UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

THE BENNETT FUNDING GROUP, INC.	CASE NO. 96-61376 Chapter 11
Debtors	Substantively Consolidated

RICHARD C. BREEDEN, TRUSTEE FOR
THE BENNETT FUNDING GROUP, INC. and
BENNETT MANAGEMENT AND DEVELOPMENT
CORPORATION

Plaintiff

vs. ADV. PRO. NO. 97-70099A

STANDARDBRED ENTERPRISES, LTD.,
HELMER, JOHNSON & MISIASZEK AND
N.W. INVESTORS II, L.L.C.

Defendants

STANDARDBRED ENTERPRISES, LTD.

Third Party Plaintiff

vs.

N.W. INVESTORS II, L.L.C.

Third Party Defendant

APPEARANCES:

SIMPSON, THACHER & BARTLETT Attorneys for § 1104 Trustee 425 Lexington Avenue New York, New York 10017	KENNETH G. CROWLEY, ESQ. Of Counsel
HELMER, JOHNSON & MISIASZEK Attorneys for Standardbred Enterprises, Ltd. 405 Court Street Utica, New York 13502	MICHAEL MISIASZEK, ESQ. Of Counsel
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RONALD M. TERENZI, ESQ.
Of Counsel

Hon. Stephen D. Gerling, Chief U.S. Bankruptcy Judge

MEMORANDUM-DECISION, FINDINGS OF FACT,
CONCLUSIONS OF LAW AND ORDER

Richard C. Breeden, the chapter 11 trustee appointed in the cases herein ("Trustee") initially filed a complaint against Standardbred Enterprises, Ltd. ("Standardbred") on April 26, 1997, pursuant to sections 105, 541, 542, 544, 548 and 550 of the Bankruptcy Code (11 U.S.C. §§101-1330) ("Code"). On June 12, 1997, the Trustee sought to amend his complaint to include a cause of action against N.W. Investors II, L.L.C. ("NW") and Helmer, Johnson and Misiaszek ("HJM"), counsel to Standardbred. The Court granted the Trustee's motion and on June 30, 1997, the Trustee filed his First Amended Adversary Proceeding Complaint.

The Trustee alleges that between 1991 and 1993 Patrick Bennett ("P.Bennett") purchased 121,525 shares of Mid-State Raceway Inc. ("MidState"), the owner and operator of Vernon Downs Racetrack, generally utilizing funds transferred to him from Bennett Management &

Development Corporation ("BMDC") for no consideration.[1] The Trustee contends that thereafter P.Bennett transferred 126,657 shares of Mid-State stock to Standardbred, a corporation whose sole shareholder is alleged to be Gwen Bennett, P.Bennett's wife.

The Trustee goes on to allege that as consideration for the stock transfer, Standardbred made and delivered to P.Bennett a note ("Standardbred Note") in the sum of $1,950,000, a note which is alleged Standardbred had no ability to repay. Additionally, the Trustee asserts that on or about March 1, 1996, P.Bennett transferred the Standardbred Note to NW and on or about October 1996, Standardbred and NW entered into a Security and Escrow Agreement whereby the MidState stock was placed in escrow with HJM, Standardbred's attorneys, to be held pending P.Bennett's repayment of the Standardbred Note to NW. In the event of default, the stock would be turned over to NW. Finally, the Trustee asserts that in April 1997, NW alleges that there was a default under the Standardbred Note and when NW demanded the

turnover of the stock, HJM refused.

The Trustee makes the legal argument that the transfers from BMDC to P.Bennett were made with an intent to defraud creditors of BMDC and other Bennett entities, that the transfer from P.Bennett to Standardbred was fraudulent against BMDC and other Bennett entities, and finally, the transfer of stock by Standardbred to NW was a further extension of the prior fraudulent transfers. Thus, the Trustee demands the return of the Mid-State stock.

On August 1, 1997, NW filed its answer, and on August 4, 1997, Standardbred filed its

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[1] On March 29, 1996, the Bennett Funding Group, Inc. ("BFG") and BMDC, along with two other related corporate entities filed voluntary petitions for relief under chapter 11 of the Code. The cases were substantively consolidated on July 25, 1997.

answer, which included a demand for a jury trial.

The Trustee alleges that at one time P.Bennett was a director and Chief Financial Officer of BFG and Director, President, Chief Financial Officer and shareholder of BMDC. *See* Complaint at ¶ 8. Standardbred's Answer contains what it has identified as its "First Affirmative Defense and a First Counterclaim," asserting that the action commenced by the Trustee is frivolous and that Standardbred's reputation and ability to manage its affairs have been damaged. Standardbred requests that the complaint be dismissed and that it be awarded $1 million, together with costs and disbursements. NW's Answer contains no counterclaims and no request for a jury trial.

