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, as trustee for
THE BENNETT FUNDING GROUP, INC., et al.

Plaintiff

vs.	ADV. PRO. NO. 98-41254A

NELSON FERNANDES

Defendant

APPEARANCES:

HISCOCK & BARCLAY, LLP Attorneys for Trustee Financial Plaza P.O. Box 4878 Syracuse, New York 13221-4878	ROBERT LIDDELL, ESQ. Of Counsel
NELSON FERNANDES 9 Fox Run Denville, New Jersey 07834	

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

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

In this adversary proceeding, the chapter 11 trustee, Richard C. Breeden ("Trustee"), seeks to avoid and recover as fraudulent transfers certain pre-petition payments made to Nelson Fernandes ("Defendant") by Aloha Leasing, a Division of The Bennett Funding Group, Inc.

("BFG").[1] On August 28, 2001, Defendant filed a motion in the form of a letter brief for summary judgment, seeking amendment or vacatur of an Order of this Court, dated November 13, 1998 ("Vacatur Motion"). Defendant also filed a separate motion on August 28, 2001, seeking dismissal of the adversary proceeding and requesting sanctions against the Trustee pursuant to Rule 9011(b) of the Federal Rules of Bankruptcy Procedure ("Fed.R.Bank.P.") ("Dismissal Motion"). The Trustee filed opposition to the motions on September 10, 2001.

Both motions were heard at the Court's motion term on September 13, 2001, in Utica, New York. Following oral argument, the parties were afforded an opportunity to file memoranda of law, and the matter was submitted for decision on October 9, 2001.

JURISDICTIONAL STATEMENT

The Court has jurisdiction over the parties and subject matter of the adversary proceeding pursuant to 28 U.S.C. § 1334 and 157(a), (b)(1), (b)(2)(A), and (H).

FACTS

On or about August 30, 1989, the Defendant was issued an assignment of a purported lease of equipment between Aloha Leasing, as lessor, and the State of New Jersey, as lessee. *See*

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[1] The Trustee serves as the chapter 11 trustee of the consolidated estates of BFG, Bennett Receivables Corporation, Bennett Receivables Corporation II, Bennett Management and Development Corporation, The Processing Center, Inc., Resort Service Company, Inc., American Marine International, Ltd. and Aloha Capital Corporation (collectively, the "Debtors").

Exhibit A, attached to the Dismissal Motion. Under the terms of the assignment, Defendant was assigned

> as to the financial ability of the Lessee to pay its entire right, title and interest in and to the annexed above named lease (the Lease), including all rental and other payments due and to become due thereunder . . . .

See id. At the time of the assignment, the alleged aggregate unpaid rentals totaled $18,720. *See id.* The amount of investment listed in the Statement of Purchased Leases, identifying the Defendant as the assignee, totaled $16,472.62, with a monthly payment of $520 over 36 months. *See* Exhibit D, attached to the Dismissal Motion.

The Trustee commenced the adversary proceeding by the filing of a complaint ("Complaint") on February 12, 1998. Relevant to the motion herein, the Trustee's second cause of action brought pursuant to Code § 544(b) and §§ 271-276 of the New York Debtor and Creditor Law ("NYD&CL"), seeks a determination that payments made to the Defendant by BFG within six years of March 29, 1996, are voidable. *See* ¶ 32 of the Complaint. According to Exhibit A, attached to the Complaint, the Trustee sought to recover $2,247.38, the difference between the initial investment of $16,472.62 and the amount of the payments made to the Defendant of $18,720. However, Trustee allegedly notified Defendant that he had withdrawn any claims for recovery of payments made to the Defendant prior to March 29, 1990.[2]

On March 13, 1998, the Defendant filed his Answer to the Complaint and also asserted

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[2] According to the Settlement Package sent to the Defendant on or about March 14, 2001, the amount invested was $14,009.44 and payments received between March 30, 1990 and August 30, 1992, totaled $15,600. Trustee seeks to recover $1,590.56 representing the interest received on the initial investment. *See* Exhibit G, attached to Defendant's Dismissal Motion. Under the settlement formula, Trustee sought payment from the Defendant of $118.11 if made by July 12, 2001. *See* Exhibit C of Affidavit of Mark D. Sonnelitter, sworn to on August 3, 2001, and filed on August 6, 2001, in support of the Trustee's Memorandum of Law in Opposition to Defendant's Motion.

a counterclaim to which the Trustee filed an answer on June 23, 1998. The counterclaim, labeled as a "Cross-claim," seeks $10,000 in damages for intentional emotional distress, as well as costs and attorney's fees as a result of the Trustee's "fallacious claims."

As factual background in his Complaint, the Trustee alleges that the Debtors had "engaged in the apparent business of equipment leasing and financing through which the Debtors conducted a Ponzi scheme . . . The Debtors financed their capital and cash flow needs through a Ponzi scheme accomplished by, among other things, (i) obtaining investments and leases by pledging the same lease multiple times to investors and pledging that same lease to a financial institution and (ii) pledging to investors fictitious leases."[3] *See* Complaint at ¶ 9.

The Complaint further alleges that the Defendant acquired one or more of these investments, receiving payments in excess of the investment amount. The Trustee seeks to recover either the total amount of the payments or, in the alternative, the excess of the amount invested, as fraudulent transfers.

On November 13, 1998, the Court signed an Order staying the adversary proceedings commenced against the former investor defendants, including the Defendant herein, "until further order of the Court." ("Stay Order")

DISCUSSION

Vacatur Motion

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[3] In the Trustee's Supplemental Memorandum of Law, filed October 9, 2001, it is alleged that the lease assigned to the Defendant was fictitious.

