UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEW JERSEY

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| In Re:<br><br>HOME EASY, LTD,<br><br>Debtor. | CHAPTER 7<br><br>CASE NO. 23-19151 (RG) |
| BENJAMIN A. STANZIALE, JR.,<br>CHAPTER 7 TRUSTEE FOR<br>HOME EASY, LTD.,<br><br>Plaintiff,<br>v.<br><br>EMERSON RADIO CORP.,<br><br>Defendant. | ADV. PRO. NO.: 24-1177 (RG) |

**OPINION**

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## MATTER BEFORE THE COURT

Before the Court is a Motion (ECF 9) filed by Defendant, Emerson Radio Corporation ("Defendant" or "Emerson"), to Dismiss the Complaint filed by Benjamin A. Stanziale Jr. , Chapter 7 Trustee ("Plaintiff" or "Trustee") for Home Easy, Ltd. ("Debtor" or "Home Easy"); the Trustee's Brief in Opposition to Defendant's Motion to Dismiss. (ECF 11); and Emerson's Reply in support of the Motion (ECF 14).

A hearing was conducted on November 14, 2024, at which Evan M. Lazerowitz, Esq. of Cooley LLP and Kristen M. Harvilla, Esq. of Stevens and Lee P.C. appeared on behalf of the movant, Emerson Radio Corporation, and Patricia A. Staiano, Esq and Robert B. Rosen, Esq, of Hellring Lindeman Goldstein& Siegal LLP, appeared on behalf of Plaintiff, Benjamin A. Stanziale, Jr., the Chapter 7 Trustee for Home Easy, Ltd. The Chapter 7 Trustee, Benjamin A. Stanziale, Jr., also appeared. At that time, the Court reserved decision.

The following constitutes this Court's findings of facts and conclusions of law.

## I BACKGROUND AND PROCEDURAL HISTORY

Home Easy filed a voluntary Chapter 11 petition on October 16, 2023 (Case No. 23-19151). The Debtor filed a prior Chapter 11 petition on June 15, 2022 (Case No. 22-14897) that was dismissed on July 12 , 2022 on the Court's Order to Show Cause.

The Debtor in this case moved to convert the case to a Chapter 7 case on October 25, 2023 and the case was converted by Order entered on November 29, 2023. The Trustee, Benjamin A. Stanziale Jr., was appointed on November 29, 2023 by the United States Trustee.

On April 10, 2024, the Trustee filed the instant Complaint against Emerson for Turnover and Other Relief.

As alleged in the pleadings, the Debtor and Emerson were involved in pre-petition litigation in the U.S. District Court for the District of Delaware. In addition, the Debtor and Emerson entered into a pre-petition Term Sheet (the "Term Sheet") upon which the Complaint is based (See ECF 1, Ex. A.)

**Summary of Complaint**

The Trustee alleges herein that Emerson owes the Debtor $4.1 million as follows:

1. The Debtor paid Emerson $4.1 million based on a future license agreement. No license agreement was executed by the parties and no license exists for which any license fee is due.
2. Emerson refused to return the $4.1 million to the Debtor, and the Trustee brought this adversary proceeding to demand return of the funds.
3. The Trustee alternatively brings this action for breach of contract, breach of the implied covenant of good faith and fair dealing, fraud, promissory estoppel, conversion and unjust enrichment to recover the $4.1 million wrongfully in the possession of Emerson.
4. Background Facts.
    a. On July 12, 2022, Emerson, Home Easy, and Emerson Quiet Kool Co., Ltd. ("EQK") entered into an agreement entitled "Term Sheet for Settlement and Licensing Agreement". *See* Complaint Exhibit A. The Term Sheet was signed to 1) provide the Debtor, Home Easy, with a license to use the trademark EMERSON QUIET KOOL (the "Trademark") and 2) settle a trademark infringement action filed by Emerson against Home Easy and EQK, pending in the US District Court for the District of Delaware styled *Emerson Radio Corp. v. Emerson Quiet Kool Co., Ltd and Home Easy Ltd.*, Civil Action No. 20-1652 (the "Delaware Action").
    b. In the Delaware Action, Emerson asserted Home Easy and EQK committed trademark infringement. The litigation continued for more than 4 years, and a default judgement was entered against Home Easy and EQK in the amount of $6.5 million ("the Judgement"). Home Easy and EQK appealed in the judgment to the Third Circuit, which appeal was pending at the time of the execution of the Term Sheet.
    c. Pursuant to the Term Sheet, the parties were to enter into a license agreement with Emerson licensing to Home Easy the right to use the Trademark for the sale of Home Easy's portable air conditioners, compact residential air conditioners (also referred to as wall room air condition units) and residential room dehumidifiers (all of those are "licensed Goods.") The Agreement contained material terms subject to the execution of a final license agreement. *See Complaint* Exhibit A at 1. In the

Term Sheet, Emerson was referred to as "licensor " and Home Easy was referred to as "licensee."

d. In accordance with the Term Sheet, and upon execution of the license agreement, the Delaware Action would be settled and all money claims that Emerson had against Home Easy and EQK would be satisfied upon Home Easy's full and complete compliance with the Term Sheet and license agreement.

e. The Term Sheet provided that, Home Easy was to pay Emerson a royalty of 2% (two percent) of the net sales of the Licensed Goods sold under the Trademark, and a minimum guaranteed annual royalty in the amount of $500,000 to be paid to Emerson each year of the term of the license agreement.

f. The Term Sheet also required Home Easy to pay Emerson a "License Commencement Fee" ("LCF") of $3.6 million, separate from the royalty payments. The LCF is payable in two installments: $2 million upon the signing of the Term Sheet and $1.6 million, along with the first minimum guaranteed royalty payment of $500,000, within thirty (30) days thereafter.

g. In the Term Sheet, Emerson promised to Home Easy and EQK that it would enter into a final license agreement based on the terms set forth in the Term Sheet. Emerson also promised that any amounts paid to Emerson by Home Easy under the terms of the Term Sheet would not be used by Emerson as a set off against the amount due to it under the Judgement or any future monies that Home Easy or EQK would owe to Emerson resulting from the Delaware Action.

h. On July 13, 2022, in reliance on Emerson's representations and promises, and in anticipation of entering into the license agreement, Home Easy arranged for the initial $2.0 million payment (constituting the first part of the License Commencement Fee) to be wired to Emerson. The wire payment was sent and accepted by Emerson. Emerson has acknowledged that the $2 million wire payment it received was made on behalf of Home Easy. The wire transfer specifically reflected that the $2 million payment was made pursuant to the terms of the Term Sheet.

i. On August 11, 2022, again, in reliance on Emerson's promises and in furtherance of the promised license agreement, Home Easy arranged for the second payment of $2.1 million (constituting the balance of the License Commencement Fee and the first minimum guaranteed royalty payment for the trademark license) to be wired to Emerson, and that $2.1 million was sent and accepted by Emerson. Emerson acknowledged that this $2.1 was made on behalf of Home Easy and was made pursuant to the terms of the Term Sheet.

j. Home Easy Industrial Co. Ltd., a Chinese company affiliated with Home Easy ("Home Easy Industrial"), loaned Home Easy $4.1 million. Home Easy signed a promissory note agreeing to repay the $4.1 million to Home Easy Industrial irrespective of which entity actually wired the money to Emerson. The effect of the

wire transfers to Emerson was that Home Easy performed under the terms of the Term Sheet and paid to Emerson the License Commencement Fee and the first installment of the guaranteed minimum royalty payment of $500,000, together totaling $4.1 million.

k. No formal license agreement was executed between Home Easy and Emerson. Emerson never gave permission to Home Easy to use the Trademark so that no monies, royalties or guaranteed payments of any kind became due to Emerson.

l. In the drafts of the formal license agreement, Emerson made material changes to the terms of the license that were inconsistent with the Term Sheet and were unacceptable to Home Easy. As a result, Home Easy did not sign the drafts of the license agreement prepared and revised by Emerson.

m. The fact that no formal license agreement was executed, and no license was extended to Home Easy did not vitiate the enforceability of the other terms of the Term Sheet, including Emerson's promise that the monies paid to Emerson under the Term Sheet were not to be used as a setoff against the monies due to Emerson under the Judgment.

n. The court in the Delaware Action did not rule that the Term Sheet was not enforceable because no license agreement had been signed. Instead, the Court concluded that the Term Sheet contained a condition precedent to the settlement, namely, the execution of a license agreement, and that, because no license agreement was executed, there was no settlement. The court in the Delaware Action did not rule, however, that Emerson had the right to keep the $4.1 million paid by Home Easy in connection with the proposed license or that the $4.1 million could be used to pay down the Judgment.

o. Emerson did nothing that would entitle it to keep the $4.1 million, and there was no consideration or other benefit given to Home Easy by Emerson for the payment of the $4.1 million. Emerson contended in the Delaware Action that the Term Sheet provided that the $4.1 million was nonrefundable. Emerson misreads the Term Sheet. The $4.1 million would be non-refundable only if Home Easy did not pay the License Commencement Fee and if Home Easy failed to make the payments that were due to Emerson under the license agreement. Home Easy did pay the License Commencement Fee. There is no payment due to Emerson because there is no license agreement. Thus, the $4.1 million is refundable. It was understood by Home Easy that Emerson would not retain the $4.1 million if there was no license agreement executed, and Emerson agreed that the monies paid were not to be used to set off any amount due under the Judgment.

p. On December 13, 2023, the Trustee wrote a letter to Emerson and demanded the return of the $4.1 million. Emerson has continued to retain and has not returned the $4.1 million to the Trustee.

5. The Complaint alleges the following counts:

**Count One –Turnover of Assets of the Estate.** The $4.1 million paid to Emerson by Home Easy was in connection with a license agreement between Emerson and Home Easy. The license agreement never materialized and the $4.1 million must be returned to the estate so that all creditors, including Emerson and Home Easy Industrial, which loaned the $4.1 million to Home Easy, can share in the assets of the estate. Pursuant to 11 U.S.C. §542, the Trustee may seek the turnover of all property of the bankruptcy estate. Pursuant to 11 U.S.C. §704(a), the Trustee has a statutory duty to collect property of the estate and account for all property received. Thus, the Trustee demands judgment against Emerson directing that for the benefit of the Debtor's estate Emerson turnover the $4.1 million, together with pre-judgment and post-judgment interest in the amounts allowed by law, costs of suit, and such further relief as the Court may deem appropriate.

**Count Two – Breach of Contract.** Pursuant to the Term Sheet, Home Easy paid Emerson $4.1 million, the sole consideration for which was the license to be granted by Emerson to use the Trademark in connection with the sale of the Licensed Goods. The $4.1 million consisted of a $3.6 million License Commencement Fee and $500,000 representing the first guaranteed minimum license royalty payment. Emerson did not grant Home Easy the license to use the Trademark and did not return the $4.1million to Home Easy. Thus, Emerson breached its obligation under the Term Sheet to either grant Home Easy the use of the Trademark or, if no license was granted, refund the monies to Home Easy. Therefore, the Trustee demands judgment against Emerson for compensatory damages in the amount of $4.1 million, pre-judgment and post-judgment interest in the amounts allowed by law, costs of suit, and such further relief as the Court may deem appropriate.

**Count Three – Breach of the Implied Covenant of Good Faith and Fair Dealing.** Implicit in the Term Sheet is a covenant of good faith and fair dealing. Even if Emerson were not contractually obligated to refund the $4.1 million in the event a license agreement was not executed, then Emerson still engaged in conduct, apart from its contractual obligations, without legitimate motives and in bad faith for the purpose of inequitably depriving Home Easy of the $4.1 million contrary to and to the detriment of Home Easy's reasonable expectations, by not refunding the $4.1 million to Home Easy after it was clear that no license agreement would be consummated. Home Easy has been damaged in the amount of $4.1 million by reason of Emerson's breach of the covenant of good faith and fair dealing. Therefore, the Trustee demands judgment against Emerson for compensatory damages in the amount of $4.1 million, pre-judgment and post-judgment interest in the amounts allowed by law, costs of suit, and such further relief as the Court may deem appropriate.

**Count Four – Fraud.** Emerson expressly represented to Home Easy in the Term Sheet that any payments made to Emerson pursuant to the Term Sheet or pursuant to any license agreement subsequently entered would not be applied toward or used by Emerson to offset the monies due to Emerson resulting from the Judgment or other monetary relief granted to it in the Delaware Action. Relying on this representation, Home Easy wired the money. Emerson evidently contends it has the right to keep the $4.1 million which it will apply to or use to offset any amounts due to it based on the Judgment or resulting from the Delaware Action, and Home Easy suffered damages because of Emerson's false representation. Thus, the Trustee demands judgment against Emerson for compensatory damages in the amount of $4.1 million, pre-judgment and post-judgment interest in the amounts allowed by law, punitive damages, costs of suit, and such further relief as the Court may deem appropriate.

**Count Five – Promissory Estoppel.** Emerson promised that any monies paid to it pursuant to the terms of the Term Sheet would not be applied toward or used to offset any amounts due to Emerson under the Judgment or any other monetary relief granted in the Delaware Action. Home Easy reasonably relied on that promise when it paid the $4.1 million to Emerson. Home Easy relied on the promise to its detriment when it paid $4.1 million to Emerson only for Emerson to later claim that it could keep the money as an offset against the money due under the Judgment. Therefore, the Trustee demands judgment against Emerson for compensatory damages in the amount of $4.1 million, pre-judgment and post-judgment interest in the amounts allowed by law, costs of suit, and such further relief as the Court may deem appropriate.

**Count Six – Conversion.** Emerson has wrongfully maintained control over the $4.1 million, which money rightfully belongs to Home Easy. Once the court in the Delaware Action determined that no license agreement had been effectuated, that money should have been returned to Home Easy, as Emerson no longer was authorized to retain it. Despite the Trustee's demand for return of the funds, Emerson has refused to turn the money over to the Trustee and has interfered with the Trustee's rights to it. Thus, Emerson has improperly exercised dominion and control over the $4.1 million and thus converted Home Easy's assets and funds. Accordingly, the Trustee demands judgment against Emerson for compensatory damages in the amount of $4.1 million, pre-judgment and post-judgment interest in the amounts allowed by law, punitive damages, costs of suit, and such further relief as the Court may deem appropriate.

**Count Seven – Unjust Enrichment.** Through the payment to Emerson of $4.1 million. Home Easy conferred a benefit on Emerson, in exchange for which Home Easy expected that Emerson would provide it with a license to use the Trademark in connection with the Licensed Goods. Emerson's retention of the $4.1 million, without providing Home Easy with the license or other consideration for the payment of the $4.1 million, would unjustly

enrich Emerson at Home Easy's expense and to Home Easy's detriment. Emerson should be compelled by this Court to make restitution to the Trustee for the $4.1 million it received from Home Easy. Therefore, Trustee demands judgment against Emerson for compensatory damages in the amount of $4.1 million, pre-judgment and post-judgment interest in the amounts allowed by law, costs of suit, and such further relief as the Court may deem appropriate.

## II SUMMARY OF MOTION (ECF 9), OPPOSITION (ECF 11) AND REPLY (ECF 14)

### A. Summary of Motion to Dismiss case pursuant to F. R. C. P. 12(b)(1), 12(b)(6), 12(b)(7)

On June 3, 2024, Emerson filed the Motion to Dismiss the Adversary Complaint (ECF 9) and argues that the Trustee lacks standing to bring claims that do not implicate property of the estate, and the Complaint should be dismissed pursuant to Fed. R. Civ. P, 12(b)(1) and Bankruptcy Rule 7012. In addition, Emerson argues the Trustee has failed to name necessary parties and the Complaint should be dismissed pursuant to Fed. R. Civ. P, 12(b)(7) and 19 and Bankruptcy Rules 7012 and 7019. Further, Emerson asserts the Complaint fails, as a matter of law, to state any claims against Emerson and the Complaint should be dismissed pursuant to Fed. R. Civ. P, 12(b)(6) Bankruptcy Rule 7012. Specifically, the Trustee argues the Complaint should be dismissed pursuant to Fed. R. Civ. P, 12(b)(6) because: (a) the claims are barred by *in pari delicto*; (b) the turnover claim fails because the property transferred is not estate property; (c) the quasi contract claims cannot continue when a contract exists; (d) New Jersey's economic loss doctrine bars the fraud and conversion claims; and (e) the breach of contract claim must be dismissed because there is no allegation that Emerson breached a provision of the term sheet and the implied covenant claim is not sufficiently plead and is duplicative of the breach of contract claim.

1. The Defendant asserts here:

a. For almost 7 years, Emerson has successfully pursued the Debtors[1] and their principals and cohorts through litigation in the US District Courts for the Districts of Delaware and New Jersey, the Third Circuit, and the U.S. Patent and Trademark Office, to stop their blatant and ongoing infringement of Emerson's intellectual property rights.

b. Emerson has prevailed in every substantive matter, in every jurisdiction, against the Debtors, and courts have issued rulings defaulting, enjoining, and sanctioning the Debtors.

c. The Complaint seeks the "return" of two pre-petition payments that were made by nondebtor Home Easy Industrial Co., Ltd. ("Home Easy Industrial"), a foreign corporation, in July and August 2022 pursuant to a Term Sheet to which debtors EQK, Home Easy, the non-debtor Liang Jiucheng (hereinafter, the "Guarantor"), and Emerson were parties. At that time, the Delaware District Court had entered a default judgment and permanent injunction against Home Easy and EQK barring them from infringing on Emerson's trademark.

d. EQK and Home Easy filed their first chapter 7 petitions in June 2022. Despite having no obligation to even consider discontinuing its litigation, Emerson extended an olive branch to Home Easy by engaging in negotiations over a pathway for the Debtors to utilize the EMERSON QUIET KOOL trademark again.

e. Those negotiations culminated in the execution of the Term Sheet, which was designed to outline the contours of a final settlement and license agreement, place all of the ongoing litigation among the parties at a standstill and impose certain

[1] The Debtors refer to Emerson Quiet Kool Co. Ltd. ("EQK") (Case No. 23-18987-RG), American Ductless AC Corp. ("Ductless") (Case No. 23-18988-RG), and Home Easy Ltd. ("Home Easy.")

payment and other obligations on Home Easy, EQK, and the Guarantor. The final agreements were never consummated.

f. The Term Sheet itself was clear that final settlement was subject to negotiation and execution of a final licensing agreement, as well as Home Easy's full compliance with the Term Sheet. The parties could not come to terms on a final license agreement because of Home Easy's own intransigence.

g. Additionally, no further annual royalty payments were made to Emerson under the Term Sheet. This would have been required if the Term Sheet operated as an actual license. The District of Delaware sided with Emerson and denied Home Easy and EQK's motion to compel enforcement of the Term Sheet.

