

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW HAMPSHIRE**

In re:

Bk. No. 02-12844-JMD
Chapter 11

Atlantic Orient Corporation,
Debtor

Atlantic Orient Corporation,
Plaintiff

v.

Adv. No. 02-1132-JMD

AOC Energy LLC, et al.,
Defendants

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MEMORANDUM OPINION

I. INTRODUCTION

On May 1, 2003, Atlantic Orient Corporation (the “Debtor”) filed a Motion to Hold Defendant AOC Energy LLC and Certain Third Parties Acting in Concert with Energy in Contempt and for an Award of Damages and Sanctions (the “Contempt Motion”) (Doc. No. 73). In response to AOC Energy’s Objection (Doc. No. 76) and Answer (Doc. No. 96) to the Contempt Motion, on

July 3, 2003, the Debtor filed a Motion to Strike the Defense on the Contempt Motion That Has Been Asserted by AOC Energy, Seaforth, Lombardi and Mason Because Such Defenses Are Barred by the Doctrine of Res Judicata and to Exclude Any Evidence Related to Such Defenses (the “Motion to Strike”) (Doc. No. 105). AOC Energy filed its Objection to the Motion to Strike on July 14, 2003 (the “Objection”) (Doc. No. 108). After conducting a hearing on July 16, 2003, the Court took the matter under advisement.

This Court has jurisdiction of the subject matter and the parties pursuant to 28 U.S.C. §§ 1334 and 157(a) and the “Standing Order of Referral of Title 11 Proceedings to the United States Bankruptcy Court for the District of New Hampshire,” dated January 18, 1994 (DiClerico, C.J.). This is a core proceeding in accordance with 28 U.S.C. § 157(b).

II. FACTS

On September 16, 2002, the Debtor filed a voluntary petition under Chapter 11 of the Bankruptcy Code. On September 20, 2002, the Debtor commenced this adversary proceeding against AOC Energy and other parties seeking injunctive relief. After conducting hearings on September 20 and 24, 2002, the Court issued a Temporary Restraining Order (the “TRO”) (Doc. No. 13). The TRO ordered the Debtor’s landlord to permit the Debtor to have access to its books and records pending a hearing on a request for a preliminary injunction (the “Injunction”). On September 27, 2002, the Court held an evidentiary hearing on the Debtor’s request for the Injunction. At the conclusion of the evidentiary hearing the Court stated its findings and rulings on the record and granted the Injunction (Doc. No. 15). The Injunction provided:

[the] Court hereby enjoins the Defendants AOC Energy LLC and Darrell Hotchkiss, James Heath, Robert Sherwin, and their respective officers, agents, servants, employees, and attorneys from interfering in anyway with the Debtor’s access to and use of its property,

being the property described in the Notice of UCC Sale issued by the secured party and purportedly sold at auction held on September 9, 2002. This injunction extends to any persons acting in concert or participation with any of the parties explicitly enjoined herein and who receive actual notice of the order by personal service or otherwise. The Debtor shall be entitled to use, lease, sell, or otherwise dispose of such property to the full extent permitted under Title 11 of the United States Code.

(emphasis added). The Debtor filed a motion to convert the preliminary injunction into a permanent injunction on November 15, 2002 (Doc. No. 28) (the “Injunction Motion”). AOC Energy responded with a motion for summary judgment against the Debtor (Doc. No. 30) (the “SJ Motion”). At the commencement of the hearing on the Injunction Motion and the SJ Motion on December 23, 2002, the parties agreed on the record that they were both asking the Court to render a final decision on the permanent injunction issue based upon the evidentiary record established at the September 27, 2002, hearing. On February 20, 2003, the Court converted the Injunction to a permanent injunction (the “Permanent Injunction”) (Doc. No. 58). The central issue in both hearings and the Court’s decisions granting the Injunction and the Permanent Injunction was the passage of title of the Debtor’s assets as a result of a purported secured party auction sale.¹

The Debtor’s Contempt Motion alleges that AOC Energy and other third parties are using or attempting to use the Debtor’s technology and are engaging in a pattern of conduct intended to interfere with the Debtor’s operation of its business and use of its technology. The Debtor contends that this behavior violates the Permanent Injunction granted by the Court. In response to the Debtor’s Contempt Motion, AOC Energy filed an Answer, stating that AOC Energy had pre-

¹ The factual history of this case is summarized in the Court’s opinion AOC Energy LLC, et al v. Atlantic Orient Corp. (In re Atlantic Orient Corp.), 290 B.R. 456 (Bankr. D.N.H. 2003).

existing rights to some of the Debtor's technology² and furthermore, that the technology is in the public domain and is no longer exclusive to the Debtor.

