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UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEW JERSEY

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| In re:<br><br>CLOUDEEVA, INC., *et al.*,[1]<br><br>Debtors. | Chapter 11<br><br>Case No. 14-24874 (KCF)<br><br>(Jointly Administered) |

**REPLY MEMORANDUM OF LAW IN FURTHER SUPPORT OF THE MOTION OF BARTRONICS ASIA PTE LTD. FOR ENTRY OF AN ORDER (I) DIRECTING THE APPOINTMENT OF A CHAPTER 11 TRUSTEE OR, IN THE ALTERNATIVE, (II) DISMISSING THE CHAPTER 11 CASES**

[1] The Debtors in these Chapter 11 Cases, along with the last four digits of each Debtor's tax identification number, are: Cloudeeva, Inc., a Delaware corporation (5326), and Cloudeeva, Inc., a Florida corporation (2227). The corporate headquarters of Cloudeeva, Inc., a Delaware corporation are located at 104 Windsor Center Drive, Suite 300, East Windsor, New Jersey 08520.

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Bartronics Asia Pte. Ltd. ("**BAPL**"), by and through its undersigned counsel, respectfully submits this reply in further support of its *Motion for Entry of an Order (I) Directing the Appointment of a Chapter 11 Trustee or, In the Alternative, (II) Dismissing The Chapter 11 Cases* [Docket No. 96] (the "**Motion**").[2]

## PRELIMINARY STATEMENT

1. If these Cases are to continue in Chapter 11, a trustee must be appointed because Adesh Tyagi has proven that he is unfit to serve as a fiduciary to the Debtors, their creditors, shareholders, and other stakeholders (including employees and contractors). Among other things, Tyagi has failed to comply with his fiduciary obligations by misappropriating company funds for his own personal use, diverting customers to a related company under his direct or indirect control, and grossly mismanaging the business in such a way that it is now reliant on factoring accounts receivable to meet its payroll obligations.

2. Notwithstanding this and other egregious conduct, in opposition to BAPL's request for the appointment of a trustee, the Debtors beseech this Court to grant current management a "second chance" to correct pre-petition "mistakes" and "errors in judgment." At the same time, however, the Debtors concede that they are transferring customers to Systems America, a competing company controlled by Tyagi's wife, purportedly to alleviate customer uncertainty resulting from the commencement of these Cases.[3] Thus, by the Debtors' own admission, Tyagi is taking advantage of the customer unease caused by the Chapter 11 filings by transferring customer contracts to Systems America—without full disclosure or the approval of this Court—thereby creating a windfall for Tyagi's family at the expense of the Debtors' estates.

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[2] Capitalized terms not defined herein shall have the meaning ascribed to them in the Brief in Support of Motion of Bartronics Asia Pte Ltd. for Entry of an Order (I) Directing the Appointment of a Chapter 11 Trustee or, In the Alternative, (II) Dismissing The Chapter 11 Cases [Docket No. 45]

[3] [redacted]

For this reason and others, if these Cases remain in Chapter 11, a trustee must be appointed to protect the Debtors' business from Tyagi's blatant conflict of interest.

3. However, in the weeks since the Cases were commenced, it has become clear to BAPL that the best interests of creditors, shareholders, and the Debtors' estates will not be served by continuing in Chapter 11 (even under the supervision of a trustee), but only by dismissal of these Cases in their entirety. As Debtors' counsel advised this Court at the first day hearing (and as BAPL agrees), "at the end of the day, what we have here is a difficult shareholder dispute." That dispute was set to be tried this month in a California JAMS arbitration after nearly a year of costly motion practice and discovery.[4] The California Superior Court overseeing the arbitration was set to hear BAPL's motion to appoint a receiver to take control of Cloudeeva Delaware the morning after these Cases were commenced. Thus, it could not be more clear that these Cases were filed as a strategic maneuver by which Tyagi went shopping for what he perceived to be a more favorable forum (*i.e.*, a forum less familiar with his mismanagement and other misconduct) in which to litigate a two-party dispute that was on the verge of resolution in California, with the likely outcome that Tyagi would have been removed from his position of control over Cloudeeva Delaware.

4. Rather than submitting any credible evidence demonstrating that these Cases serve a legitimate bankruptcy purpose, the Debtors rely almost exclusively on a single paragraph in Mr. Tyagi's First Day Declaration, in which he contends that these filings were necessitated by the costs of litigating with BAPL, and "the California State Court's severe restrictions on the Debtors' ability to factor receivables." Opp. at 26. However, neither the costs of litigation nor the Debtors' desire to factor receivables justifies the continuation of these Cases. While the

[4] See Supplemental Declaration of Elizabeth Pappy, ¶¶ 6-14.

Debtors have removed the California Action and moved to transfer it to this Court, their assertion that the California Action can "be resolved in the context of negotiation of a chapter 11 plan of reorganization, a much more economical and efficient means," is patently absurd. Opp. at 1. The California arbitration was set to conclude this week, with a decision to be entered shortly thereafter. As a result of these Chapter 11 filings, the arbitration has been stayed indefinitely; indeed, the Debtors' motion to transfer the removed California Action to this Court is not even scheduled to be heard until September 8, 2014. Rather than orchestrating an efficient resolution of Tyagi's disputes with BAPL, these Cases have instead re-started the clock on a matter that has been litigated (at great cost to all parties) for nearly a year, causing indefinite delay and giving rise to additional motion practice and the retention of additional lawyers. Moreover, the Debtors have failed to adequately address the critical question of whether, even if their motion to transfer the California Action to this Court is granted, this Court will be a proper forum in which to litigate a state law dispute that the parties are bound by contract to submit to arbitration.[5]

5. Likewise, although the Debtors' claimed need for additional factoring is evidence of Tyagi's gross mismanagement (as the company never resorted to factoring when it was controlled by BAPL), that need did not justify the commencement of these Cases, as there are no provisions of the Bankruptcy Code that give a company any greater right to factor receivables than it would have outside of bankruptcy. Had the Debtors complied with the terms by which the California Court permitted them to factor, including by submitting to complete transparency and disclosure to BAPL, these Cases could have been avoided. Indeed, had the Debtors demonstrated a legitimate need for factoring in order to meet payroll prior to commencing these Cases, and had they complied with the disclosure requirements imposed by the California Court,

[5] In the event that this Court does not dismiss these Cases, BAPL intends to file a motion for relief from stay requesting that the Court abstain in order to allow the California arbitration to go forward.

