

**UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NEW YORK**

In Re:

**Ira Bristol Industries, Inc., n/k/a
Welcher Industries, Inc.,**

BK. NO. 92-21616

Debtor.

WELCHER INDUSTRIES, INC.,

Plaintiff,

vs.

A.P. NO. 94-2027

**DUANE M. FISHER, INC., d/b/a
DUANE M. FISHER & ASSOCIATES,
DUANE M. FISHER and CHRISTOPHER
MADDOCK,**

Defendants.

BACKGROUND

On June 10, 1992, the Debtor, Ira Bristol Industries, Inc., which operated a machine tool business, filed a petition initiating a Chapter 11 case and post-petition changed its name to Welcher Industries, Inc. ("Welcher"). On September 28, 1992, Ira L. Bristol ("Ira Bristol") and Jean Bristol ("Jean Bristol") (collectively the "Bristols"), husband and wife and each an officer of Welcher, filed a petition initiating a Chapter 7 case.

On January 8, 1993, after Donald L. Salamone, Esq. ("Salamone") had become its sole shareholder, Welcher commenced an adversary proceeding against the Bristols to have certain obligations and liabilities alleged to be due from the Bristols determined to be non-dischargeable (Adversary Proceeding #93-2006); Dorothy Lodico ("Lodico"), a physician and the spouse of Salamone, commenced an adversary proceeding against the Bristols to have a \$60,000.00 obligation due from the Bristols determined to be non-dischargeable (Adversary Proceeding #93-2007); and LCA Leasing Corp. ("LCA") commenced an adversary proceeding against the Bristols to have any

indebtedness, obligations or liabilities which might be due from the Bristols determined to be non-dischargeable (Adversary Proceeding #93-2008).

On March 2, 1993, an action commenced by Salamone against LCA and Nymat Machine Tool Corp. ("Nymat") in New York State Supreme Court, seeking damages on several causes of action including an alleged failure to honor a commitment to lend, was removed to the Bankruptcy Court and assigned Adversary Proceeding #93-2046. Also on March 2, 1993, an action commenced by LCA against Nymat in New York State Supreme Court was removed to the Bankruptcy Court and assigned Adversary Proceeding #93-2047.

On April 8, 1993, Welcher commenced an adversary proceeding against LCA and Nymat seeking damages on several causes of action including the alleged failure of LCA and Nymat to honor a commitment to lend (Adversary Proceeding #93-2074). Thereafter, Adversary Proceedings #93-2008 (LCA vs. the Bristols), #93-2046 (Salamone vs. LCA and Nymat) and #93-2047 (LCA vs. Nymat) were consolidated with Adversary Proceeding #93-2074.

On January 19, 1994, after the Bristols had plead guilty to a number of criminal charges in New York State Supreme Court, a Stipulation and Order was entered settling Adversary Proceedings #93-2006 and #93-2007, the Welcher and Lodico actions against the Bristols, which included the entry of money judgments against the Bristols for obtaining money by fraud (\$255,000 in favor of Welcher and \$60,000 in favor of Lodico), and it was determined that the indebtedness evidenced by each judgment was non-dischargeable.

On June 30, 1994, a Settlement Agreement and Order was entered settling the adversary proceeding commenced by LCA against Nymat (Adversary Proceeding #93-2047).

On April 21, 1994, LCA and Nymat each filed a Motion for Summary Judgment in the adversary proceedings commenced by Salamone and Welcher against LCA and Nymat (Adversary Proceedings #93-2046 and #93-2074). On September 13, 1994, an Order was entered approving the

settlement of the Salamone and Welcher actions against Nymat.

On September 14, 1994, the Court issued a Decision and Order denying the LCA Motion for Summary Judgment, which Decision and Order is now on appeal to the United States District Court for the Western District of New York.

On February 11, 1994, Welcher commenced this adversary proceeding (the "Fisher Adversary Proceeding") against Duane M. Fisher, Inc., d/b/a Duane M. Fisher & Associates ("Fisher, Inc."), Duane M. Fisher ("Fisher") and Christopher Maddock ("Maddock") seeking damages on several causes of action including fraud, negligence, malpractice and a cause of action under the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §1961-68 ("RICO").

