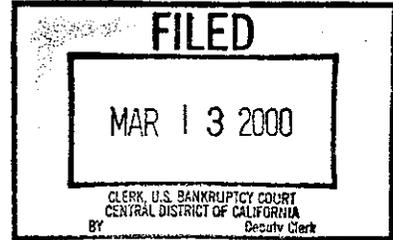
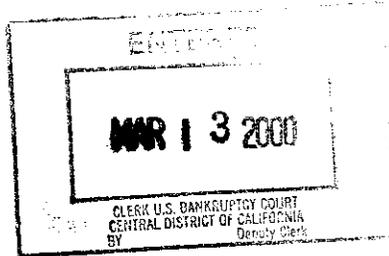


FOR PUBLICATION



UNITED STATES BANKRUPTCY COURT FOR THE
CENTRAL DISTRICT OF CALIFORNIA

In re:)
SIZZLER RESTAURANTS)
INTERNATIONAL, INC.,)
Debtor.)

BK CASE NO. SV 96-16075-AG
(Jointly administered with:
Case Nos. SV 96-16076-AG
SV 96-16077-AG
SV 96-16078-AG
SV 96-16079-AG)

XX Affects all Debtors.)

SIZZLER USA RESTAURANTS, INC.)
Plaintiff,)
vs.)
BELAIR & EVANS LLP,)
Defendant.)

Chapter 11
ADV. NO. 98-1720-AG
MEMORANDUM DISPOSITION RE
COUNTER-CLAIMANT'S MOTION TO
APPROVE VOLUNTARY DISMISSAL
OF ADVERSARY PROCEEDING; OR
ALTERNATIVELY FOR PERMISSIVE
ABSTENTION

BELAIR & EVANS LLP,)
Counterclaimant,)
vs.)

SIZZLER USA RESTAURANTS, INC.;)
KATHRYN T. McGUIGAN;)
NATIONAL UNION FIRE)
INSURANCE CO.,)
Counterclaim Defendants.)

1 Counter-claimant Belair and Evans, LLP ("Belair"), attorneys at
2 law, seeks court approval of the voluntary dismissal of its counter-
3 claim against counterclaim defendant, Kathryn T. McGuigan ("McGuigan"),
4 pursuant to Fed. R. Civ. P. 41(a)(2), or, alternatively, requests that
5 the court abstain from hearing the counter-claim, pursuant to 28 U.S.C.
6 1334(c)(1).

7 This motion came on for hearing on August 27, 1999. Following
8 supplemental briefing from the parties regarding whether the court has
9 subject matter jurisdiction over the counter-claim, the motion was
10 argued further and submitted on October 22, 1999.

11
12 **STATEMENT**

13 In June, 1996, Sizzler Restaurants International, Inc.
14 ("Sizzler") filed a Chapter 11 petition in bankruptcy. The estate was
15 administered by Sizzler as the debtor-in-possession. Sizzler's Plan
16 of Reorganization was confirmed in August, 1997.

17 Beginning in 1992, Belair represented Sizzler in numerous
18 personal injury matters in New York and New Jersey. In September,
19 1998, Sizzler filed a complaint against Belair for declaratory and
20 injunctive relief and for turnover pursuant to 11 U.S.C. Sec. 542,
21 seeking to prevent Belair from filing additional proofs of claim for
22 pre-petition legal services.¹ In response, Belair filed counter-
23 claims against Sizzler, McGuigan, and National Union First Insurance
24 Company ("National"), Sizzler's insurer. At the time, McGuigan was
25

26 ¹Prior to September of 1998, Belair had filed two proofs of claim
27 for pre-petition legal services.

1 employed as Sizzler's Director of Risk Management and Vice President
2 of Human Resources.

3 In its counter-claim, Belair alleged that, both prior to and
4 after filing for bankruptcy protection, Sizzler, through McGuigan,
5 promised that it would pay Belair's outstanding fees incurred both
6 pre-petition and post-petition without Belair having to file a proof
7 of claim for those fees. Belair alleged that, in reliance on these
8 assurances, it continued to perform legal services for Sizzler.
9 Belair further alleged that it had not been paid the outstanding fees
10 and that, inasmuch as it continued to be attorney of record for a
11 number of personal injury cases in which Sizzler was a defendant,
12 there existed the possibility of having to provide additional legal
13 services for Sizzler without the likelihood that it would be paid for
14 performing those services.

15 Based on these allegations, Belair sued Sizzler and National for
16 damages on theories of contract, quantum meruit and unjust enrichment,
17 and for declaratory relief. Belair also sued Sizzler and McGuigan for
18 damages arising from fraud and negligent misrepresentation. In
19 addition to declaratory relief, Belair prayed for damages against
20 Sizzler, McGuigan and National, jointly and severally, in the amount
21 of approximately \$91,000.

22 In its counter-claim, Belair made three allegations against
23 McGuigan directly:

24 1) that McGuigan had assured Belair that the firm would continue
25 to be retained and that the firm would continue to be paid
26 notwithstanding Sizzler's bankruptcy petition, and that, in
27 reliance on these assurances, Belair agreed to continue to
28 perform services for Sizzler post-petition;

1 2) that McGuigan promised Belair that Sizzler would request that
2 the bankruptcy court authorize Belair to continue to represent
3 Sizzler and to be paid for such services, and that, based on
4 McGuigan's request and assurances, Belair advised local counsel
5 that pre- and post-bankruptcy fees would be paid; and

6 3) that, after confirmation of Sizzler's Chapter 11 plan,
7 McGuigan assured Belair that all of its bills would be paid by
8 National; requested Belair to continue performing services on
9 pending cases; and assured Belair that she would intervene and
10 obtain payment from National and would get Sizzler's bankruptcy
11 counsel, Pachulski, Stang, Ziehl & Young, to intervene with
12 National, so that Belair would not have to sue National for
13 payment.