BAPL would have negotiated with the Debtors to ensure that payroll obligations continued to be met, just as BAPL has done in the weeks since these Cases began.

6. Contrary to the Debtors' nonsensical assertion that BAPL is somehow engaged in strategic maneuvering to "destroy the Debtors' operations at any cost" (Opp. at 25), the business that Tyagi is currently mismanaging is a business that BAPL built. BAPL has been working for nearly a year—through the California Action and arbitration, and now in this Court—to take back that business by rescinding the fraudulently induced Stock Exchange Agreement that Tyagi used as a foothold to lock out BAPL and illegally gain unilateral control of the business and its resources. BAPL has not actively pursued its rescission claim at great cost and to the brink of trial only to regain a valueless asset. Nonetheless, instead of working with BAPL to protect and preserve the company's business, the Debtors blatantly disregarded the California Court's orders, leading that Court to express concern that "some of the amounts generated [by factoring] were used for a purpose other than paying billable employees and administration."[6] The Debtors should not be permitted to use their own violation of the California Court's orders to justify the filing and continuation of these Cases, which serve no recognized bankruptcy purpose.

7. As explained below, the tools of the Bankruptcy Code will provide no benefit to these Debtors. To the contrary, and by the Debtors' own admission, the filing of these Cases has harmed the company's business, as customers have become skittish and threatened to terminate (or actually terminated) their relationships with the Debtors. Nor does it appear that the Debtors will be able to propose a viable plan and emerge from bankruptcy, causing grave concerns about the possibility that, ultimately, the continuation of these Cases will lead to a liquidation of the Debtors' business. It is in the best interest of not only BAPL, as the majority shareholder of

[6] See Exhibit 43 to the Declaration of Venkata Putta submitted on August 4, 2014 in support of the Motion.

Cloudeeva Florida and as a creditor of Cloudeeva Delaware, but of all creditors, shareholders and the Debtors' estates, that the business remains viable. Dismissal is the best and only path to that outcome. If the Court dismisses these Cases, BAPL intends to immediately renew its motion for the appointment of a receiver in the California Court to protect the business pending the outcome of the arbitration proceeding.[7]

**ARGUMENT**

**I. These Cases Were Not Filed in Good Faith and Should Be Dismissed**

8. As set forth in BAPL's opening brief in support of the Motion, Bankruptcy Code Section 1112(b) provides that "on request of a party in interest, and after notice and a hearing, the court shall convert a case under this chapter to a case under chapter 7 or dismiss a case under this chapter, whichever is in the best interests of creditors and the estate, for cause." 11 U.S.C. § 1112(b). The Debtors concede that "in the absence of good faith, a court may find cause to dismiss under section 1112(b)." Opp. at 25. Courts in this Circuit focus on two overlapping factors in determining whether Chapter 11 cases were filed in good faith: (i) whether the petition was filed merely to obtain a tactical advantage in existing litigation; and (ii) whether it serves a valid bankruptcy purpose. NMSBPCSLDHB, L.P. v. Integrated Telecom Express, Inc. (In re Integrated Telecom Express, Inc.), 384 F.3d 108, 119-20 (3d Cir. 2004). Both factors weigh in favor of dismissal of these Cases.

[7] BAPL will not respond here to the Debtors' baseless accusations of misconduct by BAPL, as BAPL's conduct is not at issue on this Motion. BAPL respectfully refers to the Declaration of Venkata Putta submitted with the Motion for a response to at least certain of the Debtors' unsupported and irrelevant allegations. BAPL reserves the right to more fully address the Debtors' allegations at an appropriate time.

**A. The Debtors Commenced These Cases to Gain a Tactical Advantage in Litigating a Two-Party Shareholder Dispute.**

9. It is well settled that "[f]iling a Chapter 11 petition merely to obtain tactical litigation advantages is not within the legitimate scope of the bankruptcy laws." Cross-Appellees in 09-1432 v. BEPCO, LP (In re 15375 Mem'l Corp.), 589 F.3d 605, 625 (3d Cir. 2009) (citation omitted) (internal quotation marks omitted). Therefore, dismissal of a Chapter 11 case is appropriate under 11 U.S.C. § 1112(b) where, as here, "a debtor's reorganization effort involves essentially a two-party dispute resolvable in [another] court . . . ." In re LEASE-A-FLEET, No. 93-5475, 1995 U.S. Dist. LEXIS 18607, at *14 (E.D. Pa. Dec. 14, 1995) (citation omitted). Indeed, as another New Jersey Bankruptcy Court has recognized, "[g]enerally, where a debtor's reorganization effort involves essentially a two party dispute resolvable in state court, and the filing for relief under the Bankruptcy Code is intended to frustrate the legitimate efforts of creditors to enforce their rights against the debtor, dismissal for 'cause' is warranted." In re Ravick Corp., 106 B.R. 834, 844 (Bankr. D.N.J. 1989); see also Advanced Restoration Techs., Inc. v. Shortgrass, Inc., Civ. No. 05-2978 (JLL), 2006 U.S. Dist. LEXIS 22208, at *19-21 (D.N.J. Mar. 30, 2006) (affirming dismissal of Chapter 11 case where "the bankruptcy proceeding [was] more truly a two-party dispute"). In sum, "*Chapter 11 was never intended to be used as a fist in a two party bout. The Chapter is entitled reorganization and not litigation.*" In re HBA East, Inc., 87 B.R. 248, 260 (Bankr. E.D.N.Y. 1988) (granting motion to dismiss cases that were "essentially a two-party civil lawsuit involving non-bankruptcy law brought in the bankruptcy court in the guise of being a reorganization of some sort under Chapter 11") (emphasis added).