Welcher's Complaint in the Fisher Adversary Proceeding alleged that: (1) the defendants performed management consulting, accounting and bookkeeping services for both Welcher and the Bristols; (2) the defendants set up and maintained the financial and recordkeeping books of Welcher and the Bristols; (3) the defendants assisted Ira Bristol in establishing certain business practices and accounting practices and procedures which would facilitate and conceal his defalcations of certain of the assets of Welcher to the detriment of both Welcher and Salamone; and (4) Ira Bristol's defalcations included selling off approximately \$300,000 of the machinery and equipment of Welcher and converting the proceeds to his own use, personally appropriating to his own use the proceeds of scrap metal sales made by Welcher from July 1, 1988 through May 31, 1992 in an amount estimated to be between \$400,000 and \$1,000,000, purchasing a personal vehicle with corporate funds, creating an overpaid secretarial position for Jean Bristol and concealing the details of the payment of that salary and causing Welcher to pay substantial personal income tax obligations of the Bristols.

On April 28, 1994, the defendants filed a motion to dismiss the Welcher Complaint (the "Motion to Dismiss"). The Motion alleged that on or about July 15, 1993 Salamone, on his own

behalf as a shareholder and investor in Welcher, had commenced an action in the New York State Supreme Court, Monroe County (the "Salamone State Court Action") which sought damages against the defendants for fraud, negligence and malpractice, but not for a cause of action under RICO. The defendants in their Motion to Dismiss further alleged that the Complaint should be dismissed because the claims were identical to those being litigated in the Salamone State Court Action and because each of the causes of action in fraud, negligence, malpractice and RICO were legally insufficient. Welcher interposed an Answer to the Motion to Dismiss which included a request that, if the Court believed it was appropriate, Welcher be allowed to amend its Complaint regarding the allegations of fraud to set them forth with more specificity as required by Rule 9 of the Federal Rules of Civil Procedure.

On June 15, 1994, the Court denied the Motion to Dismiss without prejudice and directed that Welcher amend its Complaint to remove all of the allegations of damages being claimed individually by Mr. Salamone in the Salamone State Court Action and that the State Court pleadings also be amended to delete any references to Welcher's alleged damages.

On July 5, 1994, Welcher filed an Amended Complaint. The Amended Complaint contained a first cause of action for malpractice, a second cause of action for fraud, a third cause of action for negligence, a fourth cause of action under RICO, and a fifth cause of action which alleged the failure of defendants to comply with the New York State licensing regulations regarding Certified Public Accountants and Public Accountants. Welcher also filed with the Court a proposed amended complaint to be filed in the Salamone State Court Action, which included a first cause of action for fraud and a second cause of action for negligence and malpractice.

On July 25, 1994, a Motion to Dismiss was filed on behalf of the defendants (the "Second Motion to Dismiss"). Welcher filed opposition to the Second Motion to Dismiss and on September 14, 1994 the Court heard oral argument on the Motion, dismissed the cause of action for failure to

comply with New York State licensing regulations and reserved on the balance of the Motion.

On July 20, 1994, Welcher commenced an adversary proceeding (Adversary Proceeding #94-2072) against Frank Cappotelli and Joseph Petrone which sought damages against those defendants for extortion, conversion, restitution after the rescission of a contract and a violation of RICO. These causes of action were alleged to have been the result of the involvement of the defendants with Ira Bristol in various scrap metal sales by Welcher to a corporation which employed the defendants. That adversary proceeding has been transferred to the United States District Court for the Western District of New York to be consolidated with an action pending in that Court involving the same subject matter.

On November 29, 1994, an Order was entered confirming Welcher's Amended Plan dated July 14, 1994 (the "Amended Plan"). The Amended Plan provided for the payment of all claims in full over a sixty-six month term. In addition, the Amended Plan: (1) provided for the proceeds of any recoveries in the pending adversary proceedings brought by Welcher, including the Fisher Adversary Proceeding, to be paid to creditors in addition to the payments otherwise provided for under the Amended Plan; and (2) contemplated that a claim by Fisher, Inc. in the amount of \$8,196.81 for services rendered would be resolved by or in connection with the pending Adversary Proceeding.