2. Emerson, sets forth three arguments:

a. The Complaint must be dismissed under Rule 12(b)(1) and Bankruptcy Rule 7012 for lack of subject-matter jurisdiction because the Trustee lacks standing to assert these claims. The payments at issue were made by a non-debtor, Home Easy Industrial, and no funds either passed through Home Easy's bank accounts or were ever under Home Easy's dominion or control. Because the funds at issue were never the property of the Debtor's estate, the Trustee lacks standing to prosecute the Complaint under Article III of the U.S. Constitution and section 541 of the Bankruptcy Code.

b. The Complaint must be dismissed under Fed. R. Civ. P. 12(b)(7) and 19 and Bankruptcy Rules 7012 and 7019 based on the Trustee's failure to join the Guarantor, who is a necessary and indispensable party for whom joinder is not feasible. Under binding Third Circuit precedent, a co-obligee, such as the

Guarantor, is a necessary party and because the Guarantor resides in China and is not otherwise susceptible to this Court's personal jurisdiction in this suit, such party's joinder is not feasible.

c. The Complaint must be dismissed pursuant to Rule 12(b)(6) and Bankruptcy Rule 7012 for failure to state any claims upon which relief can be granted. The claims against Emerson for turnover under Section 542 of the Bankruptcy Code, quasi contracts, fraud and conversion and breach of contract and the implied covenant of good faith must be dismissed for the following reasons:

   i. *In pari delicto*: As a general matter, the claims in the Complaint must be dismissed based on the *in pari delicto* doctrine, which subjects the Trustee to the unclean hands of Home Easy and bars the pursuit of claims against a victim of Home Easy's malfeasance like Emerson.

   ii. Turnover: The Trustee's turnover claim pursuant to section 542(a) must be dismissed because the Trustee has failed to plead (and cannot plausibly plead) that the Non-Debtor Payments constitute property of Home Easy's estate or that Emerson is in possession of any property of Home Easy's estate, instead the Trustee seeks to recover non-debtor property based on disputed state law contract and tort claims.

   iii. Quasi-contract claims: The Trustee's quasi-contract claims for promissory estoppel and unjust enrichment must be dismissed because under New Jersey law, when the matters at issue are governed by a written agreement as the Trustee alleges them to be, such quasi-contract claims must fail as a matter of law.

iv. Fraud and conversion: The Trustee's fraud and conversion claims must be dismissed because the alleged conduct is the subject of the Term Sheet, making these claims barred by New Jersey's economic loss doctrine, and because they are otherwise insufficiently pleaded.

v. Breach of contract and implied covenant: The Trustee's breach of contract claim must be dismissed because it fails to identify a single specific provision of the Term Sheet that Emerson has allegedly breached and because the Trustee cannot plausibly allege any cognizable damages. The Trustee's claim for breach of the implied covenant of good faith also must be dismissed as insufficiently pleaded and merely duplicative of the breach of contract claim.

3. Emerson asserts:

a. The issues at hand stem from the July 12, 2022 "Term Sheet for Settlement and Licensing Agreement" (referred to herein as the "Term Sheet") entered into by Emerson, Home Easy, EQK, and the Guarantor. The Term Sheet was entered in anticipation of a settlement agreement that would provide Home Easy with a license from Emerson to use the trademark EMERSON QUIET KOOL and resolve trademark infringement claims asserted by Emerson against Home Easy and EQK in the Delaware Action. See *Emerson Radio Corp. v. Emerson Quiet Kool Co.,* No. CV 20-1652-GBW, 2023 WL 6387897, at *7 (D. Del. Sept. 29, 2023).

b. the Term Sheet required Home Easy to pay (i) "minimum royalty payments" of $500,000 per year "regardless of actual sales or sales activity," and (ii) "a License Commencement Fee of $3,600,000" of which "$2,000,000 shall be payable on the

date of signing the Term Sheet" and "[t]he balance due of $1,600,000 along with the 1st year license fee of $500,000 shall be payable within 30 days of signing the Term Sheet. (ECF 9, at 5). As the Trustee's Complaint sets forth, the "License Commencement Fee" was to be "separate from the payment of royalties" and meant to be the fee to incentivize Emerson to entertain a bargaining table with Home Easy. (*Id.* at 6). The Term Sheet provided that "the $2 million paid on signing the Term Sheet, and any subsequent amounts that are paid, are non-refundable if [Home Easy] fails to make the full $3,600,000 License Commitment Fee and all Minimum Annual Guarantee Royalties." *Id.*

c. Prior rulings from the Delaware District Court confirm that the Term Sheet did not convey a license to use Plaintiff's EMERSON mark unless and until certain conditions subsequent were satisfied. One of important conditions is that the parties agree to and execute a full license agreement that would dictate the terms of use. The Term Sheet clearly provided the following:

   i. The Term Sheet states it is "subject to the execution of a final license agreement (the 'License Agreement') to be promptly prepared and executed consistent with the Term Sheet" (ECF 1. Ex. A at 1).

   ii. In a section titled "Acknowledgement" it is stated that "Licensee understands that this Term Sheet does not constitute a final license agreement and that no such agreement shall be deemed to have been reached until a final license agreement has been executed by the Parties" (*Id.* at 8)

   iii. The Acknowledgement Section also states that "[u]ntil the License Agreement is finalized and signed, the Licensor (Emerson) may continue to

pursue all of its rights, remedies and actions under the law against Licensee and fully enforce the Order and Judgment against Home Easy and EQK Emerson Quiet Kool" (ECF 9, at 8)

iv. That section further states "[n]o products and/or collateral materials shall be sold or otherwise distributed until a formal License Agreement has been fully executed and Licensor has provided express written approval of the particular products and materials." *Id.*

d. Emerson points to the alleged conduct of the parties under the Term Sheet arguing that the circumstances in which the Debtors have found themselves is of their own making:

i. As the Trustee admits in his pleading, Emerson circulated a would-be final license agreement, but Home Easy declined to execute it, and no formal license agreement was ever entered into between the parties.

ii. It is undisputed from the pleadings that neither Home Easy, the Guarantor, nor any other affiliated parties made any further minimum guaranteed royalty payments or any other payments to Emerson in connection with the Term Sheet.

e. The Delaware Action:

i. As alleged in the Complaint, EQK and Home Easy previously moved to enforce a purported settlement relying on the Term Sheet in the Delaware Action. That motion was denied.

ii. the Delaware District Court made several findings and conclusions that undercut the theories of relief the Trustee asserts in his Complaint. For

instance, while the Complaint now alleges Emerson breached its obligations by failing to license the trademark, the Delaware District Court found that Home Easy and EQK had not signed the license agreement circulated by Emerson. Emerson expressly argued to the Delaware District Court that "[b]ecause [EQK and Home Easy] refused to enter into a license agreement with [Emerson], they are not licensed to sell any EMERSON branded goods and cannot generate the required Minimum Guarantee Royalties, making any amounts paid non-refundable." (Delaware Action, ECF 279 at 15). The Delaware District Court did not reject these arguments nor compel Emerson to return any of those amounts paid to it. The Delaware District Court concluded that Home Easy and EQK have not met their burden of proving that all contact terms have been agreed upon, and thus, no enforceable settlement agreement exists." *Emerson Radio Corp. Co.*, 2023 WL 6387897, at *6.

4. Emerson's Arguments under Rule 12(b)(1):

    a. The Trustee lacks standing to prosecute the complaint or undo the non-debtor payments because the non-debtor payments were never the property of the estate.

        i. A trustee may only sue to recover property of the estate and Rule 12(b)(1) provides that a court may dismiss a complaint for lack of subject matter jurisdiction. See *In re AE Liquidation, Inc.*, 435 B.R. 894, 900 (Bankr. D. Del. 2010) (citing Fed. R. Civ. P. 12(b)(1)).

ii. The Trustee does not have standing to collect money not owed to the estate. *Charles A. Stanziale, Jr. v. Richards, Layton & Finger, P.A. (In re EP Liquidation, LLC)*, 583 B.R. 304, 322 (Bankr. D. Del. 2018).

iii. Here, the funds never passed through Home Easy's bank accounts such that they constitute estate property.

iv. Additionally, the Loan Agreement between Home Easy and Home Easy Industrial does not convert non-debtor funds into debtor funds and estate property. A payment made by a third party to a creditor of the debtor will constitute estate property only when the payment represents a loan by the third party to the debtor and the debtor, rather than the lender, designates the creditor to be paid and controls the application of the loan. *See In re Schick*, 234 B.R. 337, 346 (Bankr. S.D.N.Y. 1999) (citing *Smyth v. Kaufman (In re J.B. Koplik & Co.)*, 114 F.2d 40 (2d Cir. 1940)). Conversely, a payment by a third party does not constitute estate property when "the third party lends money to the debtor for the purpose of paying a specific creditor that the lender designates, the funds are 'earmarked,' do not become property of the debtor and cannot be recovered by the trustee." *Id.* (citing *Glinka v. Bank of Vermont (In re Kelton Motors, Inc.)*, 97 F. 3d 22, 25 (2d Cir. 1996). Here, the complaint alleges that Home Easy Industrial loaned Home Easy the $4.1million. The money was wired to Emerson by Home Easy Industrial, on behalf of Home Easy. It was done so in accordance with the Loan Agreement. The Loan Agreement expressly required that Home Easy Industrial directly pay the proceeds over to Emerson, without any

amounts ever being available for Home Easy to deposit into its own account or use for any other purpose. In the proof of claim filed by Home Easy Industrial, it asserted a claim for a "Loan for payment of Prepaid License Commencement Fee" and the Loan Agreement, provides that Home Easy Industrial "shall pay the above amount [$4.1 million] to the account designated by [Home Easy] (Emerson Radio Operation) within 60 days after signing this agreement." Emerson urges that the circumstances are analogous to *In re Wagenknecht*, 971 F.3d 1209 (10th Cir. 2020) where the court held that a mother's payment to her son's attorneys for his unpaid legal bills did not implicate estate property, even though the son executed a promissory note.

v. Thus, since the money has never passed through Home Easy's account or control, it does not constitute recoverable property of the estate, and the Trustee has no standing to seek return of the funds.

b. Emerson's Arguments under Rule 12(b)(7).

i. First, the Guarantor qualifies as a necessary party because when the claims at issue are related to obligations under an agreement between the parties, the obligees (i.e., persons to whom another is obligated) to the agreement are considered necessary parties under Rule 19(a). See *Dickson v. Murphy*, 202 F. App'x 578 (3d Cir. 2006) (finding co-obligees of agreement necessary parties when complaint alleged various fraud, contract, and quasi-contract claims related to two agreements). Here, the Guarantor guaranteed "all financial and other obligations" of Home Easy under the Term Sheet

(ECF 1, Ex. A, at 5). Any hypothetical obligation to refund the Non-Debtor Payments is owed not only to Home Easy, but also the Guarantor. Home Easy and the Guarantor, therefore, are co-obligees of the alleged obligation to refund the Non-Debtor Payments that the Trustee alleges Emerson has breached. Therefore, to proceed in this case without the Guarantor subjects Emerson to potential future litigation on the same issue.

ii. Second, upon finding a party to be necessary, a court must then determine whether joinder of that party is feasible. Joinder is considered not feasible if the court cannot exercise personal jurisdiction over the absentee. Personal jurisdiction may be specific or general. (ECF 9, at 16) (citing *Ontel Prods. Corp. v. Mindscope Prods.*, 220 F. Supp. 3d 555 (D.N.J. 2016)). The Guarantor is an individual residing in China who has had no demonstrable affiliations with or activities in New Jersey that could create a basis for general and specific jurisdiction here. (ECF 9, at 16)( citing *Associated Bus. Tel. Sys. Corp. v. Danihels*, 829 F. Supp. 707, 711 (D.N.J. 1993) (citing *Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 478-79 (1985)) ("[A] contract between a forum resident and an out-of-state party will not automatically establish sufficient contacts with the forum to justify *in personam* jurisdiction.") As a result, Emerson argues the Guarantor cannot be feasibly joined.

iii. When a court determines that joinder is necessary under Rule 19(a) but not feasible, the court must then determine whether the non-joined party is

indispensable under Rule 19(b). Emerson sets forth the following non-exhaustive factors to consider under Rule 19(b):

> "[first,] to what extent a judgment rendered in the person's absence might be prejudicial to the person or those already parties; second, the extent to which, by protective provisions in the judgment, by the shaping of relief, or other measures, the prejudice can be lessened or avoided; third, whether a judgment rendered in the person's absence will be adequate; fourth, whether the plaintiff will have an adequate remedy if the action is dismissed for nonjoinder."

(ECF 9, p. 17)(quoting *Dickson*, 202 F. App'x at 581).

Here, because the Guarantor is both a necessary and indispensable party for whom joinder is not feasible under Rule 19(a) and (b), this case cannot proceed without him and must be dismissed. Factors one to three weigh in favor of dismissal. Frist, repetitive litigation and potentially different outcomes will prejudice Emerson. Second, this Court cannot shape its relief to reduce prejudice to Emerson as this Court cannot enjoin the absent party in China, from bringing a subsequent claim. Thirdly, leaving open the possibility of subsequent claims by the Guarantor would render any judgement here inadequate and be counter to public policy.

iv. Because the Guarantor is a necessary party to Trustee's claims, who cannot feasibly be joined, and is also indispensable, this entire action must be dismissed.

c. Emerson's Arguments under Rule 12(b)(6).

Emerson argues that if the Court does not dismiss the Complaint for lack of standing or failure to name a necessary party, the Complaint must be dismissed for

failure to state a claim upon which relief can be granted as the claims are either barred under New Jersey law or do not state a plausible claim for relief.

i. The claims are barred by the *In Pari Delicto* Doctrine. The doctrine of *in pari delicto* provides that a plaintiff may not assert a claim against a defendant if the plaintiff bears fault for the claim." *Official Comm. Of Unsecured Creditors v. R.F. Lafferty & Co.*, 267 F.3d 340, 348–49 (3d Cir. 2001). Under New Jersey law, the doctrine of *in pari delicto* is an equitable defense to claims in equity and means that "[i]n a case of equal or mutual fault ... the position of the [defending] party ... is the better one." *Lowenschuss v. Resorts Int'l, Inc. (In re Resorts Int'l, Inc.)*, 181 F.3d 505, 512 (3d Cir. 1999) (quoting Black's Law Dictionary (6th ed. 1990)). The doctrine may be applied uniformly across different claims because the analysis "will typically be the same." *Lafferty*, 267 F.3d at 354–55. The Trustee is subject to the *in pari delicto* doctrine as he stands in the shoes of Home Easy. See *In re NJ Affordable Homes Corp.*, No. 05-60442-DHS, 2013 WL 6048836, at *25. (Bankr. D.N.J. Nov. 8, 2013) (Because a Trustee may take no rights greater than the debtor had on the petition date under § 541, he may not use his status to insulate himself from the debtor's pre-petition wrongdoing and any applicable defenses must be applied as of the petition date without regard to pre-petition events.) *Picard v. HSBC Bank PLC*, 454 B.R. 25, 29 (S.D.N.Y. 2011) ("a bankruptcy trustee is often barred from bringing claims on behalf of the debtor's estate because of the common law doctrine of *in pari delicto*."), *amended by* 2011 WL 3477177

(S.D.N.Y. Aug. 8, 2011). Courts have applied the *in pari delicto* doctrine where plaintiffs previously engaged in trademark infringement or other illegal acts. For example, in *10 Minute Fitness Inc. v. Amentum Servs., Inc.*, 679 F. Supp. 3d 1374, 1380 (S.D. Fla. 2023), the plaintiff imported machines that U.S. Customs and Border Protection determined contained counterfeit trademarks in violation of federal law. The plaintiff hired the defendant to destroy the machines, later learned that the machines nonetheless were being sold online and sued the defendant for negligence. The court dismissed the claim on a Rule 12 motion, holding that the *in pari delicto* doctrine barred the plaintiff's claims given the that the plaintiff had engaged in trademark infringement and thus "Plaintiff is barred from recovering due to its violation of federal law." (ECF 9) (quoting *10 Minute Fitness Inc.*, 679 F. Supp. 3d, at 1380-81) (citing *Code v. Adidas Am., Inc.*, No. CV 6:23-4997, 2024 WL 637356, at *3 (D.S.C. Jan. 11, 2024)).

ii. Here, as set forth in the written opinions of the Delaware District Court and the Third Circuit, the Debtors have evaded their legal obligations and engaged in contemptuous and sanctionable conduct:

1. Obstructionist Conduct: In entering default judgment, the Delaware District Court found, and the Third Circuit affirmed, that Debtors engaged in a "pattern of delay and lack of representation that ha[s] plagued this litigation," evidenced a "pattern of willful refusals to participate in this case in good faith," and their "pattern of behavior reflected willful noncompliance with [its] court obligations and lack

of cooperation with [its] various counsel." *Emerson Radio Corp.*, 2023 WL 4453604, at *3.

2. Civil Contempt: The Delaware District Court held the Debtors in civil contempt, finding that they violated the Permanent Injunction by engaging in numerous instances of non-compliance that continued at least up to June 2023, and likely longer.

3. Exceptional Conduct: The Delaware District Court found that the case was "exceptional," thus warranting an award of attorney's fees under 15 U.S.C. § 1117(a), because of the merits and the "unreasonable manner in which Defendants litigated the case." *Emerson Radio Corp.*, 2023 WL 6387897, at *3.

4. Willful Infringement: In awarding enhanced damages under 15 U.S.C. § 1117, the Delaware District Court, finding that the Debtors engaged in willful trademark infringement, including "after default judgment." *Id.*, at *4-5.

5. Final Judgment: The Delaware District Court has entered final judgment in favor of Emerson on the following causes of action: trademark infringement under 15 U.S.C. § 1114 (Count I); trademark infringement, unfair competition, and false designation of origin under 15 U.S.C. § 1125(a)(l)(A) (Count II); false advertising under 15 U.S.C. § 1125(a)(1)(B) (Count III); violation of the Anti-Cybersquatting Consumer Protection Act under 15 U.S.C. § 1125(d) (Count IV); trademark infringement under N.J.

Stat. Ann. § 56:3-13.16 (Count V); trademark dilution under N.J. Stat. Ann. § 56:13-20 (Count VI); false designation of origin under N.J. Stat. Ann. § 56:8-2 (Count VII); trademark infringement under New Jersey common law (Count VIII); unfair competition and false designation of origin under New Jersey common law (Count IX); and cancellation of Registration No. 4,688,893 (Count X). (Delaware Action, ECF 290).

iii. Those prior judicial findings support the applicability of the *in pari delicto* doctrine. The Trustee's claims in the Complaint all implicate the Term Sheet, which was designed to provide a pathway to settle the pending litigation between Emerson and the Debtors – litigation in which the Debtors have been found liable for trademark infringement and other claims, and which settlement was never consummated. At the time the Term Sheet was executed, the Delaware District Court had entered default judgment and an injunction against the Debtors. The Trustee standing in Home Easy's shoes cannot now attempt to enforce Home Easy's alleged rights under the Term Sheet and thus benefit from the Debtor's bad acts. Thus, the Complaint must be dismissed based on the *in pari delicto* doctrine.

d. Count One –Turnover Must Be Dismissed. Emerson urges this claim must be dismissed because the Trustee has failed to plead that Emerson is in possession of property of the estate, and a turnover claim is not an available remedy where, as here, the Trustee has not plead an absolute, undisputed right to the return of the Non-Debtor Payments.

i. Under the plain language of Bankruptcy Code section 542(a) the following elements must be shown to compel turnover of property of the estate or its value: (1) during the case, (2) an entity other than a custodian (3) was in possession, custody, or control of property that a trustee could use, sell, or lease under 11 U.S.C. § 363 or that a debtor may exempt under 11 U.S.C. § 522, and (4) such property is not of inconsequential value or benefit to the estate. 11 U.S.C. § 542(a). To maintain a turnover claim, a trustee must first demonstrate that the property in the possession of a non-debtor is actually property of the estate. *In re Airway Indus., Inc.*, 354 B.R. 82, 86 (Bankr. W.D. Pa. 2006) ("A turnover under § 542 is predicated on a determination under § 541 that the property at issue is property of the estate."); *In re Heritage Org., L.L.C.*, 350 B.R. 733, 737 (Bankr. N.D. Tex. 2006) ("If the Documents are not property of the estate, then there exists no basis under Section 542(a) for their turnover.").

ii. Emerson asserts the Trustee failed to meet the third element because the Non-Debtor Payments were made by a non-debtor who was not even party to the Term Sheet and the Court has no basis to determine Non-Debtor Payments were part of the estate.

iii. Emerson further argues that it is well-settled that a turnover claim must be dismissed where, as here, the Trustee seeks to recover property based on disputed state law contract and tort claims. A turnover action cannot be maintained where there is a "legitimate dispute about the ownership of property a trustee seeks to recover." See, e.g., *In re Lexington Healthcare*

*Grp., Inc.*, 363 B.R. 713, 716 (Bankr. D. Del. 2007). In this Motion to Dismiss the Complaint, a legitimate dispute exists regarding the non-debtor payments that mandate dismissal of the turnover count. See *Id.* (dismissing turnover count on a Rule 12(b)(6) motion for return of a security deposit because the lease was "not so plain and unambiguous as to provide a clear, objective basis for concluding that the security deposit is property of the estate").

e. Count Five (Promissory Estoppel) and Count Seven (Unjust Enrichment) Must be Dismissed Given the Existence of a Valid Contract.