14 In July, 1999, the court approved a settlement between Belair,
15 Sizzler and National, whereby Belair was paid \$60,000 for its claimed
16 fees. The settlement also included an exchange of releases, with
17 Belair dismissing its counter-claim against Sizzler and National with
18 prejudice. During the process, Belair had offered to dismiss McGuigan
19 as well, either with prejudice, along with the exchange of mutual
20 releases, or without prejudice, without releases. McGuigan rejected
21 this offer.

22 On July 29, 1999, Belair filed the instant motion, requesting
23 voluntary dismissal of the counter-claim without prejudice, stating
24 that it did not wish to pursue the matter against McGuigan "at this
25 time." Alternatively, Belair requested that the court permissively
26 abstain from hearing the counter-claim. McGuigan opposed Belair's
27 motion, desiring to have the matter either litigated or dismissed with
28 prejudice. Alternatively, McGuigan asked for attorney's fees and
costs, in the event that the court approved the dismissal of the
counter-claim without prejudice.

On July 30, 1999, McGuigan requested the court to grant summary
judgment regarding Belair's counter-claim. In addition, on September

1 2, 1999, McGuigan filed a motion for leave to file a third party
2 complaint against Sizzler. These motions are pending.

3
4 DISCUSSION

5 1. The counterclaim filed by Belair against McGuigan is a core
6 proceeding.

7 "Jurisdiction is determined as of the commencement of the
8 action." Linkway Investment Co., Inc. v. Olsen (In re Casamont,
9 Ltd.), 196 B.R. 517, 521 (9th Cir. BAP 1996), citing Fietz v. Great
10 Western Savings (In re Fietz), 852 F.2d 455, 457 n.2 (9th Cir. 1988).

11 "[T]he federal district court has original and exclusive jurisdiction
12 of all cases under title 11. 28 U.S.C. Sec. 1334(a). The district
13 court has original jurisdiction of all civil proceedings arising under
14 title 11. 28 U.S.C. Sec. 1334(b). Furthermore, a bankruptcy judge may
15 hear and determine all cases arising under the Bankruptcy Code and all
16 core proceedings arising in a bankruptcy case. 28 U.S.C. Sec.

17 157(b)(1). Accordingly, for subject matter jurisdiction to exist
18 there must be at least some relationship between the proceeding and
19 the title 11 case." Mangun v. Bartlett (In re Balboa Improvements,
20 Inc.), 99 B.R. 966, 969 (9th Cir. BAP 1989). "Put another way, claims
21 that arise under or in Title 11 are deemed to be 'core proceedings,'
22 while claims that are related to Title 11 are 'noncore' proceedings."

23 Maitland v. Mitchell (In re Harris Pine Mills), 44 F.3d 1431, 1435
24 (9th Cir. 1995). "As a general rule a bankruptcy court does not have
25 jurisdiction in controversies between third parties not involving the
26 debtor or property of the estate. If, however, such controversies are
27 'related to' the underlying bankruptcy case, the court has

1 jurisdiction pursuant to 28 U.S.C. Sec. 1334(b)." Casamont, 196 B.R.
2 at 521 (internal citations omitted).

3 At the outset this court had subject matter jurisdiction over
4 Belair's counter-claim as the counter-claim constituted a core
5 proceeding. See Harris Pine Mills, 44 F.3d 1431. In the Harris Pine
6 Mills case, an action was filed in state court against the Chapter 11
7 trustee and the trustee's agents. The debtor was not named in the
8 suit. The suit alleged fraud, negligence, and negligent
9 misrepresentation surrounding the trustee's sale of assets of the
10 estate. The trustee removed the case to the district court, whereupon
11 the district court referred the case to the bankruptcy court as a core
12 matter.

13 On appeal to the Ninth Circuit, the Harris Pine Mills plaintiffs
14 disputed the district court's characterization of the matter as a core
15 proceeding, contending that the district court erred in refusing to
16 remand their action to state court. Id. at 1433-1434. The Ninth
17 Circuit upheld the district court's assertion of subject matter
18 jurisdiction under 28 U.S.C. Sec. 157(b)(2)(A) and (b)(2)(O),² id. at
19 1437, affirming the district court's determination that the suit
20 against the trustee was a core proceeding, inasmuch as the claims were
21 based upon post-petition conduct by the trustee and his agents which

22
23 ² 28 U.S.C. Sec. 157(b)(2) provides in pertinent part:
24 Core proceedings include, but are not limited to - (A) matter
25 concerning administration of the estate; . . . (O) other
26 proceedings affecting the liquidation of the assets of the estate
27 or the adjustment of the debtor-creditor or the equity security
28 holder relationship, except personal injury tort or wrongful
death claims.