DISCUSSION

A motion to dismiss a complaint for failure to state a claim upon which relief can be granted under Rule 12(b)(6) of the Federal Rules of Civil Procedure, as made applicable under Bankruptcy Rule 7012, must be granted when it appears with certainty that there is no set of facts that could be proven at trial which would entitle the plaintiff to any relief. *In re Rudaw/Empirical Software*

Products Ltd., 83 B.R. 241, 245 (Bankr. S.D.N.Y. 1988). On a motion to dismiss, the allegations must be taken as true and the complaint construed in a light most favorable to the plaintiff. *In re Nantz*, 44 B.R. 543, 544-45 (Bankr. N.D.Ill. 1984) (citing *Mathers Fund, Inc. v. Colwell Co.*, 564 F.2d 780, 783 (7th Cir. 1977)). Therefore, this Court will take as true all of the facts alleged in the Welcher Complaint for the purpose of deciding the Motion to Dismiss.

I. RICO CAUSE OF ACTION

Welcher's RICO civil cause of action under 18 U.S.C. Section 1964(c) alleges a violation of 18 U.S.C. Section 1962(c).

To state a RICO claim under § 1962(c), a complaint must allege (1) that the defendants (2) through the commission of two or more acts (3) constituting a "pattern" (4) of "racketeering activity" (5) directly or indirectly invest in, or maintain an interest in, or participate in (6) an "enterprise" (7) the activities of which affect interstate commerce. 18 U.S.C. § 1962; *Moss v. Morgan Stanley, Inc.*, 719 F.2d 5, 17 (2d Cir. 1983), *cert. denied*, *Moss v. Newman*, 465 U.S. 1025 (1984). A "pattern of racketeering activity" requires at least two acts involving racketeering activity. 18 U.S.C. § 1961(5).

Tripp v. Marine Midland Bank, N.A., Civ. 91-6217L (W.D.N.Y. March 27, 1992) (Larimer, J.).

In essence, the RICO claim asserted by Welcher is based on allegations and a theory that the "enterprise", Fisher Inc., by aiding, abetting, facilitating and concealing the actions of Ira or Jean Bristol was involved in a pattern of racketeering activity which affected interstate commerce. The claim further asserts that these actions by the defendants and the Bristols resulted in the loss by Welcher of corporate assets and opportunities which the Bristols appropriated to their own use.

Based on the pleadings and proceedings in this case, the Court must dismiss the Welcher RICO claim as being legally insufficient.

The Amended Complaint and Welcher's responses to the Second Motion to Dismiss allege that Fisher, Inc. is the wrongdoing "enterprise". To the extent that either Welcher or an enterprise

consisting of Ira Bristol and third parties involved in scrap metal sales may have been a wrongdoing "enterprise" under the RICO statute, rather than Fisher, Inc., it is clear from the facts of this case that under the holding of the United States Supreme Court in *Reves v. Ernst & Young*, 507 U.S.—, 113 S.Ct. 1163 (1993), the defendants did not participate in the operation or management of that "enterprise" to the extent required. What is required by the holding in that case is having some part in controlling or directing the affairs of the "enterprise". To the extent that the "enterprise", as alleged, is Fisher, Inc., the Court does not believe that entity committed the required predicate acts of racketeering activity, even if it were proven, as alleged, that the defendants knowingly aided and abetted the Bristols. Furthermore, the Court does not believe that such aiding and abetting could constitute a "pattern" of racketeering or that it affected interstate commerce as required by the statute.

Except for the allegations which involve the activities of Ira Bristol in scrap metal sales, the allegations of wrongdoing which the defendants are alleged to have knowingly aided and abetted, are the wrongful and, as admitted by the Bristols, fraudulent acts of a corporate officer, shareholder and director of a closely-held corporation which he founded in appropriating corporate assets and opportunities to his own use. None of these acts are among those indictable acts listed in the statute as constituting racketeering activity. To the extent that extortion, which is one of the enumerated racketeering activities, was involved in the scrap metal sales activities, those activities were not those of an "enterprise" which Fisher, Inc. could be said to have had any part in directing, as required under the "operation or management" test adopted in *Reves v. Ernst & Young*.

In addition, the allegations of aiding and abetting made against Fisher, Inc. are but a few acts and do not demonstrate the "long-term criminal conduct," which RICO was intended to address. *H.J. Inc. v. Northwestern Bell Tel. Co.*, 492 U.S. 229 (1989).