Emerson argues that because parties' rights are governed by the written agreement – the Term Sheet, the Trustee cannot argue quasi-contract remedies. Emerson asserts it is well established under New Jersey law that where an express, valid contract exists governing the matter at issue, a plaintiff cannot proceed on theories of quasi-contract, including promissory estoppel and unjust enrichment. See *Hillsborough Rare Coins, LLC v. ADT LLC*, No. CV 16-916-MLC, 2017 WL 1731695, at *6-7 (D.N.J. May 2, 2017) (dismissing claim for promissory estoppel as prohibited quasi-contract theory when a valid contract existed). Because the Trustee asserts the Term Sheet governs the Trustee's claims, any claims arising under quasi-contract theories are unavailable, and the Court should dismiss the Trustee's claims for promissory estoppel and unjust enrichment.

f. Count Four (Fraud) and Count Six (Conversion) Must be Dismissed

i. The fraud and conversion claims should be dismissed under the New Jersey's economic loss doctrine. "The economic loss doctrine prohibits plaintiffs from recovering in tort economic losses to which their entitlement only flows from a contract." *State Cap. Title & Abstract Co. v. Pappas Bus. Servs., LLC*, 646 F. Supp. 2d 668, 676 (D.N.J. 2009). Specifically, under this doctrine, a tort claim cannot be asserted alongside a breach of contract claim when the alleged tortious conduct is the subject of a contract between the parties. *Id.* Both fraud and conversion are tort claims subject to the economic loss doctrine. *Id.* at 677.

ii. Here, as to count four, because the basis for the Trustee's purported fraud claim is derived entirely from the parties' obligations under the Term Sheet, it is barred by the economic loss doctrine and must be dismissed. As to count six, when damages sought pursuant to a conversion claim are those which the claimant would be entitled to, if it all, under an agreement, the conversion claim is barred by the economic loss doctrine. See *Titan Stone, Tile & Masonry, Inc. v. Hunt Const. Grp., Inc.,* No. CIV. 05-3362-GEB, 2007 WL 174710 (D.N.J. Jan. 22, 2007).

iii. In addition to the economic loss doctrine, the fraud claim is insufficiently pleaded. Trustee's fraud claim fails to meet the heightened particularity standard required by Rule 9. Rule 9 requires that "[i]n alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake." Fed. R. Civ. P. 9(b). Trustee repeatedly and impermissibly relies on "information and belief" in alleging the key

facts of his fraud claims, not facts upon which the allegations are founded, which falls short of satisfying even a relaxed application of Rule 9. *MZL Cap. Holdings, Inc*. v. TD Bank, N.A., No. CV 14-5772-RMB-AMD, 2016 WL 4163827, at * 2 (D. N. J. Aug. 5, 2016).

iv. Even if Rule 9(b) did not apply, the Trustee still fails to allege the required elements of a fraud claim sufficient to satisfy even a Rule 8 standard. Under New Jersey law, "[t]he five elements of common law fraud are: (1) a material misrepresentation of a presently existing or past fact; (2) knowledge or belief by the defendant of its falsity; (3) an intention that the other person rely on it; (4) reasonable reliance thereon by the other person; and (5) resulting damages." *Frick v. Novartis Pharms. Corp.*, No. CIV 05-5429-DRD, 2006 WL 1344316, at *1 (D.N.J. May 16, 2006). The Trustee failed to meet any of these factors.

1. Material Misrepresentation: The Trustee alleges that Emerson represented in the Term Sheet that any payments made to Emerson would not be applied to offset monies due from the judgment in the Delaware Action. (ECF 1 ¶ 46). But this is neither a presently existing nor past fact – it is a contractual provision regarding future conduct. (ECF 9, at 29) (citing *Alexander v. Cigna* Corp., 991 F.Supp. 427, 435 (D.N.J. 1998).

2. Knowledge of Falsity: Emerson could not have known or believed that its agreement to forebear from an action in the future was false, since an agreement to refrain from action is not a fact.

3. Intent and Reasonable Reliance: There is no plausible allegation that Emerson intended and Home Easy reasonably relied on any agreement that the Non-Debtor Payments would not offset against amounts owed under the Delaware judgment because this provision exclusively benefits *Emerson*, not Home Easy. Specifically, the Term Sheet provides that if a formal license agreement is not entered into between the parties, Emerson would retain the right to collect the judgment as well as retain the nonrefundable Non-Debtor Payments. As such, there is no benefit to Home Easy in this portion of the Term Sheet in which Debtor bases its fraud claims and therefore it is axiomatic that Emerson could neither intend for Home Easy to rely on that provision nor could Home Easy have reasonably relied upon that provision in deciding to make those payments.

4. Element Five (Damages): As the Trustee alleges, Home Easy did not pay the Non-Debtor Payments, which were instead paid by Home Easy Industrial (ECF 1 ¶ 19), leaving no factual basis for Home Easy to claim any associated damages.

v. The conversion claim is insufficiently pleaded because the Trustee does not allege that any purportedly converted money ever belonged to Home Easy. Under New Jersey law, conversion is the "wrongful exercise of dominion and control over the property [owned by] another in a manner inconsistent with the [owner's] rights." *Communications Programming, Inc. v. Summit Manufacturing, Inc.*, No. CIV. A. 98-253, 1998 WL

329265, at *5 (D.N.J. June 16, 1998). To establish conversion, the money converted "must have belonged to the injured party." *Id.* Because Home Easy never owned or controlled the money used to pay the Non-Debtor Payments as discussed *supra*, the Trustee has not pleaded an actionable claim for conversion. *Id.*

vi. In addition, the conversion count is insufficiently pleaded under New Jersey law because the Complaint merely alleges that Emerson owes the money to Home Easy, i.e., as a debt. However, under New Jersey law when "money, as opposed to tangible property, is the subject of a conversion claim, New Jersey courts require that a plaintiff show something more than a contractual obligation on the part of a defendant to pay the plaintiff to establish conversion." *Scholes Elec. & Commc'ns, Inc. v. Fraser*, No. CIVA 04-3898-JAP, 2006 WL 1644920, at *5 (D.N.J. June 14, 2006). A plaintiff must instead show "that the money in question was identifiably the plaintiff's property or that the defendant was obligated to segregate such money for the plaintiff's benefit." *Id.* The Complaint entirely fails to satisfy this pleading requirement under New Jersey law and instead simply recycles the allegations in the breach of contract count seeking the return of the Non-Debtor Payments.

g. Count Two (Breach of Contact) must be dismissed because the Trustee fails to plead facts establishing the elements of a breach of contract claim.

i. "Under New Jersey law, a proper breach of contract claim includes four elements: (1) the parties entered into a valid contract, (2) the plaintiff

honored his own obligations under the contract, (3) the defendant failed to perform his obligations under the contract, and (4) the plaintiff sustained damages as a result." *MZL Cap. Holdings, Inc.*, 734 F. App'x at 105. A breach of contract claim is not sufficiently pleaded when it fails to identify the specific provision of the agreement that was breached. *Id.* Here, the alleged breaches of contract either do not correspond to provisions of the Term Sheet or are otherwise legally insufficient.

ii. First, there is no contractual obligation for Emerson to "grant Home Easy the license to use the Trademark." (ECF 1 ¶ 37). In fact, as agreed to by the Delaware Court the Term Sheet provides that this "Term Sheet does not constitute a final license agreement and that no such agreement shall be deemed to have been reached until a final license agreement has been executed by the parties." (ECF 1. Ex. A at 8). As alleged in the Complaint, and also previously found by the Delaware District Court, no final license agreement was entered into between the parties *Emerson Radio Corp.*, 2003 WL 6387897 at *6. Accordingly, Emerson never had an obligation to grant Home Easy a license to use the EMERSON QUIET KOOL mark.

iii. Second, there is no contractual obligation for Emerson to refund the Non-Debtor Payments. In fact, the Term Sheet expressly provides that the Non-Debtor Payments are nonrefundable. Specifically, the Term Sheet provides that "the $2 million paid on signing the Term Sheet, and any subsequent amounts that are paid, are non-refundable if [Home Easy] fails to make the full $3,600,000 License Commitment Fee and all Minimum

Annual Guarantee Royalties." (ECF 1, Ex. A, at 4-5). The Minimum Annual Guaranteed Royalties are "to be made for each year, regardless of actual sales or sales activity" and "The first three years of the license agreement are non-cancellable. (ECF 1. Ex A at 3). Home Easy arranged for payment of the License Commencement Fee and first Minimum Annual Guarantee Royalty by a third-party, Home Easy Industrial, (ECF 1. ¶¶ 18-19) but did not pay any subsequent Minimum Annual Guarantee Royalties due under the Term Sheet, (*Id.* ¶ 20). The Trustee, therefore, must concede that by failing to pay Minimum Annual Guarantee Royalties, Home Easy did not honor its own obligations under the Term Sheet – a necessary element of a breach of contract claim – and otherwise fails to allege a breach by Emerson – another element.

iv. Third, the Trustee alleges that "[t]o the extent [Emerson] contends that the $4.1 million it is holding can be used by it to offset the monies due to it under the judgment," Emerson has breached the Term Sheet. (*Id.* ¶ 38). This allegation is merely speculative and does not even assert that Emerson has offset monies. Emerson has not. To the contrary, Emerson's proof of claim filed in Home Easy's bankruptcy proceedings does not contain any offset of the judgment from the Delaware Action. *See* Claim No. 6. Any offset would actually benefit Home Easy by reducing the amount owed by Home Easy to Emerson. Any alleged offset cannot give rise to damages suffered by Home Easy. *Matthew v. Specializing Loan Servs. SLS*, No. CV 185727-ES-CLW, 2018 WL 6696776 (D.N.J. Dec.

20, 2018). Thus, any claim for an alleged breach pertaining to offsets of monies owed under the Judgment is legally insufficient and must be dismissed.

h. Count Three breach of the implied covenant of good faith and fair dealing is both insufficiently pleaded and merely duplicative of its breach of contract claim and must be dismissed.

i. A claim for breach of the implied covenant of good faith and fear dealing requires that the defendant acted in bad faith while engaging in conduct that denied the benefit of the bargain originally intended by the parties. *MZL Cap. Holdings*, 734 F. App'x at 105-06. A plaintiff, however, "may not sustain a separate cause of action for breach of the covenant of good faith and fair dealing based on the same conduct that has given rise to their breach of contract claims and where the terms of their contract are clear." *Hillsborough Rare Coins*, 2017 WL 1731695, at *8.

ii. Here, the Trustee, alleges no underlying facts to support this alleged bad faith and therefore fails to state a claim. The Trustee's claim is also barred as duplicative of its breach of contract claim. The Complaint alleges that Emerson's alleged bad faith conduct is "apart from its contractual obligations" but does not actually allege any facts beyond those asserted in its breach of contract claim. (ECF 1 ¶ 43). The conduct the Trustee refers to is identical to that contained in his breach of contract claim, so the claim for breach of implied covenant of good faith and fair dealing must be dismissed. *Id* at *8.

iii. Accordingly, Emerson urges that the Motion to Dismiss the Complaint with prejudice should be granted.

## B. SUMMARY OF TRUSTEE'S OPPOSITION TO EMERSON'S MOTION TO DISMISS [ECF 11]

The Trustee argues the following:

Despite Emerson's argument that the payment was made by a non-debtor and is not property of the estate, the Trustee argues that the $4.1 million was loaned to the Debtor by a third party and was wired directly to Emerson by the third party at the instruction of the Debtor for the purpose of fulfilling the Debtor's obligation under the Agreement. The Trustee argues that the Debtor controlled the $4.1 million, the Debtor designated to whom the money was paid, and thus, the Trustee, standing in the shoes of the Debtor, is entitled to its return.

### 1. Summary of Facts Asserted by Trustee

The Trustee asserts the following facts:

- On July 12, 2022, Emerson, the Debtor and Emerson Quiet Kool Co., Ltd. ("EQK") entered into the Term Sheet .
- The Term Sheet would (a) provide the Debtor with a license that would enable it to use the trademark EQK EMERSON QUIET KOOL and (b) terminate and settle the claims asserted by Emerson against the Debtor and EQK in a trademark infringement action pending in the United States District Court for the District of Delaware in the case entitled *Emerson Radio Corp. v. Emerson Quiet Kool Co., Ltd and Home Easy Ltd.*, Civil Action No. 20- 1652 (the "Delaware Action"). ( ECF 1, ¶ 11).
- In the Delaware Action, Emerson asserted the Debtor and EQK infringed on Emerson's rights through their use of the trademark EQK EMERSON QUIET KOOL, which Emerson argued was confusingly similar to its own trademark EMERSON.
- The Debtor and EQK answered Emerson's complaint and disputed Emerson's

claims. Although the Debtor and EQK raised defenses and the claims were litigated for more than four years, a default judgment was entered in the Delaware Action against the Debtor and EQK in the amount of $6.5 million (the "Judgment").

- The Debtor and EQK appealed the entry of the Judgment to the US Court of Appeals for the Third Circuit, which appeal was pending at the time the Agreement was executed. ( See ECF 1 ¶ 12). However, the Third Circuit ultimately affirmed the entry of the Judgment. According to the Trustee, the Third Circuit found that although EQK and Home Easy arguably had a meritorious defense, the District Court did not abuse its discretion in entering the default judgment. *Emerson Radio Corp. v. Emerson Quiet Kool Co.,* 2023 U.S. App. LEXIS 17434 (3d Cir. July 11, 2023).
- The Trustee states that the Third Circuit never addressed the merits of Emerson's infringement claims or the propriety of the breadth of the injunction issued by the District Court in its opinion.
- Pursuant to the Term Sheet, the parties were to enter into a license agreement, with Emerson licensing to the Debtor the right to use EQK EMERSON QUIET KOOL in connection with the sale of the Debtor's portable air conditioners, compact residential air conditioners (also referred to as wall room air conditioning units) and residential room dehumidifiers (the "Licensed Goods").
- The Agreement outlined the material terms of the license agreement, which the parties (with Emerson as "Licensor" and the Debtor as "Licensee") would memorialize in a formal license agreement following the execution of the Agreement.
- In accordance with the Term Sheet and the anticipated license agreement, Emerson's claims against the Debtor and EQK in the Delaware Action would be settled, and all money claims that Emerson had against the Debtor and EQK, including the Judgment, would be satisfied upon the Debtor's full and complete compliance with the Term Sheet and the license agreement. (ECF 1 ¶ 14).
- The Term Sheet provided that, as part of the future license agreement, the Debtor was to pay Emerson a royalty of 2% (two percent) of the net sales of the Licensed Goods sold and further provided that minimum guaranteed annual royalties in the

amount of $500,000 were due to Emerson each year of the term of the license agreement. ( ECF 1 ¶ 15).

- The Term Sheet also required the Debtor to pay to Emerson a "License Commencement Fee" of $3.6 million, which was separate from the payment of the royalties which would be payable upfront in two installments: $2.0 million upon the signing of the Term Sheet and $1.6 million, along with the first minimum guaranteed royalty payment of $500,000, within thirty (30) days thereafter. (ECF 1 ¶ 16).
- In its brief, Emerson contended that the $3.6 million License Commencement Fee was "meant to be the fee to incentivize Emerson to entertain a bargaining table" with Home Easy." (citing ECF 9, at 6.) However, the Trustee argues that there is no support in the record for this proposition. Instead, the Trustee argues that payment of the $3.6 million was an upfront fee paid by the Debtor in connection with the commencement of the license – and was part and parcel of the license and not a payment to bring Emerson to the bargaining table as Emerson argues.
- The Trustee further argues that Emerson has not attempted to classify as something else the additional $500,000 that was paid to it – which was a royalty payment that would have been due under the license agreement (if there were such an agreement).
- The Trustee states that in the Term Sheet, Emerson represented and promised the Debtor that it would enter into the license agreement based on the terms set forth in the Term Sheet and that any amounts paid to Emerson by the Debtor under the terms of the Term Sheet would not be used by Emerson as a set off against (a) the amounts due to it under the Judgment or (b) any future monies owed to Emerson resulting from the Delaware Action. ( ECF 1 ¶ 17).
- On July 13, 2022, in reliance on Emerson's representations and promises, and in anticipation of entering into the license agreement, the Trustee asserts that the Debtor arranged for the initial $2.0 million payment (constituting the first part of the License Commencement Fee) to be wired to Emerson, and such wire payment of $2 million was sent and accepted by Emerson. Emerson has acknowledged that the $2 million wire payment it received was made on behalf of the Debtor.

- On August 11, 2022, again in reliance on Emerson's representations and promises and in furtherance of the promised license agreement, the Debtor arranged for the second payment of $2.1 million (constituting the balance of the License Commencement Fee and the first minimum guaranteed license royalty payment of $500,000) to be wired to Emerson, and that $2.1 million was sent and accepted by Emerson. The Trustee asserts that Emerson has acknowledged this $2.1 million payment was made on behalf of the Debtor.
- According to the Trustee, Home Easy Industrial, loaned the Debtor $4.1 million and, pursuant to the loan agreement (the "Loan Agreement"), Home Easy Industrial made the two wire payments to Emerson totaling $4.1 million. The Debtor signed the Loan Agreement and agreed to repay the $4.1 million to Home Easy Industrial. ( ECF 1 ¶ 19).
- The Trustee states that the Loan Agreement expressly provides:

> Article 1 Party A [the Debtor] borrows US$4.1 million from Party B [HEI], with interest at an annualized rate of 6%, and the loan period is from July 1, 2022 to June 30, 2025. Party B shall pay the above amount to the account designated by Party A (Emerson Radio Operating) within 60 days after signing this agreement.

(emphasis added). (ECF 11, at 8) (Citing the Loan Agreement attached to Home Easy Industrial's Proof of Claim No. 5, filed with the Court on March 3, 2024).

- Irrespective of which entity actually wired the money to Emerson, the Trustee argues that the effect of the wire transfers to Emerson was that the Debtor performed under the terms of the Term Sheet and paid to Emerson both the $3.6 million License Commencement Fee and the first installment of the guaranteed minimum license royalty payment of $500,000, together totaling $4.1 million. (ECF 1 ¶ 19).
- The Trustee argues that the payments made to and received by Emerson totaling $4.1 million were made solely pursuant to the terms of the Term Sheet and in consideration of a license agreement that would be entered between the Debtor and Emerson, and were made in reliance on the representations and promises made by Emerson in the Term Sheet, including the representation and promise that Emerson would not use the money paid under the Term Sheet as an offset against the monies

due to it pursuant to the Judgment. However, according to the Trustee, no such license agreement was entered into between the Debtor and Emerson, and the Debtor was never given permission by Emerson, express or implied, to use the trademark EQK EMERSON QUIET KOOL. Although all the material terms of a license agreement were set forth in the Agreement, no formal license agreement was executed and no monies, royalties or guaranteed payments of any kind ever became due to Emerson. ( ECF 1 ¶ 20).

