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11 U.S.C. § 101(31)
11 U.S.C. § 547(b)(4)(B)
Fed. R. Civ. P. 56
Insider
Summary Judgment

Hostmann v. Marine Consultants, Inc., et al., Adv. No. 95-3601
In re W.S., Inc., 394-36434-dds7

5/2/97 DDS Unpublished

The trustee sought to recover as preferences transfers made to defendants during the extended preference period. The court had previously granted the trustee's motion for partial summary judgment, finding that the debtor was insolvent at the time of the transfers. (P96-22(7)). The parties then filed cross-motions for summary judgment on the issue of whether the defendants were insiders of debtor or debtor's affiliate pursuant to 11 U.S.C. § 101(31) and thus whether the extended preference period set forth in 11 U.S.C. § 547(b)(4)(B) was applicable. The court determined that there was conflicting evidence in the record on summary judgment regarding whether a partnership existed between defendants and debtor or debtor's affiliate, whether the defendants controlled debtor or debtor's affiliate, and whether defendants were managing agents of debtor's affiliate. Because the court had previously determined that the defendants were entitled to a jury trial, it was within the province of the jury to weigh the conflicting evidence. Accordingly the cross-motions for summary judgment were denied.

P97-28(7)

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UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF OREGON

In Re:) Bankruptcy Case No.
WS, INC.,) 394-36434-dds7
Debtor,) Adversary Proceeding No.
EDWARD C. HOSTMANN, Trustee,) 95-3601-dds
Plaintiff,) FINDINGS OF FACT AND
v.) CONCLUSIONS OF LAW
MARINE CONSULTANTS, INC., and)
SIPCO SERVICES & MARINE, INC.,)
Defendants.)

19 The trustee for WS, Inc. ("WSI"), the debtor, filed a
20 complaint to recover transfers exceeding \$600,000 from Marine
21 Consultants, Inc. ("MCI") and Sipco Services & Marine, Inc.
22 ("SIPCO") as preferential and as fraudulent under
23 11 U.S.C. § 547(b)(4)(B) and § 548(a)(2)(B)(i) and under
24 11 U.S.C. § 550(a). The trustee charged among other things that the
25 defendants were insiders and that the debtor made the payments
26 within a year but more than 90 days prior to bankruptcy at a time

1 when the debtor was insolvent. Plaintiff filed a motion for partial
2 summary judgment on the issue of whether the debtor was insolvent
3 within 11 U.S.C. § 101(32) at the time of the transfers.

4 Plaintiff's motion should be granted for the following reasons.

5 At the end of 1993, the debtor owed approximately \$1,100,000
6 to the defendant SIPCO arising from marine sandblasting and coating
7 services performed during the prior year on two vessels at the
8 debtor's Port of Portland facility. The debtor could not pay the
9 debt when it became due. SIPCO wished to withdraw its sandblasting
10 operation from the Port of Portland facility. The debtor wanted to
11 take over the sandblasting operation and to pay SIPCO from
12 anticipated future profits from the venture.

13 SIPCO's principals formed the defendant, MCI, under Texas law
14 on January 20, 1994, as an affiliate owned by SIPCO's parent and
15 staffed by SIPCO's president and vice president. SIPCO assigned the
16 \$1,100,000 receivable owed by WSI to the new corporation and agreed
17 to sell its Portland equipment to RIR, Inc. ("RIR"), an affiliate of
18 the debtor, under a two-year lease option contract. RIR would
19 conduct the sandblasting business. RIR agreed to pay \$100,000 as a
20 down payment on the equipment to be followed by weekly lease
21 payments of \$4,500 for 100 weeks and thereafter a lump sum purchase
22 price. MCI agreed on February 11, 1994 in a separate agreement to
23 provide management services to RIR for a weekly fee and a 25% share
24 of the profits with RIR's 75% share committed to payment of the
25 debtor's \$1,100,000 obligation. In this agreement, the debtor also
26 agreed to pay \$150,000 to reduce its \$1,100,000 debt.

1 Creditors filed an involuntary bankruptcy petition against
2 the debtor on October 27, 1994. The transfers which the trustee
3 seeks to recover consisted of payments of \$150,000 on prior debts,
4 payments of \$210,000 from RIR's share of sandblasting profits,
5 payment of \$40,000 for RIR's management fees and alleged expense
6 reimbursement, and payments under the lease option totaling
7 \$246,500. These payments were all made between February 11, 1994
8 and August 5, 1994 pursuant to the described agreements.

9 The standard governing a motion for summary judgment "mirrors
10 the standard for directed verdict under Fed. R. Civ. P. 50(a)" which
11 is that the trial judge must direct a verdict if, under the
12 governing law, there can be but one reasonable conclusion as to the
13 verdict. Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 250 (1986).
14 In ruling on the motion, the evidence of the non-movant is to be
15 believed and all justifiable inferences are to be drawn in his
16 favor. Id., at 255; Rebel Oil Co., Inc. v. Atlantic Richfield Co.,
17 51 F.3d 1421, 1435 (9th Cir. 1995). Subject to some qualifications
18 not applicable, an entity is insolvent if the sum of its debts "is
19 greater than all of such entity's property at a fair
20 valuation . . ." 11 U.S.C. § 101(32)(A).

21 Application of the foregoing rules requires a finding that
22 the debtor was insolvent at the time of the January and February
23 1994 agreements with SIPCO and MCI and at the time of the payments
24 which plaintiff seeks to recover. All of the financial statements
25 at the approximate time establish that the debtor was insolvent in a
26 balance sheet sense from the end of 1992 to the time of bankruptcy.

