United States Court of Appeals

For the Seventh Circuit
Chicago, Illinois 60604

August 19, 2008

Before

FRANK H. EASTERBROOK, *Chief Judge*

RICHARD A. POSNER, *Circuit Judge*

DIANE P. WOOD, *Circuit Judge*

No. 07-2819

ANDREW J. MAXWELL, *Plaintiff-Appellant,*	Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.
v.	No. 03 C 3524
KPMG LLP, *Defendant-Appellee.*	Joan B. Gottschall, *Judge.*

ORDER

Our opinion in this appeal invited appellee KPMG to file motions in the district court and in this court for an award of reasonable attorneys' fees. *Maxwell v. KPMG LLP*, 520 F.3d 713, 719 (7th Cir. 2008). KPMG has filed a motion for sanctions with this court pursuant to Fed. R. App. P. 38. It also has filed a motion seeking leave to file in the district court a motion for sanctions under Fed. R. Civ. P. 11 and 28 U.S.C. § 1927. Appellant Andrew J. Maxwell has responded to the motions, both personally and in his official capacity as chapter 7 trustee for the bankruptcy estates of marchFirst, Inc. Counsel for the appellant also filed separate responses to KPMG's motions.

In March 2000 an IT consulting company called Whitman-Hart merged with US Web, a company that provided internet services, forming a company called marchFirst. The

technology bubble burst shortly thereafter, and marchFirst was one of the casualties, declaring bankruptcy just 13 months after the merger. Maxwell, as trustee, sued KPMG, a company that performed independent auditing services for Whitman-Hart. Maxwell's theory was that if KPMG had disclosed that income and earning reports produced shortly before the merger were overstated, US Web would have ended the merger negotiations, and Whitman-Hart would still be around today. The complaint demanded $626 million in damages, based on the estimated value Whitman-Hart would have had absent the merger on the day that it declared bankruptcy.

The district court granted KPMG's motion for summary judgment, ruling that even if KPMG did breach its professional duties, the Trustee could not prove "loss causation" as required under Illinois law. Showing loss causation would require the Trustee to show that KPMG's breach not only caused the merger, but caused the ultimate failure of the merged company. According to the district court, no reasonable jury could find KPMG liable for that failure because subsequent events over which KPMG had no control—mainly the bursting of the tech bubble—actually caused the losses.

Maxwell appealed, arguing that the district court erred in ruling that he was required to show loss causation. In explaining the loss causation ruling, the district court cited five cases from this court and one case from the Illinois Supreme Court. Not one of these cases was cited, discussed, or distinguished in the Trustee's opening brief.

Before turning to the Rule 38 motion, Maxwell has filed a motion for leave to intervene in this appeal as an individual. At present he is a party to the suit only as trustee for the bankruptcy estates of marchFirst. We noted in our opinion that if sanctions were deemed appropriate, we might impose them on Maxwell personally, rather than on the bankrupt estate. That possibility creates for Maxwell a substantial personal interest in the outcome of the post-judgment motions that is not adequately represented by any other party to the appeal. Accordingly, we grant the motion and permit Maxwell to intervene in an individual capacity.

Second, we address KPMG's rather curious motion for leave to file a motion for sanctions in the district court. Our previous opinion already granted leave to do just that, *see Maxwell*, 520 F.3d at 719, but KPMG filed its motion for permission due to uncertainty as to whether the district court would be permitted to rule on a motion for sanctions prior to the issuance of this court's mandate. The mandate, however, issued just two days after the motion was filed, so we deny as unnecessary the motion for leave to file a motion for sanctions in the district court.

As for the motion for sanctions on appeal pursuant to Fed. R. App. P. 38, KPMG argues that it is entitled to sanctions because the trustee had no reasonable expectation of altering the district court's opinion and ignored controlling authority, including the long line of cases cited by the district court in ruling that KPMG did not cause Whitman-Hart's losses. Maxwell argues that sanctions should not be granted because the appeal was not frivolous and, even if it was, there is no evidence that he acted in bad faith. Counsel for the trustee argues along the same lines in their separate response.