- The Trustee argues that it is immaterial for purposes of this proceeding and motion why no license agreement was entered by the parties. Rather, the Trustee asserts that what is material, is that there was no license and because there was no license, no royalty payments of any kind were due to Emerson. Emerson devotes huge sections of its brief contending that no license was entered and, accordingly, there was no settlement reached. The Trustee acknowledges and agrees that no license or settlement agreement was consummated, which is why the Trustee is seeking recovery of the $4.1 million.
- The Trustee asserts that Emerson did nothing that would entitle it to keep the $4.1 million, and there was no consideration or other benefit given to the Debtor by Emerson for the payment of the $4.1 million.
- The Trustee wholly disagrees with Emerson's assertion that the $4.1 million was nonrefundable and asserts that is a misreading of the Term Sheet.
- Instead, the Trustee asserts that pursuant to pages 4-5 of the Term Sheet, the $4.1 million would be nonrefundable only if the Debtor did not pay the License Commencement Fee (which it did) and if the Debtor failed to make the royalty payments that were due to Emerson under the license agreement. Since there was no license agreement, no monies, royalties or other payments were due to Emerson under the non-existent license agreement. Accordingly, the payment of the $4.1 million, consisting of the License Commencement Fee and the first installment of the guaranteed minimum license royalty payments, was refundable. (ECF 1 ¶ 22).
- The Trustee asserts that based on information provided to the Trustee by the Debtor, it was never the intention of the Debtor that Emerson would be entitled to keep the $4.1 million if no license agreement were executed, particularly because Emerson

agreed in the Term Sheet that the monies paid under the Term Sheet were not to be used as a setoff against any amounts due under the Judgment. (ECF 1 ¶ 22).

- The Trustee notes that Emerson expressly stated that it is not setting off the $4.1 million against other money due to Emerson from the Debtor. (citing ECF 11, at 33).
- The Trustee states that after his appointment, the Trustee, through counsel, wrote a letter to Emerson's counsel dated December 13, 2023 and demanded the return of the $4.1 million. But, despite the Trustee's demand, Emerson has not returned the $4.1 million and continues to retain the $4.1 million that is property of the Debtor's estate. ( ECF 1 ¶ 23).

**2. Summary of Trustee's Legal Argument in Opposition to the Motion to Dismiss the Complaint**

**Emerson's Motion to Dismiss Pursuant to Fed. R. Civ. P. 12(B)(1) Based On "Lack of Standing" Should Be Denied**

The Trustee opposes Defendant's argument that the Trustee lacks standing because the $4.1 million that had been loaned to the Debtor by Home Easy Industrial and used to pay Emerson did not hit the Debtor's bank account but was rather wired directly from the non-debtor Home Easy Industrial to Emerson. The Trustee asserts that the cases cited by the Defendant actually show that where a debtor controls and directs the pre-petition disbursement of funds by a third party on behalf of the debtor to another third party, those funds are assets of the debtor's estate and may be recovered by a trustee. (ECF 11, at 11) (citing ECF 9, at 12 and *Wagenknecht*, 971 F.3d at 1214; *Shubert v. Lucent Techs. Inc. (In re Winstar Communs., Inc.),* 554 F.3d 382, 401-02 (3d Cir. 2009)); *In re Smith*, 966 F.2d 1527, 1533 (7th Cir. 1992); *Baker & Schultz, Inc. v. Boyer*, 506 U.S. 1030 (1992); *Schick*, 234 B.R. at 346. (citing *Smyth v. Kaufman (In re J.B. Koplik & Co.),* 114 F.2d 40 (2d Cir. 1940)).

The Trustee asserts that the cases cited by Emerson indicate that when a third party makes a loan on behalf of the Debtor for a payment of pre-petition debt, but the Debtor, not the lender,

designates the creditor to be paid with the funds, the funds are property of the estate. The Trustee adds that such pre-petition transfers from a non-debtor to a prepetition creditor of the debtor can be recovered as preferences and what property is recoverable as a preference under 547(b) and what is estate property under Section 541(a)(1) and are analogous concepts. (ECF11, n. 5) (citing *Begier v. IRS*, 496 U.S. 53, 58-69 & n.3 (1990)).

The Trustee asserts that in *Schick,* the Court contrasted the situation where the debtor directs the third party as to whom and for what purpose the payment is to be made from a situation where the third party lends money to the debtor and the lender requires the proceeds of the loan to be made to a particular party finding that only in the latter situation are the funds deemed to be "earmarked," and not property of the debtor, and cannot be recovered by a trustee.

The Trustee argues that in this case, the facts are undisputed that the Debtor borrowed the $4.1 million from Home Easy Industrial and the Debtor directed to whom, and for what purpose, Home Easy Industrial, the lender, should pay the money. The Debtor designated the creditor to be paid (Emerson) and controlled the application of those funds. Specifically, the Trustee argues (as is also set forth in the ECF 1 ¶¶ 16, 18-19 and the Loan Agreement, attached as "Part 3"to Home Easy Industrial's Proof of Claim):

> (a) pursuant to the Agreement, the Debtor was required to pay Emerson $4.1 million in consideration of, and as part and parcel of, the anticipated license agreement,
>
> (b) the Debtor borrowed $4.1 million from Home Easy Industrial to enable the Debtor to carry out its obligations with respect to the Agreement and the anticipated license agreement,
>
> (c) as directed by the Debtor, Home Easy Industrial wired that same $4.1 million to Emerson, and the wiring instructions reflected that the money was paid as per the Agreement, and
>
> (d) Emerson accepted the $4.1 million and acknowledged that the money was paid on behalf of the Debtor pursuant to the terms of the Agreement.

The Trustee asserts that for purposes of the Motion and the determination of standing, the

Court is bound to accept those pleaded facts as true and is required to construe those facts in favor of the Trustee. (ECF 11, at 12)(citing *Storino v. Borough of Point Pleasant Beach*, 322 F.3d 293, 296 (3d Cir. 2003)(citing *Warth v. Seldin*, 422 U.S. 490, 501 (1975)).

The Trustee asserts that Emerson has not provided case law that supports its position that the money had to pass through the Debtor's bank account to constitute estate property. Rather, the Trustee argues that control includes not just the physical means of control but the legal authority to exert it. (ECF 11, at 13) (citing *FBI Wind Down Inc. Liquidating Trust v. All Am. Poly Corp. (In re FBI Wind Down, Inc*.), 581 B.R. 116, 131 (Bankr. D. Del. 2019). Thus, the Trustee argues here that the Debtor had control over the $4.1 million and designated to whom the money should be paid, and the money was, in fact, paid in accordance with the Debtor's instructions and was therefore estate property that can be recovered by the Trustee.

The Trustee asserts that the facts and result in *Schick*, 234 B.R. at 346, are instructive because despite the money not passing through the debtor's bank accounts, the money nevertheless was an asset of the estate that was recoverable by the trustee. The Trustee adds that in this case, nothing has been presented by the Defendant to show the loan was made based on Home Easy Industrial's requirement that the money be used to pay Emerson – that the money was earmarked by Home Easy Industrial. (ECF 11, at 14) (citing *Winstar*, 554 F.3d at 401-02).

The Trustee contrasted the *Winstar* case in which the lender did not require the Debtor to use the loaned money to pay the old creditor with *Wagenstrecht*, 971 F.3d at 1214 (ECF 9, at13-14), where the loan was made by the debtor's mother on the condition that the debtor use the money to pay the law firm, the debtor accepted that condition, and thus, the loan was not property of the estate. The Trustee emphasizes that here it was the Debtor who designated how the $4.1 million were to be used.

The Trustee further states that Emerson confirms this by referencing in the Motion Home Easy Industrial's Proof of Claim for repayment of the $4.1 million loan. (citing ECF 9, at 13.) The Loan Agreement, attached as "Part 3" to Home Easy Industrial's Proof of Claim, expressly provided that the loan was made to the Debtor and the Debtor designated where the proceeds were to go. Thus, the Trustee argues that the monies were not earmarked by Home Easy Industrial but were under the control of the Debtor and therefore the earmarking doctrine does not apply. (ECF 11, at 15) (citing *AmeriServe Food Distrib., Inc. v. Transmed Foods, Inc.* (*In re AmeriServe Food Distribution, Inc*.), 315 B.R. 24, 30 (Bankr. D. Del. 2004)(quoting *Adams v. Anderson* (*In re Superior Stamp and Coin Co., Inc.*), 223 F.3d 1004, 1009 (9th Cir. 2000)).

Thus, the Trustee argues, he has standing to pursue this action, and the Court therefore has subject matter jurisdiction and Emerson's motion to dismiss under Rule 12(b)(1) should be denied.

**Emerson's Motion to Dismiss Pursuant to Fed. R. Civ. P. 12(B)(7) for an Asserted "Failure to Name an Indispensable Party" Should Be Denied**

The Trustee rejects Emerson's argument that the individual Guarantor is an indispensable party, as defined in Fed. R. Civ. P. 19, and that the Complaint cannot proceed without the Guarantor, and should therefore be dismissed pursuant to Rule 12(b)(7).

The Trustee argues that here the Guarantor does not fall under either subsection (A) or subsection (B) of section (1), as he asserts that complete relief can be accorded in the Guarantor's absence, and the Guarantor has not claimed an interest in the subject matter of the action and does not have one. The Trustee submits Emerson has no evidence to the contrary.

The Trustee asserts that the absence of the Guarantor in the action is immaterial to the question of the relief as between the existing parties -- whether the Debtor or Emerson is entitled to have the $4.1 million. See Fed. R. Civ. P. 19(a)(1)(A). In addition, the Trustee argues that the Guarantor has no interest "relating to the subject of the action" or the relief being sought, the return

of the $4.1 million, since the Guarantor paid none of those funds to Emerson and Emerson has, and would have, no obligation to pay the Guarantor anything. See Fed. R. Civ. P. 19(a)(1)(B).

Further, the Trustee argues that the Guarantor has not claimed any interest and is thus not a required party under the Rule. (ECF 11, at 16) (citing *US Tech Sols., Inc. v. eTeam, Inc*., 2017 U.S. Dist. LEXIS 131469 *8-9 (D.N.J. Aug. 16, 2017)).

The Trustee argues that the sole case cited by Emerson in support of its indispensable party argument, *Dickson*, 202 Fed. App'x at 580-81. supports the Trustee's position because in that case the Third Circuit found that non-joined co-obligees named in the contract at issue are generally indispensable parties and that non-joined co-obligors are not.

The Trustee argues that in this case there can be no doubt that the Guarantor is an obligor under the Agreement, not an obligee. ( ECF 1, Ex. A, at 5.) In support of this, the Trustee states that no performance is due to the Guarantor under the Agreement and Emerson has provided no factual support and cannot turn the Guarantor into an obligee by simply stating so. The Trustee asserts the Guarantor has no basis to seek the return of any or all the $4.1 million because it is undisputed from the face of the Complaint that the Guarantor advanced none of these funds, and the Guarantor has not sought such funds. Thus, the Guarantor is not a required party under Fed. R. Civ. P. 19(a)(1).

In addition, the Trustee asserts that even if the Guarantor were a required party, Emerson's argument that it would not be feasible to join him is based solely on unsupported statements that Emerson made "on information and belief" – that the Guarantor is an individual residing in China with no demonstrable affiliations with or activities in New Jersey to enable the Court to exercise personal jurisdiction over him. (citing ECF 9, at 16). The Trustee argues there is nothing in the record to substantiate the position that this Court cannot exercise personal jurisdiction over the

Guarantor and the movant bears the burden of proof. (ECF 11, at 18) (citing *CRST Expedited, Inc. v. Swift Transp. Co.*, 2018 U.S. Dist. LEXIS 81755 * 7-8 (N.D. Iowa Apr. 30, 2018); *Indian Harbor Ins. Co. v. KB Lone Star, Inc.*, 2012 U.S. Dist. LEXIS 41706 (S.D. Tex. Mar. 27, 2012)).

Thus, the Trustee argues there is no evidence on this record that the Guarantor cannot be joined, and, in the context of this motion, Emerson's argument should carry no weight.

In addition, the Trustee states that even if the Guarantor were a required party under Fed. R. Civ. P. 19(a)(1) and his joinder were not feasible, as Emerson argues, the Guarantor is still not a party without whose presence the action must be dismissed under Fed. R. Civ. P. 19(b).

Here, the Trustee states that it is a fiction that the Guarantor might have a claim against Emerson and since the Guarantor was purely an obligor under the Agreement, not an obligee, and paid no money to Emerson, it has no claim against Emerson or right to recover the $4.1 million. Therefore, the Trustee asserts no one is or would be prejudiced by the Court rendering a judgment in the Guarantor's absence and such judgment would determine solely the rights of the parties with respect to the $4.1 million, with which the Guarantor has no connection.

The Trustee states that if the Complaint were dismissed under 12(b)(7) the Trustee and the Debtor's estate would be prejudiced because the Trustee otherwise lacks a remedy to recover the $4.1 million that Emerson wrongfully has retained. Thus, based on the equities, the Trustee argues that even if the Guarantor were deemed to be a required party under Fed. R. Civ. P 19(a)(1), the motion to dismiss should still be denied so that the Trustee can pursue from Emerson the money that belongs to the Debtor's estate.

**Emerson's Motion to Dismiss Pursuant to Fed. R. Civ. P. 12(B)(6) Should Be Denied**

The Trustee urges that when evaluating a motion to dismiss under R. 12(b)(6), the court must accept all factual allegations as true, construe the complaint in the light most favorable to the

plaintiff, and then determine whether, under any reasonable reading of the complaint, the plaintiff may be entitled to relief. (ECF 11, at 20) (citing *Fowler v. UPMC Shadyside*, 578 F.3d 203, 210 (3d Cir. 2009). A complaint survives if it contains sufficient factual matter, to "state a claim to relief that is plausible on its face." (ECF 11, at 20) (citing *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009); *Levy Grp., Inc. v. Land, Sea & Rail Logistics, LLC*, 2022 U.S. App. LEXIS 9919 (3d Cir. Apr. 13, 2022); *Wanland & Assocs. v. Nortel Networks Ltd. (In re NorVergence, Inc.*), 384 B.R. 315 (Bankr. D.N.J. 2008).

There is No Basis to Dismiss the Trustee's Complaint Under the *In Pari Delicto* Defense

The Trustee rejects Emerson's argument that the *in pari delicto* defense precludes the Trustee from recovering on any of his causes of action to obtain the $4.1 million.

The Trustee argues Emerson improperly expands the scope of the *in pari delicto* defense which is inapplicable under these circumstances because Debtor's alleged prior bad acts, *i.e.*, the Debtor's infringement of Emerson's trademark rights, are separate and apart from the Term Sheet and the $4.1 million payment, and the Debtor did not commit any wrongdoing with respect to the Term Sheet or the payment to Emerson of the $4.1 million.

The Trustee asserts Emerson has conflated the doctrines of *in pari delicto* and unclean hands. While denominating its defense as one arising under the *in pari delicto* doctrine, Emerson also refers to the fact that the Debtor has unclean hands and, as a result, the Trustee, stepping into the Debtor's shoes, cannot recover on his claim. (ECF 11, p.21). But the Trustee argues the unclean hands doctrine is inapplicable because it is an equitable defense to a claim in equity. (ECF 11, at 21) (citing *Inter Med. Supplies Ltd v. EBI Med. Sys. Inc.*, 975 F. Supp. 681, 687 (D.N.J. 1997), *aff'd and remanded*, 181 F.3d 446 (3d Cir. 1999) (quoting *Pellitteri v. Pellitteri*, 266 N.J. Super. 56, 65 (App. Div. 1993)). Since the Trustee is seeking damages and not equitable relief, he argues

the unclean hands doctrine is inapplicable. (ECF 11, at 21)(citing *Tarasi v. Pittsburgh Nat'l Bank*, 555 F.2d 1152, 1156 n.9 (3d Cir.), *cert. denied*, 434 U.S. 965 (1977)).

As for *in pari delicto,* the Trustee also argues it is inapplicable because, as an initial matter, it is an affirmative defense and though not generally considered in a motion to dismiss, may be entertained if set forth on the face of the complaint. (ECF 11, at 22) (citing *Forman v. Salzano (In re Norvergence, Inc.),* 405 B.R. 709, 749 (Bankr. D.N.J. 2009) (quoting *Official Comm. of Unsecured Creditors v. R.F. Lafferty & Co.,* 267 F.3d 340, 354 (3d Cir. 2001)). Here, the Trustee states there is nothing in the Complaint that refers to or reflects any wrongdoing on the part of the Debtor in connection with that Agreement or the $4.1 million payment.

However, the Trustee states that even if the *in pari delicto* defense was ripe for decision on this motion, the defense still does not apply because it relates to Debtor's activities (*i.e.*, the Debtor's infringement of Emerson's trademark rights) before the parties entered into the Agreement and the $4.1 million was paid and to include such activities would grossly expand the *in pari delicto* doctrine.

The Trustee asserts that under New Jersey law, the doctrine of *in pari delicto* refers to the principle that a court will not enforce an illegal contract against one of the parties to that contract and where the plaintiff knowingly conspires with the defendant to undertake a wrongful action with respect to the matter at issue in the case. (ECF 11, at 22-23)(citing *Johnson v. McClellan*, 468 N.J. Super. 562, 578-579 (App. Div.), *certif. denied*, 249 N.J. 76 (2021); *R.C. Search Co. v. Torre*, 2009 N.J. Super. Unpub. LEXIS 305, *20 (App. Div. Jan. 15, 2009); *City of Cape May v. Dash*, 2008 N.J. Super. Unpub. LEXIS 1624, *36-37 (App. Div. Feb. 29, 2008)(quoting *Cameron v. Int'l Alliance of Theatrical Stage Employees*, 118 N.J. Eq. 11, 20, 176 A. 692 (E. & A. 1935)).

The Trustee argues that here, there is nothing illegal about the Term Sheet, and the alleged

wrongful conduct by the Debtor was not with respect to the matter at issue in this case. (ECF 11, at 23)(citing *Tarasi*, 555 F.2d at 1157). The Trustee asserts that Emerson has not identified, and cannot identify, any wrongdoing committed by the Debtor in connection with the transaction in question but rather points to the Debtor's actions that took place in a different setting, before the Term Sheet was negotiated and entered, and before the $4.1 million was paid which cannot be attributed to the Trustee who is seeking to recover money paid in a separate transaction from the Debtor's infringing activities.

The Trustee states Emerson's reliance on *10 Minute Fitness Inc.*, 679 F. Supp.3d at 1374 and *Code v. Adidas Am., Inc*., No. CV 6:23-4997, 2024 WL 637356 (D.S.C. Jan. 11, 2024), *dismissed*, No. 24-1143, 2024 WL 3770309 (4th Cir. Apr. 30 2024) (ECF 9, at 21) is misplaced.

In *10 Minute Fitness*, the Trustee states, *inter alia*, the court noted, based on the *in pari delicto* doctrine, that because the plaintiff's actions of importing counterfeit machines was wrongful, the plaintiff could not recover damages based on the sale of those very machines and the plaintiff's negligence claim subject to dismissal concerned the same property and the same transaction as the wrongdoing committed by the plaintiff. Thus, *in pari delicto* doctrine barred the plaintiff's claim. The Trustee stated that similarly, in the *Code* case, the plaintiff sought relief for the damages he incurred as a result of the very illegal conduct he participated in and since it was part of the same transaction for which the plaintiff sought damages, the court dismissed the claim based on the *in pari delicto* doctrine.

