

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NEW YORK

In re:

LUSTER-COATE METALLIZING
CORP. ,

Debtor.

CASE NO. 01-22764

DECISION & ORDER

C. BRUCE LAWRENCE, as Trustee,

Plaintiff,

V.

AP #03-2022

B&M PLASTICS, INC. ,

Defendants.

BACKGROUND

On July 18, 2001, Luster-Coate Metallizing Corp. ("Luster-Coate") filed a petition initiating a Chapter 11 case. The Schedules and Statements filed by Luster-Coate made the company appear to have a positive net worth of \$760,368.70 (the "Scheduled Balance Sheet"), as follows:

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Assets

I. Real Property

A. 26 Industrial St. \$ 410,000.00
B. 32 E. Buffalo St. \$ 465,000.00

II. Personal Property

A. Cash on hand \$ 100.00
B. M&T Checking Acct. \$ 9,611.94
C. Chrysler Stock \$ 14,436.31
D. Accounts Receivable \$1,019,743.42
E. Trucks & Autos \$ 22,600.00
F. Office Equipment \$ 29,500.00
G. Machinery \$1,980,000.00
H. Inventory \$ 893,946.29

TOTAL ASSETS

\$4,844,937.90

Liabilities

I. Secured Claims

A. M.C. Treasurer \$ 10,767.28
B. GE Capital (CT) \$1,107,244.59
C. GE Capital (MO) \$2,096,774.00
D. M.C. Dev. Admin. \$ 80,355.00
E. Riga Tax Collector \$ 16,694.72
F. Town of Warsaw \$ 16,867.37
G. Churchville (Vill) \$ 7,383.21
H. Warsaw (Village) \$ 7,666.37

II. Unsecured Claims \$ 740,826.72

TOTAL LIABILITIES

- \$4,084,579.26

TOTAL

\$ 760,358.64

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Luster-Coate's pre-petition financial problems and losses continued in Chapter 11, and less than seven months later, on February 6, 2002, the Chapter 11 case was converted to a Chapter 7 case. On February 5, 2003, Luster-Coate's Chapter 7 Trustee, C. Bruce Lawrence, Esq. (the "Trustee"), filed an Adversary Proceeding against B&M Plastics, Inc. ("B&M") seeking to recover an alleged avoidable preference in the amount of \$122,122.50, paid by Luster-Coate to B&M on or about May 14, 2001, within ninety (90) days of the filing of the Chapter 11 petition (the "B&M Payment").

On March 31, 2003, B&M filed an Answer, which alleged that: (1) the Court lacked subject matter jurisdiction; (2) the proper venue for the Adversary Proceeding was in Indiana, where B&M was located; and (3) on May 14, 2001, Luster-Coate was not insolvent as required by Section 547(b)(3). The B&M Answer did not assert: (1) a defense to any of the other elements that the Trustee was

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required to prove under Section 547(b);¹ or (2) any affirmative defenses available under Section 547(c).

On May 14, 2003, the Trustee filed a Motion for Summary Judgment (the "Motion for Summary Judgment") which asserted that: (1) as confirmed by Luster-Coate's Controller, Ronald F. Sanewsky ("Sanewsky"), the B&M Payment was made in response to an April 2001 Summons and Complaint that B&M had served upon Luster-Coate to collect its unpaid invoices for March and November 2000 shipments; (2) the estimated asset values that Luster-Coate used when it

¹ Section 547(b) provides that:

(b) Except as provided in subsection (c) of this section, the trustee may avoid any transfer of an interest of the debtor in property -

(1) to or for the benefit of a creditor;

(2) for or on account of an antecedent debt owed by the debtor before such transfer was made;

(3) made while the debtor was insolvent;

(4) made -

(A) on or within 90 days before the date of the filing of the petition; or

(B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and

(5) that enables such creditor to receive more than such creditor would receive if -

(A) the case were a case under chapter 7 of this title;

(B) the transfer had not been made; and

(C) such creditor received payment of such debt to the extent provided by the provisions of this title.