We already determined that this appeal "may well be frivolous," *Maxwell*, 520 F.3d at 719. KPMG emphasizes the appellant's failure to cite, discuss, or distinguish any of the loss-causation cases cited by the district court. In response, counsel for the trustee argues that "there was no reason to address each specific case" because "that entire category of cases did not apply." But an appellant's belief that cases the district court relied on in ruling against him do not apply is not an excuse for failing to explain to this court *why* they do not apply. *See Hill v. Norfolk & W. Ry. Co.*, 814 F.2d 1192, 1202 (7th Cir. 1987) (calling the "ostrich-like tactic" "unprofessional," "pointless," and sanctionable under Fed. R. App. P. 38); *see also Hartz v. Friedman*, 919 F.2d 469, 475 (7th Cir. 1990) (awarding attorneys' fees under Rule 38 because appellant "made no attempt to distinguish" numerous cases relied on by the district court); *Mars Steel Corp. v. Continental Bank N.A.*, 880 F.2d 928, 939 (7th Cir. 1989) (awarding attorneys' fees because litigant ignored contrary authority). "An appeal is frivolous when the result is foreordained by the lack of substance to the appellant's arguments." *Mars Steel*, 880 F.2d at 938. When a litigant utterly fails to address or challenge the district court's grounds for ruling against him, his arguments can fairly be called lacking in substance. KPMG also emphasizes the Trustee's claim for $628.6 million in damages, which we consider "outlandish," groundless," and "intimidating." *Maxwell*, 520 F.3d at 717, 718. In KPMG's view, once the district court set out in clear terms and with plenty of controlling authority just one of the many failures in this case, the Trustee's decision to pursue an appeal "in the apparent hope of intimidating a settlement . . . presents a classic case for sanctions."

Maxwell argues that sanctions should not be imposed because he was never warned by this court or the district court of the possibility that he could incur sanctions for pursuing his claim. But this court has warned that, "[t]he text of Rule 38, and our previous decisions applying it, provide all the notice that an attorney could reasonably demand that sanctions may be imposed . . . for the making of frivolous legal arguments in this court." *Hill*, 814 F.2d at 1202. Moreover, counsel admits that as early as June 2003 counsel for KPMG sent a letter calling the trustee's suit frivolous.

Counsel and Maxwell make one additional argument against KPMG's motion for sanctions: that it is untimely and/or waived. This argument is premised on the fact that

KPMG's fee records, attached to its motion, indicate that its attorneys researched the issue of sanctions in August 2007, before they filed their brief in this appeal, but they never threatened to seek sanctions or filed a motion until after this court issued its opinion. Counsel and Maxwell argue that either KPMG concluded that the appeal was not frivolous, in which case it should not take the opposite position now merely because it received a strongly worded favorable ruling, or it decided not to seek sanctions for strategic reasons, in which case the decision should be deemed a waiver. Neither contention has merit. A party may seek Rule 38 sanctions as soon as an appeal is filed, after this court has issued an opinion, and at any time in between. The fact that KPMG researched but did not seek sanctions earlier in this appeal has no bearing on whether or not sanctions are appropriate. Because neither counsel nor Maxwell has advanced a convincing argument for denying KPMG's motion for sanctions, we grant the motion.

The next question is whether the amount KPMG has requested—$233,227.00 in fees and $1001.99 in costs—is reasonable. Counsel acknowledges that the request is not "unreasonable per se," but they request that this court, if inclined to impose sanctions, remand this matter to the district court for an evidentiary hearing. Counsel does not identify any factual dispute that they would seek to have resolved at such a hearing; moreover, the trustee himself has provided a benchmark that suggests that KPMG's fee request is eminently reasonable: Maxwell's own bills for the appeal were almost as high even before oral argument ($202,968 in fees and $5,518.52 in costs). We therefore deny the request for remand to the district court and award KPMG the full amount it requests.

The final question is who should pay the sanction. After this appeal was decided, Maxwell and KPMG entered settlement negotiations. As a result of those negotiations, KPMG does not seek relief in this court against Maxwell in his official capacity as trustee. For this reason and because we are disinclined to impose sanctions on the bankrupt estate in any event, *see Maxwell*, 520 F.3d at 719, we turn to whether Maxwell personally, his counsel, or both should pay the sanction.