1 was "inextricably intertwined with the trustee's sale of property
2 belonging to the bankruptcy estate." Id. at 1438. In affirming the
3 district court, the Court of Appeals additionally noted that a state
4 law claim not falling under Sec. 157(b) (2) could nevertheless qualify
5 as a noncore, related proceeding. Id. at 1436-1437 and n. 8, citing
6 Piombo Corp. v. Castlerock Properties (In re Castlerock), 781 F.2d 159
7 (9th Cir. 1986). Cf. Bethlahmy, IRA v. Kuhlman (In re ACI-HDT Supply
8 Co.), 205 B.R. 231, 237 (9th Cir. BAP 1997) (distinguishing Harris
9 Pine Mills on the basis that the trustee's conduct occurred post-
10 petition).

11 Further, the core nature of the counterclaim was not altered by
12 Belair's dismissal of Sizzler. See Honigman, Miller, Schwartz & Cohn
13 v. Weitzman (In re DeLorean Motor Co.), 155 B.R. 521 (9th Cir. BAP
14 1993). In the DeLorean case, debtor's counsel filed a state court
15 malicious prosecution action against the Chapter 7 trustee, counsel
16 for the trustee, and the chairman of the debtor's creditors'
17 committee. The suit was based on the conclusion of a lawsuit in the
18 debtor's counsel's favor, wherein the trustee had alleged that the
19 debtor had fraudulently conveyed property of the estate to his
20 counsel. The trustee removed the action to the bankruptcy court.
21 Plaintiff dismissed the trustee and moved that the bankruptcy court
22 abstain and remand the action to the state court. The bankruptcy
23 court granted the motion. Id. at 522.

24 On appeal, the BAP reversed the bankruptcy court, holding that
25 the malicious prosecution suit was a core proceeding, notwithstanding
26 the fact that the trustee had been dismissed. Id. at 525. The BAP
27
28

1 reasoned that the malicious prosecution action arose "from the efforts
2 of officers of the estate to administer the estate and collect its
3 assets and therefore impacts the handling and administration of the
4 estate," and that "it is inextricably tied to the determination of an
5 administrative claim against the estate and is similarly tied to
6 questions concerning the proper administration of the estate." Id.
7 According to the BAP, the suit, as against the trustee's counsel, was
8 "essentially a suit against the trustee." Id. Cf. In re ACI-HDT, 205
9 B.R. at 236 (distinguishing DeLorean on the basis that the lawsuit
10 there implicated post-petition conduct and was the equivalent of an
11 action against the trustee).

12 In the instant case, prior to confirmation of its Plan of
13 Reorganization, Sizzler was a debtor-in-possession, its rights, powers
14 and duties being defined under 11 U.S.C. Sec. 1107(a), being compared
15 to a trustee serving in a Chapter 11 case. To the extent that the
16 counter-claim was brought against McGuigan, who during the relevant
17 time period was Sizzler's employee and agent, the counter-claim was
18 the equivalent of a suit against Sizzler, the debtor-in-possession.

19 The counter-claim alleged post-petition, as well as pre-petition,
20 conduct against McGuigan and Sizzler bearing on the administration of
21 the estate, inasmuch as their conduct affected the administration of
22 potential claims by Belair against the estate. In the words of
23 DeLorean, Belair's counter-claim is "inextricably tied to questions
24 concerning the proper administration of the estate." Consequently,
25 under the holdings of Harris Pine Mills and DeLorean Motor Co., the
26 counter-claim constituted a core proceeding under 28 U.S.C. Sec. 157

1 (A) and (O) at the time that it was filed and continued to constitute
2 a core proceeding notwithstanding the dismissal of Sizzler.

3 Accordingly, this court has jurisdiction over Belair's counter-claim.
4

5 2. Alternatively, Belair's counter-claim against McGuigan is related
6 to the Sizzler bankruptcy.

7 Assuming that the counter-claim against McGuigan is not the
8 equivalent of a suit against Sizzler, the court has jurisdiction over
9 the counter-claim on the grounds that it is related to the Sizzler
10 bankruptcy. "An action is 'related to' a bankruptcy case if the
11 outcome of the proceeding could conceivably alter the debtor's rights,
12 liabilities, options or freedom of action (either positively or
13 negatively) in such a way as to impact on the administration of the
14 bankruptcy estate. In re Fietz, 852 F.2d 455, 457 (9th Cir. 1988
15 (adopting the position of the Third Circuit as explained in Pacor,
16 Inc. v. Higgins, 743 F.2d 984, 994 (3d. Cir. 1984))." Casamont, 196
17 B.R. at 521. See also Celotex Corp. v. Edwards, 514 U.S. 300, 308 n.6
18 (1995), citing Pacor with approval.

19 In the case of In re Balboa Improvements, 99 B.R. 966 (9th Cir.
20 BAP 1989), an individual who stood to earn a fee if he could procure
21 refinancing for a buyer of certain property of the estate sued the
22 Chapter 11 debtor's attorney for damages, based on the attorney's
23 alleged misconduct administering the estate with regard to that
24 property. The BAP held that, since the action "pertains to the
25 administration of the estate by debtor's counsel and with respect to
26 an asset of the estate, . . . we believe the outcome of the action
27 directly affects the administration of the bankruptcy estate." Id. at
28

1 969. According to the BAP, the action was a proceeding at least
2 related to the bankruptcy, to the extent that it sought a
3 determination of damages between the plaintiff and debtor's counsel
4 (and was core pursuant to 28 U.S.C. Sec. 157(b)(2)(A) and (O), to the
5 extent that the judgment would determine the proper administration of
6 the estate by debtor's counsel). Id. The BAP explained that "[t]his
7 action is related since the claim for damages is based upon alleged
8 misconduct in the very administration of the estate." Id. (Moreover,
9 the BAP noted that, as the damages were claimed to have arisen from
10 misconduct in administration of the estate, the bankruptcy court could
11 entertain the action for damages under the doctrine of pendent
12 jurisdiction. Id.)