11 U.S.C. § 547 (2003).

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prepared its Schedules were greatly exaggerated, as demonstrated by the fact that: (a) Luster-Coate's Warsaw real property (the "Warsaw Property"), which it scheduled as having a value of \$410,000.00, sold for only \$77,043.64 at auction in the fall of 2002; (b) the only offer the Trustee had received for Luster-Coate's Churchville real property (the "Churchville Property"), which it scheduled as having a value of \$465,000.00, was for \$50,000.00, which was less than the amount of the outstanding real estate taxes owed on the Property; and (c) Luster-Coate's equipment, machinery and inventory, which it scheduled as having a value of \$2,926,046.29, sold for only \$266,974.50 at auction in the fall of 2002; (3) Luster-Coate had failed to schedule an unsecured claim filed on August 6, 2002 by the State of New York in the amount of \$6,341,000.00 (the "CERCLA Claim"), which alleged that Luster-Coate had a potential joint and several CERCLA environmental liability in that amount in connection with the clean-up costs that the State had incurred at the Rochester Fire Academy where Luster-Coate had dumped hazardous waste prior to filing the petition; and (4) in an attached May 14, 2003 Affidavit, Richard N. Gray, CPA ("Gray"), one of the accountants for the Trustee, after analyzing Luster-Coate's internally prepared April 30, 2001 consolidated balance sheet (the "April 2001 Balance Sheet"), which indicated a stockholders deficiency of \$153,082.00 approximately two weeks before the B&M

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Payment, expressed the opinion that the actual stockholders deficiency at that date was \$669,468.00.

On October 29, 2003, after the Court had held several pre-trials and afforded the parties time to complete voluntary discovery in connection with the Motion for Summary Judgment, B&M interposed Opposition to the Motion which asserted that: (1) Luster-Coate's Schedules, which showed a positive net worth of \$760,368.70 as of July 18, 2001: (a) demonstrated that Luster-Coate was solvent on May 14, 2001 when it made the B&M Payment; and (b) constituted sufficient evidence to rebut the presumption of insolvency set forth in Section 547(f)² (the "Section 547(f) Presumption of Insolvency"); (2) at or about the time of the B&M Payment, Luster-Coate maintained one account at HSBC Bank and two accounts at M&T Bank, but it had only listed one of the M&T Bank accounts on its Schedules; (3) any amounts on deposit in the unscheduled M&T Bank account may have affected the solvency or insolvency of Luster-Coate on the date of the B&M Payment; (4) Luster-Coate's computer system was experiencing problems in 2001

² Section 547(f) provides that:

(f) For the purposes of this section, the debtor is presumed to have been insolvent on and during the 90 days immediately preceding the date of the filing of the petition.

11 U.S.C. § 547 (2003).

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and 2002, which made all of its financial reporting at or about the time of the B&M Payment unreliable, including the internal April 2001 Balance Sheet that Gray had relied upon in expressing his opinion of insolvency; and (5) in an October 29, 2003 Affidavit, B&M's accountant, CPA James Schnell ("Schnell"), expressed the opinion that Luster-Coate was solvent on the date of the B&M Payment.

On October 31, 2003, the Trustee filed a Reply in support of the Motion for Summary Judgment which asserted that: (1) the values scheduled by Luster-Coate for its real property and machinery and equipment were based upon outdated book values or appraisals that did not take into consideration the age, condition and current market valuations for those assets; (2) an October 10, 1997 Fair Market In Place Value Report of Luster-Coate's machinery and equipment, prepared by Steves & Company three and one-half years prior to the B&M Payment, valued the machinery and equipment at only \$1,962,020.00, yet Luster-Coate scheduled it at a value of \$2,009,500.00; (3) a June 4, 2001 appraisal (the "GE Warsaw Appraisal"), prepared for GE Capital by Emminger, Hayatt, Newton and Pigeon, Inc., indicated that: (a) the fair market value of the Warsaw Property was \$200,000.00, which was significantly less than the \$410,000.00 scheduled by Luster-Coate; and (b) the liquidation value of all of Luster-Coate's machinery and equipment was