10. These Cases present a prime example of a two-party controversy that does not belong in bankruptcy. Indeed, the Debtors were correct when they advised this Court that "at the

end of the day, what we have here is a difficult shareholder dispute," as the thrust of these Cases is a fight between BAPL and Tyagi for control of Cloudeeva Delaware and nothing more. BAPL is the 62% majority shareholder of Cloudeeva Florida, holds an unsecured claim of approximately $6 million against Cloudeeva Delaware,[8] and remains the only equity holder or unsecured creditor to have actively participated in these Cases. In fact, BAPL was the only creditor to attend the meeting to appoint an official committee of unsecured creditors; as a result, no committee was formed. The pool of unsecured claims in these Cases is small and consists primarily of trade debt, the majority of which has been (or will soon be) paid pursuant to this Court's Critical Vendor Order. In short, when distilled to its essence, this is the quintessential two-party dispute that should be resolved in a more appropriate forum (here, a JAMS arbitration), as these Debtors have no justifiable need for the protections of a Chapter 11 filing.

11. Not only do these Cases present the perfect illustration of a two-party dispute that has no need for the Chapter 11 process, but the timing of the filing of these Cases leaves no doubt that Tyagi caused their initiation in order to avoid a decision by the California Court on BAPL's Receiver Motion and a conclusion of the California arbitration, both of which would have likely resulted in Tyagi being ousted from control of the company. Indeed, but for the filing of these Cases, the California Court overseeing the arbitration would have heard BAPL's Receiver Motion—which was filed at the invitation of the California Court—the morning after these Cases were commenced, and the JAMS arbitration would have concluded this week. Where, as here, "the timing of the filing of a Chapter 11 petition is such that there can be no doubt that the primary, if not sole, purpose of the filing was a litigation tactic, the petition may be dismissed as not being filed in good faith." In re 15375 Mem'l Corp., 589 F.3d at 625

[8] See BAPL's Proof of Claim against Cloudeeva Delaware, annexed to the Kaiser Decl. as Exhibit 13.

(citations omitted) (internal quotation marks omitted); see also In re Stingfree Techs., Inc., No. 08-16232bf, 2009 Bankr. LEXIS 3023, at *47 (Bankr. E.D. Pa. Feb. 4, 2009), aff'd, 427 B.R. 337 (E.D. Pa. 2010) (dismissing chapter 11 case where its "primary activity" was for the debtor to litigate an action "based largely…upon state law claims that are arbitrable").

**B. These Cases Serve No Valid Bankruptcy Purpose**

12. These Cases must be dismissed not only because they evidence Tyagi's forum shopping, but also because the continuation of these Cases will serve no valid bankruptcy purpose. Indeed, to satisfy the good faith filing requirement, Chapter 11 petitioners must "act within the scope of the bankruptcy laws to further a valid reorganizational purpose." In re 15375 Mem'l Corp., 589 F.3d at 620. Where the purported benefits justifying a Chapter 11 filing do "not add or preserve value that would otherwise be unavailable to creditors outside of bankruptcy," dismissal should be granted. Id. at 620, 625.

13. The Debtors here have submitted no evidence identifying any legitimate bankruptcy purpose for these Cases. Instead, in a half-hearted effort to justify their filing, the Debtors point to a single paragraph in Tyagi's First Day Declaration in which he says: "As a result of the California lawsuit, the huge financial drain the litigation is having on Cloudeeva's financial resources, and the California court's restrictions on Cloudeeva's ability to borrow (including restrictions on borrowing against its receivable in the form of factoring), Cloudeeva is now struggling to meet its ongoing payroll obligations." Thus, the Debtors' purported rationale for filing these Cases was the cost of litigation and their inability to sufficiently factor receivables in the California proceedings. That attempted justification falls far short of the requirements of a good faith Chapter 11 filing.

**i Neither the Financial Drain of Litigation Nor the Debtors' Desire to Factor Receivables Justifies the Continuation of These Cases**

14. The "financial drain" that Debtors blame on litigation with BAPL is a pretext for the commencement of these Cases. As explained in BAPL's opening brief and the accompanying Pappy Declaration, the Debtors incurred substantial and wholly unnecessary pre-petition litigation fees by engaging in a frivolous strategy involving, *inter alia*, (i) asserting virtually identical claims in two separate courts (in California and New Jersey); (ii) commencing a lawsuit purportedly asserting a claim against Tyagi, in which he controlled both the plaintiffs and the defendant in an action to enforce an unenforceable convertible note; (iii) suing BAPL's lawyers; and (iv) seeking to unwind a settlement agreement that would have caused considerable harm to the company had a California judge not stopped Tyagi's destructive gambit. Pappy Dec., ¶¶ 7, 14, 16, 17, 40.