The Trustee contrasts the instant situation in which the bad acts listed by Emerson do not concern the transaction that is the subject of the Complaint and therefore the *in pari delicto* doctrine does not provide a viable defense or a basis for dismissal of this action at the pleading stage. The Trustee submits that based on Emerson's reasoning, the Agreement never could have been

enforced by the Debtor (or the Trustee) because of the Debtor's past misconduct which would lead to an inequitable outcome.

The Trustee's Turnover Action Should Not Be Dismissed

As per the Trustee, Emerson asserts two purported bases for the dismissal of this claim: (1) that the $4.1 million is not estate property, (ECF 9, at 24); and (2) that the estate's claim to the property is in dispute. (ECF 9, at 25). The first argument was addressed in the Trustee's response to Emerson's claim that the Trustee lacks standing. The Trustee has opposed Emerson's standing argument by contending that the Debtor had control of the funds and directed how they were to be used, and the funds were not earmarked; thus, the funds were estate property even though they did not pass through the Debtor's bank account.

As to Emerson's argument that the estate's claim is in dispute, the Trustee argues that an objective basis must exist for the dispute. (ECF 11, at 26) (citing *LaMonica v. CEVA Grp. PLC (In re CIL Ltd.)*, 2024 Bankr. LEXIS 926, *121-122 (Bankr. S.D.N.Y. Apr. 18, 2024) (quoting *In re Lexington Healthcare Grp., Inc.*, 363 B.R. at 716); *WeldedConstr., L.P. v. The Williams Cos. (In re Welded Constr., L.P.)*, 609 B.R. 101, 126 (Bankr. D. Del. 2019); *Newman v. Tyberg (In re Steel Wheels Transp., LLC)*, 2011 Bankr. LEXIS 4582 (Bankr. D.N.J. Oct. 28, 2011)).

The Trustee asserts that Emerson has not provided the Court with any legitimate or objective basis on which the Court can conclude there is a bona fide dispute as to whether Emerson must return the money. Merely stating that there is a dispute is not enough. Otherwise, every party subject to a turnover action would be able to defeat that action simply by claiming there is a dispute. The Trustee argues there is no legitimate or bona fide dispute, and that Emerson has the $4.1 million and has no justifiable or legal basis to retain it. The Trustee asserts that as Emerson cannot identify any objectively reasonable basis to dispute that the $4.1 million is property of the bankruptcy estate, Emerson's motion to dismiss the turnover count should be denied.

The Trustee's Pleading of a Breach of Contract Claim Does Not Preclude His Pleading in the Alternative Claims of Promissory Estoppel, Unjust Enrichment or Breach of the Covenant of Good Faith and Fair Dealing

The Trustee argues that his assertion of a cause of action for breach of contract does not preclude him from pleading alternative quasi-contract causes of action for unjust enrichment and promissory estoppel, or even a cause of action for breach of the covenant of good faith and fair dealing and Fed. R. Civ. P. 8(d) specifically provides for such alternative pleading.

The Trustee states that if the Court determines Emerson was not contractually required to return the money, the Trustee has the right, particularly at the pleading stage of this action, to "back stop" that contract claim with claims sounding in quasi-contract (promissory estoppel and unjust enrichment) and a claim for breach of the covenant of good faith and fair dealing (which the Trustee specifically labeled as alternative. (ECF 11, at 29, n. 6). The Trustee cites the following cases in support of his ability to plead in the alternative: *Gap Props., LLC v. Cairo*, 2020 U.S. Dist. LEXIS 174770, *9-10 (D.N.J. Sept. 17, 2020), *Williams v. Samsung Elecs. Am., Inc.,* 2024 U.S. Dist. LEXIS 56849, *25-27 (D.N.J. Mar. 28, 2024); *Innovative Sols. & Tech., LLC v. Pro Spot Int'l, Inc.,* 2023 U.S. Dist. LEXIS 77872, *5-6 (D.N.J. May 4, 2023); *Dougherty v. Drew Univ.*, 534 F. Supp. 3d 363, 384 (D.N.J .2021); *Ass'n of N.J. Chiropractors v. Aetna, Inc.,* 2012 U.S. Dist. LEXIS 64413, *33-35 (D.N.J. May 8, 2012).

The Trustee argues that although Emerson cites *Hillsborough Rare Coins, LLC*, 2017 WL 1731695, and *Freightmaster USA, LLC* v. FedEx, Inc., No. CIV. 14-3229-KSH-CLW, 2015 WL 1472665 (D.N.J Mar. 31, 2015), to argue the Trustee cannot plead the quasi-contract claims, even in the alternative, when he has asserted that there was a breach of contract, those cases actually support the Trustee's position. Specifically, the Trustee states each case has held that, absent a claim that the contract was invalid, a party cannot plead the quasi-contract claims in the alternative

and here, Emerson has contended that there is no valid contract provision requiring it to return the $4.1 million.

Thus, the Trustee asserts that given Emerson's position that there is no contractual right that governs the parties' dispute over the money, the Trustee is permitted to plead the quasi-contractual claims in the alternative. The Trustee argues this analysis also applies to the Trustee's claim for breach of the implied covenant of good faith and fair dealing since Emerson has argued that even though the parties never entered into a license agreement, and the Debtor was never licensed the use of the Trademark, "there is no contractual obligation for Emerson to refund" the $4.1 million. (ECF 11, at 31).

The Trustee also urges that Emerson's reliance on *Hillsborough Rare Coins,* does not support Emerson's allegation that the Trustee's breach of the covenant of good faith and fair dealing should be dismissed as duplicative of the breach of contract claim, as *Hillsborough,* 2017 U.S. Dist. LEXIS 67113, *18, acknowledged a viable breach of the covenant of good faith and fair dealing claim exists when necessary to "fill in the gaps to give efficacy to a contract as written when some terms of the contract are not specific." Therefore, the Trustee states that if the Court agrees with Emerson that the explicit terms of the Agreement do not require the re-payment to the Trustee of the $4.1 million, then there is a gap in the contract's language that needs to be "filled in" so that the Debtor's reasonable expectations would be fulfilled.

In addition, the Trustee argues that the allegations in the Complaint --that the Debtor paid the $4.1 million with the expectation that Emerson would enter into a license agreement which would provide the Debtor the right to use the Trademark and if no license agreement were entered, the $4.1 million would be returned --must be taken as true. Thus, the Trustee argues Emerson, acted in bad faith and thereby violated the covenant of good faith and fair dealing, notwithstanding the

Trustee's separate claim for breach of contract. (ECF 11, at 31-32) (citing *Atl. City Racing Ass'n. v. Sonic Fin. Corp.*, 90 F. Supp. 2d 497, 510 (D.N.J. 2000)) (citing *Sons of Thunder v. Borden, Inc.*, 148 N.J. 396 (1997)).

The Trustee argues that even if the Agreement is silent on what would happen to the $4.1 million if no license agreement were entered( *i.e.* Emerson did not violate the express language of the Term Sheet), Emerson nevertheless had the obligation, pursuant to the covenant of good faith and fair dealing, to return the money if no license were consummated. Thus, the Trustee is entitled to proceed alternatively on a theory of the breach of the covenant of good faith and fair dealing with respect to the failure to refund the money. (ECF 11, at 32) (citing *Seidenberg v. Summit Bank*, 348 N.J. Super. 243, 257 (App. Div. 2002)); *Spellman v. Express Dynamics, LLC*, 150 F. Supp.3d 378, 389-90 (D.N.J. 2015)).

The Economic Loss Doctrine Does Not Preclude the Trustee's Claim for Fraud in the Inducement or Conversion

The Trustee argues that Emerson misstates the law when it asserts that because of the Trustee's breach of contract claim, and that a contract exists that covers the subject of the Trustee's fraud and conversion claims, then those claims are barred by the economic loss doctrine. (ECF 11, at 34). The Trustee asserts that even if the Court finds a valid contract between the Debtor and Emerson, the Trustee may maintain an independent cause of action against Emerson for (1) fraud, because the Trustee alleges a claim for fraud in the inducement of the contract with respect to the $4.1 million, and (2) conversion, because, as with the Trustee's other claims, a conversion claim can co-exist with a breach of contract claim if there is a dispute as to the terms of the contract or if the relief sought is outside the scope of the contract.

The Trustee alleges the Debtor was induced to enter into the Term Sheet by Emerson's leading the Debtor to believe that if no license agreement occurred then the $4.1 million would be

returned. The Trustee argues that a claim for "fraud in the inducement" gives rise to an independent cause of action for fraud regardless of the existence of a valid contract, and the economic loss doctrine does not preclude that claim. (ECF 11, at 34-35) (citing *See G&F Graphic Servs. v. Graphic Innovators, Inc.*, 18 F. Supp. 3d 583, 593 (D.N.J. 2014); *Bracco Diagnostics, Inc. v. Bergen Brunswig Drug Co.*, 226 F. Supp.2d 557, 563-564 (D.N.J. 2002); *Wilhelm Reuss GmbH & Co. KG, Lebensmittelwerk v. East Coast Warehouse & Distrib. Corp.*, 2018 U.S. Dist. LEXIS 106442 (D.N.J. June 26, 2018); *Bell Container Corp. v. Palagonia Bakery Co.*, 2019 U.S. Dist. LEXIS 223613 (D.N.J. December 26, 2019)).

The Trustee also asserts the economic loss doctrine is inapplicable to his conversion claim because if the Court were to accept Emerson's argument (that the Term Sheet does not provide for the return of the $4.1 million to the Debtor, even if no license agreement were consummated), then the Term Sheet does not provide the Trustee with any contractual remedy. The Trustee argues again that he is permitted under the Federal Rules to plead in the alternative and that is what he has done here.

The Trustee states that because, Emerson argues that there is no contractual remedy, the economic loss doctrine does not preclude the Trustee's claim, which seeks relief outside the scope of the contract. (ECF 11, at 35) ( citing *Kam Int'l v. Franco Mfg. Co.,* 2010 U.S. Dist. LEXIS 135455 (D.N.J. December 22, 2010); *Bracco*, 226 F. Supp.2d 557, 564; *Hughes v. TD Bank, N.A.*, 856 F. Supp. 2d 673, 682 (D.N.J. 2012)).

The Trustee Has Pled a Valid Claim for Fraud and Conversion

The Trustee argues that the claims for fraud and conversion should not be dismissed because, contrary to Emerson's claim, they were sufficiently pled with requisite particularity under Fed. R. Civ. P. 9(b) even though many of the allegations in the Complaint are pled on "information

and belief." The Trustee asserts that Emerson fails to account for the liberality of review accorded to a trustee's pleading of fraud in a bankruptcy matter. (ECF 11, at 36-37) (citing *Forman v. Cornerstone Realty Agency, LLC*, 2006 Bankr. LEXIS 2881*3-6 (Bankr. D.N.J. Oct. 19, 2006); *Est. of BG Petro., LLC v. Dever (In re BG Petro., LLC)*, 2024 U.S. App. LEXIS 11643, *5-6 (3d Cir. May 14, 2024); *AIRN Liquidation Trust v. S3 RE Bergenline Funding LLC (In re Nat'l Reality Inv. Advisors, LLC)*, 2024 Bankr. LEXIS 34, *7 (Bankr. D.N.J. Jan. 5, 2024); *Ehrenberg v. Sage Grp. Consulting, Inc. (In re Orion HealthCorp, Inc.)*, 2024 Bankr. LEXIS 1131, *21 (Bankr. S.D.N.Y. May 13, 2024) (quoting *Enron Corp v. Credit Suisse First Boston Int'l (In re Enron Corp.)*, 328 B.R. 58, 73 (Bankr. S.D.N.Y. 2005)).

The Trustee submits that the fact that the Trustee pled fraud on "information and belief" is not a basis for dismissal of the claim and further, the Trustee sufficiently pled all of the elements of a fraud claim. The Trustee states Emerson is wrong to argue that the Trustee failed to plead a misrepresentation of a presently existing or past fact and that the Trustee's claim is based on a future event and the Trustee urges that such argument is a misreading of the law by Emerson and the Trustee's allegations because a fraud claim in New Jersey may be based on a knowingly false representation as to future events. (ECF 11, at 38) (citing *Stochastic Decisions, Inc. v. DiDomenico*, 236 N.J. Super. 388, 395-396 (App. Div. 1989), *certif. denied*, 121 N.J. 607 (1990)) *Dover Shopping Center, Inc. v. Cushman's Sons, Inc.*, 63 N.J. Super. 384, 390 (App. Div. 1960); *Alexander v. CIGNA Corp.*, 991 F. Supp. 427, 435 (D.N.J. 1997), *aff'd*, 172 F3d 859 (1998) (quoting *Notch View Assoc., A.D.S. v. Smith*, 260 N.J. Super. 190, 202-03 (Super. Ct. Law Div. 1992)).

The Trustee asserts that his claim, pled in the alternative, is that Emerson's promise to repay the money if no license was granted, as communicated to the Debtor (ECF 1 ¶¶ 22, 48), was

false and was made by Emerson knowing that, if there were no license, it would still keep the money. Thus, the Trustee argues he has pled an actionable fraudulent misrepresentation, and the other elements of fraud are subsumed in paragraphs 46-50 of the Complaint. The Trustee states he also pled that the Debtor relied on Emerson's representations (ECF 1 ¶ 48) and that the Debtor was damaged thereby (ECF1 ¶ 50). Thus, the Trustee argues for the purposes of this Motion to Dismiss the Complaint, based on the allegations of the Complaint, the Trustee has pled a plausible claim for fraud.

The Trustee asserts (ECF 11, at 39, n 7) that there is nothing in the record or in the Complaint to support Emerson's argument that the provision in the Term Sheet that provides that Emerson would not offset any of the monies due under the Term Sheet against the Judgment actually was included to benefit Emerson, and not the Debtor, and therefore the Debtor could not have reasonably relied on it. (ECF 11, at 39, n. 7). The Trustee notes that under Emerson's argument, the Debtor would be conceding to Emerson the right to $4.1 million at the very time that the Debtor's appeal of the Judgment was pending. The Trustee disputes the Emerson's repeated argument that the Debtor did not suffer any damages because the money was not an asset of the estate.

Regarding the conversion claim, the Trustee argues that he has sufficiently pled a claim for conversion despite Emerson's argument the claim is deficient because (i) the $4.1 million never belonged to the Debtor so it could not have been converted and (ii) the $4.1 million claim is merely a claim based on a contract and a conversion claim requires more than a contractual obligation to repay the money.

Instead, the Trustee argues again that the $4.1 million was money over which the Debtor had control, and therefore it owned the money, irrespective of the fact that it never passed through

the Debtor's bank account. Next the Trustee argues again that he pled the conversion claim in the alternative to the claim for breach of contract and if, as Emerson contends, there were no contractual obligation to return the money, then the breach of contract claim is not a roadblock to the conversion claim. (ECF 11, at 40) (citing *Dougherty*, 534 F. Supp. 3d at 379 (quoting *Meisels v. Fox Rothschild LLP*, 240 N.J. 286, 222 A.3d 649, 661 (2020)). *Imps. Serv. Corp. v. Aliotta*, 2024 U.S. Dist. LEXIS 96286, *33-24 (D.N.J. May 30, 2024); *Dante v. Schwartz*, 2022 U.S. Dist. LEXIS 68242 * 36-37 (D.N.J. Apr. 13, 2002); *First Am. Title Insurance Co. v. Sadek*, 2017 U.S. Dist. LEXIS 213345 (D.N.J. Dec. 29, 2017)). The Trustee urges that "conversion is the intentional exercise of dominion and control over chattel that seriously interferes with the right of another to control that chattel." *Dougherty*, 534 F.Supp. 3d at 379.

The Trustee distinguishes the case cited by Emerson (ECF 9, at 31, *Gordon v. Nice Sys., Inc.*, 2020 U.S. Dist. LEXIS 81927(D.N.J. May 11, 2020)) because unlike the facts in Gordon, here the $4.1 million is readily identifiable, and the Trustee has alleged, in the alternative, that the money has been wrongfully diverted by Emerson to the detriment of the Debtor's estate and is not due to the estate based on a debt that Emerson owes to it, thus the Trustee alleges he has sufficiently and plausibly pled a claim for conversion.

The Trustee Has Properly Pled a Cause of Action Under New Jersey Law for Breach of Contract

The Trustee rejects Emerson's argument that the Trustee did not plead a viable cause of action because the Trustee did not identify the breach of the Agreement upon which the Trustee relies. In particular, the Trustee rejects Emerson's contention that the Trustee alleged the following three different theories for his breach of contract claim none of which were sufficiently pled: (1) Emerson contractually was required to grant a license to the Debtor; (2) Emerson

breached the Agreement by not refunding the $4.1 million when no license was granted; and (3) Emerson breached the Agreement by claiming the $4.1 million as a setoff. (ECF 11, at 41-42 (citing ECF 9, at 32.))

Instead, the Trustee asserts he has sufficiently pled a claim for breach of contract, and the allegations in the Complaint must be taken as true for the purposes of this Motion to Dismiss the Complaint. The Trustee notes that he is not contending that, pursuant to the Term Sheet, Emerson was required to grant the Debtor the right to use the Trademark. Rather, the Trustee has alleged that if Emerson elected to keep the $4.1 million, then it must enter into the license, and its refusal to do so is a breach. The Trustee argues in the alternative, as the basis for the breach of contract claim - that if Emerson elected not to license the Debtor, then it was obligated to return the $4.1 million, as that money was the consideration paid to it by the Debtor in connection with the nonexistent license agreement. The Trustee submits Emerson cannot have it both ways by keeping the money and refusing to license the Debtor to use the Trademark.

The Trustee disputes Emerson's argument that it had no contractual obligation to grant the license citing the decision in the Delaware District Court case. (ECF 11, at 42). The Trustee asserts Emerson's interpretation is in error and the Delaware District Court simply held that no license was entered into, and no settlement was reached, because the Term Sheet itself did not constitute a license agreement. The Trustee states he acknowledges that the Term Sheet did not constitute a license, although it contained all of the material terms thereof.

The Trustee argues that the Delaware District Court did not preclude the Trustee's claim that the Term Sheet was breached by Emerson when it refused to grant the license while keeping the $4.1 million and that, the Delaware District Court never addressed this issue or the propriety of Emerson retaining the $4.1 million.

The Trustee argues that while the Term Sheet did not expressly state that, if the consideration were not provided, the $4.1 million would be returned, this was clearly an implied term of the Term Sheet, especially since the Term Sheet also said that the $4.1 million would not be used by Emerson as a setoff against other amounts that were due or may be due from the Debtor to Emerson – under these circumstances, the Trustee argues there would be no reason for Emerson to keep the money.

The Trustee urges that terms of a contract may be implied in fact and enforceable by interpretation of " a promisor's word and conduct in light of the surrounding circumstances." (ECF 11, at 43)(citing *Heyman v. Citimortgage, Inc.,* 2019 U.S. Dist. LEXIS 128238, *56-57 (D.N.J. June 27, 2019) (quoting *Zelnick v. Morristown-Beard Sch.,* 445 N.J. Super. 250, 260 (Law Div. 2015)). See also *Melone v. Cryoport Inc.,* 2024 U.S. Dist. LEXIS 73519 (D.N.J. April 23, 2024)).

The Trustee argues that the surrounding circumstances here show Emerson was obligated to return the $4.1 million, and the failure to do so is a breach of contract. The Trustee further states the Court must accept the allegations in the Complaint and reject Emerson's premise that the money was nonrefundable because the Debtor failed to pay royalties for a license the Debtor was never granted.