On September 15, 1997, at the Court's request, the Trustee filed his "Submission" disputing Standardbred's right to a jury trial. Citing to *Granfinanciera v. Nordberg*, 492 U.S. 33,48-49 (1989), the Trustee asserts that since he is seeking the turnover of an intangible, namely the Mid-State stock, the action is an equitable proceeding for which Standardbred has no right to a trial by jury. In a responsive submission, Standardbred points out that in order for the Trustee to avoid the alleged fraudulent transfer the Court would be required to determine the amount of money to be repaid to NW based on its alleged security interest. Standardbred contends that "[t]here cannot be an equity action for the transfer of stock without there also being a legal claim for the value of the security interest of N.W. Investors II in the stock held by Standardbred . . . ." Standardbred argues that actions in fraud are triable by a jury and that if the action was tried in state court, it would be entitled to a jury trial. As a result, Standardbred claims that it should be entitled to a jury trial to determine the state law fraud claim in bankruptcy court.

In 1989, the Supreme Court in *Granfinanciera* held that the Seventh Amendment entitles a party to a jury trial where the cause of action against that person is solely for monetary relief in a fraudulent conveyance action and that party has not submitted a claim against the estate. *See Granfinanciera*, 492 U.S. at 47. The Court noted that a two part test is used to determine whether a party is entitled to a jury trial. "'First we compare the statutory action to 18th-century actions brought in the courts of England prior to the merger of the courts of law and equity. Second, we examine the remedy sought and determine whether it is legal or equitable in nature.'" *Id*. at 42 (citation omitted). An action at law gives a right to a jury trial under the Seventh Amendment. On the other hand, an action in equity or a mixed law-equity action does not require a jury trial. The court in *Granfinanciera* explained:

> "[W]hether the trustee's suit should be at law or in equity is to be judged by the same standards that are applied to any other owner of property which is wrongfully withheld. If the subject matter is a chattel, and is still in the grantee's possession, an action in trover or replevin would be the trustee's remedy; and if the fraudulent transfer was of cash, the trustee's actions would be for money had and received. Such actions at law are as available to the trustee to-day as they were in the English courts of long ago. *If, on the other hand, the subject matter is land or an intangible, or the trustee needs equitable aid for an accounting or the like, he may invoke the equitable process,* and that also is beyond dispute."

See id. at 44, quoting 1 G.GLENN FRAUDULENT CONVEYANCES AND PREFERENCES § 98, pp. 183-84 (rev. ed. 1940) (emphasis added).

In *Sunset Beach, Ltd. v. Stocks (In re Stocks)*, 137 B.R. 516 (Bankr. N.D. Fla. 1991) the plaintiff sought to set aside an alleged fraudulent transfer by the chapter 7 debtor of his interest in Sunset Beach, Ltd. ("sunsey") to debtor's family trust. The court in examining the rationale

of *Granfinanciera* found that the Supreme Court had "held that a party is entitled to a jury trial in an action to recover a fraudulent *monetary* transfer." *See Stocks* at 521. The court pointed out that the focus in *Granfinanciera* was clearly on the fact that the remedy being sought was for the recovery of money and was, therefore, an action at law. *See id.* The court in *Stocks* also found that as the plaintiff was seeking an order determining that the 40% interest in Sunset was property of the estate and that the transfer of Stock's interest in Sunset was void, the defendant (the family trust) was not entitled to a jury trial. *See id.* at 522.

More recently in 1995, the Bankruptcy Court for the Southern District of New York held that a fraudulent conveyance action for the transfer of stock, an intangible, is equitable relief that does not entitle a person to a jury trial under the Seventh Amendment. *See Committee of Unsecured Creditors v. 90th Street Garage Corp.* (*In re Term Industries, Inc.*), 181 B.R. 31,33 (Bankr. S.D.N.Y. 1995). At issue in that case was the ownership of shares of stock for which the committee sought a declaration that the debtor was the rightful owner. The committee also sought the avoidance of the transfer of the stock and the turnover of the stock certificates. *See id.* The court distinguished *Granfinanciera* by stating that the relief sought in the *Granfinanciera* fraudulent conveyance action was money payments, a legal remedy, whereas the relief sought in *90th Street Garage* was the transfer of stock, an equitable remedy. The court concluded that there was no right to a jury trial.

Based on the analyses in *Stocks* and *90th Street Garage*, the Trustee's request seeking the avoidance of the transfer of the shares of Mid-State stock and their turnover to BMDC's estate is equitable in nature and, therefore, Standardbred is not entitled to a jury trial. The Trustee is

not seeking to recover money; rather, he is seeing to recover an intangible.