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\$496,675.00 (the "GE Machinery Appraisal"); (4) Richard Vullo, Esq. ("Vullo"), the bankruptcy attorney for Luster-Coate, indicated in a deposition that: (a) Luster-Coate's manufacturing facilities and its machinery and equipment were very old and in very poor condition; and (b) Luster-Coate had no other more current information for the values of its real properties and machinery and equipment when its Schedules were prepared, so it relied upon 1997 appraisals that were obtained in connection with its borrowings from GE Capital; (5) Vullo further indicated in his deposition testimony that he did not believe that when Luster-Coate filed its petition: (a) it was solvent; and (b) its assets, if sold, would bring enough to even pay its secured creditors, GE Small Business and GE Capital, which together were owed approximately \$2,900,000.00; and (6) the auctioneer (the "Auctioneer") for the Trustee indicated in a deposition that, based upon the competitive bidding at the auction and the age and condition of the equipment, he believed that the machinery, equipment and inventory of Luster-Coate were sold for a fair value.

In an October 31, 2003 Affidavit submitted by the Trustee, Sanewsky expressed the opinion that Luster-Coate was insolvent at the time it made the B&M Payment.

DISCUSSION

I. Summary Judgment

_____ Fed.R.Civ.P. 56, incorporated by reference in Fed.R.Bankr.P. 7056, "provides that summary judgment shall be granted when there is no genuine issue as to any material fact and the moving party is entitled, as a matter of law, to a judgment in its favor." *In re Bennett Funding Group, Inc.*, 220 B.R. 743 (Bankr. N.D.N.Y. 1997), citing *Federal Deposit Ins. Corp. v. Bernstein*, 944 F.2d 101, 106 (2d Cir. 1991). The moving party has the initial burden of demonstrating that there is no genuine issue of material fact for trial. *In re Corcoran*, 246 B.R. 152, 158 (Bankr. E.D.N.Y. 2000), citing *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986). Once the moving party has met its initial burden, "the non-movant must then come forward with sufficient evidence on the elements essential to its case to support a verdict in its favor." *Corcoran*, 246 B.R. at 158, citing *Celotex Corp. v. Catrett*, 106 S.Ct. 2548 (1986).

In deciding to grant or deny summary judgment, "the trial court must resolve all ambiguities and draw inferences in favor of the party against whom summary judgment is sought." *Bennett Funding Group, Inc.*, 220 B.R. at 751, citing *LaFond v. General Physics Servs. Corp.*, 50 F.3d 165, 171 (2d Cir. 1995); *Corcoran*,

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246 B.R. at 156, citing *Reyes v. Delta Dallas Alpha Corp.*, 199 F.3d 626, 627-28 (2d Cir. 1999). However, the non-moving party "must do more than simply show that there is some metaphysical doubt as to the material facts." *Repp v. Webber*, 132 F.3d 882, 889 (2d Cir. 1997) citing *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. at 586 (1986) (further citations omitted). Summary judgment is therefore inappropriate if any evidence exists in the record upon which a reasonable inference may be drawn in favor of the non-moving party. *Id.*, citing *Chambers v. TRM Copy Ctrs. Corp.*, 43 F.3d 29, 37 (2d Cir. 1994).

II. Overview of Decision

As more thoroughly discussed herein, I find that: (1) there are no genuine issues of material fact to be resolved at a trial, even after all ambiguities and inferences are resolved in favor of B&M; (2) the evidence presented and assertions made by B&M regarding the solvency or insolvency of Luster-Coate on the date of the B&M Payment are not sufficient to overcome the Section 547(f) Presumption of Insolvency; (3) even if the Court found that the evidence presented and assertions made by B&M were sufficient to overcome the Section 547(f) Presumption of Insolvency, the Trustee has met his burden to show, by a preponderance of the evidence, that all of the requirements of Section 547(b) have been met in

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connection with the B&M Payment. Thus, the B&M Payment is an avoidable preferential transfer.

III. Section 547(b)(3) Insolvency

We know from the decisions of courts that have addressed the question of insolvency for purposes of Section 547(b)(3) that: (1) as set forth by the United States Court of Appeals for the Second Circuit in *Roblin Industries, Inc. V. Ford Motor Company*, 78 F.3d 30 (2d Cir. 1996): (a) the trustee bears the burden of proving insolvency by a preponderance of the evidence; (b) pursuant to Section 547(f), there is a rebuttable presumption that the debtor was insolvent during the ninety days preceding the filing of the bankruptcy petition; (c) a creditor may rebut the presumption by introducing some evidence that the debtor was not in fact insolvent at the time of the alleged avoidable preferential transfer; (d) "insolvent," as defined in Section 101(32), is a financial condition such that the sum of an entity's debts is greater than all of its property, at a fair valuation; and (e) fair value, in the context of a going concern, is determined by the fair market price of an entity's assets that could be obtained if sold in a prudent manner within a reasonable period of time to pay its debts; (2) as set forth in *Miller & Rhoads, Inc.*, 146 B.R. 950 (Bankr. E.D. Va. 1992) and the cases cited therein: (a) a balance sheet test based upon asset values is used for the purpose of

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establishing solvency or insolvency: (b) scheduled asset values are not determinative of whether a debtor was solvent or insolvent for purposes of avoiding a transfer as preferential when the schedules are materially flawed; and (c) fair valuation is generally defined as the going concern or fair market price value, unless a business is on its deathbed, in which case liquidation value is the more appropriate basis for valuation; and (3) as set forth in *In re Coated Sales, Inc.*, 144 B.R. 663 (Bankr. S.D.N.Y. 1992), "courts often utilize the well established bankruptcy principles of 'retrojection' and 'projection,' which provide for the use of evidence of insolvency on a date before and after the preference date as competent evidence of the debtor's insolvency on the preference date."

IV. Trustee's Evidence of Insolvency

_____The Trustee has provided credible evidence that Luster-Coate was insolvent on the date of the B&M Payment, as follows:

1. Luster-Coate scheduled the Warsaw Property for \$410,000.00. However: (a) the GE Warsaw Appraisal, dated approximately one month after the B&M Payment and one month before Luster-Coate filed its petition, valued the property at \$200,000.00; and (b) ultimately the Property sold at auction for \$77,043.64. In view of: (a) the GE Warsaw Appraisal; (b) the age and condition of the Warsaw plant, as testified to by Vullo; and (c) Luster-Coate's prepetition losses

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and inability to find a buyer, which along with a number of other factors indicate that it was no longer a going concern and that its assets could not be reasonably valued at going concern,³ the value of the Warsaw Property at the time of the B&M Payment would not reasonably have exceeded \$200,000.00;

2. Luster-Coate failed to schedule in any manner the CERCLA Claim as a potential joint and several liability. This potential liability of in excess of \$6,000,000.00, which Luster-Coate was aware of since 1993, existed at the time of the B&M Payment. The CERCLA Claim has not been objected to by the Trustee, B&M or any other party, and it appears from all of the documentation presented along with the Claim, that Luster-Coate may have substantial CERCLA liability. Even though B&M has been afforded substantial time for discovery, it did not come forward with any evidence that demonstrates that: (a) the CERCLA Claim is invalid; (b) Luster-Coate would have a liability of substantially less than

³ These factors include that: (1) as testified to by Sanewsky at his deposition, Luster-Coate had insufficient working capital and borrowing availability to operate as a going concern, and the shareholders were unwilling or unable to infuse additional capital into the company; (2) on its own financial statements, specifically the April 2001 Balance Sheet, it was insolvent; (3) even if the April 2001 Balance Sheet was flawed, the company was operating on the belief that it was insolvent; (4) Luster-Coate had begun depositing accounts receivable collections into an account other than the HSBC Blocked Account, in violation of its loan agreements with GE Capital; (5) Luster-Coate's SBA guaranteed loan was demanded; (6) Luster-Coate's secured creditors were obtaining updated appraisals, including liquidation appraisals; (7) Luster-Coate could not sell its powder coating operation; and (8) B&M and others were suing Luster-Coate which was not paying its debts in the ordinary course of business.