13 In the instant case, Belair is asserting a claim for damages
14 against McGuigan based on allegations of her misconduct in the
15 administration of the bankruptcy estate. Consequently, under In re
16 Balboa Improvements, Belair's counter-claim is related to the Sizzler
17 bankruptcy, so as to give this court jurisdiction over the counter-
18 claim.

19 An alternative basis for related to jurisdiction can be found in
20 Sizzler's duty to indemnify McGuigan should she be found liable on the
21 counter-claim. Belair sued McGuigan for statements she allegedly made
22 in her capacity "as Director of Risk Management and/or Vice President
23 of Sizzler" and as an "authorized agent" of Sizzler. In the course of
24 opposing a motion by McGuigan to disqualify Sizzler's bankruptcy
25 counsel, Sizzler, through its Vice President and General Counsel,
26 Michael B. Green, "agreed to indemnify Ms. McGuigan to the extent
27
28

1 required by Cal. Labor Code Sec. 2802."³ Declaration of Michael B.
2 Green, in support of Sizzler's Opposition to McGuigan's Motion to
3 Disqualify Pachulski, et al.

4 Under the terms of Sec. 2802, were McGuigan found to have been
5 acting within the scope of her employment, this would trigger
6 indemnification liability on the part of Sizzler, unless McGuigan,
7 while making the alleged actionable statements, was acting unlawfully
8 and knew that she was acting unlawfully.

9 To date it has not been asserted that McGuigan knowingly acted
10 unlawfully. McGuigan's claim of indemnification against Sizzler
11 impacts on the administration of the estate inasmuch as it raises
12 questions about the appropriateness of Sizzler's conduct in the course
13 of estate administration. Furthermore, under the terms of the plan of
14 reorganization, this court retains jurisdiction to adjudicate the
15 claim of indemnification. See Debtor's Second Amended Plan of
16 Reorganization, As Modified, Article XII, Section 1.

17 In those circuits which have adopted the Pacor standard, courts
18 have routinely found suits between non-debtors to be related to the
19 bankruptcy, where the debtor is contractually obligated to indemnify
20 the non-debtor defendant. In re Master Mortgage, Inc., 168 B.R. 930,

21 _____
22 ³ Section 2802 provides:

23 An employer shall indemnify his employee for all that the
24 employee necessarily expends or loses in direct consequence of
25 the discharge of his duties as such, or of his obedience to the
26 directions of the employer, even though unlawful, unless the
27 employee, at the time of obeying such directions, believed them
28 to be lawful.

1 934-935 (Bankr. W.D. Mo. 1994), citing cases (noting that courts have
2 found related to jurisdiction where "[t]here is an identity of
3 interest between the debtor and the third party, usually an indemnity
4 relationship, such that a suit against the non-debtor is, in essence,
5 a suit against the debtor or will deplete assets of the estate").⁴

6 While Sizzler's duty to indemnify is not based on an
7 unconditional contractual obligation, this court is persuaded by those
8 cases which have refused to read Pacor as requiring an unconditional
9 indemnification agreement. See Lindsey v. O'Brien, Tanski et al. (In
10 re Dow Corning Corp.), 86 F.3d 482, 491 (6th Cir. 1996) ("[i]t has
11 become clear following Pacor that 'automatic' liability is not
12 necessarily a prerequisite for a finding of 'related to'
13 jurisdiction"); Kelley v. Nodine (In re Salem Mortgage Co.), 783 F.2d
14 626, 634 (6th Cir. 1986) (sec. 1334 "does not require a finding of
15 definite liability of the estate as a condition precedent to holding
16 an action related to a bankruptcy proceeding").⁵ The counter-claim is

17
18 ⁴ See Michigan Employment Security Comm'n v. Wolverine Radio
19 Co., Inc. (In re Wolverine), 930 F.2d 1132, 1143 (6th Cir. 1991);
20 Philippe v. Shape, Inc., 103 B.R. 355, 358 (D. Maine 1989); Kossmann v.
21 TJX Cos., Inc., 136 B.R. 640, (W.D. Pa. 1991); Stanger v. Athos Steel
22 Aluminum, Inc. (In re Athos Steel), 71 B.R. 525, 536 (Bankr. E.D. Pa.
1987); Williams v. Shell Oil Co., 169 B.R. 684, 690 (S.D. Cal. 1994);
Beneficial Nat'l Bank v. Best Reception Systems, Inc. (In re Best
Reception), 220 B.R. 932, 949 (Bankr. E.D. Tenn. 1998).

23 ⁵ In holding that related to jurisdiction did not exist, the
24 Pacor court observed that "[the non-debtor defendant] is not a
25 contractual guarantor of [the debtor], nor has [the debtor] agreed to
26 indemnify [the non-debtor defendant], and thus a judgment in the [non-
27 debtor] action could not give rise to any automatic liability on the
28 part of the estate." Id. As a result, some courts have read Pacor as
holding that an unconditional indemnification agreement is necessary

1 at least related to the Sizzler bankruptcy in that Sizzler is
2 obligated to indemnify McGuigan if the requirements of Sec.2802 are
3 met. The remote possibility that Sizzler could avoid having to
4 indemnify McGuigan under Sec. 2802 has little if any bearing on
5 whether the court has jurisdiction over the counter-claim.