15. More importantly, however, the Debtors have failed to take reasonable post-petition steps to conserve litigation costs, undermining their contention that these Cases were filed because of the financial burdens of litigation. Indeed, contrary to the Debtors' false representation to this Court on August 15, 2014 that they filed a Notice of Removal of the New Jersey Superior Court action that is duplicative of the California Action (Opp. at 27), they did not remove that case until August 18, 2014. In fact, after these Cases were commenced, the Debtors filed a motion in that action asking the New Jersey Superior Court to, *inter alia*, (i) authorize substituted service so that the Debtors could drag additional defendants into that case; and (ii) compel BAPL and numerous other defendants to participate in discovery by responding to more than 90 interrogatories. Fortunately, the Debtors' efforts to continue litigating that action simultaneously with these Cases were thwarted when, on August 4, 2014, the New Jersey Superior Court granted BAPL's November 2013 motion to stay the case pending a decision in

the California arbitration. It was only after BAPL's motion to stay was granted that the Debtors removed that action to this Court. Thus, the Debtors' frivolous litigation tactics have continued even after these Cases were purportedly filed to conserve litigation costs. Notably, the Debtors have offered no explanation as to how commencement of these Cases might be economically efficient from a litigation perspective, as they have necessitated the retention of new counsel at what must be significant cost to the Debtors' estates.[9]

16. In any event, however, the alleged financial distress caused to the Debtors by the "huge financial drain of litigation" was not a justifiable reason to plunge into Chapter 11. It is unclear how these bankruptcy filings will alleviate that "drain," as the Debtors purport to have every intention of proceeding with the California arbitration before this (or some other) Court. See In re Integrated Telecom, 384 F.3d at 122 ("We do not see how bankruptcy offers [the debtor] any relief from [financial] distress, *which has no relation to any debt* owed by [the debtor]") (emphasis added). The cases cited by the Debtors in support of the proposition that litigation costs can justify Chapter 11 filings are inapposite, as the Debtors' litigation with BAPL would not have resulted in a potentially crippling judgment against them, but would have merely resolved a dispute at the parent level as to the rightful ownership of Cloudeeva Delaware, i.e., the operating Debtor. Thus, these cases provide no support for the Debtors' argument that mounting litigation costs are sufficient to justify a Chapter 11 filing. See In re The Bible Speaks, 65 B.R. 415, 426-28 (Bankr. D. Mass. 1986) (holding that dismissal not warranted where court found that a significant judgment in the litigation would "probably terminate [the debtor's] existence"); In re Johns-Manville Corp., 36 B.R. 727, 729 (Bankr. S.D.N.Y. 1984) (denying motion to dismiss where debtor faced "approximately 16,000 lawsuits pending as of the filing date," with the

[9] The fees of Debtors' bankruptcy counsel, to the extent allowed, will have to be paid in full in cash in order for a plan of reorganization to be confirmed. See 11 U.S.C. 1129(a)(9).

prospect of the "filing of an even more staggering number of suits" over the next 20-30 years); Baker v. Latham Sparrowbush Assocs. (In re Cohoes Indus. Terminal Inc.), 931 F.2d 222, 225 (2d Cir. 1991) (denying dismissal where, as a result of litigation, debtor faced, *inter alia*, the loss of its lease, which the debtor expected to render it insolvent).

17. Furthermore, a close look at the Debtors' corporate structure reveals that pre-petition legal expenses should have been rightfully incurred only at the Debtors' parent level (i.e., by Cloudeeva Florida), and should have had little to no impact on the financial affairs of Cloudeeva Delaware. Rather, Cloudeeva Delaware should have remained a passive bystander in the fight between Tyagi and Cloudeeva Florida, on the one hand, and BAPL, on the other hand, to take control of Cloudeeva Delaware. Instead, Tyagi used Cloudeeva Delaware funds not only to pay his personal legal fees in connection with the California Action in violation of a preliminary injunction, but he also appears to have caused Cloudeeva Delaware to fund what is, at its core, a dispute between its shareholders. So long as these Cases continue, Cloudeeva Delaware will continue to fund that dispute. In view of the foregoing, the costs of litigation did not justify the filing of these Cases, but were merely a pretext for Tyagi's forum shopping to escape what the Debtors concede were "setbacks" suffered in the California Action. Opp. at 9.

18. Likewise, the Debtors' claimed need for additional factoring beyond that permitted by the California Court does not provide a legitimate basis for the continuation of these Cases. There is nothing about the bankruptcy process that grants factoring rights beyond those existing outside of bankruptcy. See In re 15375 Mem'l Corp., 589 F.3d at 620 (affirming dismissal where "the purported benefits [of the Chapter 11 filing] did not add or preserve value that would otherwise be unavailable to creditors outside of bankruptcy"). As demonstrated by BAPL's willingness to consent to supervised factoring solely for the purpose of meeting payroll

obligations in connection with these Cases, BAPL would have agreed to similar factoring outside of bankruptcy under the auspices of a receiver appointed by the California Court. The Debtors made that impossible when, in violation of the California Court's orders, they "made misstatements concerning the anticipated costs of factoring," and "did not make contemporaneous reports to Bartronics stating the amount generated by the factoring, the costs associated therewith and the identity of the payees and in what amounts," leading the California Court to express its concern that "some of the amounts generated were used for a purpose other than paying billable employees and administration."[10] The Debtors should not be permitted to take advantage of their own violation of the California Court's orders and abuse of the factoring process to justify the continuation of these Cases in order to obtain additional factoring.