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\$6,000,000.00; or (c) Luster-Coate would have a liability of less than \$760,000.00, which when added to the scheduled unsecured claims would result in a revised Scheduled Balance Sheet that would show a negative net worth. A CERCLA Claim liability of in excess of \$6,000,000.00 would have made Luster-Coate insolvent when the B&M Payment was made, even if its Schedules were otherwise in all respects accurate;

3. Luster-Coate's May 31, 2001 Notice of Revolving Credit Advance (the "Borrowing Advance Notice") delivered to GE Capital and signed by Sanewsky as Controller, indicated that \$417,189.53 or thirty percent (30%) of Luster-Coate's accounts receivables were ineligible, indicating that they were aged and at least to some extent uncollectible (Exhibit B to B&M's October 29, 2003 Responding Affirmation). If the same factor of thirty percent (30%) is applied to Luster-Coate's scheduled accounts receivable, the result would be a fair value accounts receivable amount of \$713,820.38;⁴

4. The GE Machinery Appraisal valued Luster-Coate's machinery and equipment on June 4, 2001 at a liquidation value of just under \$500,000.00. The value of Luster-Coate's machinery and equipment

⁴ This level of accounts receivable is more consistent with the accounts receivable reported on Luster-Coate's 2001 corporate income tax return (Exhibit E to the Motion for Summary Judgment) which showed accounts receivable at the beginning of 2001 as \$785,117.00 and at the end of 2001 as \$841,886.00.

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at the time of the B&M Payment would not reasonably have exceeded \$750,000.00 based upon: (a) the age and condition of the machinery and equipment, as testified to by Vullo; (b) the factors which indicate that Luster-Coate was no longer a going concern on the date of the B&M Payment; and (c) the testimony of the Auctioneer, which indicated that in October 2002 the machinery, equipment and inventory of Luster-Coate was sold together for a fair auction, essentially liquidation value of approximately \$265,000.00;

5. In his October 31, 2003 Affidavit, Sanewsky expressed the opinion that Luster-Coate was insolvent at the time of the B&M Payment;

6. Vullo, an attorney with over thirty years of commercial and bankruptcy law experience, who is also a Chapter 7 Panel Trustee, testified in his deposition that he did not believe that when Luster-Coate filed its petition: (a) it was solvent; and (b) because of the age and poor condition of its assets, the sale of all of Luster-Coate's assets would bring more than \$2,900,000.00;

7. A reconstructed balance sheet of Luster-Coate at the time of the preparation of its Schedules, adjusting for the Court-determined values of only the Warsaw Property, accounts receivable, machinery and equipment and unsecured claims, would produce a balance sheets with a negative net worth, as follows:

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Assets

I. Real Property

A.	26 Industrial St.	\$ 410,000.00	\$200,000.00	(-\$210,000.00)
B.	32 E. Buffalo St.	\$ 465,000.00		

II. Personal Property

A.	Cash on hand	\$ 100.00		
B.	M&T Checking Acct.	\$ 9,611.94		
C.	Chrysler Stock	\$ 14,436.31		
D.	Accounts Receivable	\$1,019,743.42	713,820.38	(-\$305,923.10)
E.	Trucks & Autos	\$ 22,600.00		
F.	Office Equipment	\$ 29,500.00		
G.	Machinery	\$1,980,000.00	<u>750,000.00</u>	(-1,230,000.00)
H.	Inventory	\$ 893,946.29		

TOTAL ASSETS **\$3,099,014.00**

Liabilities

I. Secured Claims

A.	M.C. Treasurer	\$ 10,767.28		
B.	GE Capital (CT)	\$1,107,244.59		
C.	GE Capital (MO)	\$2,096,774.00		
D.	M.C. Dev. Admin.	\$ 80,355.00		
E.	Riga Tax Collector	\$ 16,694.72		
F.	Town of Warsaw	\$ 16,867.37		
G.	Churchville (Vill)	\$ 7,383.21		
H.	Warsaw (Village)	\$ 7,666.37		