6
7 3. Abstention is inapplicable to the counter-claim.

8 On the basis that the bankruptcy court has jurisdiction over the
9 counter-claim, Belair contends that the court should exercise its
10 powers of permissive abstention, pursuant to 28 U.S.C. Sec.
11 1334(c)(1), and abstain from adjudicating the matter.⁶ In opposition,
12 McGuigan asserts that abstention is not appropriate, inasmuch as there
13 is no pending state court proceeding to which this court could defer.

14 In In re Tucson Estates, 912 F.2d 1162, 1167 (9th Cir. 1990), the
15

16 for the existence of related to jurisdiction. See Williams, 169 B.R.
17 at 689 (concluding that "Pacor dictate[s] that 'related to'
18 jurisdiction attaches only where cross-claims arising out of a civil
19 action are directly, contractually linked to the bankrupt party");
20 Best Reception, 220 B.R. at 948 (concluding that, in Pacor, "the Third
21 Circuit concluded that indemnity rights do not give rise to 'related
22 to' jurisdiction in the absence of automatic liability"). This court
declines to accept a reading of Pacor which requires an unconditional
indemnification agreement or otherwise automatic liability on the part
of the debtor in order to find the existence of related to
jurisdiction.

23 ⁶ 28 U.S.C. Sec. 1334(c)(1) provides:

24
25 Nothing in this section prevents a district court in the interest
26 of justice, or in the interest of comity with State courts or
27 respect for State law, from abstaining from hearing a particular
28 proceeding arising under title 11 or arising in or related to a
case under title 11.

1 Ninth Circuit set forth twelve factors which a court ought to consider
2 in deciding whether to abstain under sec. 1334(c)(1). Included in
3 this list is "the presence of a related proceeding commenced in state
4 court or other nonbankruptcy court." Id. Citing Tucson Estates and
5 acknowledging the existence of a related proceeding as "a factor," the
6 Court of Appeals held, in Security Farms v. International Bhd. of
7 Teamsters, 124 F.3d 999, 1009 (9th Cir. 1997), that the absence of a
8 pending state court proceeding is dispositive of the issue of whether
9 the trial court should permissively abstain. The court explained:

10 Abstention can exist only where there is a parallel proceeding in
11 state court. That is, inherent in the concept of abstention is
12 the presence of a pendant state court action in favor of which
the federal court must, or may, abstain.

13 To require a pendant state action as a condition of
14 abstention eliminates any confusion with 28 U.S.C. Sec. 1452(b),
15 which provides district courts with the authority to remand civil
16 actions properly removed to federal court, in situations where
17 there is no parallel proceeding. Section 1334(c) abstention
should be read *in pari materia* with section 1452(b) remand, so
that the former applies only in those cases in which there is a
related proceeding that either permits abstention in the interest
of comity, section 1334(c)(1), or that, by legislative mandate,
requires it, section 1334(c)(2).

18 Id. at 1009-1010.⁷

19 Given the lack of a pending parallel state court action here, the
20 court is precluded from exercising its discretion to abstain from
21 adjudicating Belair's counter-claim.

22
23
24 ⁷ An earlier case, Eastport Assocs. v. City of Los Angeles (In
25 re Eastport), 935 F.2d 1071 (9th Cir. 1991), held that the fact that a
26 state court proceeding had never been initiated was merely "another
27 factor weighing against abstention." Id. at 1078 (emphasis added).
While not referencing Eastport, Security Farms nonetheless appears to
have invalidated its holding on this point.

1
2 4. The court will conditionally grant Belair's
3 motion to approve voluntary dismissal of its counter-claim
4 pursuant to Fed. R. Civ. P. Rule 41.

5 As an alternative to a request that the court permissively
6 abstain from hearing its counter-claim, Belair has asked that the
7 court approve a voluntary dismissal of the counter-claim pursuant to
8 Fed. R. Civ. P. Rule 41(a)(2). Specifically, Belair seeks to dismiss
9 the counter-claim without prejudice.

10 Once a defendant has, as in the instant case filed an answer,
11 Rule 41(a)(2) applies. It provides that a plaintiff cannot dismiss
12 the action without leave of court. Hamilton v. Shearson-Lehman Am.
13 Express, Inc., 813 F.2d 1532, 1535 (9th Cir. 1987). Rule 41(a)(2)
14 further provides that, in ordering an action dismissed, the court may
15 impose "such terms and conditions as [it] deems proper." Fed. R. Civ.
16 P. Rule 41(a)(2). The purpose of the rule is to permit a plaintiff to
17 dismiss an action without prejudice so long as the defendant will not
18 be prejudiced or unfairly affected by dismissal. Stevedoring Serv. of
19 Am. v. Armilla Int'l, 889 F.2d 919, 921 (9th Cir. 1989).

20 Consequently, courts generally allow dismissal without prejudice
21 unless the defendant will suffer "some plain legal prejudice as a
22 result of the dismissal." Hamilton v. Firestone Tire & Rubber Co.,
23 Inc., 679 F.2d 143, 145 (9th Cir. 1982). The Ninth Circuit has
24 defined legal prejudice in this context as "prejudice to some legal
25 interest, some legal claim, [or] some legal argument." Westlands
26 Water Dist. v. United States, 100 F.3d 94, 97 (9th Cir. 1996).