19. The decision by the District Court for the Eastern District of Pennsylvania in Argus Group 1700, Inc. v. Steinman, 206 B.R. 757 (E.D. Pa. 1997) is particularly instructive. In affirming dismissal of Chapter 11 cases for lack of good faith, the Argus Court considered the following factors (among others), all of which are relevant here: (i) the cases were filed only days after it became apparent that the debtors would be required to appear at a show cause hearing to explain why a receiver should not be appointed; (ii) the debtors contended that the state trial court failed to treat them fairly, and thus sought an alternative forum in which to litigate; (iii) the debtors claimed that they were "running out of funds rapidly because of the…litigation," but did not take appropriate steps to minimize continued litigation costs; and (iv) the debtors removed the litigation on the same day the bankruptcy cases were filed, evidencing their intent to forum shop. Id. at 765. Similarly, the Debtors here (i) commenced these Cases the day before a hearing on a motion to appoint a receiver over Cloudeeva Delaware;

[10] See Exhibit 43 to the Declaration of Venkata Putta submitted on August 4, 2014 in support of the Motion.

(ii) blame the filing of these Chapter 11 Cases on the California Court's "severe restrictions on the Debtors' ability to factor receivables"; (iii) allege that the Cases are justified because the Debtors were suffering from a "huge financial drain" as a result of the California Action, but continued to attempt to litigate the New Jersey Superior Court Action after the Cases were commenced; and, (iv) removed the California Action almost immediately after the Cases were filed. For all of the foregoing reasons, these Cases should be dismissed because they were not filed in good faith.

**ii The Bankruptcy Process Will Provide No Benefit to the Debtors' Estates**

20. Where, as here, "a petitioner has no need to rehabilitate or reorganize, its petition cannot serve the rehabilitative purpose for which Chapter 11 was designed." In re SGL Carbon Corp., 200 F.3d 154, 166 (3d Cir. 1999) (citing cases); see also Connell v. Coastal Cable T.V., Inc. (In re Coastal Cable T.V., Inc.), 709 F.2d 762, 764 (1st Cir. 1983) (Breyer, CJ) (remanding to the District Court a Chapter 11 case that hinged on a shareholder dispute and observing that "there must be some relation—at least an arguable relation—between the chapter 11 plan and the reorganization-related purposes that the chapter was designed to serve"). Dismissal is warranted where a Chapter 11 case will serve no rehabilitative or reorganizational purpose.

21. Here, no rehabilitative purpose can be served by a plan of reorganization, even if the Debtors were in a position to propose one. Most notably, the Debtors have no funded debt in need of restructuring. [redacted]

[11] At the time of filing of this Reply, the Debtors have not yet filed their Schedules of Assets and Liabilities and Statements of Financial Affairs. As a result, BAPL has no information regarding other assets or liabilities of Cloudeeva Florida.

[redacted]

22. Similarly, the Debtors have no trade debt that needs to be restructured under a plan. Nor do they have any other obligations that are commonly addressed in corporate reorganizations, including, for example, executory contracts to be rejected, collective bargaining agreements to be modified, or environmental liabilities to be discharged.

23. Furthermore, the vast majority of Debtors' pre-petition vendors are being (or will be) paid in full pursuant to the Critical Vendors Motion that has already been granted by this Court. See *Final Order Authorizing, But Not Directing, the Debtors to Pay Pre-Petition Claims of Certain Critical Vendors* [Docket No. 80].[12]

24. The Debtors' generic argument that they have filed these cases in order to "maximize the value of their estates" (Opp. at 26) rings hollow. First, the debt the Debtors seek to incur by factoring accounts receivable is extraordinarily expensive, imposes a strain on the Debtors' operations, and cannot realistically serve as a permanent form of financing.[13] Failure to arrange proper financing to cover the costs of these Chapter 11 Cases evidences the Debtors'

[12] Notably, every version of the 13-week budget that the Debtors provided in support of their Factoring Motion proposes to pay approximately $1.1 million of pre-petition payroll-related taxes in full during the course of these Cases, even though Section 1129(a)(9)(C) of the Bankruptcy Code affords a debtor an option to pay off Section 507(a)(8) claims, such as these, over a period of five years under a plan of reorganization. See 11 U.S.C. 1129(a). The Debtors' reluctance to avail themselves of this provision of the Bankruptcy Code lends further support to the conclusion that they filed these Cases with no intent to reorganize. It is also abundantly clear that if the Debtors need to borrow in bankruptcy to pay off these back taxes, they can just as easily (and perhaps even less expensively) borrow and pay them off outside of bankruptcy.

[13] BAPL realizes that some limited factoring may be appropriate to address the Debtors' immediate cash needs and has agreed, on the record, to allow the Debtors to borrow an amount sufficient to fund payroll and payments to critical vendors. BAPL has agreed to such factoring because of its very strong desire that the Debtors' business survive and, once again, prosper as it did in the days before Tyagi when no factoring was necessary and seven-figure profits were common.

lack of planning, and the haste with which these Cases were filed on the eve of a hearing on BAPL's Receiver Motion in the California Action.

25. In fact, the Debtors concede that the business is actually being harmed by these Cases, as customers have become skittish about continuing their relationships with a business in bankruptcy. See, e.g., Transcript of First Day Hearing at 16:21-25; Kaiser Dec. Ex. 2.[14]

## II. If These Cases Continue, a Trustee Must Be Appointed

26. For the reasons set forth above, the best interests of the Debtors and their estates will only be served by the dismissal of these Cases. As noted, if these Cases are dismissed, BAPL intends to immediately renew its Receiver Motion in the California Court to protect the business pending the outcome of the arbitration proceeding. However, if this Court does not dismiss these Cases, the appointment of a Chapter 11 trustee will be necessary.

