**NOT FOR PUBLICATION**

# UNITED STATES BANKRUPTCY APPELLATE PANEL FOR THE FIRST CIRCUIT

---

**BAP NO. NH 05-047**

---

**Bankruptcy No. 04-14151-JMD**

---

**ROBOTIC VISION SYSTEMS, INC. (n/k/a ACUITY CiMATRIX, INC.) and AUTO IMAGE ID, INC.,**
**Debtors.**

---

**PAT V. COSTA,**
**Appellant,**
**v.**
**ROBOTIC VISION SYSTEMS, INC. (n/k/a ACUITY CiMATRIX, INC.), AUTO IMAGE ID, INC., UNITED STATES TRUSTEE, INTEL CORPORATION, MIDDLEFIELD VENTURES LLC, and STEVEN M. NOTINGER, Chapter 7 Trustee,**
**Appellees.**

---

**Appeal from the United States Bankruptcy Court for the District of New Hampshire (Hon. J. Michael Deasy, U.S. Bankruptcy Judge)**

---

**Before**
**Lamoutte, Haines and Carlo, United States Bankruptcy Appellate Panel Judges.**

---

**Charles A. Dale, III, Esq., David Himelfarb, Esq., and Elisabeth Schreuer, Esq. on brief for Appellant.**

**Olga L. Bogdanov, Esq. on brief for Appellee, Steven M. Notinger, Chapter 7 Trustee.**

**James F. Raymond, Esq., Kathryn A. Coleman, Esq., and Craig A. Bruens, Esq., on brief for Appellees, Intel Corporation and Middlefield Ventures, Inc.**

---

**April 11, 2006**

---

**Per Curiam.**

This is an appeal by Pat V. Costa ("Costa"), the former Chief Executive Officer and Chairman of the Board of the debtors, Robotic Vision Systems, Inc. and Auto Image ID, Inc. (the "Debtors"), from the bankruptcy court's order approving a settlement agreement ("Settlement Agreement") between the Official Committee of Unsecured Creditors (the "Committee"), and Intel Corporation and its subsidiary, Middlefield Ventures Inc. (collectively, "Intel"), secured creditors of the Debtors. Costa argues that the bankruptcy court abused its discretion by approving the Settlement Agreement because the agreement violated the priority scheme for distribution of estate property set forth in the Bankruptcy Code[1] by compromising assets in such a way that general, unsecured creditors were paid ahead of secured creditors, including Costa; and the Committee had not met its burden of proving that the settlement was reasonable and in the best interests of the Debtors' estates.

We conclude that the bankruptcy court failed to make adequate findings of fact and conclusions of law, thus precluding appellate review. Accordingly, for the reasons set forth below, we vacate the order approving the Settlement Agreement and remand for further proceedings consistent with this opinion.

## BACKGROUND

In April, 2003, the Debtors entered into a settlement agreement with Intel which provided, among other things, for the Debtors' release of certain claims against Intel, and Intel's

[1] All references to the "Bankruptcy Code" or to specific sections are to the Bankruptcy Reform Act of 1978, as amended prior to April 20, 2005, 11 U.S.C. § 101, et seq.

payment of $1 million to the Debtors.[2] In connection with the settlement, Intel agreed to loan the Debtors $4 million in two tranches to fund their operations. In addition, Costa agreed to subordinate his rights to payment from the Debtors until Intel's indebtedness was paid in full.[3]

Intel made an initial $2 million loan to the Debtors in April, 2003. In November, 2003, the Debtors entered into a credit and security agreement with RVSI Investors, LLC ("RVSI Investors"), which provided for revolving loans and other financial accommodations. In December, 2003, the Debtors requested Intel to make the second $2 million loan, asserting that they had satisfied certain conditions required under the loan documents. Intel refused, alleging violations of certain confidentiality provisions of the settlement agreement. Although the Debtors claimed that the alleged violations did not excuse Intel's obligation to make the second $2 million loan, they did not pursue any legal action against Intel. In April, 2004, the Debtors went "out of formula" under the loan agreement with RVSI Investors and in November, 2004, RVSI Investors called a default.