27 The decision to grant a voluntary dismissal under Rule 41(a)(2)
28

1 is addressed to the sound discretion of the court. Sams v. Beech
2 Aircraft Corp., 625 F.2d 273, 277 (9th Cir. 1980). "In exercising
3 this discretion, the court must make three separate determinations:
4 (1) whether to allow dismissal at all; (2) whether the dismissal
5 should be with or without prejudice; and (3) what terms and
6 conditions, if any, should be imposed." Burnette v. Godshall, 828
7 F.Supp. 1439, 1443 (N.D. Cal. 1993), aff'd sub nom Burnette v.
8 Lockheed Missiles & Space Co., 72 F.3d 766 (9th Cir. 1995). See also
9 United States v. One Tract of Real Property, 95 F.3d 422, 425 (6th
10 Cir. 1996) (by providing that a dismissal under Rule 41(a)(2) is
11 without prejudice "[u]nless otherwise specified," the rule "implicitly
12 permits the district court to dismiss an action with prejudice in
13 response to a plaintiff's motion to dismiss without prejudice").

14 McGuigan objects to dismissal without prejudice. She urges the
15 court to dismiss the counter-claim with prejudice or deny the
16 dismissal. McGuigan asserts that the court may not dismiss the action
17 without prejudice inasmuch as (1) she is entitled to a resolution of
18 the fraud claims which Belair has brought against her; (2) the court
19 has dismissed the counter-claim as against Sizzler without prejudice;
20 (3) she should not have to face the prospect of a second lawsuit on
21 these same charges, were Belair to decide to refile the action in
22 state court at some point in the future; and (4) her interest in a
23 future suit for malicious prosecution against Belair would be
24 compromised by a dismissal without prejudice. Alternatively, were the
25 court inclined to dismiss without prejudice, McGuigan seeks attorney's
26 fees and costs incurred in defending against the counter-claim as a

1 condition of a dismissal.

2 McGuigan's argument that the two-dismissal rule bars the court
3 from approving a dismissal without prejudice lacks merit. The two-
4 dismissal rule contained in subsection (a)(1) is not implicated here,
5 given that Belair seeks dismissal pursuant to Rule 41(a)(2). See
6 Sutton Place Development Co. v. Abacus Mortgage Investment Co., 826
7 F.2d 637, 640 (7th Cir. 1987) ("[b]y its own clear terms the 'two
8 dismissal rule applies only when the second dismissal is by notice
9 under Rule 41(a)(1). It does not apply to . . . dismissal by court
10 order under Rule 41(a)(2)") (internal quotations omitted), cited with
11 approval in Lake at Las Vegas Investors Gp., Inc. v. Pacific Malibu
12 Development Corp., 933 F.2d 724, 727 (9th Cir. 1991). Cf. American
13 Cyanamid Co. v. McGhee, 317 F.2d 295, 298 (5th Cir. 1963) (noting that
14 Rule 41(a)(2) provides that the court may order a second dismissal,
15 gained pursuant to that subsection, to be with prejudice if the
16 repeated request is "obsessively prejudicial").

17 Also without merit is McGuigan's argument that she should not
18 have to face the prospect of a second lawsuit filed in state court.
19 The Ninth Circuit has held that the possibility of a later suit does
20 not rise to the level of legal prejudice which would allow the court
21 to deny Belair a dismissal without prejudice. Hamilton v. Firestone,
22 679 F.2d at 145.

23 However, there is merit to McGuigan's claim that she will suffer
24 legal prejudice as a result of a dismissal without prejudice because
25 her ability to bring suit against Belair for malicious prosecution
26 would be compromised. McGuigan claims that Belair is acting with
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1 malice and without reasonable grounds in maintaining the counter-claim
2 against her as an individual. A determination on the merits is
3 necessary to maintain a malicious prosecution claim under California
4 law. See McCubrey v. Veninga, 39 F.3d 1054, 1055 (9th Cir. 1994).
5 However, a dismissal without prejudice pursuant to Rule 41(a)(2)
6 leaves the parties where they would have stood had the lawsuit never
7 been brought. See Ryan v. Loui (In re Corey), 892 F.2d 829, 835 (9th
8 Cir. 1989), quoting Humphreys v. United States, 272 F.2d 411, 412 (9th
9 Cir. 1959) ("a suit dismissed without prejudice pursuant to Rule
10 41(a)(2) leave the situation the same as if the suit had never been
11 brought in the first place"). It is reasonable for McGuigan to fear
12 that a dismissal without prejudice would make it impossible for her to
13 be heard regarding her claim of malicious prosecution, and therefore
14 impossible for her to gain recompense for the damage suffered to her
15 reputation by virtue of the fraud allegations.⁸

17 ⁸ McGuigan's claim that she is entitled to a resolution on the
18 merits simply because she needs to clear her reputation is off the
19 mark. First, "plain legal prejudice [does not] arise from defendant's
20 missed opportunity for a legal ruling on the merits." Watson v.
21 Clark, 716 F.Supp. 1354, 1355 (D. Nev. 1989), citing In re Fed.
22 Election Campaign Act Litigation, 474 F.Supp. 1051, 1052 (D. D.C.
23 1979), aff'd without opinion, 909 F.2d 1490 (D.C. Cir. 1990). Second,
24 while McGuigan is probably correct that a dismissal without prejudice
25 will, under the circumstances of this case, effectively foreclose her
26 opportunity to clear her name, this does not in and of itself appear
27 to rise to the level of legal prejudice under Westlands, inasmuch as
28 prejudice to one's career reputation does not constitute prejudice to
a legal interest, legal claim or legal argument.