### A. There is No "Management Team" That Needs to Remain

27. The Debtors' primary argument in opposition to the appointment of a trustee is that current management is essential to the viability of their business. This boilerplate argument is particularly specious here. Tyagi, who touts his purported successes, has controlled the business for approximately one year. In that single year he has turned a profitable business that historically relied on cash flow to fund its operations into one that has resorted to factoring to make payroll. Moreover, the business is hardly "dependent on the relationships Mr. Tyagi has

[14] Finally, for the reasons explained in the opening brief, these Cases should be dismissed because they were filed without proper corporate authority. Although the Debtors contend that the petitions were somehow duly authorized (Opp. at 30), they do not dispute that by filing a Chapter 11 petition on behalf of Cloudeeva Delaware, Tyagi breached his obligation under the Principles of Understanding, in which he acknowledged and agreed to take no corporate action on Cloudeeva Delaware's behalf. Moreover, while the Debtors argue that BAPL's designated board member, Mr. Srinivas Yella, was never confirmed through proper corporate formalities, the California Court ordered Tyagi (not BAPL) to confirm Yella as a director of Cloudeeva Florida and to "complete the necessary corporate formalities." Once again, Tyagi attempts to take advantage of his own disregard for orders issued by the California Court in an effort to legitimize these Cases.

built." See Opp. at 13. To the contrary, the relationships that are critical to the business were developed by Bartronics America, Inc. (long before the Stock Exchange Agreement was executed in December 2012). [redacted]

[redacted]

**B. Tyagi's Pre-Petition Conduct is Highly Relevant to the Trustee Request**

28. In arguing against the appointment of a trustee, the Debtors also advance the baseless contention that the Court should disregard extensive evidence of Tyagi's pre-petition misdeeds and his criminal background, claiming that this Court must focus on the Debtors' post-petition conduct.[15] But Section 1104(a)(1) is clear on its face that cause for the appointment of a trustee includes "fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by current management, *either before or after the commencement of the case*." 11 U.S.C. § 1104(a)(1) (emphasis added); see also Gomez v. U.S. Trustee, No. 7:09-CV-00496, 2010 WL 582706, at *2 (W.D. Va. Feb. 18, 2010) (rejecting debtors' argument that a trustee cannot be appointed based on pre-petition, non-bankruptcy-related criminal convictions, asserting that this argument was "contrary to the plain language of the governing statute, which expressly provides

[15] The cases cited by the Debtors merely hold that, in considering whether to appoint a trustee for cause, the focus is on current management, rather than prior management. See, e.g., In re Bergeron, No. 13-02912-8-SWH, 2013 Bankr. LEXIS 4556, at *23, 28-29 (Bankr. E.D.N.C. Oct. 31, 2013) (holding that a pre-petition civil contempt conviction was not sufficient to justify the appointment of a trustee); In re Sletteland, 260 B.R. 657, 671-72 (Bankr. S.D.N.Y. 2001) (holding that because, *inter alia*, the violation of fiduciary duty cited by the moving party had already been the subject of a full investigation, the appointment of an examiner was not necessary). BAPL does not dispute this. However, that does not mean that current management's pre-petition misdeeds are not appropriately considered. In fact, In re Eagle Creek Subdivision, LLC, No. 08-04292-8-JRL, 2009 Bankr. LEXIS 632, at *2 (Bankr. E.D.N.C. Mar. 9, 2009), which the Debtor cites for the proposition that the Court must narrow its focus to the actions of current management, explicitly holds that "when current management has been tainted by the misdeeds of prior management, the court may also consider the actions of prior management." Id. at *7.

that dishonesty, 'either before or after' the commencement of the bankruptcy case, justifies the appointment of a trustee.'"); Fraidin v. Weitzman (In re Fraidin), 43 F.3d 1466, at *2 (4th Cir. 1995) (upholding appointment of a trustee, despite evidence of proper conduct during the bankruptcy case, where the bankruptcy court found that a "[pre-petition] pattern of dishonesty justified the appointment of a trustee").[16]

29. The Motion sets forth a list of Tyagi's pre-petition misconduct *relating to the Debtors*, even separate and apart from his criminal history, establishing that Tyagi cannot be trusted to serve as a fiduciary for the estates, including (but not limited to) the following: (i) he secretly orchestrated a corporate coup that installed himself as the sole director of Cloudeeva Delaware, violating the terms of the Stock Exchange Agreement and a "Principles of Understanding" document, in which Tyagi acknowledged and agreed that he would take no corporate action on behalf of Cloudeeva Delaware; (ii) he then defied an order of the California Court designating BAPL's director appointee as a director of Cloudeeva Delaware and requiring Tyagi to take the necessary formal action to complete the appointment; (iii) he caused the Debtors to pay $140,000 of his personal attorneys' fees, and refused to comply with a court order requiring that he repay those funds; and (iv) in April 2014, in violation of the preliminary injunction ordered by the California Court, Tyagi caused the Debtors to use $195,000 of

[16] The Debtors argue that Tyagi's criminal background should somehow be disregarded because it purportedly does not "directly implicat[e] the bankrupt estates." See Opp. at 19. That argument not only defies reason, but is factually incorrect. [redacted]

company funds to pay a purported debt to a defunct entity owned by Tyagi (i.e., LIS), while at the same time the Debtors were forced to factor their receivables to make payroll.[17]

**C. The Debtors' Post-Petition Conduct Establishes the Need for a Trustee**

30. The Debtors' contention that there is no evidence of post-petition conduct that warrants the appointment of a trustee is simply not true. As described below, even though these Cases are less than one month old, the Debtors have already demonstrated their dishonesty, lack of candor, failure to comply with the Bankruptcy Code and resistance to making fundamental disclosures to the Court.

