generally do not. Id. Suits which augment the estate but which  
3 have no effect on the allowance of a creditor's claim simply  
4 cannot be part of the claims-allowance process. Id. Thus, a  
5 court could allow a bank's claim before hearing argument on the  
6 trustee's complaint, and this chronology would be both logical  
7 and consistent with the Bankruptcy Code. Id.

8 Here, the debtors ask for money damages to compensate the  
9 estate for the destruction of the debtors' business. If the  
10 debtors win, the estate is enlarged, and this may affect the  
11 amount Comerica and other creditors ultimately recover on their  
12 claims, but it has no effect whatever on the allowance of  
13 Comerica's claims. Thus, the debtors' right to a jury trial on  
14 their lender liability claims is not waived because their claims  
15 are not part of the claims-allowance process.

16 **3. The Debtors Have Not Waived Their Right to a Jury**  
17 **Trial by Virtue of Having a Compulsory**  
18 **Counterclaim**

19 Comerica asserts that a compulsory counterclaim filed by a  
20 debtor may be decided in the same manner as the claim because it  
21 is part of the same legal controversy. Comerica relies on In re  
22 Lion Country Safari, Inc., 124 B.R. 566 (Bankr. C.D.Cal. 1991).  
23 Comerica's reliance on In re Lion Country Safari is misplaced.  
24 The court does not find that the debtors' counterclaim is  
25 compulsory.

26 Federal Rule of Bankruptcy Procedure 7013 incorporates by  
27 reference Rule 13 of the Federal Rules of Civil Procedure with  
28 some modifications which are not relevant in the case at hand.

1 FRCP 13 provides in part:

2 (a) **Compulsory Counterclaims.** A pleading shall  
3 state as a counterclaim any claim which at the  
4 time of serving the pleading the pleader has  
5 against any opposing party, if it arises out of  
6 the transaction or occurrence that is the subject  
7 matter of the opposing party's claim and does not  
8 require for its adjudication the presence of third  
9 parties of whom the court cannot acquire  
10 jurisdiction...

11 (b) **Permissive Counterclaims.** A pleading may  
12 state as a counterclaim any claim against an  
13 opposing party not arising out of the transaction  
14 or occurrence that is the subject matter of the  
15 opposing party's claim.

16 A compulsory counterclaim must arise out of the same  
17 transaction or occurrence. In determining whether two claims  
18 arise out of the same transaction or occurrence, the Ninth  
19 Circuit applies the "logical relationship" test. In re Lion  
20 Country Safari, 124 B.R. at 569 citing Pochiro v. Prudential  
21 Ins. Co. of Am., 827 F.2d 1246, 1249 (9<sup>th</sup> Cir. 1987); In re  
22 Bulson, 117 B.R. 537, 541 (9<sup>th</sup> Cir. BAP 1990). This test calls  
23 for the court to determine if the essential facts of the various  
24 claims are so logically connected that considerations of  
25 judicial economy and fairness dictate that all issues should be  
26 resolved in one lawsuit. Id. A logical relationship exists when  
27 the counterclaim arises from the same aggregate set of operative  
28 facts as the initial claim, in that the same operative facts  
serve as the basis of both claims or the aggregate core of facts  
upon which the claim rests activates additional legal rights  
otherwise dormant in the defendant. In re Lile, 96 B.R. 81, 85  
(Bankr. S.D.Tex. 1989) (quoting U.S. v. Aronson, 617 F.2d 119  
(5<sup>th</sup> Cir. 1980)).

1 In this case, the claims do not pass the logical  
2 relationship test. The claims clearly did not arise out of the  
3 same set of facts, transaction, or occurrence. The first claim  
4 by Comerica against the debtors is based on a loan transaction  
5 between the debtors and Pacific Western Bank, which Comerica  
6 acquired after the claim arose. The other claim is based on a  
7 completely separate loan transaction between the debtors and  
8 Plaza Bank, which Comerica also acquired after the claim arose.  
9 It is only by mere coincidence that the debtors must now sue and  
10 be sued by Comerica Bank. It is not disputed by the parties  
11 that the two loan transactions giving rise to the claims are  
12 completely unrelated to each other. Thus, by no stretch of the  
13 imagination do the claims arise out of the same transaction or  
14 occurrence. The debtors' counterclaim is therefore not a  
15 compulsory counterclaim governed by Lion Country Safari.  
16 Therefore, the debtors have not waived their Seventh Amendment  
17 right to a jury trial on their counterclaim.

18 **III. CONCLUSION**

19 Based on the foregoing, the debtors' motion for a prior  
20 separate trial is granted in part. The court holds that  
21 separate trials of the claim and counterclaim is necessary and  
22 that the debtors have a right to a jury trial on their  
23 counterclaim. The court denies the motion in part in that the  
24 debtors' counterclaim will not be tried prior to plaintiff's  
25 non-dischargeability claim. The statements in this order shall  
26 constitute the court's findings of facts and conclusions of law  
27 pursuant to Federal Rule of Bankruptcy Procedure 7052.

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