

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

IN RE:)	
)	
ITT EDUCATIONAL SERVICES, INC., <i>et al.</i> ¹)	Case No. 16-07207-JMC-7A
)	
Debtors.)	Jointly Administered

**TRUSTEE’S MOTION TO COMPROMISE AND SETTLE
CERTAIN CLAIMS WITH THE CALIFORNIA FRANCHISE TAX BOARD**

Deborah J. Caruso, the chapter 7 trustee in this case (the “Trustee”), by counsel, requests, pursuant to 11 U.S.C. §§ 105(a) and 363 and Rule 9019 of the Federal Rules of Bankruptcy Procedure, approving the terms of a proposed settlement by and between the Trustee, not individually but solely in her capacity as the chapter 7 trustee for, and acting for and on behalf of ITT (as defined below), and ITT’s bankruptcy estate, on the one hand, and the California Franchise Tax Board (the “FTB”), on the other hand, regarding ITT’s filed protests contesting Notices of Proposed Assessments issued by FTB after audits for the 2008, 2009, and 2010 tax years on the following grounds:

I. JURISDICTION

1. The Court has jurisdiction over this motion pursuant to 28 U.S.C. §§ 157 and 1334. This matter is a core proceeding within the meaning of 28 U.S.C. § 157(b).
2. Venue is proper in this district pursuant to 28 U.S.C. §§ 1408 and 1409.
3. The statutory predicates for relief are sections 105 and 363 of the United States Code (the “Bankruptcy Code”) and Rule 9019 of the Federal Rules of Bankruptcy Procedure (the “Bankruptcy Rules”).

¹ The debtors in these cases, along with the last four digits of their respective federal tax identification numbers are ITT Educational Services, Inc. [1311]; ESI Service Corp. [2117]; and Daniel Webster College, Inc. [5980].

II. BACKGROUND

4. On September 16, 2016 (the “Petition Date”), ITT Educational Services, Inc. (“ITT”), ESI Service Corp. (“ESI”) and Daniel Webster College, Inc. (“DWC,” and together with ITT and ESI, the “Affiliated Debtors”) filed voluntary petitions for relief under chapter 7 of the Bankruptcy Code. The Trustee was appointed interim trustee under section 701 of the Bankruptcy Code in each of the Affiliated Debtors’ bankruptcy cases on the Petition Date, and in accordance with section 702(d) of the Bankruptcy Code, became the permanent case trustee on November 1, 2016 following the conclusion of the meeting of creditors held pursuant to section 341(a) of the Bankruptcy Code.

5. On October 4, 2016, the Court entered its *Order Granting Motion for Joint Administration of Chapter 7 Cases* [Docs 221 & 222], directing the Affiliated Debtors’ bankruptcy cases to be jointly administered for procedural purposes only.

6. On or about January 25, 2017, the FTB filed its original proof of claim in ITT’s bankruptcy case (Claim No. 1880) (the “FTB POC”). After various amendments to the FTB POC, the FTB filed its final amendment to the FTB POC on or about December 4, 2019, asserting a secured claim in the amount of \$894,576.00 related to the 2008 tax year, an unsecured priority claim in the amount of \$8,693,953.76 related to the 2008, 2009, 2010 and 2016 tax years, and an unsecured general claim in the amount of \$1,504,421.80 related to the 2008, 2009, and 2010 tax years.²

² The FTB also filed claims in the DWC bankruptcy case—Claim No. 374 and 511. Claim No. 511 in DWC was disallowed in its entirety and Claim No. 374 in DWC was allowed as a section 507(a)(5) priority claim in the modified amount of \$823.54. See *Order Sustaining Trustee’s 4th Omnibus Objection to Claims Pursuant to Bankruptcy Rule 3007(d)(5)* [DWC Doc 90]. Claim No. 374 in DWC was paid in full pursuant to the *Order Granting Trustee’s Motion for Authority to Make Interim Distributions to Holders of Allowed Priority Claims and Allowed Unsecured Claims* [DWC Doc 98]. The FTB also filed a separate claim in the ITT bankruptcy case—Claim No. 3392. Claim No. 3392 was disallowed in its entirety. See *Order Sustaining Trustee’s 25th Omnibus Objection to Claims Pursuant to Bankruptcy Rule 3007(d)(5)* [Doc 4419].