31. The most troubling of this post-petition conduct relates to Systems America, a company owned by Tyagi's wife. [redacted] Id. Significantly, it was these types of transactions (among others) that the former Senior Vice President of Business Development, Robert Kaleta, alleges that he brought to the attention of Tyagi as being illegal and

[17] [redacted] Notably, the California Court stated that the information relating to the LIS transaction "was not so confidential that either disclosure or its substance or its use was offensive" and that it "was soon to be disclosed to Bartronics in any event." Id.

improper. See Putta Dec. Ex. 47 (Complaint ¶ 9: Mr. Kaleta alleging that he "was being instructed to bill clients under Systems American [*sic*], instead of Cloudeeva, to shelter money from a pending lawsuit with a third party company, Bartronics"). It is undisputed that Tyagi fired Kaleta in March 2014.

32. Moreover, the Bankruptcy Code *prohibits* the assignment of the Debtors' contracts to Systems America, [redacted] without court approval. See 11 U.S.C. § 363(b) (property of the estate cannot be transferred out of the ordinary course of business without notice and a hearing); §§ 365(a), 365(f)(2)(A) (requiring court approval for debtor to assume and assign executory contracts). The Debtors have not sought such approval, nor have they represented that they will do so in the future.

33. Here, the Debtors' contracts with their customers are their lifeblood, yet they are freely dispensing with those assets in the dark, without seeking this Court's approval (which is required) and without providing the most basic disclosures as to those transactions. This type of conduct, now occurring *before this Court*, is exactly what drove the California Court to conclude that "continuing violations of disclosure requirements reasonably can be inferred to be an attempt to hide internal company transactions." See Putta Dec. Ex. 43. The Debtors were given a full and fair opportunity to establish the *bona fides* of the critical issue of their dealings with Systems America, but have entirely failed to do so. [redacted]

Silence on such a critical issue speaks volumes.

34. Significantly, *after* the filing of the Motion, Systems America launched its website (see Kaiser Dec. Ex. 4), which is registered under Tyagi's own name (and not under his

wife's name). See Kaiser Dec. Ex. 5. The website describes the business as providing "Cloud Services", "Mobility" and "Big Data" solutions. See Kaiser Dec. Ex. 6. The Debtors' website uses the same language in describing the Debtors' services. See Kaiser Dec. Ex. 7. The website also identifies Systems America's California headquarters as being located at 2603 Camino Ramon in San Ramon (see Kaiser Dec. Ex. 8), which is only steps away from Cloudeeva's California headquarters located at 2633 Camino Ramon. Moreover, recent internet job postings for Cloudeeva positions direct candidates to contact an individual who is associated with Systems America. See Kaiser Dec. Ex. 9 & Ex. 10.

35. At a minimum, there is an undisputable conflict of interest—that has only become more pervasive post-petition—arising from Tyagi's continuing role as Debtors' management, where the Debtors acknowledge that they are now assigning contracts to and billing through his wife's company. In short, *Tyagi and his wife are now personally profiting from the decision of the Debtors' customers and vendors to terminate their contracts as a result of the Chapter 11 filings that Tyagi caused the Debtors to initiate*. If the Cases are not dismissed, this clear-cut conflict of interest certainly compels the appointment of a trustee in order to protect the value of the estates. See Oklahoma Refining Co. v. Blaik (In re Oklahoma Refining Co.), 838 F.2d 1133, 1136 (10th Cir. 1988) ("There are many cases holding that a history of transactions with companies affiliated with the debtor company is sufficient cause for the appointment of a trustee where the best interest of the creditors require.") (citations omitted); In re Embrace Sys. Corp., 178 B.R. 112, 128-29 (Bankr. W.D. Mich. 1995) (appointing a trustee where the debtor had potential cause of action against an affiliated entity controlled by a current shareholder/former consultant of the debtor and for which the current president of the debtor acted as a consultant); In re McCorhill Publ'g, Inc., 73 B.R. 1013, 1017 (Bankr. S.D.N.Y. 1987) (appointing a trustee

where the debtor's directors had conflicting interests in affiliated entities for which the debtor had assumed or paid various expenses or obligations). If a trustee is not appointed, Tyagi will have free reign to continue transitioning business to Systems America, which BAPL fears will ultimately force the Debtors to liquidate under Chapter 7 (with no downside to Tyagi, who will step out of the smoldering ruins of Cloudeeva and resume operations under the Systems America platform).

36. The Debtors have also failed to be candid with this Court regarding their relationship with Cloudeeva India, a company owned by Tyagi's father. As part of their first day motions, the Debtors initially attempted to lull this Court into immediately authorizing the payment of $145,000 to that company, under the guise of a payment to "foreign vendors," without disclosing the identity of the company and its affiliation to Tyagi. See *Motion for Entry of an Order Authorizing, But Not Directing, the Debtors to Pay Certain Pre-Petition Claims of Certain Foreign Vendors* [Docket No. 9]. [redacted]

[redacted] The records of the Ministry of Corporate Affairs for the Government of India, *produced by the Debtors*, show that Mr. Tyagi was appointed as a director of Cloudeeva India in March 2014. See Kaiser Dec. Ex. 12.