The Trustee also highlighted his allegation in the Complaint that, if Emerson were to assert that it could keep the $4.1 million as a setoff against other money due from the Debtor to Emerson, that would constitute a separate breach of the Agreement. (ECF 11, at 45) (citing ECF 1, ¶¶ 17, 38.) The Trustee asserts Emerson has assured the Court it has not set off the $4.1 million, as evidenced by its filed Proof of Claim. But, if Emerson wants the Court to rely on the position that it is not seeking to set off the $4.1 million against other amounts claimed due, then Emerson should be bound by that in the future. However, the Trustee alleges Emerson has not stated affirmatively

that it will not, in the future, assert the right to keep the $4.1 million as a setoff. The Trustee argues that any such set off would benefit one creditor, Emerson, at the expense of all creditors, who should share in any recovery in this adversary proceeding.

## C. SUMMARY OF EMERSON REPLY [ECF 14]

### The Trustee Lacks Standing to Prosecute the Complaint or Undo the Non-Debtor Payments

Emerson in its Reply repeats its argument that the Trustee's Complaint should be dismissed for lack of standing pursuant to Rule 12(b)(1) because the non-Debtor payments were made by non-debtor Home Easy Industrial directly to Emerson, and Emerson asserts Home Easy lacked dominion or control over the funds. Emerson argues that as an initial matter, the Trustee does not address Emerson's argument that under Rule 12(b)(1), that the Trustee bears the burden of demonstrating that the Court has subject matter jurisdiction over this matter, and that Emerson's "factual attack" on the Complaint obligates the Trustee to come forward with evidence – and not mere reliance on allegations in the Complaint – to establish subject matter jurisdiction. (ECF 14, at 3) (citing *In re Citadel Watford City Disposal Partners, L.P.*, 603 B.R. 897, 902 (Bankr. D. Del. 2019).

Emerson argues that the Trustee has failed to meet his burden of proof by not submitting any evidence in support of subject matter jurisdiction beyond the bare allegations in the Complaint and the Complaint does not overcome the undisputed documentary evidence, including the Loan Agreement and proof of claim submitted by Home Easy Industrial. (ECF 14, at 3 (comparing *Wark v. Delaware River & Bay Auth.*, No. CIV. 05-982-RBK, 2005 WL 2086146, at *1 (D.N.J. Aug. 26, 2005)). Emerson notes that even if the Court applies a Rule 12(b)(6) standard to Emerson's subject matter jurisdiction arguments, the Trustee's claims still fail given

the unambiguous language of the Loan Agreement and Home Easy Industrial's proof of claim – both of which can be considered by this Court under Rule 12(b)(6). (ECF 14, at 3, n. 2) (citing *Mayer v. Belichick*, 605 F.3d 223, 230 (3d Cir. 2010); *U.S. Bank N.A. v. DHL Global Forwarding* (*In re Evergreen Solar, Inc.)*, No. 11-12590-MFW, Adv. No. 13-50486-MFW, 2014 WL 300965, at *1 (Bankr. D. Del. Jan. 28, 2014)).

Emerson asserts the payments were made directly by a non-debtor utilizing loan proceeds that the Debtor never exercised any control over and further, the Complaint does not and cannot plausibly allege that the Debtor exercised any direct control over the Non-Debtor Payments. (ECF 14, at 4) (citing ECF 1 ¶ 19).

Emerson , as set forth in the Motion, states that the purported Loan Agreement did not grant Home Easy any control over the loan proceeds as would be required to make them property of the estate but instead, the Loan Agreement expressly limits the use of the loan to paying Emerson by obligating Home Easy Industrial, within 60 days after signing the Loan Agreement, to "pay the above amount [$4.1 million] to the account designated by Party A (Emerson Radio Operating)." ( See Proof of Claim No. 5-1, Part 3). Emerson contends that Home Easy Industrial itself confirmed this "incontestable fact" by filing a proof of claim here for what it describes as a "Loan for payment of Prepaid License Commencement Fee [i.e., the Non-Debtor Payments]." ( ECF 14, at 4) (citing Proof of Claim No. 5-1, Part 2, Item 8). Emerson asserts that as a result, the funds were "earmarked" to Emerson and unavailable to pay other creditors of Home Easy.

Emerson argues that earmarked funds are not estate property where there is "an agreement between the new lender and the debtor that the new funds will be used to pay a specified antecedent debt." (ECF 14, at 5) (citing *Schubert v. Lucent Techs., Inc.* (*In re Winstar*

*Commc'ns, Inc.*), 554 F.3d 382, 400 (3d Cir. 2009); 5 Collier on Bankruptcy P 547.03 (16th 2024)). Emerson argues that in determining whether an agreement exists that obligates a lender to pay specific debt, the "proper inquiry is …whether the debtor had the right to disburse the funds to whomever it wished, or whether [the] disbursement was limited to a particular old creditor or creditors under the agreement with the new creditor." (ECF 14, at 5) (citing *Adams v. Anderson,* (*In re Superior Stamp & Coin Co*.), 223 F.3d 1004, 1009 (9th Cir. 2000); *AmeriServe Food Distribution, Inc.*, 315 B.R. at 30. Emerson further argues that loan funds cannot be property of the estate when the loan is not a general loan, the loan has conditions to pay a particular creditor, and the funds could not have become available to all creditors. (ECF 14, at 5-6) (citing *In re Engstrom, Inc.*, 648 B.R. 617, 629 (Bankr. E.D. Wis. 2021), *aff'd,* No. 21-cv-1070, 2022 WL 2788437 (E.D. Wis. July 15, 2022), *aff'd*, 71 F.4th 640 (7th Cir. 2023); *In re Magellan E & P Holdings, Inc.*, 654 B.R. 98, 105 (Bankr. S.D. Tex. 2023) , *aff'd,* Case No. H-23-3453, 2024 WL 3092451 (S.D. Tex. June 21, 2024)).

Emerson urges that the Trustee incorrectly argues that the Loan Agreement represents a direction by the Debtor, Home Easy, to the non-debtor Home Easy Industrial to pay a specific creditor, which the Trustee alleges defeats application of the earmarking doctrine. (ECF 14, at 6 (citing ECF 11, at 14-15). Emerson submits that the Trustee's position is at odds with both decades of earmarking law and the express terms of the underlying agreement which contains an express term requiring non-debtor Home Easy Industrial to pay the loan proceeds to Emerson. Emerson argues the Loan Agreement does not provide for any other authorized use of the loan proceeds but rather represents an agreement by Home Easy Industrial that within 60 days after it signed the loan, Home Easy Industrial would pay the proceeds to Emerson, and not to any other party or for any other use.

Emerson cites as direct support, the Ninth Circuit's decision in *Superior Stamp* (ECF 14, at 6-7) (citing *Superior Stamp*, 223 F.3d at 1005-06) in which the court rejected the same argument raised by the Trustee here and instead found the debtor lacked control over the funds because the bank "agreed to fund the payments to the extent necessary but only on the express condition that the amounts involved be paid to [the individual creditor]." Emerson further cites *Engstrom*, 71 F.4th at 640; *Wagenknecht*, 971 F.3d at 1213.

Emerson disagrees with the Trustee's reliance on *In re Schick*, 234 B.R. at 337. Stating that the case is inapposite because, unlike here, it involved two loans that did not place any restrictions on the debtor's use of funds. (ECF, at 8) (comparing *AmeriServe Food Distribution, Inc.*, 315 B.R. at 30).

Emerson asserts that here, the Loan Agreement designates Emerson as the recipient of the loaned funds, the funds could not be paid to any other person or entity, and contrary to the Trustee's unsupported argument, it is "irrelevant whether the debtor or the lender . . . proposes a particular creditor as the recipient of the funds," so long as the underlying agreement conditions the loan on payment of that specific creditor. (ECF 14, at 8) (citing *Superior Stamp*, 223 F.3d at 1010.) Accordingly, Emerson urges that the loaned funds do not constitute property of the estate.

**The Complaint Must be Also Dismissed for Failure to Name a Necessary Party**

Emerson repeats its argument in the Motion that a party to a contract giving rise to the claims in the complaint is both "necessary" and "indispensable." (ECF 14, at 9) (citing *Tullett Prebon PLC v. BGC Partners, Inc.*, 427 F. App'x 236, 239 (3d Cir. 2011); *Dickson*, 202 F. App'x at 578.

Emerson states that the Trustee does not contest the fact that the Guarantor is a party to the Term Sheet and could not claim otherwise because Emerson argues that the Term Sheet

defines the Guarantor as a party to the agreement on its first page and it bears the Guarantor's signature as a party. Emerson asserts that as a party to the Term Sheet, the Guarantor is an indispensable party to this action and subjecting Emerson to these claims arising from the Term Sheet action without one of the parties to that contract is the very harm that Rule 19 is designed to guard against. (ECF 14, at 9)(citing *Fiscus v. Combus Fin. AG*, No. 03-1328-JBS, 2007 WL 4164388, at *5 (D.N.J. Nov. 20, 2007)). Further, Emerson asserts that the sole case the Trustee cites in support of his contrary argument, *U.S. Tech. Sols., Inc. v. eTeam, Inc.*, No. CV 17-1107-SDW-LDW, 2017 WL 35352022, at *3 (D.N.J. Aug. 16, 2017), does not hold otherwise.

In addition, Emerson asserts that the Trustee does not dispute that joinder is not feasible when the court cannot exercise personal jurisdiction over the absentee. Emerson has argued that the Guarantor has no discernable contacts with New Jersey besides being a party to the Term Sheet, which it alleges is not enough. (ECF 14, at 10) (citing *Associated Bus. Tel. Sys. Corp. v. Danihels*, 829 F. Supp. 707, 711 (D.N.J. 1993) (citing *Burger King Corp.*, 471 U.S. at 478-79).

Emerson states that the Trustee offers no evidence that such contacts exist but instead the Trustee cites two cases which are distinguishable because, unlike here where the Guarantor's identity and residence in China are known, in the Trustee's cited cases each plaintiff failed to identify the indispensable parties, let alone their citizenship. (ECF 14, at 10) (citing *CRST Expedited, Inc.*, 2018 WL 2016274, at *4; *Indian Harbor Ins. Co.*, 2012 WL 1038658, at *5.

Emerson submits that, contrary to the Trustee's arguments, the Term Sheet itself demonstrates that the Guarantor is an indispensable party to this action as a contracting party and cannot be joined because he is not subject to this Court's jurisdiction. Accordingly, the Trustee's claims must also be dismissed for failure to join the Guarantor,

**The Complaint Fails to State Any Claims for Relief Against Emerson**

The Claims are Barred by the *In Pari Delicto* Doctrine

Emerson rejects the Trustee's argument that *in pari delicto* does not apply to this matter because Home Easy's past misconduct does not concern the transaction that is the subject of the Complaint, the Term Sheet. (ECF 14, at 11) (citing ECF 11, at 25). Emerson asserts that the Trustee's argument is predicated upon the misplaced contention that Debtor Home Easy's misconduct and the Term Sheet are each a "separate transaction." Emerson asserts that the Trustee's argument is not supported by any case-law and artificially attempts to separate the Term Sheet and Home Easy's infringement into separate transactions even though they were quite obviously all part of a single course of misconduct by Home Easy.

Emerson argues that *in pari delicto* applies to misconduct committed "in the course of an integrated transaction" (ECF 14, at 11) (citing *Gastaldi v. Sunvest Resort Communities, LC*, No. 08-62076-CIV, 2010 WL 457243, at *13 (S.D. Fla. Feb. 3, 2010)) and/or involving the same "subject matter." (ECF 14, at 11)( citing *In re Decade, S.A.C., LLC*, 635 B.R. 735, 772–73 (Bankr. D. Del. 2021)).

Emerson argues that here the execution of the Term Sheet and Home Easy's misconduct in the underlying pre-petition litigation are inextricably linked and at the time the Term Sheet was executed, the Delaware District Court had entered a default judgment and permanent injunction against Home Easy that had the effect of halting Home Easy's ability to derive revenue from selling infringing products. Emerson asserts that it agreed to enter into the Term Sheet as an alternative to immediately enforcing its judgment against Home Easy.

Emerson submits it would be inequitable to permit Home Easy to recover amounts due and owing under the Term Sheet where those claims arise out of Home Easy's trademark

infringement and misconduct with respect to Emerson. (ECF 14, at 12) (citing *Miller v. Interfirst Bank Dallas, N.A.*, 608 F. Supp. 169, 172 (N.D. Tex. 1985); *c.f. In re Ampal-Am. Israel Corp.*, 545 B.R. 802, 812 (Bankr. S.D.N.Y. 2016)).

Emerson states, contrary to the Trustee's interpretation, that the cases it cited in the Motion stand for exactly this proposition. (ECF 14, at 12)(citing *10 Minute Fitness Inc.*, 679 F. Supp. 3d at 1380)(holding plaintiff could not sue defendant based on *in pari delicto* – even though plaintiff's hiring of defendant was a separate transaction from its trademark infringement – "due to its violation of federal law."); *Code*, 2024 WL 637356, at *3 (accepting the defendant's argument that relief sought by plaintiff was bared by *in pari delicto* because it was based on conduct in which the plaintiff participated and for which the plaintiff was convicted).

Count One (Turnover) Must be Dismissed

Emerson argues that the turnover claim must be dismissed because the Trustee has not plausibly alleged that the Non-Debtor Payments constitute estate property that can be returned to the bankruptcy estate as set forth in the instant Motion to Dismiss the Complaint.

Emerson asserts that turnover claims are a remedy limited to what is "acknowledged to be property of the bankruptcy estate," and cannot be utilized to decide "the rights of parties in legitimate contract disputes." (ECF 14, at 13)(citing *In re Olympus Healthcare Grp., Inc.*, 352 B.R. 603, 611 (Bankr. D. Del. 2006)).

Emerson states that the inclusion by the Trustee of breach of contract and quasi-contract claims in the Complaint demonstrates the facial invalidity of the turnover count. (ECF 14, at 13)(citing *In re Hechinger Inv. Co., of Del., Inc.*, 282 B.R. 149, 162 (Bankr. D. Del. 2002)). Emerson submits that the Trustee makes no attempt to distinguish the Third Circuit cases cited in the Motion dismissing turnover counts under identical circumstances and therefore Count I of the Complaint should be dismissed as premature.

Count Five (Promissory Estoppel) and Count Seven (Unjust Enrichment) Must be Dismissed Given the Existence of a Valid Contract

Emerson asserts that the Trustee's claims for promissory estoppel and unjust enrichment are just reiterations of the Trustee's breach of contract claim and cannot independently proceed as set forth in the Motion to Dismiss the Complaint. (ECF 14, at 14)(citing *Hillsborough Rare Coins, LLC*, 2017 WL 1731695, at *6-7; *Freightmaster USA, LLC*, 2015 WL 1472665, at *6. Emerson suggests that the Trustee essentially concedes this point by arguing he can plead these counts in the alternative.

Emerson argues that quasi-contractual claims like those the Trustee asserts cannot be pursued alongside a breach of contract claim where the enforceability of the parties' express contract is not at issue. (ECF 14, at 14)(citing *SCP Distributors, LLC v. Nicholas Pools, Inc*., No. 22-6721-ZNQ-RLS, 2023 WL 6130635, at *5 (D.N.J. Sept. 19, 2023)). Instead, Emerson argues that quasi-contractual claims must be dismissed when there is agreement as to the existence of a valid contract and the conduct underlying the breach of contract claim is the sole basis for the quasi-contractual claims. (ECF 14, at 14)(citing *Adler Engineers, Inc. v. Dranoff Properties, Inc*., No. 14-921-RBK-AMD, 2014 WL 5475189, at *12 (D.N.J. Oct. 29, 2014)). Emerson argues that "a quasi-contractual claim can only move forward as an alternative to a breach of contract claim where the enforceability of the express contract is at issue." (ECF 14, at 14)(quoting *SCP Distributors, LLC.*, 2023 WL 6130635, at *5).

In support of its argument Emerson asserts that the Trustee's quasi-contractual claims all rely on the identical conduct relied upon for the breach of contract claim. Specifically, Emerson points out that the Trustee alleges for the breach of contract claim that Emerson was "contractually required" to return the Non-Debtor Payments if the parties did not execute a

license agreement and the Trustee seeks to recover under the quasi-contract claims for the same conduct and under the same alleged obligation. (ECF 14, at 15) (citing ECF 11, at 35).

Emerson asserts that the Trustee not only failed to challenge the enforceability of the Term Sheet but relies on its enforceability and is thus limited now to alleging this conduct as a breach of the Term Sheet.

Emerson states it is not challenging whether the Term Sheet is enforceable. Instead, Emerson's position is that the enforceable Term Sheet contains no provision requiring Emerson to refund the Non-Debtor Payments and rather expressly states such Non-Debtor Payments were non-refundable. Emerson argues that neither party has argued the Term Sheet is not an enforceable contract and therefore, the Trustee cannot proceed with his quasi- contractual claims alongside his breach of contract claim, even if such claims are alleged in the alternative.

Emerson argues that the cases cited by the Trustee support Emerson's argument since in such cases the courts permitted quasi-contractual claims to proceed because, unlike the circumstance here:

(i) the conduct that the plaintiff sought to recover for was not clearly addressed in the parties' express agreement, or

(ii) there were substantial questions regarding the enforceability of the parties' express agreement.

(ECF 14, at 16)(citing *Gap Props., LLC*, 2020 WL 7183509, at *4; *Williams*, 2024 WL 1328133, at *9-10; *Innovative Sol. & Tech., LLC*, 2023 WL 3260031, at *2-3; *Dougherty*, 534 F.Supp.3d at 384; *Ass'n of N.J. Chiropractors*, 2012 WL 1638166, at *11.

Count Four (Fraud) Must be Dismissed

Emerson repeats its assertion in the Motion to Dismiss that the New Jersey's economic loss doctrine bars the Trustee's claim for "fraud" and asserts the Trustee is incorrectly attempting to now recharacterize his claim for "fraud" in the Complaint as a legally distinct claim for "fraud

in the inducement." (ECF 14, at 17) (citing *State Cap. Title & Abstract Co.*, 646 F. Supp. 2d at 676.

Emerson argues that the Trustee is not permitted to recast his pleadings in an opposition to a motion to dismiss (ECF 14, at 17) (citing *Frederico v. Home Depot*, 507 F.3d 188, 202 (3d Cir. 2007).) and rather, the Trustee must seek relief to add an additional claim such as through Rule 15 which he has not sought.

Next, Emerson argues that the Trustee cannot set forth a claim for fraud in the inducement either under Rule 9 (which Emerson does not concede applies) or Rule 8. Emerson argues that under New Jersey law:

> "[t]he five elements of fraud in the inducement track those of common law fraud: '(1) a material misrepresentation of a presently existing or past fact; (2) knowledge or belief by the defendant of its falsity; (3) an intention that the other person rely on it; (4) reasonable reliance thereon by the other person; and (5) resulting damages.'"

(ECF 14, at 17-18)(quoting *Munenzon v. Peters Advisors, LLC*, 553 F. Supp. 3d 187, 205 (D.N.J 2021)). Emerson asserts that fraud in the inducement claims require a pre-contractual statement which has not been plead here. (ECF 14, at 18)(citing *Bracco Diagnostics, Inc.*, 226 F. Supp. 2d at 563; *Intimateco LLC v. Apparel Distribution, Inc.*, No. cv 23-1759-SRC, 2023 WL 7986336, at *7 (D.N.J. Nov. 17, 2023).

Emerson does not disagree with the cases cited by the Trustee that state that fraud in the inducement claims are not barred by the economic loss doctrine. But Emerson argues these cases are not applicable because, among other things, the Trustee has pleaded no such pre-contractual statement. (ECF 14, at 18, n. 5) (citing G*&F Graphic Servs. v. Graphic Innovators, Inc.*, 18 F. Supp. 3d 583 (D.N.J. 2014); *Wilhelm Reuss GmbH & Co KG, Lebensmittel Werk*, 2018 WL

3122332; *Bell Container Corp.*, 2019 WL 8105297.