Shortly thereafter, the Debtors filed Chapter 11 petitions, and the United States Trustee duly appointed the Committee. As of the bankruptcy filing, the Debtors' principal secured creditors were (1) RVSI Investors, holding senior secured pre-petition claims arising from an extension of credit; (2) Intel, holding second priority secured pre-petition claims arising from the

---

[2] At trial, the Committee's counsel stated that the agreement "settled a long litany of claims by the debtor against Intel with respect to Intel's alleged interference with the business of [the debtor] and other claims."

[3] Costa's subordinated indebtedness included a loan evidenced by a convertible note executed on December 4, 2002, in the principal amount of $500,000.

first $2 million tranche, and (3) Costa, holding third priority secured pre-petition claims arising from a $500,000 convertible loan.

Although the Debtors were authorized to use cash collateral, they still needed new funding, and Intel agreed to loan them $2 million. The bankruptcy court entered an order approving the debtor-in-possession loan on February 17, 2005 ("DIP Order"). As a precondition to receipt of the loan, both the Debtors and Costa, in his individual capacity, released Intel from all claims arising out of the pre-petition relationship between Intel and the Debtors.[4] Although the Debtors released their claims against Intel, the DIP Order authorized the Committee to assert all of the Debtors' pre-petition "Claims and Defenses" (as defined in the order) against Intel.[5] The parties dispute whether this provision constituted an *assignment* to the Committee of the Debtors' pre-petition claims against Intel, or whether it simply conferred *standing* upon the Committee to pursue those claims on behalf of the Debtors' estates.

After an investigation, the Committee determined that the Debtors possessed various causes of action against Intel. Because many of the other possible claims against Intel pre-dated the Debtors' April, 2003 release, the primary claim against Intel stemmed from its failure to lend the second $2 million tranche in December, 2003. After extensive negotiations, the parties entered into the Settlement Agreement resolving their dispute. Pursuant to the Agreement, Intel agreed that:

---

[4] The Debtors' release was included in the DIP Order. Costa's release was made pursuant to a separate document.

[5] The DIP Order required the Committee to investigate any such claims and to commence an action against Intel by February 23, 2005, or any such claims would be waived. This time was extended by an agreement of the parties.

> [A]ny and all net proceeds of the sale, refinancing or other disposition of assets of the Debtors or other entity whose assets are subject to Intel's security interest . . . shall be paid, unless otherwise directed by the Court, to the Creditors' Committee for the benefit of allowed administrative, priority and unsecured creditors. Upon entry of the Bankruptcy Court's order approving this Agreement, the Pre-Petition Indebtedness shall be deemed forgiven and Intel shall have no right to payment on account of the Pre-Petition Indebtedness.

In exchange for Intel's assignment or waiver of its pre-petition secured claim, the Committee and the Debtors agreed to release all pre-petition claims against Intel.

The Committee filed a motion seeking bankruptcy court approval of the Settlement Agreement, and Costa objected. The Debtors and RVSI Investors also filed limited objections which were ultimately resolved. The bankruptcy court held a hearing on the Settlement Agreement and at the conclusion of the hearing, the court stated:

> All right. Well, I want to look at this a little bit more and – and read some of these documents that I haven't had a chance to look at, but now, based on these arguments, I have some better idea of what to look at and can do it somewhat more efficiently, and, hopefully, the two-day trial the end of this week is going away, so that should give me some time to get to it.

Thereafter, the bankruptcy court issued an order approving the Settlement Agreement ("Settlement Order"). The Settlement Order does not address Costa's objections, but merely states that "the relief requested in the Motion and the terms of the Settlement Agreement are in the best interests of the Debtors, their estates, and creditors." Costa appealed.