AOC Energy's Answer prompted the Debtor to file its Motion to Strike, alleging that res judicata and collateral estoppel bars AOC Energy's defenses based on ownership or rights to use the Debtor's technology. The narrow issue before the Court is whether AOC Energy can use as a defense their claim of ownership or rights to use the Debtor's technology, other than those derived from the secured party auction sale. For the reasons discussed below, the Motion to Strike shall be denied.

III. DISCUSSION

A. Preclusion

In Migra v. Warren City Sch. Dist. Bd. of Educ., the United States Supreme Court expressed its preference for the use of the terms "issue preclusion" and "claim preclusion" to refer to the preclusive effect of a judgment in foreclosing future litigation rather than the more traditionally utilized terms "collateral estoppel" and "res judicata." 465 U.S. 75, n. 1 (1984); see also 18 Wright & Miller, Federal Practice & Procedures § 4402 (2d ed. 2003). Issue preclusion refers to the effect of a judgment in foreclosing relitigation of a matter that has been actually litigated and decided. Id. In order to effectuate the public policy in favor of minimizing redundant litigation, issue preclusion bars the relitigation of issues actually adjudicated, and essential to the judgment, in a prior litigation between the same parties. Id.; Kaspar Wire Works v. Leco Eng'g and Mach., Inc., 575 F.2d 530, 535 (5th Cir. 1978). This is often referred to as direct or collateral

² Specifically the 15/50 wind turbine.

estoppel. Id. Claim preclusion or true res judicata generally refers to the effect of a judgment in foreclosing litigation of a matter that never has been litigated, because of a determination that it should have been advanced in an earlier suit. Id. The aim of claim preclusion is to avoid multiple suits on identical entitlements or obligations between the same parties by the redetermination of identical issues of duty and breach. Id.; Kaspar, 575 F.2d at 535.

1. Issue Preclusion

The elements of issue preclusion are:

1. the determination must be over an issue which was actually litigated in the first forum;
2. that determination must result in a valid and final judgment;
3. the determination must be essential to the judgment which is rendered by, and in, the first forum;
4. the issue before the second forum must be the same as the one in the first forum; and
5. the parties in the second action must be same as those in the first.

National Labor Relations Bd. v. Donna-Lee Sportswear Co., Inc., 836 F.2d 31, 33 (1st Cir. 1987).

The Court need not look past the first element.

The permanent injunction dealt solely with the passage of title of the Debtor's assets as a result of a secured party's purported auction sale. The Debtor filed its request for a preliminary injunction for the sole purpose of invalidating the secured party auction sale in which AOC Energy was the high bidder. For the Debtor to argue otherwise is disingenuous at best. AOC Energy, through its agent, placed the winning bid for all the Debtor's assets, but before payment was completed the Debtor filed for protection under Chapter 11 of the Bankruptcy Code. Immediately after its bankruptcy filing, the Debtor initiated this adversary proceeding seeking to enjoin AOC Energy from taking possession of the Debtor's assets. The Court then conducted a series of hearings to resolve the issue of ownership of the assets in respect to the auction sale. AOC Energy argued that an auction sale was final at the fall of the hammer and the Debtor successfully

contended that an auction sale was not final until payment was completed. At no time did either party argue or brief the Court on any other issue. No portion of the hearings, the evidence, the arguments of the parties or the Court's ruling on the Permanent Injunction covered intellectual property rights, licensing or whether the Debtor's technology was proprietary, confidential or in the public domain. The ruling on the Permanent Injunction dealt with the terms and conditions surrounding a purported sale of property at a UCC auction. The Court does not understand how the Debtor can argue that this ruling invalidated a valid prepetition license to manufacture the Debtor's wind turbines.³ Following the Debtor's argument the Court questions whether its ruling invalidates all licenses the Debtor granted prepetition as well, or just those that the Debtor no longer wishes to acknowledge.

The Debtor points out that if the technology was either licensed to AOC Energy or in the public domain, then why would AOC Energy attempt to buy the Debtor's assets at the auction sale. The Court can envision many reasons for such actions such as the elimination of a competitor or attempting to eliminate a potential dispute over rights to technology that was either licensed or in the public domain.

However, if AOC Energy used its access as bidder to the Debtor's assets to acquire the Debtor's confidential or proprietary technology then AOC Energy may well be in violation of the Permanent Injunction. However, such allegations have not been pled. In fact, AOC Energy has asserted that 1) it was granted a license by the Debtor to manufacture and market its technology and 2) the technology is in the public domain. Neither one of these issues were litigated during either the TRO or the Permanent Injunction. Accordingly, issue preclusion will not prevent AOC

³ Assuming that AOC Energy can prove at the hearing on the Contempt Motion that it had a valid license.