II. Unsecured Claims \$ 740,826.72 6,740,826.72 (+6,000,000.00)

TOTAL LIABILITIES \$10,084,579.00

TOTAL **\$-7,635,565.00**

(Without CERCLA Claim)

(\$-1,635,565.00)

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8. In view of: (a) Vullo's testimony that when preparing its Schedules Luster-Coate did not fully address the then current value of the Churchville Property, but relied upon an old appraisal; and (b) the failure of the Trustee to obtain a viable offer for the Property in excess of the past-due real estate taxes, which are less than \$100,000.00, it was unreasonable for Luster-Coate to schedule the Property at \$465,000.00, or for the Court to accept that value in connection with a Section 547 avoidable preference insolvency analysis. Furthermore, in the substantial time afforded to B&M, it failed to produce any other evidence of the value of the Churchville Property as of the date of the B&M Payment, including an appraisal; and

9. In view of: (a) the value obtained for Luster-Coate's machinery, equipment and inventory at the October 2002 sale; (b) the factors which indicate that Luster-Coate was no longer a going concern on the date of the B&M Payment; and (c) the Eligible Inventory on the Borrowing Advance Notice was only \$260,000.00, it was not reasonable for Luster-Coate to schedule its inventory at \$894,000.00, or for the Court to accept that value in connection with a Section 547 insolvency analysis.

V. B&M's Evidence of Solvency

B&M has asserted that Luster-Coate's Schedules, which show a positive net worth, are sufficient to both rebut the Section 547(f) Presumption of Insolvency and demonstrate that Luster-Coate was

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solvent on the date of the B&M Payment. However, it is clear that Luster-Coate did not do a critical analysis of the line items in its asset Schedules to present a fair value of those assets on July 18, 2001. Furthermore, an analysis of the various line items of its assets and liabilities Schedules, as set forth in this Decision & Order, indicate that Luster-Coate's Schedules are flawed and did not accurately or fairly set forth the fair value of its assets or the extent of its liabilities,⁵ either for purposes of providing sufficient credible evidence to overcome the Section 547(f) Presumption of Insolvency, or to overcome the credible evidence presented by the Trustee that Luster-Coate was insolvent on the date of the B&M Payment.

Furthermore, Schnell's opinion of Luster-Coate's solvency, as presented by B&M, is not based upon such assumptions and a critical analysis does not warrant the Court affording it any credibility.

B&M was afforded substantial time to do discovery and to develop credible evidence of solvency, either to support Luster-Coate's asset values as set forth in its Schedules, or to otherwise demonstrate that the fair value of its assets exceeded its liabilities on the date of the B&M Payment. B&M did little with the time afforded to it, and it has not provided sufficient evidence to: (1) rebut the Section 547(f) Presumption of

⁵ As many debtors do, Luster-Coate prepared its Schedules primarily to properly disclose all of its assets, and not with a view to presenting the fair value of those assets at the time it filed its bankruptcy petition.

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Insolvency; (2) demonstrate that there is a material issue of fact on the question of insolvency on the date of the B&M Payment; or (3) otherwise demonstrate, given the Trustee's evidence, that Luster-Coate was solvent on the date of the B&M Payment.

To the contrary, notwithstanding the Section 547(f) Presumption of Insolvency, the Trustee has met his burden to demonstrate by a preponderance of the evidence that Luster-Coate was insolvent on the date of the B&M Payment.

CONCLUSION

The B&M Payment is an avoidable preferential transfer. B&M shall pay to the Trustee \$122,122.50 together with interest at the federal judgment rate of 1.24%⁶ from February 5, 2003 to the date of payment, which shall be paid no later than February 23, 2004. Should B&M fail to make the required payment by February 23, 2004, the Trustee may enter a judgment.

IT IS SO ORDERED.

/s/
HON. JOHN C. NINFO, II
CHIEF U.S. BANKRUPTCY JUDGE

Dated: February 3, 2004

⁶ This is the average rate applicable during this time period.