1 All of the executives in charge of the debtor and its finances also
2 perceived the debtor to be insolvent in a balance sheet sense during
3 the times in question. Defendants provided no evidence to the
4 contrary and no reasonable inference in favor of solvency at the
5 times in question can be drawn. The issue should not be submitted
6 to a jury.

7 Price Waterhouse, in an audited financial statement, found
8 the debtor to be insolvent at the end of 1992. See Exhibit D.
9 Thereafter, every internal financial statement of the debtor showed
10 that the negative relationship between assets and liabilities
11 worsened as time went on. The deficit of assets to liabilities
12 almost doubled between December 31, 1992 and June 30, 1994 from
13 \$6,273,275 to \$12,800,000. See Exhibit D, I, J and K. Liabilities
14 during this period increased from approximately \$16,000,000 to over
15 \$25,000,000 while assets only increased from \$10,000,000 to
16 \$12,500,000. In listing liabilities and nontangible assets in the
17 financial statements, the debtor at the time exercised its
18 reasonable business judgment in adjusting for collectability of
19 accounts and accrual of liabilities.

20 Defendants have not shown the adjustments to be wrong. The
21 internal financial statements possessed integrity because management
22 used this information, dismal as it was, to make business decisions
23 at the time and appeared not to question its reliability. With
24 respect to the value of the tangible assets, the debtor obtained an
25 actual physical appraisal from Consilium, Inc. as of May 30, 1993
26 which found value to range from \$3,366,000 to \$1,457,000 depending

1 on whether one adopted a fair market value in continued use
2 valuation or an orderly liquidation value. See Exhibit E. The
3 debtor used the higher appraisal valuation in its internal
4 accounting, which valuation closely approximated the book value.

5 While there is an obvious difference between book value as
6 used by the accountants who prepared the financial statements and
7 "fair value" as used in 28 U.S.C. § 101(32)(A), the difference
8 diminishes in the light of Consilium's appraisal. In regard to
9 asset value, the evidence is sufficient to carry the movant's
10 initial burden under summary judgment principles. The appraisal and
11 the large amount by which liabilities exceed assets distinguishes
12 this case from In the Matter of Lamar Haddox, 40 F.3d 118 (5th Cir.
13 1994) which condemned sole reliance on book value as evidence of
14 fair value.

15 All three of the debtor's senior executives testified in
16 depositions that the debtor was insolvent in a balance sheet sense
17 at the approximate times in question. Stephen J. Toth, chief
18 financial officer of the debtor through April 1994, testified that
19 there was never a time that WSI's assets exceeded its liabilities.
20 He based his testimony on fair valuation and on financial statements
21 which are available. See Toth Deposition, Exhibit G to plaintiff's
22 Concise Statement of Material Facts at 106. Mr. Tore Steen, a
23 senior executive of the debtor and former member of the debtor's
24 board of directors, testified that the debtor's liabilities were
25 greater than the value of its assets. See Exhibit L, plaintiff's
26 Concise Statement of Facts at 44. Douglas T. Watson, chairman of

1 the board, testified that the debtor's liabilities probably greatly
2 exceeded its assets. See Exhibit A attached to plaintiff's Concise
3 Statement of Material Facts at 265.

4 Defendants' objection that plaintiff's motion for summary
5 judgment is not supported by admissible evidence is rejected. The
6 affidavits of Steven J. Toth and Bruce A. Shepard satisfy
7 Fed. R. Civ. P. 56(e) in establishing that the financial statements
8 and other exhibits are admissible in evidence. See Exhibit N and O
9 attached to plaintiff's Memorandum and Reply to Defendants'
10 Memorandum in Opposition to Plaintiff's Motion for Partial Summary
11 Judgment.

12 Defendants' argument that there is a fact issue as to
13 solvency created by the schedules and by the "Ponderosa Deal" must
14 be rejected. Weeks before the filing of the creditors' petition and
15 about the time the debtor ceased operation, the debtor conveyed
16 almost all of its physical assets to Cascade General, Inc. in a
17 complex transaction involving Ponderosa Acquisition Corporation
18 resulting in a reduction of its debt which, if the bankruptcy
19 schedules were augmented by omitted values, would cause the debtor
20 to become marginally solvent. As a consequence, defendants argued
21 that at the time of the alleged preferential transfers, either the
22 value of the debtor's assets or the sum of its liabilities shown in
23 prior financial statements were respectively understated or
24 overstated so as to raise a fact issue as to solvency. The argument
25 is based upon speculation, particularly as to collateral information
26 which itself is speculation and, because of the absence of evidence,

1 unfairly and unreasonably attempts to turn the appraisals, financial
2 statements, and testimony upside down without regard to
3 consideration of the large amount of claims which have been filed.
4 Undoubtedly, defendants may revisit this issue in the trial of other
5 issues under 11 U.S.C. § 547(b) (5).

6 Defendants supplied no evidence of solvency or any material
7 establishing that there is a conflict in the evidence or that there
8 is a fact issue to be submitted to a jury. Assets owned by third
9 parties are not relevant to the issue of the debtor's solvency and
10 the defendants' arguments for adjustments to the debtor's assets and
11 liabilities shown either in prior financial statements or in the
12 bankruptcy schedules are unsupported speculation at best. There is
13 no fact issue to be tried and plaintiff is entitled as a matter of
14 law to a favorable ruling on this issue.

15 For the foregoing reasons, a separate order should enter
16 granting summary judgment to plaintiff, finding the debtor to have
17 been insolvent at the time of the transfers sought to be recovered.

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20 DONAL D. SULLIVAN
Bankruptcy Judge

21 cc: Fred M. Granum
22 Gregg D. Johnson
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