Emerson argues that here the alleged fraudulent representations were made in the agreement (as opposed to a precontractual statement). Emerson also claims there are no references in the Complaint to communications other than the alleged promises made in the agreement and Home Easy's interpretation of provisions of the Term Sheet is not a pre-contractual representation that can support a fraud in the inducement claim.

Emerson further notes that the allegations in the Complaint also do not support the first element of fraud - material misrepresentation of an existing or past fact. (ECF 14, at 19, n.6) (citing *Bergen Beverage Distributors LCC v. E. Distributors, Inc.*, No. 2:17- CV-04735-WJM, 2022 WL 833373, at *9 (D.N.J. Mar. 21, 2022); *Billings v. Am. Exp. Co.*, No. CIV.A. 10-3487, 2011 WL 5599648, at *11 (D.N.J. Nov. 16, 2011)).

Emerson argues that the Trustee cannot show the requisite "reliance" on representations because Home Easy's payment of the non- Debtor payments were made pursuant to the express obligations in the Term Sheet and cannot constitute plausible allegations of conduct inducing Home Easy to enter the Term Sheet but rather constitute allegations of its performance after entering into the Term Sheet. (ECF 14, at 19) (citing *Wenzel v. Nautilus Ins. Co.*, No. 10-6270, 2011 WL 1466323, at *5 (D.N.J. Apr. 18, 2011), *aff'd*, 474 F. App'x 862 (3d Cir. 2012)). As for the remaining elements of fraud, Emerson argues there was no representation made by Emerson that Emerson could have known was false or intended the Trustee to rely upon. (ECF 14, at 20, n.7). Further, as for damages, Emerson points out Home Easy did not pay the Non-Debtor Payments and therefore the Trustee cannot claim associated damages. (ECF 14, at 20, n. 7).

Emerson argues that for both "fraud in the inducement" as well as "fraud", the economic

loss doctrine bars claim that are not extrinsic to a contract, including the Trustee's claim here that pertains to performance under the Term Sheet. (ECF 14, at 20) (citing *State Cap. Title & Abstract Co., LLC,* 646 F. Supp. 2d at 676; *Wenzel*, 2011 WL 1466323, at *6).

Count Six (Conversion) Must be Dismissed

Emerson asserts that for similar reasons, the economic loss doctrine bars the claim of "conversion" because, as Emerson states the Trustee's cited authorities recognize, a tort claim only survives preclusion under the economic loss doctrine if it is based on conduct extraneous to a contract. (ECF 14, at 20-21) (citing *Bracco Diagnostics, Inc.*, 226 F. Supp. 2d at 564; *Hughes v. TD Bank, N.A.*, 856 F. Supp. 2d 673, 682 (D.N.J. 2012)). Emerson states *Kam Int'l v. Franco Mfg. Co. Inc.,* No. CIV.A 2:10-02733, 2010 WL 5392871 (D.N.J. Dec. 22, 2010), cited by the Trustee, is inapposite. (ECF 14, at 21, n.8).

Emerson states that the Trustee does not allege conduct *extraneous* to the Term Sheet that would enable a tort claim for conversion but rather, the conversion claim hinges on the conduct addressed in the Term Sheet, which is the refundability of the Non-Debtor Payments, which Emerson argues the Term Sheet itself expressly provides are non-refundable. Emerson rejects the Trustee's argument that because the Term Sheet does not provide a contractual remedy for the refund of payments, refundability is therefore extraneous to the contract and may be pursued by way of a tort claim. Emerson argues the Trustee's interpretation of "extraneous" is not consistent with the economic loss doctrine and conduct that is expressly addressed by a contractual provision is *intrinsic* to a contract and cannot be pursued under a tort theory. (ECF 14, at 21) (citing *Innovative Cosm. Concepts, LLC v. Brown Packaging, Inc.*, No. 18-5939, 2020 WL 7048577, at *4 (D.N.J. Apr. 28, 2020)) .

Emerson adds that pleading in the alternative is not appropriate because it is only permissible when the validity of the contract is in dispute. (ECF 14, at 21)(citing *Shapiro v.*

*Barnea*, No. cv 06-811-JBS, 2006 WL 3780647, at *4 (D.N.J. Dec. 21, 2006)). Emerson states again that it is not the validity of the Term Sheet that is in question but rather the interpretation of its express terms.

Emerson further argues that the claim of conversion should be dismissed because of the Trustee's failure to allege that the funds purportedly converted belonged to Home Easy as required in New Jersey. (ECF 14, at 22) (citing *Communications Programming, Inc.*, 1998 WL 329265, at *5; *Scholes Elec. & Commc'ns, Inc. v. Fraser*, No. CIVA 04- 3898-JAP, 2006 WL 1644920, at *5 (D.N.J. June 14, 2006)). Emerson states the Trustee's authority (ECF 11, at 4, citing *Dante v. Schwartz*, Civ. A. No. 20-01047, 2022 WL 1104996 (D.N.J. April 13, 2022)) is inapposite because the plaintiffs therein were not alleging a breach of contract claim.

Count Two (Breach of Contact) Must be Dismissed

Emerson repeats its argument in the Motion that the allegations in the Complaint of breach of contract are not supported by any actual contractual obligation upon Emerson and the express provisions of the Term Sheet imposed no obligation on Emerson to grant a license to Home Easy, to refund the Non-Debtor Payments, or to offset any payments against the judgment.

Emerson argues the Trustee is asking the Court, to infer an implied term that would require Emerson to refund the Non-Debtor Payments if the parties did not enter into the license which Emerson asserts contradicts the Term Sheet's express provisions. Emerson cites *Moser v. Milner Hotels*, 6 N. J. 278, 78 A.2d 393 (1951) for the proposition that an implied contract cannot exist when there is an existing express promise. Emerson argues this also applies to implied terms of a contract which cannot override an express term contained in a written agreement. (ECF 14, at 23) (citing *Kas Oriental Rugs, Inc. v. Ellman*, 394 N. J. Super. 278, 926

A.2d 387, 287 (N.J. App. Div. 2007)).

Thus, Emerson argues the Term Sheet expressly provides that the non-Debtor payments are non-refundable if Home Easy failed to pay the License Commencement Fee and all Minimum Annual Guarantee Royalties and since there is no dispute from the Trustee that the Debtor failed to pay the Minimum Annual Guarantee Royalties (citing ECF 11, at 51), Emerson argues there can be no dispute that the Non-Debtor Payments are non-refundable under the express terms of the Term Sheet.

Emerson states that neither of the cases cited by the Trustee support his position that an implied term may override the express terms of a contract. (ECF 14, at 24, n. 9) (citing *Heyman*, 2019 WL 2642655, at *24; See also *Melone*, 2024 WL 1743108, at *11(there was no express written contract between the parties)).

Emerson further argues that the Trustee's contention Emerson breached the Term Sheet by using the Non- Debtor Payments to setoff other payments owed to Emerson is insufficient because, as Emerson states was established in the instant Motion: (a) there are no express or implied obligations on Emerson about setoffs that can support any type of breach claim; (b) there are no allegations that Emerson has actually done so; and (c) even if Emerson did, there would be no damages to Home Easy. (ECF 14, at 24).

Count Three (Breach of the Implied Covenant) Must be Dismissed

Emerson argues that the Trustee's claim for breach of the implied covenant of good faith and fair dealing should fail for the same reasons as the Trustee's breach of contract claim. Emerson states that it is well-established under New Jersey law that a plaintiff cannot proceed with a claim for breach of the implied covenant of good faith and fair dealing where the claim arises from the same conduct underlying a breach of contract claim. (ECF 14, at 25) (citing

*Hahn v. OnBoard LLC*, No. 2:09-cv-03639-DRD-MAS, 2009 WL 4508580, at *6 (D.N.J. Nov. 16, 2009); *Elite Personnel, Inc. v. PeopleLink, LLC*, No. CIV. A. 15-1173, 2015 WL 3409475, at *3 (D.N.J. May 27, 2015)).

Emerson argues that the Trustee has alleged no conduct in his breach of contract claim that would not be encompassed within his claim for breach of the implied covenant of good faith and fair dealing and the Trustee has not alleged that the Term Sheet is unenforceable which Emerson states is necessary to support pleading a claim for breach of the implied covenant of good faith and fair dealing even in the alternative.

## III THE NOVEMBER 25 HEARING

The parties' oral arguments closely reflected their written arguments in the Motion to Dismiss the Complaint, Opposition, and Reply. Emerson provided further description of the Delaware Action filed in 2017, stating that the Debtor, Home Easy, was found to have infringed upon Emerson's trademark. After the decision was issued in the Delaware Action in April of 2022, an injunction was in placed on the Debtors to prevent further trademark infringement. Emerson asserts that without complying with the injunction, Home Easy appealed the decision by the Delaware District Court, and subsequently filed bankruptcy in June 2022. Emerson stated that for its part, rather than enforce its judgment, it engaged in settlement discussions with Home Easy which resulted in the Term Sheet.

Emerson described the Term Sheet as a pathway for Home Easy to utilize Emerson's trademarks, pursuant to the terms of a license agreement that was to be negotiated. Emerson submitted that the Debtor could benefit from the stay of the pending trademark litigation, until the license agreement was fully consummated. In exchange of the Term Sheet, Debtor was required of two things: 1) minimum royalty payment of $500,000 a year regardless of actual sale activity

and 2) that Debtor pay a license commencement fee of $3.6 million, in which $2 million would be paid upon the signing of the Term Sheet, and the remining $1.6 million along with the first license fee payable within 30 days. The Term Sheet provides that none of the payments were refundable, and all the payments were guaranteed by the Guarantor Liang Jiucheng, who resides in Hong Kong, China.

The Trustee argued that the parties entered the Term Sheet and expected to enter into a Licensing Agreement. According to the Trustee, the parties did not ultimately enter into a Licensing Agreement because Emerson kept changing the terms of such agreement. Trustee insisted that discovery in preparation for the trial in this case will show Emerson's failure to reach certain benchmarks. Thus, it would be premature to dismiss the Trustee's claims now.

According to the Trustee, the Term Sheet should be interpreted as providing that when the Debtor eventually received the licenses, the funds paid would be non-refundable. However, because the parties never consummated the Licensing Agreement, and Debtor never received the license, it would be unfair for Emerson to keep the funds.

The Trustee further argued that he has standing in his turnover claim because the funds were a loan from Home Easy Industrial, and the money was wired to Emerson under the instruction of the Debtor and, as per case law, the Debtor had control over the funds, and they belong to the Debtor's estate.

## IV ANALYSIS

### A. Dismissal of the Complaint under Fed. R. Civ. P. 12(b)(1)

Fed. R. Civ. Pro. 12(b)(1) made applicable to this proceeding by Fed. R. Bankr. P. 7012, provides that a party may assert the defense of lack of subject-matter jurisdiction by motion. A factual 12(b)(1) challenge attacks allegations underlying the assertion of jurisdiction in the

complaint, and it allows the defendant to present competing facts. *Constitution Party of Pa. v. Aichele*, 757 F.3d 347, 358 (3d Cir. 2014). When considering a factual challenge, "the plaintiff [has] the burden of proof that jurisdiction does in fact exist," the court "is free to weigh the evidence and satisfy itself as to the existence of its power to hear the case," and "no presumptive truthfulness attaches to [the] plaintiff's allegations...." *Mortensen v. First Fed. Sav. & Loan Ass'n*, 549 F.2d 884, 891 (3d Cir. 1977). And, when reviewing a factual challenge, "a court may weigh and consider evidence outside the pleadings." *Constitution Party of Pa.*, 757 F.3d at 358 (internal quotation marks omitted). On motion to dismiss for lack of subject matter jurisdiction, no presumption of truthfulness attaches to plaintiff's allegations. *CNA v. United States*, 535 F.3d 132, 139 (3d Cir. 2008), *as amended* (Sept. 29, 2008). Therefore, a 12(b)(1) factual challenge strips the plaintiff of the protections and factual deference provided under 12(b)(6) review. See *Hartig Drug Co. Inc. v. Senju Pharm. Co.*, 836 F.3d 261, 268 (3d Cir. 2016).

Emerson argues that because the $4.1 million from Home Easy Industrial never passed through the Debtor's bank accounts, but rather was sent from Home Easy Industrial directly to Emerson, the funds were never property of the Debtor's estate and therefore, the Trustee lacks standing to pursue recovery of funds that did not belong to the Debtor for lack of subject matter jurisdiction based on Fed. R. Civ. P. 12(b)(1).

The Trustee argues that on July 13, 2022, Home Easy arranged for the initial $2 million to be wired to Emerson, the wire payments were sent and accepted by Emerson and Emerson acknowledged the $2 million wire payment it received was made on behalf of Home Easy. (ECF 1, ¶18) Further, on August 11, 2022, Home Easy arranged for the second payment of $2.1 million to be wired to Emerson, and Emerson again acknowledged the $2.1 million payment it received was made on behalf of Home Easy. *Id.* The Trustee argues that the $4.1 million is the property of

the estate because the Debtor had control over the funds, and they were not "earmarked" but rather were transferred to Emerson under the direction of the Debtor and as a loan to the Debtor. The Trustee also refers to the Loan Agreement attached to the Proof of claim (Claim No. 5) filed by Home Easy Industrial to support that the funds were a loan to the Debtor.

When a third party lends money to a debtor for the purpose of paying a specific creditor that the lender designates, the funds are considered "earmarked," and do not become property of the debtor and cannot be recovered by the trustee. *Schick*, 234 B.R. at 346. In contrast, a payment made by a third party to a creditor of the debtor will amount to a transfer of the debtor's property "when the payment represents a loan by the third party to the debtor and the debtor, rather than the lender, designates the creditor to be paid and controls the application of the loan." *Id*. (citing 5 Lawrence P. King, *et al., Collier on Bankruptcy* ¶ 547.03[2], at 547–24 (rev. 15th ed.1999)). The fact that the funds do not touch a debtor's bank account is not dispositive as to whether the funds are or are not property of the debtor.

At this stage in the litigation, the Trustee has set forth a plausible argument that the funds were a loan to the Debtor and that the Debtor exerted the requisite control over such funds subject to further development through discovery and trial. Therefore, the Motion to Dismiss the Adversary Complaint pursuant to Rule 12(b)(1), made applicable to this proceeding by Fed. R. Bankr. P. 7012 is denied without prejudice.

**B. Dismissal of the Complaint under Fed. R. Civ. P. 12(b)(7) and (19)**

Fed. R. Civ. P. 12(b)(7), made applicable to this proceeding by Fed. R. Bankr. P. 7012, provides that a party may assert the defense of failure to join a party under Rule 19 by motion. Rule 19, made applicable to this proceeding by Fed. R. Bankr. P. 7019 provides, in pertinent part, that "[i]f a person who is required to be joined if feasible cannot be joined, the court must determine

whether, in equity and good conscience, the action should proceed among the existing parties or should be dismissed."

Fed. R. Civ. P. 19 determines whether a non-joined party is indispensable and must be joined in the action. *Dickson*, 202 F. App'x at 580. Rule 19 mandates a two-step process: (1) the court first must determine whether the absent party is "necessary" under Rule 19(a); and (2) if the party is "necessary" and joinder is not feasible, then the court must decide whether the party is "indispensable" under Rule 19(b). *Tullett Prebon PLC*, 427 F. App'x at 239-40. The question under Rule 19(b) is whether "in equity and good conscience" the court should proceed without the non-joined parties. *Dickson*, 202 F. App'x at 581.

Rule 19(b) provides factors that should be considered by the court in making the determination of whether to proceed or dismiss the action. Those factors include:

> [F]irst, to what extent a judgment rendered in the person's absence might be prejudicial to the person or those already parties; second, the extent to which, by protective provisions in the judgment, by the shaping of relief, or other measures, the prejudice can be lessened or avoided; third, whether a judgment rendered in the person's absence will be adequate; fourth, whether the plaintiff will have an adequate remedy if the action is dismissed for nonjoinder.

*Id.* This is not an exhaustive list of factors that can be considered, but these are the most important factors. See *Gardiner v. V.I. Water & Power Auth.*, 145 F.3d 635, 640–41 (3d Cir.1998). *Dickson*, 202 F. App'x at 581. If the court determines that the non-joined party is indispensable, the suit must be dismissed. *Id*.

Rule 19(a)(1) defines a necessary party as:

> A person who is subject to service of process and whose joinder will not deprive the court of subject-matter jurisdiction must be joined as a party if:
>
> (A) in that person's absence, the court cannot accord complete relief among existing parties; or
>
> (B) that person claims an interest relating to the subject of the action and is so situated that disposing of the action in the person's absence may:

> (i) as a practical matter impair or impede the person's ability to protect the interest; or
>
> (ii) leave an existing party subject to a substantial risk of incurring double, multiple, or otherwise inconsistent obligations because of the interest.

Fed. R. Civ. P. 19(a)(1); *Tullett Prebon PLC*, 427 F. App'x at 239.

Emerson asserts that the Guarantor is an individual who resides in China and who has had no demonstrable affiliations with or activities in New Jersey that could create a basis for general or specific jurisdiction. *See, e.g.*, *Associated Bus. Tel. Sys. Corp.*, 829 F. Supp. at 711 (citing *Burger King Corp.*, 471 U.S. at 478-79 ("[A] contract between a forum resident and an out-of-state party will not automatically establish sufficient contacts with the forum to justify *in personam* jurisdiction."). As a result, Emerson argues the Guarantor cannot be feasibly joined, and the second part of the Rule 19(a) analysis is satisfied.

The Trustee argues that the absence of the Guarantor in this action is immaterial to the issues before the Court because the Guarantor has no interest "relating to the subject of the action" or the relief being sought; the Guarantor paid none of the funds to Emerson, Emerson has no obligation to pay the Guarantor anything and further, the Guarantor has not claimed as interest.

The Trustee also argues that the Guarantor is not an obligee but an obligor and obligors are not indispensable parties. *Dickson*, 202 Fed. App'x at 578 ("In the context of Rule 19(a)… generally a co-obligor was not necessary….") Additionally, the Trustee argues that even if the Guarantor were a required party, there is nothing in the record that would substantiate that this Court cannot exercise personal jurisdiction over the Guarantor.

The Trustee points out that if the action were dismissed on this ground, the Trustee and the Debtor's estate would be prejudiced because the Trustee would then lack a remedy to recover the $4.1 million, he alleges Emerson has wrongfully retained.

At this early stage in the litigation and on the record currently before the Court, there are not enough facts developed regarding the circumstances resulting in the guaranty, the relationships between and among the Debtor, Home Easy Industrial and the Guarantor, and the related transactions, to determine conclusively that the Guarantor is an indispensable party, and this Court cannot maintain in personam jurisdiction over the Guarantor. Further, as the Trustee asserts, if the case were dismissed on this basis, the Trustee, and by extension the estate, would be left without a remedy.

Therefore, the Motion to Dismiss the Adversary Complaint pursuant to Rule 12(b)(7) and (19), made applicable to this proceeding by Fed. R. Bankr. P. 7012 and 7019, is denied without prejudice.

**C. Dismissal of the Complaint under Fed. R. Civ. P. Rule 12 (b)(6)**

When considering a motion to dismiss a complaint for failure to state a claim upon which relief can be granted pursuant to Fed. R. Civ. P. 12 (b)(6), which is made applicable to bankruptcy proceedings by Fed. R. Bankr. P. 7012., a court must accept all well-pleaded allegations in the complaint as true, view them in the light most favorable to the plaintiff, and determine whether, under any reasonable reading of the complaint, the plaintiff may be entitled to relief. *Phillips v. Cnty. of Allegheny*, 515 F.3d 224, 231 (3d Cir. 2008). To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to state a claim for relief that is plausible on its face. *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007); *Fowler v. UPMC Shadyside*, 578 F.3d 203, 210 (3d Cir. 2009). "A claim has facial plausibility when the pleaded factual content allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Iqbal*, 556 U.S. at 662 (citing *Twombly*, 550 U.S. at 556).