Energy from asserting that it had a valid license or that the technology was in the public domain as defenses to the Debtor's Contempt Motion.

2. Claim Preclusion

The elements of claim preclusion are:

1. a final judgment on the merits in an earlier suit;
2. sufficient identity between the causes of action asserted in the earlier and later suits; and
3. sufficient identity between the parties in the two suits.

Gonzalez v. Banco Cent. Corp. et al, 27 F.3d 751, 755 (1st Cir 1994). Again the Debtor cannot overcome the second element because it has not demonstrated that the issues now before the Court are in any way similar or identical to the causes of action asserted in its Complaint. Accordingly, claim preclusion will not prevent AOC Energy from asserting that they had a valid license or that the technology was in the public domain as defenses to the Debtor's Contempt Motion.

B. Compulsory Counterclaim

Although neither party has raised it directly, the Court has an obligation to address the implication of Fed. R. Civ. P. 13(a) ("Rule 13(a)"), made applicable in adversary proceedings by Fed. R. Bankr. P. 7013. Rule 13(a) states that:

A pleading shall state as a counterclaim any claim which at the time of serving the pleading the pleader has against any opposing party, if it arises out of the transaction or occurrence that is the subject matter of the opposing party's claim and does not require for its adjudication the presence of third parties of whom the court cannot acquire jurisdiction. But the pleader need not state the claim if (1) at the time the action was commenced the claim was the subject of another pending action, or (2) the opposing party brought suit upon the claim by attachment or other process by which the court did not acquire jurisdiction to render a personal judgment on that claim, and the pleader is not stating any counterclaim under this Rule 13.

Fed. R. Civ. P. 13(a). There are at least four tests to determine whether a counterclaim is compulsory in the First Circuit:

1. Are the issues of fact and law raised by the claim and counterclaim largely the same?
2. Would res judicata bar a subsequent suit on the defendant's claim absent the compulsory counterclaim rule?
3. Will substantially the same evidence support or refute the plaintiff's claim as well as the defendant's counterclaim?
4. Is there any logical relation between the claim and the counterclaim?

Iglesias v. Mutual Life Ins. Co. of N.Y., 156 F.3d 237, 241 (1st Cir. 1998); McCaffrey v. Rex Motor Transp., Inc., 672 F.2d 246, 248 (1st Cir. 1982). Obviously the first and third tests do not apply since the Debtor's claim dealt with issues of UCC law and AOC Energy's "counterclaim"⁴ deals with issues of intellectual property law. The Court has already addressed the second test in this opinion. This leaves the fourth test, the so called "logical relationship" test.

Under the logical relationship test a counterclaim qualifies as compulsory only if: it arises out of the same aggregate of operative facts as the original claim in two senses: (1) that the same aggregate or operative facts serves as the basis of both claims; or (2) that the aggregate core of facts upon which the original claim rests activates additional legal rights in a party defendant that would otherwise remain dormant.

McCaffrey, 672 F.2d at 249. Applying this test, AOC Energy's counterclaim is permissive and not compulsory. First, the aggregate of operative facts giving rise to the Debtor's claims are entirely different from the facts supporting AOC Energy's counterclaim.⁵ Second, AOC Energy's ability to use the Debtor's technology because of either a prior license or public domain bears no logical relation to the Debtor's claim that the UCC auction sale was not consummated before its Chapter 11 filing. Accordingly, the Court finds that AOC Energy's counterclaim was not compulsory and therefore it is not barred.

⁴ For the purpose of this discussion the Court will refer to AOC Energy's defense of a prior license and public domain as a counterclaim of the Debtor's original claim.

⁵ See the section III.A.2 of this opinion.

IV. CONCLUSION

For the reasons set forth in this Memorandum Opinion, the Court finds that AOC Energy is not prevented from asserting that it had a valid license or that the technology was in the public domain as defenses to the Debtor's Contempt Motion.⁶ The Court shall enter a separate order denying the Motion to Strike. This opinion constitutes the Court's findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052.

Dated: November 13, 2003

/s/ J. Michael Deasy
J. Michael Deasy
Bankruptcy Judge

⁶ The Court notes that the issue involved in the Contempt Motion is whether or not AOC Energy violated the Permanent Injunction. If AOC Energy rightfully or wrongly used the Debtor's technology at any time prepetition or postpetition, other than through its access through the auction sale, then the Contempt Motion will be denied. This Court need not decide the issues regarding licenses and public domain, these will be issues for another court at another time.