7. The amounts listed on the FTB POC were primarily based on Notices of Proposed Assessment issued by the FTB after audits for the 2008, 2009, and 2010 tax years, together with interest and penalties associated with those tax years. Prior to the Petition Date, ITT filed protests contesting the Notices of Proposed Assessment, which were still pending on the Petition Date.

III. COMPROMISE AND SETTLEMENT

8. Following the Petition Date, the Trustee, with the assistance of her CPAs and financial advisors at BGBC Partners, LLP (“BGBC”), engaged in settlement discussions with the FTB regarding the resolution of the contested Notices of Proposed Assessment. Such discussions have resulted in a proposed compromise and settlement that has been memorialized in the *Settlement Agreement* (the “Agreement”) attached to this motion as Exhibit 1.

9. Pursuant to the Agreement, to resolve the dispute identified in ITT’s protest to the Notices of Proposed Assessment, the Trustee, on behalf of ITT, will agree that ITT owes taxes in the amount of \$570,599.00 for the 2008 tax year, \$709,625.00 for the 2009 tax year, and \$1,165,208.00 for the 2010 tax year, together with any interest or penalties associated with those tax years. These amounts shall be immediately assessed pursuant to the California Revenue and Taxation Code section 19088 and the FTB is authorized to use any and all available credits, including the \$895,376.00 credit listed on the FTB POC, and all overpayments related to the 2011, 2012 and 2015 tax years to offset the outstanding balance due for the 2008, 2009 and 2010 tax years.

10. Pursuant to the Agreement, after all offsets, the FTB will file an amendment to the FTB POC, which shall reflect an allowed unsecured priority claim pursuant to section 507(a)(5) of the Bankruptcy Code in the amount of \$117,261.74 and a general unsecured claim in the

amount of \$233,041.60. The amended FTB POC is to be paid in accordance with the distribution scheme provided in section 726 of the Bankruptcy Code.

11. The Agreement is a final and conclusive resolution of the FTB POC and all tax, penalties, interest or other additions to or refunds of California income/franchise tax liability of ITT related to any taxable year ending prior to the Petition Date.

12. The Agreement is effective upon the following: (a) execution by all parties; (b) approval of the Agreement by the FTB's Executive Officer; (c) approval of the Agreement by the three-member Franchise Tax Board, itself, or waiver of this requirement; and (d) Court approval of the Agreement. All conditions for effectiveness have been satisfied or waived as of the filing of this motion, with the exception of Court approval.³

III. RELIEF REQUESTED

13. The Trustee requests entry of an order, pursuant to sections 105(a) and 363 of the Bankruptcy Code and Bankruptcy Rule 9019, (a) approving the settlement between the Trustee and the FTB as contained in the Agreement, (b) authorizing the Trustee to enter into the Agreement, and (c) directing the FTB to amend the FTB POC to reflect an allowed unsecured priority claim pursuant to section 507(a)(5) of the Bankruptcy Code in the amount of \$117,261.74 and a general unsecured claim in the amount of \$233,041.60, which once amended, shall be paid in accordance with the distribution scheme as provided in section 726 of the Bankruptcy Code.

IV. GROUNDS FOR GRANTING RELIEF

14. A court may authorize a trustee to enter into a settlement so long as it is a sound exercise of the trustee's business judgment. *See* 11 U.S.C. § 363(b); *In re UAL Corp.*, 443 F.3d

³ The Agreement also provides that it shall have no force or effect if these conditions are not met by January 31, 2022, unless extended. The parties have reached an agreement extending the January 31, 2022 deadline.