In Westlands, the Ninth Circuit held that uncertainty over water
rights if the matter remained unresolved was insufficient to
constitute plain legal prejudice. 100 F.3d at 97 (rejecting the
Eighth Circuit's holding in Paulucci v. City of Duluth, 826 F.2d 780,

1 Belair seeks to dismiss its counter-claim against McGuigan as it
2 appears to have received the basic elements of relief by settling with
3 Sizzler. Further litigation at this point would not appear to be cost
4 effective for Belair. Belair's indication that it did not wish to
5 pursue the matter in state court if this action is dismissed without
6 prejudice is significant. A result which prevents a legal claim from
7 being able to be brought prejudices that claim and thus constitutes
8 legal prejudice under Westlands.

9 While the court "do[es] not mean to imply that by filing a
10 counterclaim in malicious prosecution, or by professing an intention
11 to do so later, any defendant may defeat any motion for dismissal
12 without prejudice," Selas Corp. of Amer. v. Wilshire Oil Co. of Tex.,
13 57 F.R.D. 3, 6 (E.D. Pa. 1972), the court finds in Selas support for
14 its conclusion that a dismissal without prejudice under the
15 circumstances of this case would prejudice McGuigan. In Selas, a
16 corporate employee was sued as an individual, along with the
17 corporation, for damages arising from alleged violation of securities

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19 783 (8th Cir. 1987), that the trial court did not abuse its discretion
20 when it denied the motion to voluntarily dismiss the action where a
21 failure to resolve the claim would generate uncertainty about title to
22 land and possibly jeopardize development). But see Radiant Technology
23 Corp. v. Electrovert USA Corp., 122 F.R.D. 201, 204 (N.D. Tex. 1988)
24 ("[t]he nature of a plaintiff's claims may be such that, if the
25 defendant is not afforded the opportunity for vindication on the
26 merits in this forum, it will incur legal prejudice. This may be so
27 due to . . . the character of the allegations of plaintiff's
28 complaint").

25 It appears that, in the Ninth Circuit, the issue of McGuigan's
26 need to clear her reputation is best handled within the context of her
27 ability to file a malicious prosecution suit if Belair's counter-claim
28 is dismissed without prejudice.

1 and banking laws. The plaintiff settled with the corporation, gaining
2 much of the relief it sought in instituting the suit, and then moved
3 to dismiss the employee without prejudice under Rule 41(a)(2). Id. at
4 5. The court found that a dismissal without prejudice "would, under
5 the circumstances of this case, constitute clear legal prejudice to
6 the defendant." Id. at 6. The court explained that, "[w]hile we
7 express no opinion whatever on the merits of [the employee's] claim
8 [for malicious prosecution], we think he has a right at some point at
9 least to be heard on it." Id.

10 Finally, in reaching a determination whether Belair ought to be
11 granted a dismissal without prejudice, the court also considers the
12 fact that McGuigan has pending a motion for summary judgment.
13 Paulucci v. City of Duluth, 826 F.2d 780, 783 (8th Cir. 1987) ("[i]n
14 Pace v. Southern Express Co., 409 F.2d 331, 334 (7th Cir. 1969), the
15 court identified the following factors to be considered in deciding a
16 Rule 41(a)(2) motion: . . . and (4) the fact that a motion for summary
17 judgment has been filed by the defendant"). An attempt to avoid an
18 adverse decision on the merits may constitute legal prejudice. See
19 Phillips USA, Inc. v. Allflex USA, Inc., 77 F.3d 354, 358 (10th Cir.
20 1996) ("a party should not be permitted to avoid an adverse decision
21 on a dispositive motion by dismissing a claim without prejudice");
22 Pace v. Southern Express Co., 409 F.2d 331, 334 (7th Cir. 1969)
23 (affirming the denial of plaintiff's motion to dismiss without
24 prejudice on the basis that, inter alia, plaintiff "was attempting to
25 deprive the defendant of a ruling on the summary judgment motion by
26 its dismissal tactic").

1 McGuigan could not defeat Belair's motion to dismiss simply by
2 filing a motion for summary judgment, and her success on summary
3 judgment is uncertain. However, the fact that McGuigan has filed a
4 motion for summary judgment, and that a dismissal without prejudice
5 would allow Belair to avoid a decision on the merits weighs, even if
6 slightly, in favor of McGuigan.⁹ See Kovalic v. DEC Int'l, Inc., 855
7 F.2d 471, 474 (7th Cir. 1988) ("[t]he enumeration of the factors to be
8 considered in Pace is not equivalent to a mandate that each and every
9 such factor be resolved in favor of the [plaintiff] before dismissal
10 is appropriate") (internal quotations omitted).

11 The court finds that Belair is not entitled to voluntarily
12 dismiss its counter-claim against McGuigan without prejudice. If
13 otherwise, McGuigan would suffer legal prejudice, both by being
14 effectively foreclosed from bringing a subsequent action for malicious
15 prosecution against Belair, and from Belair's avoidance of a
16 resolution of McGuigan's motion for summary judgment.