Maxwell contends that he should not be held liable for the sanctions because he acted in good faith, and a bankruptcy trustee "may be held personally liable only for a willful and deliberate violation of his fiduciary duties," *In re Chicago Pacific Corp.*, 773 F.2d 909, 915 (7th Cir. 1985), and is "not liable in any manner for mistakes in judgment where discretion is allowed," *In re Hutchinson*, 5 F.3d 750, 753 (4th Cir. 1993) (quoting *In re Cochise College Park, Inc.*, 703 F.2d 1339, 1357 (9th Cir. 1983)). A circuit split has developed on the question of the proper standard to which a trustee should be held before he is held personally liable, *see, e.g., Ford Motor Credit Co. v. Weaver*, 680 F.2d 451, 461-62 (6th Cir. 1982) (willful and deliberate); *Sherr v. Winkler*, 552 F.2d 1367, 1375 (10th Cir. 1977) (same); *but see In re Cochise*, 703 F.2d at 1357 (negligence); *In re Smyth*, 207 F.3d 758 (5th Cir. 2000) (gross

negligence); *see also, e.g.*, Theresa J. Pulley Radwan, *Trustees in Trouble: Holding Bankruptcy Trustees Personally Liable for Professional Negligence*, 35 Conn. L. Rev. 525, 533 (2003), but in this circuit Maxwell is personally liable only if he willfully and deliberately violated his fiduciary duties. *See Chicago Pacific*, 773 F.2d at 915; *see also Matter of Linton*, 136 F.3d 544, 545 (7th Cir. 1998) ("If [a trustee] is burdened with having to defend against suits by litigants disappointed by his actions on the court's behalf, his work for the court will be impeded."). Maxwell points out that the record suggests no willful or deliberate fiduciary misconduct on his part, nor does KPMG argue that any occurred. Maxwell attached an affidavit to his response explaining that he retained counsel to investigate and, if appropriate, pursue legal claims against KPMG. Maxwell does not have any professional expertise in the areas of accounting or auditing malpractice, and so---though he regularly consulted with counsel and the experts they recommended and monitored the litigation---he ultimately relied upon counsel's judgment that this lawsuit and the subsequent appeal were in the best interests of marchFirst's creditors. In the absence of any contrary evidence, we do not find that Maxwell willfully violated his fiduciary duties. Accordingly, Maxwell is not personally liable for the sanction.

Counsel, on the other hand, are liable for the sanctions if their arguments are objectively frivolous. Citing *Depoister v. Mary M. Holloway Found'n*, 36 F.3d 582, 588 (7th Cir. 1994), counsel argue that, on the contrary, they too should not be sanctioned because there is no evidence that they acted in bad faith. The court in *Depoister* noted the party's apparent good faith in declining to sanction him, but the court's *other* reason for denying sanctions was the reasonableness of his contentions on appeal. *Id.* Moreover, this court has held that whether a party should be sanctioned under Rule 38 depends merely on whether a party's arguments could reasonably be supposed to have any merit; the standard is objective. *See Mars Steel*, 880 F.2d 928, 938 ("The standard [for imposing Rule 38 sanctions] depends on the work product: neither the lawyer's state of mind nor the preparation behind the appeal matter."); *Hill*, 814 F.2d at 1202 ("The standard for the imposition of sanctions under Rule 38 is an objective one, however; it has nothing to do with the mental state of the person sanctioned."). Thus even if counsel subjectively believed this appeal had merit, as they say, it does not insulate them from liability for sanctions. In their response to the motion for sanctions, counsel rehash the arguments they presented on appeal, attempting to explain how each was grounded in Illinois court law and, as noted above, defending the fact that they ignored the cases cited by the district court because, in their view, those cases were inapposite. To the extent that the sanction is meant to punish this "ostrich-like" tactic, such punishment is more appropriately directed at counsel rather than Maxwell personally. Counsel also argues that the decision to file a complaint against KPMG was an informed decision reached after reasonable investigation and expert consultation, but argument concerning the decision to file the complaint should be made to the district court. Counsel does not maintain that any expert consultation informed their decision to take an appeal.

For these reasons, Maxwell's counsel is required to pay a sanction of $233,227.00 in fees and $1001.99 in costs to KPMG.