IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

	:	CIVIL ACTION NO. 04-629
IN THE MATTER OF:	:	
EASTERN CONTINUOUS FORMS, INC.,	:	
Debtor.	:	
	:	
LAWRENCE J. LICHTENSTEIN, TRUSTEE,	:	
Plaintiff/Appellee,	:	
v.	:	
ADD B. ANDERSON, JR., and	:	
KEYBIS CORPORATION,	:	
Defendants/Appellants.	:	
	:	BANKRUPTCY NO. 00-31757

Opinion and Order

Newcomer, S.J. October 28, 2004

Presently before the Court is an appeal filed by Defendants/Appellants Keybis Corporation (“Keybis”) and Add B. Anderson, Jr. (“Add Anderson”) (collectively, “Defendants”), seeking to vacate judgment entered by the United States Bankruptcy Court for the Eastern District of Pennsylvania (“Bankruptcy Court”) in favor of Plaintiff/Appellee Lawrence J. Lichtenstein, Trustee of Eastern Continuous Forms (“ECF”). For the following reasons, the Bankruptcy Court’s Orders dated January 8, 2004 and March 2, 2004 are AFFIRMED. An appropriate Order follows.

I. BACKGROUND

Since the 1960's, Keybis was in the business of printing and selling business forms in Montgomery County, Pennsylvania. In 1995, Add Anderson, the sole shareholder of Keybis, decided to shop the company for sale. After shopping the company around to buyers in the industry ("strategic buyers"), the assets were eventually sold to a buyer from outside the industry ("financial buyer"). Financial buyer Philip Moseman ("Moseman") and his partner John Randolph, entered into negotiations with Add Anderson and his broker for the purchase of Keybis' assets. Moseman engaged in a due diligence investigation consisting of an evaluation of financial information, a tour of the plant, and discussions with Add Anderson about Keybis' customer base. During this shopping period, Moseman was prohibited from contacting Keybis' customers because Add Anderson wanted to avoid any deleterious effect on the existing account relationships if the sales transaction failed to occur. As a result of the prohibition on contacting existing customers, the Purchase Agreement contained various representations and warranties. The relevant provisions state that:

> [Keybis] enjoys good working relationships under all of its distributor, sales representative, broker and similar agreements necessary to the normal operation of its business

and that:

> [Keybis] has not . . . suffered any material

> adverse change in its working capital, condition, financial or otherwise, assets, liabilities, customer base, business operations or prospects.
>
> Purchase Agreement, at §§ N,H.

In exchange for the warranties, Keybis agreed to indemnify ECF for any such breach. See Purchase Agreement, at § 14.B. On August 31, 1997, Keybis and ECF entered into an asset purchase agreement ("Purchase Agreement") for the sale of substantially all of Keybis' assets. In addition to the Purchase Agreement, Add Anderson individually entered into a Consultation Agreement and a Noncompetition Agreement with ECF, for which he personally received $163,336.00.

Prior to the closing of the Purchase Agreement, Keybis' largest customer was UARCO, Inc. ("UARCO"), a long-standing customer that accounted for 28% of Keybis' sales. Because Moseman was prohibited from contacting UARCO, he relied on the representations and warranties as well as the indemnification clause to protect his investment. Before the closing in 1997, Moseman had engaged in discussions with Add Anderson and Alan Anderson (no relation), the Keybis salesperson in charge of the UARCO account, and at that time, no employee or agent of Keybis revealed anything to Moseman about UARCO's financial stability. Yet, James Anderson (no relation), one of Add Anderson's brokers, provided credible testimony that he discussed UARCO's financial situation with Add Anderson in June 1996. James Anderson testified that he told Add Anderson that UARCO was on the verge of bankruptcy, and went on to discuss the impact of a potential UARCO sale on the value of Keybis.

On December 31, 1997, Standard Register Company acquired UARCO’s American division, and a few months later ECF lost virtually all of the business previously done with UARCO. The termination of the ECF/UARCO relationship is at the center of this dispute. The Trustee asserts claims against Keybis for breach of representations and warranties essentially arguing (1) that Keybis had a basis of knowledge at the time of the sale that UARCO was financially unstable and would likely be sold, and (2) that Keybis was required to disclose this knowledge. The Trustee also asserted a claim against Add Anderson for participation in the breach. The Trustee sought indemnification. A trial was held in June 2003, and the Bankruptcy Court found both Keybis and Add Anderson liable. Judgment was entered on December 9, 2003. On January 8, 2003, the Bankruptcy Court issued a Second Amended Order reducing the amount of the judgment. On March 2, 2004, the Bankruptcy Court issued an Opinion and Order awarding Trustee fees, costs, and prejudgment interest. Defendants timely filed their Notice of Appeal to both Orders.

II. STANDARD OF REVIEW

This Court has jurisdiction over this appeal pursuant to 28 U.S.C. § 158(a)(1). A bankruptcy court’s factual findings may only be set aside if they are clearly erroneous. <u>See</u> <u>IRS v. Pransky</u>, 318 F.3d 536, 542 (3d Cir. 2003). A bankruptcy court's legal conclusions are subject to de novo review by the district court on appeal. <u>See id.</u> Finally, a bankruptcy court's exercise of discretion is reviewed for an abuse thereof. <u>In re Trans World</u>, 145 F.3d 124, 131 (3d Cir. 1998). An abuse of discretion exists where the court's decision rests upon a clearly erroneous finding of fact, an errant conclusion of law, or an improper application of law to fact. <u>International Union, UAW v. Mack Trucks, Inc.</u>, 820 F.2d 91, 95 (3d Cir. 1987).

III. DISCUSSION

A. <u>Fraudulent Concealment</u>

The Purchasing Agreement provides that ECF must initiate indemnification claims within one-year of the closing. <u>See</u> APA § 14(c). The limitation period "will not apply in the event of a judicial or arbitrators' determination of *fraudulent concealment* by the Seller." <u>Id.</u> at § 6(N) (emphasis added). Appellants argue that the phrase "fraudulent concealment" should be interpreted in accordance with its common law meaning, which generally operates to toll a statute of limitations rather than vitiate it altogether. In contrast, the Appellee contends the phrase should be interpreted to vitiate the one-year time limitation in the event of fraudulent concealment. This Court agrees with the Bankruptcy Court that the language in the APA's fraudulent concealment exception is latently ambiguous. Under such circumstances, it is the Court's responsibility to give effect to the intention of the contracting parties. See Mace v. Atlantic Refining & Marketing Corp., 785 A.2d 491, 496 (Pa. 2001); O'Farrell v. Steel City Piping Co., 403 A.2d 1319, 1324 (Pa. Super. 1979).

After a review of the plain language of the fraudulent concealment exception, the provision nullifies the one-year time limitation. The language of the provision reveals that the time-bar "*will not apply* in the event of a judicial or arbitrators' determination of fraudulent concealment by the Seller." Purchase Agreement at § 6(N) (emphasis added). The prohibitory language suggests that the time-bar would be cancelled in the event of fraudulent concealment. Appellants' application of "fraudulent concealment" to merely toll the limitation period is misplaced because this interpretation would not give meaning to all the terms of the contract, specifically the "will not apply" language.[1] In addition, if the fraudulent concealment exception in the APA was merely a tolling provision, its inclusion in the

[1] See In re Walnut Equip. Leasing Co., Inc., No. 97-19699DWS, 00-0864, 2003 WL 21262710, at *9 (Bankr. E.D. Pa. May 28, 2003) ("It is hornbook law that in construing a contract a court should give meaning to all its words and phrases and adopt a construction that avoids surplusage."); Wyoming Valley West Sch. Dist. V. Northwest Sch. Dist., 695 A.2d 949, 953 (Pa. Commw. Ct. 1997) ("[N]o provision of a contract should be treated as surplusage or redundant if any reasonable meaning consistent with other parts of the agreement can be given to it. . .").

agreement would be excessive and unnecessary.[2] Accordingly, this Court does not find any clear error of law in the Bankruptcy Court's reasoning.

B. Breach of Representations and Warranties in the Purchase Agreement

There is sufficient evidence to support a finding that Appellants concealed information, thereby breaching the Purchase Agreement warranty mandating disclosure of any material, adverse change in Keybis's customer base. See Purchase Agreement § 6(N). Appellants clearly had a "basis of knowledge" that a division of UARCO was about to be sold, which would affect a material portion of Keybis' normal business with UARCO. See Purchase Agreement at § 6(N). First, James Anderson testified that he informed Add Anderson of UARCO's impending sale.[3] Then, Add Anderson chose to retain a different broker and instructed the new broker to consider buyers who were not already in the business form printing industry (financial buyers).[4] At the insistence of Add Anderson and in return for the included contractual

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[2] Generally, the phrase "fraudulent concealment" refers to an implied equitable doctrine that serves to toll the running of a statute of limitations, rather than vitiating it altogether. See Matthews v. Kidder, Peabody & Co., Inc., 260 F.3d 239, 256 (3d Cir. 2001)(quoting Davis v. Grusemeyer, 996 F.2d 617, 624 (3d Cir. 1993)) ("Fraudulent concealment is an equitable doctrine [that] is read into every federal statute of limitations.").

[3] See Deposition of James Anderson at 41, 72.

[4] See Statement of Uncontested Facts at ¶ 15.

representations and warranties, ECF agreed not to perform a due diligence inquiry of any of Keybis's customers. (June 23, 2003 Tr. 9-10, 127.) Add Anderson's testimony was the only evidence to the contrary of these findings. After considering all of the evidence, the Bankruptcy Court properly found that, prior to the execution of the APA Appellants were aware that UARCO was likely to be sold. Clearly Appellants had "knowledge, or a basis for knowledge," as to UARCO's financial situation and probable sale. The failure to inform Appellee, as required by the APA, constituted a breach of a warranty. Accordingly, due to the Appellants' concealment of UARCO's instability, the one year time limitation pertaining to indemnification claims is inapplicable, and the present action was timely brought.

C. Participation Theory of Liability

The Bankruptcy Court correctly found that Defendant Add Anderson is personally liable for his willful misconduct. Under the participation theory of liability, a corporate officer may be held personally liable for participating in wrongful acts on behalf of the corporation. See Wicks v. Milzoco Builders, Inc., 470 A.2d 86, 93 (Pa. Super. 1983). Pennsylvania law recognizes the participation theory as a basis of liability for a corporate officer's misfeasance. See id. at 93; Village at Camelback Property Owners Ass'n v. Carr, 538 A.2d 528 (Pa. Super. 1988) (hereinafter "Village"). While often applied in tort actions, the participation theory has also been used "where the cause of action was a breach of contract." Newbridge Sec., Inc. v. Lloyd Sec., Inc., No. 90-3314, 1990 U.S. Dist. LEXIS 12856, at *6 (E.D. Pa. Sept. 28, 1990). The participation theory can be applied to impose individual liability on a corporate officer "for the breach of any promises or representations which he extends not in his capacity as an officer but personally in his individual capacity." Loeffler v. McShane, 539 A.2d 876, 879 (Pa. Super. 1988) (citing Village, 538 A.2d at 534). In this case, there is sufficient evidence to establish that Defendant Add Anderson extended promises in his individual capacity. In addition to the Purchase Agreement, he personally entered into separate consulting and non-competition agreements with ECF prior to closing. Based on these agreements, Defendant Anderson had a substantial, direct, and individual interest in the all of the agreements and therefore is subject to personal liability.[5] Accordingly, the Bankruptcy Court properly applied the participation theory to find Add Anderson personally liable for his willful misconduct.

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[5] As the sole shareholder of Keybis, he received 100% of the purchase and sale proceeds of Keybis. Under the three year consulting agreement, Anderson was to receive $4,166.00 per month. Under the non-competition agreement, Anderson was to receive $1,666.00 per month for a period of 60 months.

D. The Bankruptcy Court Did Not Err In Assessing Compensatory Damages

In assessing compensatory damages, the Bankruptcy Court did not abuse its discretion in admitting Mr. Wheeler's expert testimony, and did not err in its assessment of lost profit damages.

1. Mr. Wheeler's Testimony

Appellant contends that the Appellee's expert, Robert Wheeler ("Wheeler"), did not meet the minimum threshold for admissibility under Federal Rule of Evidence 702 and Daubert. Because the Appellant does not challenge the evidentiary issues concerning Wheeler's qualifications, but only the reliability of his testimony under Daubert, the Court need only resolve one issue. The Court finds that the Bankruptcy Court did not abuse its discretion in admitting the testimony.

Generally, an expert's opinion is reliable if it "based on the 'methods and procedures of science' rather than on 'subjective belief or unsupported speculation'; the expert must have 'good grounds' for his or her belief." In re Paoli R.R. Yard PCB Litig., 35 F.3d 717, 742 (3d Cir. 1994) (hereinafter "Paoli II") (quoting Daubert v. Merrell Dow Pharmaceuticals, Inc., 509 U.S. 579, 589 (1993). In this case, Wheeler is a certified turnaround professional, providing analytical services for troubled corporations. He holds a MBA from New York University and twenty-five years of experience in the management consulting field. While he has never done so in his professional career, Wheeler testified as to lost profits. According to Appellee, Wheeler's methodology was based on the same forecasting techniques to determine what a company's profits would be in the future. (Jun. 24, 2003 Tr. at 16.)

This Court finds that Wheeler's methodology itself was reliable and does fit the facts in calculating ECF's lost profits based on the applicable Daubert factors; however, it questions the assumptions underlying the methodology.[6] The Bankruptcy Court acknowledged that while the methodology "is likely to be fairly simple, it's the assumptions that may be problematic, the devil['s] in the details." (Jun. 24, 2003 Tr. at 19.) After Appellant's voir dire of Wheeler, the Bankruptcy Court noted that it too was sensitive to its gatekeeping function not to let in "voodoo science."[7] (Jun. 24, 2003 Tr. at 18.) Nevertheless, the gatekeeper function is not a substitute for testing the assumptions underlying the expert witness' testimony on cross-

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[6] (Jun. 24, 2003 Tr. at 26.) (Wheeler testifying that the contribution margin technique is "really the only technique to use in forecasting" and is "accepted by almost every major bank of the United States . . . ..").

[7] See Elock v. Kmart Corp., 233 F.3d 734, 746 (3d Cir. 2000) (quoting Kumho Tire Co., Ltd. v. Carmichael, 526 U.S. 137, 152 (1999) (noting that "Daubert's gatekeeping requirement . . . make[s] certain that an expert, whether basing testimony upon professional studies or personal experience, employs in the courtroom the same level of intellectual rigor that characterizes the practice of an expert in the relevant field . . .. [T]he trial judge must have considerable leeway in deciding in a particular case how to go about determining whether particular expert testimony is reliable.").

examination. See United States v. Mitchell, 365 F.3d 215, 245 (3d Cir. 2004) (quoting Stecyk v. Bell Helicopter Textron, Inc., 295 F.3d 408, 414 (3d Cir. 2002)) (explaining that "[a] party confronted with an adverse expert witness who has sufficient, though perhaps not overwhelming, facts and *assumptions* as the basis for his opinion can highlight those weaknesses through effective cross-examination.") (emphasis added). Therefore, Appellant was on notice to elicit the weaknesses of the assumptions underlying Wheeler's expert testimony. Appellant was ultimately successful in discrediting these assumptions given the Bankruptcy Court's conclusion that "Mr. Wheeler's testimony as to lost profits was most unpersuasive, and . . . [that Court] accorded it virtually no probative weight." (Opin. at 33). While Appellant wishes that the Bankruptcy Court had excluded it, the argument turns more on the weight of the evidence than the admissibility of the testimony. Therefore, because the methodology was reliable and the Bankruptcy Court had good grounds to admit the testimony, this Court concludes that the trial court did not abuse its discretion.

2. The Bankruptcy Court Did Not Err in Its Assessment of Lost Profit Damages.

The Bankruptcy Court did not err in its assessment of the time period for lost profit damages. Generally, a bankruptcy court's award of damages may only be disturbed if it is found to be clearly erroneous. See In re B. Cohen & Sons Caterers, Inc., 108 B.R. 482, 485 (E.D. Pa. 1989). In this case, Appellants argue that the Bankruptcy Court erred in projecting UARCO lost profits for an additional year. Appellant's expert witness, David Glusman ("Glusman"), performed a three-year calculation, while Wheeler used five years. Wheeler's five-year projection was based on the duration of the Non-Competition Agreement and bank loan in connection with the Purchase Agreement. This Court does not find any evidence in the record for why Glusman used a three-year analysis. The Bankruptcy Court attempted to discern a reasonable time period to project lost profits given the conflicting expert testimony, and found that a four-year period is a reasonable period since it split the difference between the expert opinions. Thus, because neither Party has cited any case law or statutory authority to suggest that the duration of a lost profit projection is a legal issue, the Bankruptcy Court's determination is not clearly erroneous.

Appellants further argue that the Court erred in substituting Year 1999 lost profits in place of Year 1998 lost profits. Without recounting the specifics of Glusman's regression analysis, he calculated a projected UARCO sales shortfall by subtracting the year's actual sales from the year's projected UARCO sales.[8] The Bankruptcy Court essentially disregarded Year 1998 because it understated the effect of the loss of UARCO business had on ECF. That Court noted that the primary reason why UARCO actual sales were so high, as compared to Years 1999 and 2000, was because the large majority of UARCO sales in 1998 preceded the year-end sale of one of UARCO's divisions. After the sale, the actual UARCO sales decreased. The post-sale figures are the most relevant for purposes of calculating damages because Appellants should have disclosed their knowledge regarding the sale of UARCO. In its final analysis, the Bankruptcy Court applied the 1999 Net Loss amount for both Years 1998 and 1999, and the 2000 Net Loss amount for 2000 and 2001. This Court finds that this was a reasonable damages award and not clearly erroneous given that these substitutions were made to account for the damages resulting from the immediate loss to ECF after the sale of UARCO to Standard Register.

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[8]

Fiscal Year	Projected UARCO sales	Actual UARCO sales	Projected UARCO shortfall	Projected UARCO Net Loss
1998	$ 2,261,200	$1,284,720	$ 976,480	$ 85,586
1999	$ 2,397,200	$129,057	$ 2,268,143	$ 198,797
2000	$ 2,533,200	$128,900	$ 2,531,911	$ 221,916
3 Year Total				$ 506,299

E. The Bankruptcy Court Did Not Abuse Its Discretion In Awarding Prejudgment Interest to Plaintiff.

In its Opinion, the Bankruptcy Court found that the award of prejudgment interest is discretionary. This legal determination has support in Pennsylvania law. See Melley v. Pioneer Bank, N.A., 834 A.2d 1191, 1204 (Pa. Super. 2003) (quoting Kaiser v. Old Republic Ins. Co., 741 A.2d 748, 755 (Pa. Super. 1999) (noting that "[Pennsylvania's] courts have generally regarded the award of prejudgment interest as not only a legal right, but also as an equitable remedy awarded to an injured party at the discretion of the trial court."). Consequently, this Court will review the Bankruptcy Court's reasoning for the discretionary award under an abuse of discretion standard.

In determining whether discretionary prejudgment interest is appropriate, the Pennsylvania Supreme Court has found that the finder of fact must consider all the circumstances of the case. See Marrazzo, 263 A.2d at 337. According to that Court, "one important element" is whether the fault for nonpayment rests with the defendant or the plaintiff. See Frank B. Bozzo, Inc. v. Electric Weld Div. of Ft. Pitt Div. of Spang Industries, Inc., 498 A.2d 895, 900 (Pa. Super. 1985) (citing Marrazzo). The Court in Marrazzo explained this element as follows:

> If the fault in nonpayment of the claim rests with the defendant he cannot complain if he is required to compensate for the delay. If on

> the other hand the fault lies with the plaintiff by reason of an excessive and unconscionable demand, one which the defendant is required to protect himself against by litigation, he should not be penalized for the unwarranted conduct of the plaintiff and required to pay damages for the delay in the settlement of the claim. . . . The burden of proving that the demand was unreasonable is upon the defendant.
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> Marrazzo, 263 A.2d at 338 (emphasis added)(in-vernal citations omitted).

In this case, Defendants have not satisfied their burden that the demand was unreasonable. While the demand was significantly higher than the actual judgment, nothing in the record demonstrates that Defendants made settlement counteroffers in line with the amount of the verdict or that they were inclined to settle at all. See Mar. 2, 2004 Opinion at 11. Nevertheless, Plaintiff is not entirely without fault in light of its high damage demands. Therefore, this Court finds that because both parties are somewhat at fault for nonpayment, Defendants have not satisfied their burden to show that the demand was unreasonable. Moreover, the equities favor granting prejudgment interest to make the Plaintiff whole. For the above reasons, the Bankruptcy Court's award is affirmed.

F. The Bankruptcy Court Did Not Abuse Its Discretion In Awarding Plaintiff Reasonable Fees and Costs.

Appellants claim that the Bankruptcy Court abused its discretion in awarding the Trustee $19,506.40 in fees and costs for Mr. Wheeler, the Trustee's expert. See id. at 16-7.

Appellants do not dispute that their indemnity obligation under the Agreement excludes expert fees, but instead object on the basis that Mr. Wheeler's testimony was insufficiently reliable. This Court finds that Mr. Wheeler's fee testimony was, on the whole, of some assistance to the Bankruptcy Court, particularly in aiding that Court to determine the number of years necessary to calculate lost profits. See Dec. 9, 2003 Opin. at 35 (discussing the Court's splitting the difference between the experts' opinions and ultimately choosing a four (4) year period as a factor in calculating damages). Thus, this Court finds there was no abuse of discretion here.

IV. CONCLUSION

The Court affirms the Bankruptcy Court's findings. An appropriate Order follows.

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

	CIVIL ACTION NO. 04-629
IN THE MATTER OF: EASTERN CONTINUOUS FORMS, INC., Debtor.	
LAWRENCE J. LICHTENSTEIN, TRUSTEE, Plaintiff/Appellee, v. ADD B. ANDERSON, JR., and KEYBIS CORPORATION, Defendants/Appellants.	BANKRUPTCY NO. 00-31757

O R D E R

AND NOW, this 28th day of October, 2004, upon consideration of Brief of Appellants (Doc. 7), Brief of Appellee, and Appellants’ Reply, it is hereby ORDERED that the Bankruptcy Court’s Second Amended Order dated January 8, 2004, and Order dated March 2, 2004 are AFFIRMED.

AND IT IS SO ORDERED.

s/____________________________
Clarence C. Newcomer, S.J.