17 Beyond opposing dismissal without prejudice, McGuigan has urged
18 the court to dismiss Belair's counter-claim with prejudice. The court
19 may consider McGuigan's request if Belair has had an opportunity to
20 oppose such a dismissal. See One Tract, 95 F.3d at 426 ("the
21 plaintiff is entitled to an opportunity to be heard in opposition to
22 dismissal with prejudice"). McGuigan having requested dismissal with
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24 ⁹ McGuigan filed her motion on July 30, 1999, after Belair had
25 filed its motion seeking approval of a voluntary dismissal on July 29,
26 1999. However, it is unlikely that McGuigan filed her motion in
27 response to Belair's motion, in an to manipulate the summary judgment
28 factor.

1 prejudice in her response in opposition to Belair's motion, Belair had
2 the opportunity to argue against a dismissal with prejudice in its
3 reply brief and at the hearing on its motion. Thus, it is appropriate
4 for the court to consider whether dismissal with prejudice is
5 warranted. See id. (holding that it is not an abuse of the trial
6 court's discretion to dismiss with prejudice upon plaintiff's motion
7 to dismiss without prejudice, where defendant requested in his filings
8 that the dismissal be with prejudice, and the plaintiff had an
9 opportunity to argue against such action at the hearing).

10 Belair argues that the court should not dismiss its counter-claim
11 with prejudice because, in a subsequent malicious prosecution suit, a
12 dismissal could give rise to the inference that Belair lacked
13 reasonable grounds for maintaining the counter-claim against McGuigan.
14 We agree with the court in Selas that this is not "a factor which
15 ought seriously to influence our decision here, both because the
16 possibility of injustice seems remote and because it is not entirely
17 relevant under the standards for deciding a motion for voluntary
18 dismissal." 57 F.R.D. at 5 n.2.

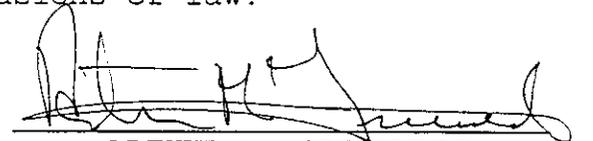
19 However, the court may not dismiss Belair's counter-claim with
20 prejudice without first giving Belair the opportunity to withdraw its
21 motion and proceed with litigating the counter-claim. See Lau v.
22 Glendora Unified School Dist., 792 F.2d 929, 931 (9th Cir. 1986)
23 (plaintiff must be given "a reasonable period of time within which
24 [either] to refuse the conditional voluntary dismissal by withdrawing
25 [the] motion for dismissal or to accept the dismissal despite the
26 imposition of conditions"); One Tract, 95 F.3d at 426 (abuse of
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1 granting McGuigan's request to dismiss with prejudice the
2 counterclaim. Belair's motion to dismiss without prejudice is denied.

3 If Belair timely elects to proceed with prosecuting the counter-
4 claim, the court will set a further status conference hearing
5 regarding McGuigan's motion for summary judgment and request to file a
6 third party complaint.

7 The contents of this Memorandum of Decision has constitute the
8 court's findings of fact and conclusions of law.

9 DATED" MARCH 13, 2000

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11 ARTHUR M. GREENWALD
12 United States Bankruptcy Judge
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5 UNITED STATES BANKRUPTCY COURT
6 CENTRAL DISTRICT OF CALIFORNIA
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8 In re:) BK CASE NO. SV 96-16075-AG
9 SIZZLER RESTAURANTS)
INTERNATIONAL, INC.,) (Jointly administered with:
10 Debtor.) Case Nos. SV 96-16076-AG
11) SV 96-16077-AG
SV 96-16078-AG
SV 96-16079-AG)

12 XX Affects all Debtors.

13 SIZZLER USA RESTAURANTS, INC.)

14 Plaintiff,)

15 vs.)

16 BELAIR & EVANS LLP,)

17 Defendant.)

Chapter 11
ADV. NO. 98-1720-AG

18 BELAIR & EVANS LLP,)

19 Counterclaimant,)

20 vs.)

21 SIZZLER USA RESTAURANTS, INC.;)

22 KATHRYN T. McGUIGAN;)

23 NATIONAL UNION FIRE)

INSURANCE CO.,)

24 Counterclaim Defendants.)
25

NOTICE OF ENTRY OF JUDGMENT OR
ORDER AND CERTIFICATE OF
MAILING

26 TO ALL PARTIES IN INTEREST ON THE ATTACHED SERVICE LIST:

27 You are hereby notified, pursuant to Local Bankruptcy Rule 9021-1(1)(a)(v), that a judgment or
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1 order entitled MEMORANDUM DEPOSITION RE COUNTER-CLAIMANT'S MOTION TO
2 APPROVE VOLUNTARY DISMISSAL OF ADVERSARY PROCEEDINGS; OR
3 ALTERNATIVELY FOR PERMISSIVE ABSTENTION was entered on ~~MAY 23 2000~~

4 I hereby certify that I mailed a copy of this notice and a true copy of the order or Judgment to the
5 person(s) and entities listed on _____
6

7 DATED: ~~MAY 23 2000~~

JON D. CERETTO, Clerk

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10 By _____
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12 (A copy of the judgment or order must be attached to this notice.)
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