565, 571 (7th Cir. 2006) (use under section 363 of the Bankruptcy Code must “[make] good business sense”); *In re Schipper*, 933 F.2d 513, 515 (7th Cir. 1991) (section 363 involves exercise of fiduciary duties and requires an “articulated business justification”); *see also In re Olde Prairie Block Owners, LLC*, 448 B.R. 482, 492 (Bankr. N.D. Ill. 2011) (same). Moreover, when applying the “business judgment” standard to a use of estate property under section 363 of the Bankruptcy Code, a trustee’s judgment is “entitled to great judicial deference as long as a sound business reason is given.” *See In re Efoora, Inc.*, 472 B.R. 481, 488 (Bankr. N.D. Ill. 2012).

15. Similarly, Bankruptcy Rule 9019(a) sets forth the requirements for compromises and settlements and permits a bankruptcy court to approve a trustee’s “compromise or settlement” after notice and a hearing, if such settlement is “fair and equitable . . . and in the best interests of the bankruptcy estate.” *Depoister v. Mary M. Holloway Found.*, 36 F.3d 582, 586 (7th Cir. 1994); *see also In re Energy Co-op., Inc.*, 886 F.2d 921, 927 (7th Cir. 1989) (“The benchmark for determining the propriety of a bankruptcy settlement is whether the settlement is in the best interest of the estate.”); *In re Smith*, No 02-16450-JKC-7A, 2008 Bankr. LEXIS 2821, *6 (Bankr. S.D. Ind. Sept. 10, 2008) (same). Settlements should be approved unless “the settlement ‘falls below the lowest point in the range of reasonableness.’” *In re Commercial Loan Corp.*, 316 B.R. 690, 698 (Bankr. N.D. Ill. 2004) (quoting *Energy Co-op.*, 886 F.2d at 929); *In re Doctors Hosp. of Hyde Park, Inc.*, 474 F.3d 421, 426 (7th Cir. 2007); *see also In re Artra Grp., Inc.*, 300 B.R. 699, 702 (Bankr. N.D. Ill. 2003). Settlements and compromises are favored in bankruptcy because they expedite case administration and reduce unnecessary administrative costs. *Fogel v. Zell*, 221 F.3d 955, 960 (7th Cir. 2000). In determining whether a compromise is in the best interests of the estate, the Court must compare “the settlement’s terms with the litigation’s probable costs and probable benefits.” *In re Am. Reserve Corp.*, 841 F.2d 159, 161

(7th Cir. 1987); *see also Doctors Hosp.*, 474 F.3d at 426 (“Among the factors the court considers are the litigation’s probability of success, complexity, expense, inconvenience, and delay, including the possibility that disapproving the settlement will cause wasting of assets.” (internal quotation marks and citations omitted); *Commercial Loan*, 316 B.R. at 697 (holding that relevant factors a bankruptcy court should consider in approving a settlement include “the litigation’s probability of success, its complexity, and its ‘attendant expense, inconvenience and delay’” (quoting *Am. Reserve Corp.*, 841 F.2d at 161)).

16. Here, the proposed compromise and settlement memorialized in the Agreement provides for a resolution of the contested Notices of Proposed Assessments issued by the FTB prepetition for the 2008, 2009 and 2010 tax years, resulting in significantly reduced tax liability for ITT’s bankruptcy estate. Such resolution was negotiated by the Trustee’s CPAs and financial advisors, BGBC.

17. For the foregoing reasons, the Trustee has determined, in the exercise of her sound business judgment, that the Agreement is fair, equitable, in the best interest of the Affiliated Debtors’ bankruptcy estates, and well within the range of reasonableness for approval under Bankruptcy Rule 9019(a). Accordingly, the Trustee submits that the Court should approve the settlement between the Trustee and FTB as contained in the Agreement and authorize the Trustee to enter into the Agreement.

V. NOTICE

18. Pursuant to the *Notice, Case Management and Administrative Procedures* (the “Case Management Procedures”) approved by the Court on October 4, 2016 [Doc 220], the Trustee will serve a copy of this motion, including the exhibits, on the following (as defined in the Case Management Procedures): (a) the Core Group; (b) the Request for Notice List; (c) the Appearance List; and (d) the FTB.