However, Standardbred contends that NW, also a named defendant, has an alleged security interest in the Mid-State stock. The defendant argues that according to Code § 550(e)(1)(A), the Trustee will have to satisfy the security interest of NW in order to avoid the alleged fraudulent conveyance. Standardbred further asserts that the Court would have to determine a sum of money to pay NW in the event the Trustee is successful, thereby entitling NW to a jury trial.

In its answer NW has not demanded a jury. Nor has it asserted any counterclaims against the Trustee seeking monetary relief. Yet, Standardbred appears to be making arguments not with respect to any relief it may be seeking, but rather with respect to relief to which it believes NW will be entitled. Standardbred has no standing to demand a jury trial based on the rights of another defendant. Further, the Trustee alleges that NW is not a bonafide purchaser or holder in due course and, therefore, arguably Code § 550(e)(1)(A) would be unavailable to it.

With respect to Standardbred's counterclaim, the Court notes that a number of courts have "construed counterclaims filed in an adversary proceeding as claims against the bankruptcy estate which divest a defendant in an adversary proceeding of the right to a jury trial." *See Carmel v. Galam (In re Larry's Apartment, L.L.C.)*, 210 B.R. 469, 473 (D. Ariz. 1997) (collecting cases); *see also Peachtree Lane Assoc., Ltd. v. Granader*, 175 B.R. 232, 237 (N.D. Ill. 1994) (agreeing with reasoning of *In re Hudson*, 170 B.R. 868 (E.D.N.C. 1994) that "the defendant lost its right to a jury trial by filing a counterclaim seeking a piece of the disputed *res*, the debtor's estate, which was subject to the bankruptcy court's equitable power to allow and disallow claims.

Regardless of whether the counterclaim was permissive or compulsory, it represented the defendant's attempt to obtain a portion of the debtor's estate." *See Hudson,* 170 B.R. at 875). The court in *Peachtree* deemed this rationale appropriate even though some of the defendants' counterclaims (e.g. slander of title, commercial disparagement, tortious interference with economic advantage, etc.) arose postpetition. *See Peachtree*, 175 B.R. at 237. Not all courts, however, have concluded that asserting a counterclaim in an adversary proceeding constitutes a waiver of ones right to a jury trial when one has not filed a proof of claim. *See, e.g., NDEP Corp. v. Handl-It, Inc. (In re NDEP Corp.)*, 203 B.R. 905 (D. Del. 1996); *J.T. Moran Financial Corp. v. Am. Consolidated Financial Corp. (In re J.T. Moran Financial Corp.)*, 124 B.R. 931 (S.D.N.Y. 1991) and *Beard v. Braunstein*, 914 F.2d 434, 442 (3d Cir. 1990). The court in *J.T. Moran* reasoned that the filing of a counterclaim should not constitute consent to the bankruptcy court's jurisdiction as that "would be to condone jurisdiction by ambush." *See J.T. Moran*, 124 B.R. at 940. In *NDEP Corp.* and *J.T. Moran* the defendants' counterclaims were not compulsory, whereas in *Beard* they were. In all three cases the adversary proceeding was found to be a non-core proceeding. The court in *Beard* noted that the adversary proceeding under consideration involved prepetition contracts for rent which were "only tangentially related to the bankruptcy." *See Beard*, 914. F.2d at 445. In *NDEP Corp.* the court found that the resolution of the adversary proceeding, which involved alleged prepetition breach of a supply contract, would not impact on the distribution of property of the estate. *See NDEP Corp.*, 124 B.R. at 912. So too the adversary proceeding in *J.T. Moran* also involved an alleged breach of a prepetition contract. The above three cases are distinguishable from the matter herein. Claims based on fraudulent transfers are

core proceedings subject to the jurisdiction of the bankruptcy court. *See Larry's Apartment* at 474.

Standardbred has asserted a counterclaim seeking to recover $1 million from the Trustee based on the assertion that the complaint herein is frivolous and has interfered with the conduct of Standardbred's affairs. Standardbred's counterclaim does not arise from the prepetition occurrence or transaction which is the underlying basis for the Trustee's complaint. Rather, it stems from the Trustee's complaint itself. The bare allegation that the Trustee's complaint is frivolous and has in someway interfered with the management of Standardbred's business affairs is not a basis for allowing it to circumvent the jurisdiction of this Court. Accordingly, Standardbred has no right to a jury trial under the facts and allegations herein.

IT IS SO ORDERED.

Dated at Utica, New York

this 27th day of October1997

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STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge