IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
VICTORIA DIVISION

In re:	**§**	**Chapter 11**
	§	
HII TECHNOLOGIES, INC., *et al.*[1]	**§**	**15-60070 (DRJ)**
Debtors	**§**	**(Jointly Administered)**

OBJECTION TO HAMILTONS' MOTION TO PRESERVE SETOFF RIGHTS
(Refers to Docket #427)

The Honorable David R. Jones, United States Bankruptcy Judge:

HII Technologies, Inc. ("HII") and its above-captioned affiliated debtors (collectively, the "Debtors"), file this Objection to the Motion to Preserve Creditors' Right to Setoff Claims Against Debtors' Estates (the "Motion," docket #427),[2] and would respectfully show the Court as follows:

Preliminary Statement

1. The Hamiltons did not include the required local rule 9013-1 notice conspicuously on the first page of the Motion. The purpose of local rule 9013 is to provide fair notice to creditors who may not otherwise be aware of the deadline (such as the trade creditors in this case). Out of an abundance of caution, the Debtors are responding to the Motion within 24 days of the Motion's filing date (March 24, 2016). At a minimum, proper notice of the objection deadline should be given to creditors through some remedial notice. Alternatively, the motion should be struck as the rules permit.

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[1] The Debtors in these chapter 11 cases, along with the last four digits of each Debtor's tax identification number, are: (i) Apache Energy Services, LLC (4404); (ii) Aqua Handling of Texas, LLC (4480); (iii) HII Technologies, Inc. (3686); (iv) Sage Power Solutions, Inc. fka KMHVC, Inc. (1210); and (v) Hamilton Investment Group, Inc. (0150).

[2] The Motion was filed by William Mark Hamilton ("Mark"), Sharon K. Hamilton ("Sharon"), William Craig Hamilton ("Craig"), S & M Assets, LLC ("S&M"), and H2 Services, LLC ("H2") (collectively, the "Hamiltons").

Jurisdiction and Venue

2. This Court has jurisdiction over this motion pursuant to 28 U.S.C. §§ 157 and 1334. Venue of the Debtors' chapter 11 cases in this district is proper pursuant to 28 U.S.C. §§ 1408 and 1409. This is a core proceeding pursuant to 28 U.S.C. § 157(b).

3. The statutory predicate for the relief sought is section 553 of the Bankruptcy Code. The Court has authority to enter final orders granting this relief.

Relief Requested

4. The Debtors request that this Court enter an order denying the Motion.

Factual Background

5. On or about August 11, 2014, HII purchased 100% of Hamilton Investment Group, Inc. ("HIG"), a frac-water transfer company in Guthrie, Oklahoma, from William Mark Hamilton and his wife Sharon K. Hamilton via a Stock Purchase Agreement ("SPA"). William Mark Hamilton and Sharon K. Hamilton were represented to be the sole owners of HIG.

6. After the sale of HIG to HII, HIG and William Mark Hamilton executed an employment agreement. William Mark Hamilton was HIG's President, and he oversaw HIG's day-to-day operations.

7. After the sale of HIG to HII, HIG entered into various leases of both real and personal property from William Mark Hamilton, Sharon K. Hamilton, William Craig Hamilton, S&M Assets, LLC (owned by William Mark Hamilton and his wife Sharon K. Hamilton) and H2 Services, LLC (owned by William Craig Hamilton). The board of directors of both HII and HIG did not approve these self-interested transactions. No third-party fairness opinion concluded that these transactions were objectively fair.

8. HIG terminated William Craig Hamilton, William Mark Hamilton, and Sharon K. Hamilton on June 4, 2015.

9. William Mark Hamilton, Sharon K. Hamilton, and S&M Assets filed suit against HII and HIG on June 26, 2015, seeking monies owed under three (3) of the self-interested lease agreements and an undocumented "loan" allegedly for $2.4 million.[3]

10. On September 18, 2015 (the "Petition Date"), the Debtors each filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code.

11. The Debtors continue to administer their assets as debtors-in-possession pursuant to sections 1107 and 1108 of the Bankruptcy Code.

OBJECTIONS TO MOTION

The Hamiltons do not meet the statutory requirements for setoff.

12. The Hamiltons cite 11 U.S.C. § 553 as authority to preserve a setoff right that would dollar-for-dollar reduce any amounts they owe. The statute does not provide the Hamiltons with the relief requested, because they have failed to meet its requirements.

13. Under the bankruptcy code, the filing of a petition creates an "estate" comprised of all the assets of the Debtor. 11 U.S.C. §§ 301, 541. The estate is not liable for the Debtors' prebankruptcy debts except as set forth in the claims payment process. Setoff based on prepetition conduct is available in bankruptcy only when both opposing claims arise prepetition and are "mutual" (meaning that both obligations are held by 1) the same parties, 2) in the same

[3] An accounts payable was kept on the books for the working capital adjustment but no separate "loan" obligation exists. The HII board did not approve of an undocumented "loan". Numerous legal restrictions applicable to HII prevent it from incurring a $2.4 Million loan obligation without a board-authorized note, a fact of which the Hamiltons were keenly aware. To the extent that the Hamiltons' claim relates to the SPA working capital adjustment, no demand was timely made under the SPA, and no proof of claim was timely filed to assert liability for breach of the SPA's working capital adjustment. Finally, the SPA (as discussed below) was induced by fraud and cannot be the basis for a claim against HII, if such a claim had been timely made and a proof of claim timely filed.

right, and 3) in the same capacity). 11 U.S.C. § 553(a); *Meyer Med. Physicians Grp., Ltd. v. Health Care Serv. Corp.*, 385 F.3d 1039, 1041 (7th Cir. 2004); *In re Davidovich*, 901 F.2d 1533, 1537 (10th Cir. 1990); *In re Public Serv. Co.*, 884 F.2d 11 (1st Cir. 1989); 5 COLLIER ON BANKRUPTCY ¶ 553.03[3] (16th ed.) Further, mutuality is strictly construed. *See In re Baja Boats*, 1997 Bankr. LEXIS 2125 at *19 (Bankr. N.D. Ohio 1997); *In re Communicall Cent., Inc.*, 106 B.R. 540, 545 (Bankr. N.D. Ill. 1989); 5 COLLIER ON BANKRUPTCY ¶ 553.03[3] (16th ed.).

14. With respect to the issue of capacity, a Debtor-in-possession suing as a trustee is not the same as the prepetition debtor. *In re OPM Leasing Serv.*, 68 B.R. 979, 986 (Bankr. S.D.N.Y. 1987) ("[O]bligations owing between a creditor and a pre-petition debtor may not be setoff against obligations owing between that same creditor and the debtor's estate since the requisite mutuality of obligations is absent."). Similarly, a Litigation Trustee is not the same as a prepetition debtor. Thus, the Hamiltons cannot satisfy the capacity element now (while the litigation rights are held by the Debtors-in-possesion), and will not be able to satisfy the capacity element postconfirmation (when the litigation rights are transferred to the Litigation Trust). As a result, the Motion should be denied.

15. In addition, as setoff requires claims related to the same parties, the alleged wrongs of Mr. Flemming cannot be used to setoff against the Debtors. *In re Candor Diamond Corp.*, 76 B.R. 342 (Bankr. S.D.N.Y. 1987) (principal of corporation not the same as corporation for mutuality). To the extent the Hamiltons' setoff rights relate to wrongs by persons other than the Debtors, the Motion should be denied.

16. Finally, even if the Hamiltons satisfied all conditions precedent for setoff (which they cannot), Fifth Circuit caselaw is clear that setoff is not available in connection with an action to recover fraudulent transfers. *See In re McConnell*, 934 F.2d 662, 667 (5th Cir. 1991)

("Section 553(a) setoffs, however, do not apply to actions by the Trustee to recover fraudulent transfers.") (citing *Mack v. Newton*, 737 F.2d 1343, 1366 (5th Cir. 1984) ("It would defeat the purpose of the Bankruptcy Act's provisions relating to fraudulent transfers to allow [creditors] to offset the value of the property thus transferred to them by the amount of their unsecured claim against [the debtor].")); *see also In re Acequia, Inc.*, 34 F.3d 800, 817 (9th Cir. 1994). The Motion should be denied with respect to any alleged setoff rights related to avoidance actions.

Even if the Hamiltons met the statutory requirements for setoff (which they do not), the Court has discretion to deny, and should deny, the Motion.

17. Courts have wide discretion to disallow setoff. *See, e.g., Brook v. Chase Bank USA, N.A. (In re Acosta-Garriga)*, 566 Fed. Appx. 787, 789 (11th Cir. 2014) ("[T]he right to set off is not absolute. Whether to allow set off is a decision that lies within the sound discretion of the bankruptcy court.") (citing *In re Kingsley*, 518 F.3d 874, 877 (11th Cir. 2008)); *Meyer Med. Physicians Grp., Ltd. v. Health Care Serv. Corp.*, 385 F.3d 1039, 1041 (7th Cir. 2004) (same); *In re S. Indus. Banking*, 809 F.2d 329 (6th Cir. 1987) ("when justice dictates, setoff must be denied"); *In re Shortt*, 277 B.R. 683, 688 (Bankr. N.D. Tex. 2002) ("Courts have construed the language of section 553(a) to be permissive in nature, rather than mandatory. Application of section 553(a), when properly invoked before a court, rests in the discretion of that court, which exercises such discretion under the general principles of equity.").

18. Key to exercising that discretion is whether the setoff would harm the reorganization. *See, e.g., In re Lincoln*, 144 B.R. 498 (Bankr. D. Mont. 1992) (setoff denied where collection necessary for reorganization); *In re Cloverleaf Farmers Co-op*, 114 B.R. 1010 (Bankr. D. S.D. 1990) (setoff denied as inconsistent with the rehabilitation of American farmers); *In re IML Freight*, 65 B.R. 788, 792 (Bankr. D. Utah 1986) (legislative history shows setoff appropriately denied in reorganization cases); *In re Penn Cent. Transp.*, 315 F. Supp. 1281

(E.D. Pa. 1970) (setoff denied because it would frustrate railroad reorganization process), *aff'd*, 453 F.2d 520 (3d Cir.), cert. denied, 408 U.S. 923 (1972).

19. The Court should deny the Hamiltons' attempt to preserve their setoff rights, as allowing setoff by insiders under these circumstances is inequitable. It would also will harm the reorganization of the Debtors.

CONCLUSION

20. The Hamiltons have failed to meet the requirements for setoff and, even if they did, the equities are such that setoff should not be allowed. As a result, the Motion should be denied.

The Debtors respectfully request that the Court deny the Motion and grant the Debtors such other and further relief, both at law and in equity, to which they may be justly entitled.

Dated: April 14, 2016.

MCKOOL SMITH, P.C.

By: */s/ Hugh M. Ray, III*
Hugh M. Ray, III
State Bar No. 24004246
600 Travis, Suite 7000
Houston, Texas 77002
Tel: 713-485-7300
Fax: 713-485-7344

Counsel for Debtors-in-Possession

CERTIFICATE OF SERVICE

The undersigned certifies that on April 14, 2016, a true and correct copy of this document was served via the ECF system to the parties on the ECF service list, including the United States Trustee, and the pleading is being delivered to the Noticing Agent for service upon the parties on the Master Service List.

/s/ Hugh M. Ray, III
Hugh M. Ray, III

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF TEXAS
VICTORIA DIVISION

In re:	§	**Chapter 11**
	§	
HII TECHNOLOGIES, INC., *et al.*[1]	§	**15-60070 (DRJ)**
Debtors	§	**(Jointly Administered)**

ORDER DENYING MOTION TO PRESERVE RIGHT TO SETOFF
(Refers to Docket No. 427)

On consideration of the Motion to Preserve Creditors' Right to Setoff Claims Against Debtors' Estates ("Motion") (docket #427) filed by William Mark Hamilton, Sharon K. Hamilton, William Craig Hamilton, S&M Assets, LLC, and H2 Services, LLC, any objections filed thereto, and the argument of counsel, if any, the Court rules as follows:

The Motion is DENIED.

SIGNED: _____, 2016.

_____
UNITED STATES BANKRUPTCY JUDGE

[1] The Debtors in these chapter 11 cases, along with the last four digits of each Debtor's tax identification number, are: (i) Apache Energy Services, LLC (4404); (ii) Aqua Handling of Texas, LLC (4480); (iii) HII Technologies, Inc. (3686); (iv) Sage Power Solutions, Inc. fka KMHVC, Inc. (1210); and (v) Hamilton Investment Group, Inc. (0150).