NOTICE IS GIVEN, that pursuant to the Case Management Procedures, any objection to this motion must be in writing and filed with the Bankruptcy Clerk by no later than **4:00 p.m.** (prevailing Eastern time) on **February 9, 2022**. Parties not represented by an attorney may deliver any written objection to this motion as follows: (a) by U.S. mail, courier, overnight/express mail at Clerk, United States Bankruptcy Court, Re: *In re ITT Educational Services, Inc., et al.*, 116 U.S. Courthouse, 46 East Ohio Street, Indianapolis, IN 46204; or (b) by publicly accessible drop box available at the Indianapolis Division located at the New York Street and Pennsylvania Street entrance.

The objecting party must also serve a copy of the written objection upon the Trustee's counsel, at Counsel for Trustee Deborah J. Caruso, Rubin & Levin, P.C., 135 N. Pennsylvania Street, Suite 1400, Indianapolis, IN 46204 (mtheisen@rubin-levin.net). **If an objection is NOT timely filed, the requested relief may be granted without a hearing.**

NOTICE IS FURTHER GIVEN that in the event an objection to this motion is timely filed, a hearing on this motion and such objection will be conducted on **February 16, 2022** at **1:30 p.m.** (prevailing Eastern Time), in Room 325 of the United States Courthouse, 46 East Ohio Street, Indianapolis, IN 46204. Interested parties may also participate at the hearing by conference call by calling 1-888-273-3658, passcode 6349352#.

WHEREFORE, the Trustee respectfully requests entry of an order: (i) approving the settlement between the Trustee and the FTB as contained in the Agreement; (ii) authorizing the Trustee to enter into the Agreement; (iii) directing the FTB to amend the FTB POC to reflect an allowed unsecured priority claim pursuant to section 507(a)(5) of the Bankruptcy Code in the amount of \$117,261.74 and a general unsecured claim in the amount of \$233,041.60, which once amended, shall be paid in accordance with the distribution scheme as provided in section 726 of the Bankruptcy Code, and (iv) granting the Trustee all other just and proper relief.

Respectfully submitted,

RUBIN & LEVIN, P.C.

By: /s/ Meredith R. Theisen

Meredith R. Theisen

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CERTIFICATE OF SERVICE

I hereby certify that on January 17, 2022, a copy of the foregoing *Trustee's Motion to Compromise and Settle Certain Claims with the California Franchise Tax Board* was filed electronically. Pursuant to Section IV.C.3(a) of the Case Management Procedures, notice of this filing will be sent to the following parties through the Court's Electronic Case Filing System. Parties may access this filing through the Court's system.

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I further certify that on January 17, 2022, pursuant to Section IV.C.3(c) of the Case Management Procedures, a copy of the foregoing *Trustee's Motion to Compromise and Settle Certain Claims with the California Franchise Tax Board* was emailed to the following:

CEC Red Run, LLC: Alan M. Grochal at agrochal@tydingslaw.com
SWRE Deal V Building, LLC: Paul Weiser at pweiser@buchalter.com
Tarrant County/Dallas County: Elizabeth Weller at dallas.bankruptcy@publicans.com
Northwest Natural Gas Company: Ashlee Minty at Ashlee.Minty@nwnatural.com
Solar Drive Business, LLC: Chris W. Halling at challing@hallingmeza.com
Market-Turk Company: Jordan A. Lavinsky at jlavinsky@hansonbridgett.com
Taxing Authority for Harris County, Texas: John P. Dillman at houston_bankruptcy@lgbs.com
Texas Comptroller of Public Accounts: Rachel Obaldo at rachel.obaldo@oag.texas.gov
Clear Creek Independent School District: Carl O. Sandin at csandin@pbfc.com
Synchrony Bank: Recovery Management Systems Corporation at claims@recoverycorp.com
Bexar County: Don Stecker at sanantonio.bankruptcy@publicans.com
SWRE Deal V Building, LLC: Nancy K. Swift at nswift@buchalter.com
TN Dept. of Revenue: Michael Willey at michael.willey@ag.tn.gov
Florida Department of Education: Benman D. Szeto at benman.szeto@fldoe.org
Last Second Media, Inc.: T. Todd Eglund at tegland@beldenblaine.com
Hung Duong: Kevin Schwin at kevin@schwinlaw.com
Travis County: Kay D. Brock at kay.brock@traviscountytexas.gov
Able Building Maintenance: Scott D. Fink at bronationalecf@weltman.com
Marathon Ventures, LLC: Daniel M. Karger at kargerlaw@gmail.com
Oklahoma County Treasurer: Tammy Jones at tammy.jones@oklahomacounty.org
JM Partners LLC: John Marshall at jmarshall@jmpartnersllc.com