In October, 2005, the Debtors' bankruptcy case was converted to Chapter 7, and Steven M. Notinger ("Trustee") was appointed as the Chapter 7 Trustee. Thereafter, the Panel entered an order substituting the Trustee for the Committee as appellee in this appeal.

## JURISDICTION

A bankruptcy appellate panel is duty-bound to determine its jurisdiction before proceeding to the merits even if not raised by the litigants. See In re George E. Bumpus, Jr. Constr. Co., 226 B.R. 724 (B.A.P. 1st Cir. 1998). A bankruptcy appellate panel may hear appeals from "final judgments, orders and decrees [pursuant to 28 U.S.C. § 158(a)(1)] or with leave of the court, from interlocutory orders and decrees [pursuant to 28 U.S.C. § 158(a)(3)]." Fleet Data Processing Corp. v. Branch (In re Bank of New England Corp.), 218 B.R. 643, 645 (B.A.P. 1st Cir. 1998). "A decision is final if it 'ends the litigation on the merits and leaves nothing for the court to do but execute the judgment.'" Id. at 646 (citations omitted). A bankruptcy court's order approving a settlement or compromise is a final order. See Pawtucket Credit Union v. Haase (In re Haase), 306 B.R. 415, 418 (B.A.P. 1st Cir. 2004); Beaulac v. Tomsic (In re Beaulac), 294 B.R. 815, 818 (B.A.P. 1st Cir. 2003).

## STANDARD OF REVIEW

Appellate courts generally apply the clearly erroneous standard to findings of fact and *de novo* review to conclusions of law. See TI Fed. Credit Union v. DelBonis, 72 F.3d 921, 928 (1st Cir. 1995); Western Auto Supply Co. v. Savage Arms, Inc. (In re Savage Indus., Inc.), 43 F.3d 714, 719-20 n.8 (1st Cir. 1994). The approval of a compromise is within the sound discretion of the bankruptcy court, and a reviewing court will not overturn a decision to approve a compromise absent a clear showing that the bankruptcy court abused its discretion. See Jeffrey v. Desmond, 70 F.3d 183, 185 (1st Cir. 1995); see also ARS Brook, LLC v. Jalbert (In re ServiSense.com, Inc.), 382 F.3d 68, 71 (1st Cir. 2004); In re Anolik, 107 B.R. 426, 429 (D. Mass. 1989) (collecting cases). "Of course, if we determine 'that a bankruptcy court's findings are too

indistinct, [we] may decline to proceed further and remand for more explicit findings.'" Groman v. Watman (In re Watman), 301 F.3d 3, 8 (1st Cir. 2002) (quoting Brandt v. Repco Printers & Lithographics, Inc. (In re Healthco Int'l, Inc.), 132 F.3d 104, 108 n.5 (1st Cir. 1997)).

## DISCUSSION

The bankruptcy court had to determine whether the Settlement Agreement violated the bankruptcy priority scheme for distribution of estate property, by allowing the general, unsecured creditors to receive money while bypassing Costa's alleged secured claim. If the court concluded that the Settlement Agreement did not offend the priority scheme, the court had to determine whether the Settlement Agreement was fair and equitable.

If a security interest is properly perfected, this interest must be satisfied from the property it encumbers, before any proceeds from the sale of that property are made available to unsecured claimants. See Unsecured Creditors' Committee v. Stern (In re SPM Mfg. Corp.), 984 F.2d 1305, 1312 (1st Cir. 1993). Parties in a bankruptcy proceeding may not avoid the distribution scheme by private agreement. In re CGE Shattuck, LLC, 254 B.R. 5, 11 (Bankr. D.N.H. 2000). Costa argues that the Settlement Agreement violated the distribution scheme by compromising assets in such a way that unsecured creditors were paid ahead of secured creditors, including Costa. The Trustee contends that the agreement did not violate the distribution scheme because (i) Costa did not hold a perfected lien that must be satisfied from the proceeds of the Claims and Defenses against Intel, and (ii) he was not entitled to any proceeds from the Claims and Defenses because he released all individual claims against Intel, and subordinated his pre-petition claim to that of Intel.

The bankruptcy court made no determination as to whether the Settlement Agreement complied with the distribution scheme. Likewise, the court made no findings as to whether Costa has a perfected lien, nor whether a purported lien by Costa would attach to the Intel proceeds because of the nature of his lien or in spite of his release and subordination.

If the bankruptcy court determined that the Settlement Agreement did not violate the distribution scheme, the court had to determine whether the Settlement Agreement was fair and equitable. A bankruptcy judge approves the compromise of a claim pursuant to Bankruptcy Rule 9019(a).[6] The bankruptcy court considers the following factors when deciding whether to approve a settlement or compromise: (i) the probability of success in the litigation being compromised; (ii) the difficulties, if any, to be encountered in the matter of collection; (iii) the complexity of the litigation involved, and the expense, inconvenience and delay attending it; and, (iv) the paramount interest of the creditors and a proper deference to their reasonable views in the premise. See Jeremiah v. Richardson, 148 F.3d 17, 23 (1st Cir. 1998) (quoting Jeffrey, 70 F.3d at 185). The court's consideration of these factors should demonstrate whether the compromise is fair and equitable, and whether the claim the debtor is giving up is outweighed by the advantage to the debtor's estate. See id. Generally, a bankruptcy judge's failure to consider the four factors would be grounds for finding that the bankruptcy judge abused his discretion. In re Anolik 107 B.R. at 429.

---

[6] Bankruptcy Rule 9019(a) provides:

> On motion by the trustee and after a hearing on notice to creditors, the debtor and indenture trustees as provided in Rule 2002(a) and to such other entities as the court may designate, the court may approve a compromise or settlement.

Costa argues that the factual record presented by the Committee was insufficient to show that the Settlement Agreement was fair and equitable. At the hearing on the Settlement Agreement, the bankruptcy court asked probing questions and clearly demonstrated an understanding of the factors which are considered when deciding whether to approve a compromise. Nonetheless, the court did not make findings on all of the factors at the hearing. At the conclusion of the hearing, it was likewise clear that the court had not made a decision as to whether to approve the Settlement Agreement, specifically indicating that the matter would be given further consideration at a later date. Thereafter, the bankruptcy court issued the Settlement Order, which includes no findings nor conclusions, except the statement that the Settlement Agreement is in the best interests of the Debtors, their estates, and creditors.

As a reviewing court, the Panel lacks factual findings and a record from which we can make a determination as to whether approval of the Settlement Agreement is in error or an abuse of discretion. The Panel can not infer reasons for the result nor can we substitute our factual findings for those of the trial court. Under similar circumstances reviewing courts have remanded for further development of the record and for a statement of reasons for approval. See, e.g., Continental Illinois Nat'l Bank & Trust Co. v. Widett, Slater & Goldman, P.C., 47 B.R. 925, 927 (D. Mass. 1985) (remanding to bankruptcy court for further development of the record and for a statement of reasons for approval of compromise); see also Bezanson v. Thomas (In re R&R Assocs. of Hampton), 402 F.3d 257, 264 (1st Cir. 2005) ("If . . . we determine that the bankruptcy court findings are too vague or incomplete to enable meaningful appellate review, we may remand to the bankruptcy court for further proceedings and more explicit findings of fact."); In re Watman, 301 F.3d at 8; In re Healthco, 132 F.3d at 108.

We regretfully find that the bankruptcy court's factual findings and legal conclusions are incomplete. Accordingly, we will remand this case to the bankruptcy court for explicit findings.

## CONCLUSION

For the reasons stated herein, we vacate and remand for further proceedings consistent with this opinion. The bankruptcy court may take more evidence if it deems necessary to carry out this mandate. We do not retain jurisdiction over this proceeding.