The United States Supreme Court has set forth a two-step analysis for adjudicating a motion to dismiss. *Iqbal*, 129 S. Ct. at 1949-50. First, a court should identify and reject labels, conclusory allegations, and formulaic recitation of the elements of a cause of action. Second, a court must draw on its judicial experience and common sense to determine whether the factual content of a complaint plausibly gives rise to an entitlement to relief. The court must infer more than the mere possibility of misconduct. *Id*. This does not impose a "probability requirement" at the pleading stage but requires a showing of "enough facts to raise a reasonable expectation that discovery will reveal evidence of the necessary element." *Phillips*, 515 F.3d at 234 (quoting *Twombly*, 550 U.S. at 556).

In deciding motions to dismiss under Rule 12(b)(6), courts generally consider only the allegations in the complaint, exhibits attached to the complaint, matters of public record, and documents that form the basis of the claim. See *In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1426 (3d Cir. 1997). A court may also take judicial notice of a prior judicial opinion. *McTernan v. City of York*, 577 F.3d 521, 526 (3d Cir. 2009); *Buck v. Hampton Twp. Sch. Dist.*, 452 F.3d 256, 260 (3d Cir. 2006).

**Dismissal of the Complaint Based on In Pari Delicto**

As this Court stated in *Norvergence*, Inc., 405 B.R. at 747 (citing *Lafferty*, 267 F.3d 340, 354 (3d Cir.2001)): "The doctrine of *in pari delicto* provides that a plaintiff may not assert a claim against a defendant if the plaintiff bears fault for the claim."

Further:

> The *in pari delicto* doctrine is an affirmative defense that must be raised by the parties. *In re Total Containment, Inc.,* 335 B.R. at 621. (citing *Lafferty,* at 354). Even though an affirmative defense is not routinely considered on a motion to dismiss, it may be entertained if it "is established on the face of the complaint." *Id.* (citing *Leveto v. Lapina,* 258 F.3d 156, 161 (3d Cir.2001)).

*In re Norvergence, Inc.*, 405 B.R. 709, 749 (Bankr. D.N.J. 2009)

Thus, as an initial matter, the Court must decide whether the *in pari delicto* defense is ripe at this time, or whether the issues should be reserved for further discovery. The Complaint include the following recitation of facts on the Debtor's prior bad conduct:

> …Upon information and belief, the Agreement was signed in anticipation of an overall settlement agreement that would (a) provide Home Easy with a license to use the trademark EMERSON QUIET KOOL (the "Trademark") and (b) terminate and settle the claims asserted by ERC against Home Easy and EQK in a trademark infringement action pending in the United States District Court for the District of Delaware in the case entitled *Emerson Radio Corp. v. Emerson Quiet Kool Co., Ltd and Home Easy Ltd.*, Civil Action No. 20-1652 (the "Delaware Action").
> 12. In the Delaware Action, ERC asserted that Home Easy and EQK had infringed on Emerson's rights through the use of the Trademark. Home Easy and EQK answered ERC's complaint and disputed ERC's claims. Notwithstanding Home Easy's and EQK's defenses to ERC's claims, and the fact that the claims had been litigated for more than four years, the judge in the Delaware Action entered a default judgment against Home Easy and EQK in the amount of $6.5 million (the "Judgment"). Home Easy and EQK appealed the entry of the Judgment to the United States Court of Appeals for the Third Circuit, which appeal was still pending at the time of the execution of the Agreement.

ECF 1, ¶¶11-12.

This case has a history of litigation in the Delaware District Court including findings regarding the Debtor's bad acts as described in the Motion to Dismiss and during the Hearing. But this Court determines that the issue is not ripe at this time and should be reserved for further discovery. Affirmative defenses like the *in pari delicto* doctrine are not routinely considered in a motion to dismiss and the Court declines to do so now. Thus, dismissal of any counts based on the *in pari delicto* defense at this time is premature and these issues will be reserved for further discovery.

Therefore, at this time, the Motion to Dismiss the Adversary Complaint based on the *in pari delicto* doctrine is denied without prejudice and the issue is reserved.

**Dismissal of Count One**
**(Turnover of the Assets of the Estate Pursuant to 11 U.S.C. §542)**

In Count One of the Complaint, the Trustee seeks turnover pursuant to 11 U.S.C §542(a) of the $4.1 million Home Easy Industrial paid Emerson on the basis that such funds are estate property. Emerson has moved to dismiss Count One on the basis that the funds were "earmarked" and were never Debtor's property because they were paid directly by Home Easy Industrial to Emerson and are not subject to turnover. Emerson also asserts the turnover claim should be dismissed because the Trustee is seeking to recover property based on disputed contract and tort claims. Thus, the turnover claim is, at best, premature.

Reviewing the Trustee's claims as true for the purpose of evaluating dismissal of Count One under Rule 12(b)(6), the Trustee has set forth a plausible claim that the funds were a loan to the Debtor and that the Debtor exerted the requisite control over the funds and therefore they constitute property of the estate. As set forth above, a payment made by a third party to a creditor of the debtor will amount to a transfer of the debtor's property "when the payment represents a loan by the third party to the debtor and the debtor, rather than the lender, designates the creditor to be paid and controls the application of the loan." *Schick* at 346 (citing *Collier*, ¶ 547.03[2], at 547–24).

The record has not been sufficiently developed at this stage of the case to rebut the Trustee's allegations and this issue is reserved and subject to further development through discovery and trial.

Therefore, the movant's request for dismissal of Count One for turnover under 11 U.S.C §542(a) pursuant to Rule 12(b)(6), made applicable to this proceeding by Fed. R. Bankr. P. 7012 is denied without prejudice.

**Dismissal of Count Five (Promissory Estoppel), Count Seven (Unjust Enrichment) and Count Three (Implied Covenant of Good Faith and Fair Dealing)**

Emerson argues that because the Trustee is relying on a written contract – the Term Sheet, the Trustee cannot maintain the quasi-contract causes of action under Count Five for Promissory Estoppel, Count Seven for Unjust Enrichment and Count Three under the Implied Covenant of Good Faith and Fair Dealing. Emerson also argues that Count Three (the implied covenant of good faith and fair dealing) is duplicative of Count Two (the breach of the contract claim).

The Trustee argues that these counts were pled in the alternative which is specifically allowed by Fed. R. Civ. P. 8(d) and applicable case law. See *Innovative Sols. & Tech., LLC*, 2023 WL 3260031, at *2:

> Generally, the Federal Rules of Civil Procedure permit parties to "plead alternative and inconsistent legal causes of action that arise out of the same facts." *Nieves v. Lyft, Inc.*, No. 17-6146, 2018 WL 2441769, at *19 (D.N.J. May 31, 2018). Rule 8 states that "[a] party may set out 2 or more statements of a claim or defense alternatively or hypothetically, either in a single count or defense or in separate ones." Fed. R. Civ. P. 8(d)(2). A party may also "state as many separate claims or defenses as it has, regardless of consistency." Fed. R. Civ. P. 8(d)(3). Although Plaintiff cannot ultimately recover under breach of contract and promissory estoppel theories for the same alleged wrongful conduct, this does not preclude Plaintiff from initially pleading both claims.

However, Emerson argues that the existence of the contract (the Term Sheet) is not in dispute and quasi-contractual claims cannot be pursued with a breach of contract claim where the parties are not disputing the enforceability of the parties' express contract. Courts have found that: "[W]here there is an express contract covering the identical subject matter of [a quasi-contract] claim, [a] plaintiff cannot pursue [that] quasi-contractual claim." *All Seasons Home Improvement Co. v. Arch Concept Constr., Inc.*, Civ. No. 16-0751-FLW, 2018 WL 3928787, at *8 (D.N.J. Aug.

16, 2018) (quoting *Duffy v. Charles Schwab & Co., Inc.*, 123 F. Supp. 2d 802, 814 (D.N.J. 2000)). Further,

> It is a well settled rule that an express contract excludes an implied one. An implied contract cannot exist when there is an existing express contract about the identical subject. The parties are bound by their agreement, and there is no ground for implying a promise. It is only when the parties do not agree that the law interposes and raises a promise[, forming the basis of a quasi-contract claim.]

*SCP Distributors, LLC v. Nicholas Pools Inc.*, No. CV 22-6721-ZNQ-RLS, 2023 WL 6130635, at *5 (D.N.J. Sept. 19, 2023) (quoting *Moser*, 78 A.2d at 394 (internal quotations marks and citations omitted)).

As set forth in *SCP Distributors, LLC*, 2023 WL 6130635, at *5 (D.N.J. Sept. 19, 2023) "where express contracts exist concerning the same subject matter alleged in a quasi-contract claim, the quasi-contractual claim can only move forward as an alternative to a breach of contract claim where the enforceability of the express contract is at issue." As set forth by the District Court in *All Seasons Home Improvement Co.*, 2018 WL 3928787, at *8 (citing *Duffy*, 123 F.Supp.2d at 814 (D.N.J. 2000)("quasi-contract liability will not be imposed when a valid, unrescinded contract governs the rights of the parties.")

However, at the pleading stage, the Plaintiff is permitted to assert alternative and even inconsistent claims:

> Although a plaintiff cannot ultimately recover for both breach of contract and quantum meruit claims, this does not preclude a plaintiff from initially pleading both claims. Generally, the Federal Rules of Civil Procedure permit parties to "plead alternative and inconsistent legal causes of action that arise out of the same facts.". Rule 8 states that "[a] party may set out 2 or more statements of a claim or defense alternatively or hypothetically, either in a single count or defense or in separate ones." Fed. R. Civ. P. 8(d)(2). A party may also "state as many separate claims or defenses as it has, regardless of

> consistency." Fed. R. Civ. P. 8(d)(3). As a result, the Court will not dismiss this claim as to [Defendant] on these grounds.

*Somerset Orthopedic Assocs., P.A. v. Horizon Healthcare Servs., Inc.,* No. CV 19-8783, 2020 WL 1983693, at *10 (D.N.J. Apr. 27, 2020)(quoting *Nieves v. Lyft, Inc.*, No. 17-6146, 2018 WL 2441769, at *19 (D.N.J. May 31, 2018)).

Since the Trustee has asserted plausible claims in the alternative, the Court declines to dismiss the quasi-contract claims now, at this stage in the case. The record on the quasi-contract claims, and whether they are based on the parties' contractual relationship and alleged breach of the Term Sheet or something additional, requires development and will be reserved for discovery and trial.

Therefore, the dismissal of Count Three (the Implied Covenant of Good Faith and Fair Dealing), Count Five (Promissory Estoppel) and Count Seven (Unjust Enrichment) is denied without prejudice.

**Dismissal of Count Four (Fraud)**

Emerson argues that Count Four for fraud should be dismissed because the claim is barred under New Jersey's economic loss doctrine which bars plaintiffs from recovering in tort economic losses (such as from fraud) when their entitlement to recovery only flows from a contract. Emerson argues that the Trustee's claim for fraud as set forth in the Complaint flows entirely from the Term Sheet and is not separate and distinct from the performance of the contract. See *State Cap. Title & Abstract Co.*, 646 F. Supp. 2d at 677 ( finding " a claim of common law fraud that is intrinsic to the underlying agreement, as is the case here, is barred by the economic loss doctrine.)

Emerson also argues that the Trustee incorrectly attempted in his Opposition (ECF 11) to recharacterize his claim for "fraud" as a claim for "fraud in the inducement", which is a distinct legal concept. Emerson asserts that the Trustee is not permitted to recast his pleadings in an opposition to a motion to dismiss and must seek relief to add an additional claim (such as through Rule 15), which he has not sought. Further, Emerson argues that the Trustee has not asserted a pre-contractual statement and thus, has not established the elements of a fraud in the inducement claim.

The elements of fraud in the inducement track the elements of common law fraud: "(1) a material misrepresentation of a presently existing or past fact; (2) knowledge or belief by the defendant of its falsity; (3) an intention that the other person rely on it; (4) reasonable reliance thereon by the other person; and (5) resulting damages." *Munenzon*, 553 F. Supp. 3d at 205. But fraud in the inducement is a distinct legal concept.

Emerson further asserts that the Trustee's fraud count should be dismissed because it lacks the specificity required under R. 9(b), made applicable to this proceeding by Fed. R. Bankr. P. 7009 because the allegations are based on information and belief.

The Trustee, for his part, argues that Paragraph 48 of the Complaint is sufficient to plead both fraud and fraud in the inducement claims. The ECF 1, ¶48 sets forth the following:

> Upon information and belief, in reliance on ERC's representation and the promise made in the Agreement that the payments to ERC pursuant to the terms of the Agreement would not be used to offset the monies due to ERC resulting from the Judgment or other monetary relief granted to it in the Delaware Action, Home Easy arranged for the payment to ERC of the License Commencement Fee ($3.6 million) and the first installment of the minimum guaranteed royalty payments ($500,000). Upon information and belief, ERC led Home Easy to believe that, if the proposed license agreement never materialized, ERC would return to Home Easy the $4.1 million because ERC promised that it would not use that money to offset the monies due under the Judgment, which was then on appeal, and there would be no other justification for ERC to keep the money.

The Court finds that the allegations in the Complaint, including Paragraph 48, are not sufficient under Fed. R. Civ. P. 8(a) or (9), made applicable to this proceeding via Fed. R. Bankr. P. 7008 and 7009 to set forth a claim for fraud in the inducement. Thus, to the extent the Trustee seeks to allege "fraud in the inducement" such claim is not specifically set forth in the Complaint and the Trustee must seek leave to amend the complaint to assert such claim. See *Frederico*, 507 F.3d at 202 ("It is axiomatic that the complaint may not be amended by the briefs in opposition to a motion to dismiss.")

However, as the Trustee has pointed out, in the bankruptcy context, trustees have been given more leeway when alleging fraud since they are outsiders to the allegedly fraudulent transactions:

> While Fed. R. Civ. P. 9(b) requires assertions of fraud to be plead with specificity, "[c]ourts have also noted that, in the bankruptcy context, Rule 9(b) should be interpreted liberally, particularly when the trustee, a third party outsider to the fraudulent transaction, is bringing the action." *In re MacGregor Sporting Goods, Inc.*, 199 B.R. 502, 514-15 (Bankr. D.N.J. 1995); *see also In re Fedders N. Am., Inc.*, 405 B.R. 527, 544 (Bankr. D. Del. 2009) (quoting *In re Harry Levin, Inc.*, 175 B.R. 560, 567 (Bankr. E.D. Pa. 1994) ("[t]his is because of the trustee's 'inevitable lack of knowledge concerning acts of fraud previously committed against the debtor, a third party' "); *In re Norvergence, Inc.*, 405 B.R. 709, 733 (Bankr. D.N.J. 2009) (quoting *In re Oakwood Homes Corp.*, 325 B.R. 696, 698 (Bankr. D. Del. 2005) (following the "Third Circuit's relaxed standard of applying Rule 9(b) that has been carved out for bankruptcy trustees who are pleading fraudulent transfer counts"). Because the Plaintiff is a liquidating trust established under the Debtors' Plan, it is appropriate to apply this relaxed standard to the S3 Lenders' motion.

*In re Nat'l Reality Inv. Advisors, LLC*, 2024 WL 74428, at *3.

In light of the more relaxed standard for the Trustee's claims and given the early stage of this litigation, dismissal of Count Four is premature.

Therefore, dismissal of Count Four for Fraud is denied without prejudice at this time, subject to the Trustee, within thirty (30) days from the date of this Opinion, filing a motion to

amend the Complaint to include a claim for fraud in the inducement. Issues of plausibility of the fraud and/or fraud in the inducement claims will be addressed at that time.

**Dismissal of Count Six (Conversion)**

To prove conversion, a plaintiff must show: "the tortfeasor exercised dominion over its money and repudiated the superior rights of the owner and such repudiation must be manifested in the injured party's demand for funds and the tortfeasor's refusal to return the monies sought." *Importers Serv. Corp. v. Aliotta*, No. 22CV4640-EP-JBC, 2024 WL 2765620, at *12 (D.N.J. May 30, 2024) (internal citations omitted).

Similar to Emerson's argument for dismissal of Court Four for Fraud, Emerson argues that Count Six for Conversion should be dismissed because such claim is barred under New Jersey's economic loss doctrine which bars plaintiffs from recovering in tort economic losses when their entitlement to recovery only flows from a contract. Emerson argues that the Trustee's claim for conversion as set forth in the Complaint results entirely from the Term Sheet and is not separate and distinct from the performance of the contract.

However, the Court finds the conversion claim has been plausibly pled and it would be premature to dismiss it at this time. "The Supreme Court of New Jersey has explained that, as to conversion, a plaintiff must allege that there was "some repudiation by the defendant of the owner's right, or some exercise of dominion over them by him inconsistent with such right, or some act done which has the effect of destroying or changing the quality of the chattel." *Dante*, 2022 WL 1104996, at *12 (quoting *Meisels*, 222 A.3d at 660). Further, a claim of conversion of money may be supported by showing the money belonged to the injured party and is identifiable. *Id*.

While ultimately Emerson may be able to defeat the Trustee's quasi-contract and tort

claims, this case is at the pleading stage and the Plaintiff is permitted to assert alternative and even inconsistent claims.

Therefore, the Motion to Dismiss Count Six for Conversion is denied without prejudice.

**Dismissal of Count Two (Breach of Contract)**

The Trustee asserts that Emerson breached its obligations under the Term Sheet because Emerson was required to either grant the Debtor a license agreement or refund the $4.1 million paid by Home Easy. Alternatively, the Trustee argues that if Emerson elected to not enter into the License Agreement with the Debtor, then it was obligated to return the $4.1 million, as that money was the consideration paid to it by the Debtor in connection with the License Agreement. Emerson argues that the Term Sheet expressly states that the fees are not refundable, and the Debtor breached the contract first by not paying the rest of the royalty fees. Emerson argues an express term of a contract trumps all implied terms.

However, "[u]nder New Jersey law, "[a] contract may be: (1) express, including oral or written[;] (2) implied-in-fact[;] and (3) implied-in-law." *Melone*, 2024 WL 1743108, at *11 (quoting *Scagnelli v. Schiavone*, 538 F. App'x 192, 193 (3d Cir. 2013)). The Court finds that the breach of contract claim has been plausibly pled. The Trustee has alleged there is a gap in the terms of the Term Sheet because there was never a final version of the licensing agreement. Based on the record before the Court at this early stage in the case, the Trustee has pled a plausible claim for breach of contract, and it would be premature to dismiss the breach of contract claim at this time. "Whether the parties acted in a manner sufficient to create implied contractual terms is a question of fact," and therefore, not appropriate for resolution at this stage absent a dearth of factual allegations. *Melone*, 2024 WL 1743108, at *11 (citing *Troy v. Rutgers*, 774 A.2d 476, 483 (N.J. 2001)).

Therefore, the Motion to Dismiss Count Two for Breach of Contract is denied without prejudice.

## V. CONCLUSION

For the reasons set forth herein, Emerson's Motion to Dismiss the Adversary Complaint is denied without prejudice.

The Trustee shall, within thirty (30) days from the date of this Opinion, file a motion to amend the Complaint to include a claim for fraud in the inducement. Issues of plausibility of the fraud and/or fraud in the inducement claims will be addressed at that time.

Counsel shall submit an Order in conformance with this Opinion.

Dated: April 29, 2025

Honorable Rosemary Gambardella
United States Bankruptcy Judge