I further certify that on January 18, 2022, pursuant to Section IV.C.3(c) of the Case Management Procedures, a copy of the foregoing *Trustee's Motion to Compromise and Settle Certain Claims with the California Franchise Tax Board* was mailed by first-class U.S. Mail, postage prepaid, and properly addressed to the following:

Franchise Tax Board
Bankruptcy Section MS A340
P.O. Box 2952
Sacramento, CA 95812

/s/ Meredith R. Theisen

Meredith R. Theisen

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EXHIBIT 1

[Agreement]

SETTLEMENT AGREEMENT

This settlement agreement (the "Agreement") is entered into as of November __, 2021 (the "Execution Date") by and between Deborah J. Caruso, as duly appointed chapter 7 trustee of ITT Educational Services Inc., and not in her individual capacity (hereinafter, the "Debtor"), on the one hand, and the California Franchise Tax Board (the "FTB") on the other hand. The Trustee and the FTB shall be referred to as the "Parties".

Recitals

A. On or about September 16, 2016 (the "petition date") the Debtor commenced a voluntary case under chapter 7 of the Bankruptcy Code in the United States Bankruptcy Court for the Southern District of Indiana (the "Bankruptcy Court") entitled *In re ITT Educational Services, Inc., et al.*, Case No. 16-07207-JMC-7A (the "Bankruptcy Case."¹)

B. On or about September 16, 2016, Deborah J. Caruso was appointed as the Chapter 7 trustee of the Bankruptcy estate.

C. On or about October 4, 2016, the court set the bar date for governmental units to file proofs of claim in Debtor's cases for March 15, 2017 (the "Bar Date")

D. On or about January 25, 2017, FTB filed its original proofs of claims in the Bankruptcy Case as Claim No. 1880. After various amendments to its proof of claim, FTB filed its final amended proof of claim on or about December 4, 2019, on the claim register as Claim No 1880 ("FTB's Proof of Claim") asserting a secured claim in the amount of \$894,576 related to the 2008 tax year; an unsecured priority claim in the amount of \$8,693,953.76 related to the 2008, 2009, 2010 and 2016 tax years; and an unsecured general claim in the amount of \$1,504,421.80 related to the 2008, 2009, and 2010 tax years. Additionally FTB filed protective claims with amounts listed as TBD for the 2011 - 2015 tax years based on potential IRS claims for those tax years. .

E. The amounts listed on FTB's Proof of Claim were primarily based on Notices of Proposed Assessment issued by FTB after audit for the 2008, 2009, and 2010 tax years, together with interest and penalties associated with those tax years. ITT Educational Services Inc. filed protests contesting the Notices of Proposed Assessment.

F. The Parties engaged in negotiations regarding the nature, amount, and priority of the FTB's Proof of Claim and have reached an agreement as to the amount and treatment of the FTB's Proof of Claim on the terms and conditions set forth herein.

G. Now, therefore, in consideration of the foregoing, the Parties stipulate and agree as follows:

¹ This case is being jointly administered with two other related entities; ESI Services Corp and Daniel Webster College, Inc.