Furthermore, Welcher has failed to allege how the activities of the alleged "enterprise", Fisher, Inc., affected interstate commerce within the meaning, intent and requirements of the statute.

The fact that any of the defendants may have used the mails to forward tax returns or financial information is not sufficient on the facts and circumstances of this case to meet the requirement of affecting interstate commerce.

II. CAUSES OF ACTION FOR FRAUD, NEGLIGENCE, AND MALPRACTICE

From a review of the pleadings and proceedings in this case, the Court believes that the Plaintiff has set forth sufficient allegations in nature, extent and specificity, which when taken as true and analyzed together with the assertions of the defendants in the Second Motion to Dismiss, warrant the Court denying the Motion to Dismiss. Welcher's allegations that the Defendants aided, abetted, facilitated and concealed the actions of the Bristols go beyond mere assertions that they failed to discover or disclose the wrongdoing. The assertions are that the Defendants with full knowledge of the wrongdoing facilitated and concealed it.¹

III. FUTURE PROCEEDINGS IN THE ADVERSARY PROCEEDING

At oral argument on the Second Motion to Dismiss the parties appeared to concede that should Welcher's RICO claim be dismissed, it may be in the best interests of the parties and overall judicial economy that Welcher's remaining claims and the Salamone State Court Action be heard together since they involve essentially the same facts. In its response to the Second Motion to

¹ Accountants may be liable to their client for damages resulting from failure to exercise care which would be observed by an ordinary prudent member of the profession, or for fraud or misconduct exercised in a professional capacity. 76 N.Y. JUR 2D *Malpractice* §6 (1989). See, e.g., *In re Mid-Atlantic Fund, Inc.*, 39 B.R. 88 (S.D.N.Y. 1984) (bankruptcy trustee adequately pleaded a negligence claim against the debtor's former accountants for failure to perform in accordance with standards of the accounting profession); *Fund of Funds, Ltd. v. Arthur Andersen & Co.*, 545 F.Supp. 1314, 1359-62 (S.D.N.Y. 1982) (accounting firm liable for common law fraud based on material misrepresentations made with scienter).

Dismiss, Welcher indicated that it might be in the best interests of the parties and overall judicial economy that the Salamone State Court Action be removed to Bankruptcy Court. However, in view of the facts that: (1) since the oral argument on the Second Motion to Dismiss Welcher has had its Amended Plan confirmed, and therefore has obtained the principal relief which it sought in the federal courts; (2) the Salamone State Court Action is pending in State Court; and (3) the Salamone and remaining Welcher causes of action are purely state law causes of action, and not federal claims, it may that it would be more appropriate for the remaining causes of action of both Welcher and Salamone to be heard together in State Court.²

CONCLUSION

The Second Motion to Dismiss Welcher's causes of action under 18 U.S.C. Section 1964(c) and for violation of the New York State Licensing regulations is in all respects granted. The Second Motion to Dismiss Welcher's causes of action for fraud, negligence and malpractice is in all respects denied. This matter is set down for telephonic pretrial conference on January 24, 1995 at 2:00 o'clock, to be initiated by Mr. Abramowitz, the attorney for Welcher, at which time the Court will discuss in detail with the parties whether Welcher's remaining causes of action will be heard in this Court or in the State Court.

IT IS SO ORDERED.

² It has been established that state courts have concurrent jurisdiction to hear civil claims under RICO. Therefore, Welcher could have brought its action against the defendants in state court, including its RICO claim. There is no jurisdictional requirement to proceed in the federal bankruptcy forum. *See Tafflin v. Levitt*, 493 U.S. 455, 458-59 (1990), *reh'g denied*, 495 U.S. 915 (1990); *Stochastic Decisions, Inc. v. DiDomenico*, 995 F.2d 1158 1171 n.5 (2d Cir. 1993) *cert. denied*, 114 S.Ct. 385 (1993); *Simpson Elec. Corp. v. Leucadia, Inc.*, 72 N.Y.2d 450, 452 (1988).

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/s/

HON. JOHN C. NINFO, II
U.S. BANKRUPTCY COURT JUDGE

Dated: December 30, 1994