37. Finally, during the first day hearing, Debtors' counsel represented to the Court that the Debtors intended to remove two New Jersey Superior Court actions (in which BAPL is a party) to this Court in order to avoid "the overwhelming costs of litigating what are very similar issues among similar parties." See Tr. of July 23, 2014 Hr'g 12-13. However, as noted, the day after these cases were commenced, the Debtors filed a motion in one of the pending New Jersey Superior Court actions (in which the Debtors assert claims virtually identical to those asserted in the California proceedings), seeking, *inter alia*, to reinstate the complaint against certain defendants who had been dismissed for lack of service and to compel discovery. Pappy Decl. ¶ 41, Ex. P. The Debtors subsequently removed that action on August 18, 2014 (days before the hearing on this Motion), and only *after* the New Jersey Superior Court granted BAPL's motion to stay that action pending a decision in the California arbitration proceedings.[18]

**D. Absent Dismissal, the Appointment of a Chapter 11 Trustee is in the Best Interests of the Estates**

38. It remains abundantly clear that, if these cases are not dismissed, the appointment of a trustee "is in the interests of creditors, any equity security holders, and other interests of the estate." 11 U.S.C. § 1104(a)(1). The Debtors argue, however, that a trustee should not be appointed under the "bests interests" prong of Section 1104(a) on essentially three grounds: (i) that BAPL cannot demonstrate that the Debtors are untrustworthy; (ii) that the Debtors' customers and creditors have confidence in current management; and (iii) that BAPL has not shown that other parties' interests are served by the appointment of a trustee. None of these arguments withstand scrutiny.

[18] In contrast, the Debtors filed a notice of removal of the California Action on July 23, 2014, two days after the Chapter 11 filings.

39. First, the Debtors' claim that management is trustworthy is belied by the extensive record of Tyagi's dishonesty, self-dealing and other malfeasance, as documented extensively in the Motion.

40. Second, the Debtors' contention that customers and creditors have confidence in current management is a flight of fancy. As noted, Tyagi had no role in operating the Debtors' business prior to executing his corporate coup in July 2013, and he is not responsible for creating or managing the Debtors' current customer relationships. If these Cases are not dismissed, the appointment of a trustee (who can hire industry-specific personnel to assist in operations) will bring much needed stability and protection to the business.

41. Third, the Debtors' contention that BAPL is merely "one particular party" that is "unhappy with current management" (see Opp. at 24) is knowingly disingenuous. BAPL and its affiliates currently have a 62% common equity interest and an approximately $50 million preferred equity interest in the Debtors, as well as an unsecured claim of approximately $6 million against Cloudeeva Delaware (which BAPL believes is the largest unsecured claim against the Debtors).[19] No committee of unsecured creditors has been appointed.[20] There are no other unsecured creditors or equity holders that have actively participated in these cases. The Debtors' unsecured claims pool is small and comprised mainly of trade debt, a substantial portion of which has been paid (or is likely to soon be paid) through the Critical Vendor Order. Thus, these Cases boil down to little more than a two-party dispute between BAPL and Tyagi.

42. If these Cases are not dismissed, Debtors' management—*i.e.*, Tyagi—simply cannot remain in possession of the estates where he has been locked in a bitter and lengthy

[19] See Kaiser Dec. Ex. 14.

[20] BAPL is the only creditor that attended the meeting to appoint an official committee of unsecured creditors.

dispute with BAPL, the *only* economic party in interest actively involved in these Cases, and where he is only acting in a management role after effecting a corporate coup that ousted BAPL from control. Indeed, the Court need only skim the Debtors' opposition to the Motion, which levels a barrage of vitriolic accusations against BAPL (whose conduct is not at issue on the Motion), to understand that if these Cases are not dismissed and a trustee not appointed, the Cases will be paralyzed and unable to move forward in the right direction.

**CONCLUSION**

WHEREFORE, BAPL respectfully requests that this Court (i) dismiss these Chapter 11 Cases; or, in the alternative, (ii) appoint a Chapter 11 trustee; and (iii) grant such other and further relief as is just and proper.

Dated: August 19, 2014
Roseland, New Jersey

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**UNITED STATES BANKRUPTCY COURT**
**FOR THE DISTRICT OF NEW JERSEY**

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|---|---|
| In re:<br><br>CLOUDEEVA, INC., et al.,[1]<br><br>Debtors. | Chapter 11<br><br>Case No. 14-24874 (KCF)<br><br>(Joint Administration Requested) |

**DECLARATION OF ELIZABETH M. PAPPY IN FURTHER SUPPORT OF MOTION OF BARTRONICS ASIA PTE LTD. FOR ENTRY OF AN ORDER (I) DIRECTING THE APPOINTMENT OF A CHAPTER 11 TRUSTEE OR, (II) IN THE ALTERNATIVE, DISMISSING THE CHAPTER 11 CASES**

**[FILED UNDER SEAL]**

[1] The Debtors in these Chapter 11 cases, along with the last four digits of each Debtor's tax identification number, are: Cloudeeva, Inc. a Delaware Corporation (5326) ("**Cloudeeva Delaware"**) and Cloudeeva, Inc., a Florida Corporation (2227) ("**Cloudeeva Florida**; collectively with Cloudeeva Delaware, the "**Debtors**").

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**UNITED STATES BANKRUPTCY COURT**
**FOR THE DISTRICT OF NEW JERSEY**

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| In re:<br><br>CLOUDEEVA, INC., et al.,[1]<br><br>Debtors. | Chapter 11<br><br>Case No. 14-24874 (KCF)<br><br>(Joint Administration Requested) |

**TRANSMITTAL DECLARATION OF SHOSHANA B. KAISER IN SUPPORT OF MOTION OF BARTRONICS ASIA PTE LTD. FOR ENTRY OF AN ORDER (I) DIRECTING THE APPOINTMENT OF A CHAPTER 11 TRUSTEE OR, IN THE ALTERNATIVE, (II) DISMISSING THE CHAPTER 11 CASES**

**[FILED UNDER SEAL]**

[1] The Debtors in these Chapter 11 Cases, along with the last four digits of each Debtor's tax identification number, are: Cloudeeva, Inc. a Delaware corporation (5326) and Cloudeeva, Inc., a Florida corporation (2227). The corporate headquarters of Cloudeeva, Inc., a Delaware corporation are located at 104 Windsor Center Drive, Suite 300, East Windsor, New Jersey 08520, (the "**Debtors**").