Agreement

1. This Agreement shall be effective on the "Effective Date," which shall be the date when the last of the following has occurred: (a) All parties have executed this Agreement; (b) FTB's Executive Officer has approved this Agreement; (c) the three-member Franchise Tax Board, itself, has approved this Agreement, or FTB has waived this requirement; (d) the Bankruptcy Court has approved this Agreement. This Agreement shall have no force or effect if it does not become effective by January 31, 2022, unless the Parties agree, in writing, to extend the deadline.

2. To resolve the dispute identified in Debtor's protest, the Debtor agrees that Debtor owes taxes in the amount of \$570,599 for the 2008 tax year, \$709,625 for the 2009 tax year, and \$1,165,208 for the 2010 tax year, together with any interest or penalties associated with those tax years. These amounts shall be immediately assessed pursuant to California Revenue and Taxation Code section 19088 and FTB is authorized to use any and all available credits, including the \$895,376 credit listed on FTB's Proof of Claim, and all overpayments related to the 2011, 2012 and 2015 tax years to offset the outstanding balance due for the 2008, 2009 and 2010 tax years.

3. FTB will file an amended claim 1880 which shall be allowed as an unsecured priority claim in the amount of \$117,261.74 and an unsecured general claim in the amount of 233,041.60 against ITT Educational Services, Inc. and paid in accordance with the Chapter 7 distributions scheme as provided in 11 USC § 726.

4. This Agreement shall be final and conclusive with respect to FTB's Proof of Claim and all tax, penalties, interest or other additions to or refunds of California income/franchise tax liability of ITT Educational Services Inc. related to any taxable year ending prior to the Petition Date (the "Subject Tax Years"). The Parties agree not to raise , by way of Notice of Proposed Assessment, proofs of claim, audit, motion, claim for refund, offset, and/or interest abatement any further adjustment to the amounts owed by the Debtor, as described in paragraph 2. This Agreement shall be binding upon all successors and assigns of each of the Parties to the Agreement.

5. This Agreement is a settlement of certain disputed tax matters, including the associated interest thereon. It is expressly understood and agreed by the Parties that in agreeing to such settlement neither Party has made any concessions regarding the merits of its positions or the merits of the other Party's positions regarding such disputed tax matters. Except as otherwise expressly set forth herein, this Agreement shall have no effect whatsoever upon the correctness of Taxpayers' returns and/or claims for refund for any year other than the Subject Tax Years.

6. This Agreement contains the entire agreement by and between the Parties with respect to the subject matter hereof, and all prior understandings or agreements, if any, are merged into this Agreement. There have been no prior oral or written understandings or agreements that are not part of this agreement.

7. This Agreement may only be changed, modified or otherwise altered in a writing executed by all the Parties to this Agreement. Oral modifications are not permitted.

8 For purposes of construing this Agreement, none of the Parties shall be deemed to have been the drafter of the Agreement.

9 Each of the Parties agrees to submit to the jurisdiction of the Bankruptcy Court for any action to enforce or interpret this Agreement, except to the extent that the Bankruptcy Court determines that it lacks jurisdiction.

10 Facsimile or other electronic copies of signatures on this Agreement are acceptable, and a facsimile or other electronic copy of a signature on this Agreement is deemed an original.

11 This Agreement may be executed in counterparts, each of which is deemed an original, but when taken together constitute one and the same document.

12 Each party shall bear the fees and costs arising from the actions of its own counsel and/or representative in connection with this dispute and the settlement thereon, including, but not limited to, those fees and/or costs related to the execution of this Agreement and the attendant responsibilities resulting therefrom.

13 This Agreement and the obligations of the Parties hereunder shall be binding on the Parties only if signed by all of the Parties and approved in accordance with the terms of the Bankruptcy Code. If an order by the Bankruptcy Court is required, the terms of that order must be approved by all of the Parties.

The Parties have executed and delivered this Agreement as of the date first set forth above.

The Bankruptcy Estate of ITT Education Services, Inc CALIFORNIA FRANCHISE TAX BOARD

By: _____
Name: Deborah J. Caruso
Title: Chapter 7 Trustee of ITT Educational Services Inc

By: _____
Name: Jozel Brunett
Title: Chief Counsel, State of California Franchise Tax Board