Defendant asserts that the Complaint fails to state a cause of action and even if it were determined to be valid, it is unfair to him and others similarly situated not to be able to present a position and have the matter decided. Defendant contends that the settlement offers made by the Trustee arguably violate the Stay Order.

The Trustee argues that it was the settlement process that was the basis for the Trustee seeking the Stay Order in the first place. The Trustee estimates that within 30-60 days of the hearing on Defendant's motion (September 13, 2001), any extensions granted to the defendants will have run out and at that point, the Trustee could "deal with what's left."

Given that almost 180 days have elapsed since said hearing, the Court will grant the Defendant's Vacatur Motion and vacate that portion of its Stay Order which applies to him and other "non-settled" former investor defendants based on the representations made by the Trustee's counsel at the hearing that he needed at most 60 days to complete the settlement process.

Dismissal Motion

As an initial matter, the Defendant raises a question concerning the standing of the Trustee to file a complaint against him on behalf of Aloha Leasing, which is not named as one of the Debtors. Defendant points out that the assignment he received was executed in the name of "Aloha Leasing." However, as this Court has previously found, "Aloha Leasing" was simply the trade name used by BFG in many of its transactions. *See In re The Bennett Funding Group, Inc.*, 203 B.R. 30, 37 (Bankr. N.D.N.Y. 1996). It is BFG which is the legal entity and a debtor herein, and it is BFG whose rights are being asserted by the Trustee. Indeed, the assignment given to the Defendant is captioned "Aloha Leasing, A Division of The Bennett Funding Group,

Inc." *See* Exhibit A, attached to the Dismissal Motion. Therefore, the Court concludes that the Trustee has standing to file the Complaint on behalf of BFG.

Defendant also seeks to have the Trustee's Complaint dismissed on the basis that it fails to state a claim upon which relief can be granted.[4] As a basis for his Dismissal Motion, the Defendant contends that there is a legal distinction between "pledge" and "assignment." The Defendant asserts that the lease was assigned to him and he owns it.[5] Therefore, any payments received by the Trustee from the lessee were received as an agent or conduit. Under this theory, Defendant argues that the payments to the Defendant in no way diminished the Debtors' estate. The Defendant asserts that the Trustee's use of the word "pledge" in the Complaint, rather than "assignment," is simply an attempt by the Trustee to place BFG in a position of having retained ownership of the lease.

The Court interprets the Defendant's motion as one brought pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure ("Fed.R.Civ.P."), made applicable to this proceeding by Fed.R.Bankr.P. 7012. In considering such a motion, the Court must accept all of the non-movant's allegations as true, and will grant the motion to dismiss "only if it is clear that no relief could be granted under any set of facts that can be proved consistent with the allegations." *Hishon v. King & Spaulding,* 467 U.S. 69, 73, 104 S.Ct. 2229, 2232, 81 L.Ed.2d (1984) (citation

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[4] The Trustee's first cause of action, based on Code § 548, is appropriately dismissed since it applies only to transfers made one year prepetition. As the last payment to the Defendant was August 30, 1992, there is no factual basis for the Trustee to seek recovery from the Defendant on his first cause of action. *See* Exhibit G, attached to Defendant's Dismissal Motion.

[5] Although a letter addressed to the Defendant from BFG references the enclosure of the "municipal lease" along with copies of the assignment, the Defendant acknowledges that he did not have either an original or a copy of the lease in his possession.

omitted).

While Defendant takes exception to the Trustee's labeling the transaction as a "pledge," pursuant to NYD&CL § 270, "pledge" is included in the definition of "conveyance," as is "assignment" and the "payment of money." In this case, the Trustee is seeking to avoid and recover payments made to the Defendant between March 30, 1990 and August 30, 1992. He is not seeking to avoid the underlying transaction, whether labeled as an "assignment" or "pledge."[6]

In order to succeed with his second cause of action based on Code § 544(b) and NYD&CL §§ 273-275 for constructive fraud, the Trustee must prove (1) that the transfer or conveyance was made for less than fair consideration and (2) that at the time of the transaction, the transferor was either insolvent, a defendant in an action for money damages, engaged in a business with unreasonably small capital or about to incur debts beyond its ability to pay. *See Breeden v. Thomas*, Adv. Pro. 98-40892, slip op. at 8-9 (Bankr. N.D.N.Y. April 29, 1999) (citation omitted). Under NYD&CL § 276, a transfer is avoidable if it is made "with actual intent, as distinguished from intent presumed in law, to hinder, delay or defraud either present or future creditors." *Id.* at 7-8. The Defendant does not deny receiving the payments identified by the Trustee in his Complaint. He simply argues that the payments were rightfully his based on the assignment. This argument, of course, presupposes that a lease existed and that the payments

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6 The Defendant also argues that since the Trustee cannot make a claim for the lease payments as the owner of the leases, the Trustee's only alternative would have been to attack the assignment itself. Defendant correctly points out that since the assignment was executed more than six years prepetition, the statute of limitations prevents the Trustee from avoiding the assignment as fraudulent pursuant to Code § 544.

were made by the lessee[7] to BFG, which in turn made payments to the Defendant. As noted above, on a motion made pursuant to Fed.R.Civ.P. 12(b)(6), the Court must examine the Trustee's allegations and determine whether there is any set of facts which would warrant a finding in favor of the Trustee. At a minimum, if the Trustee is able to establish that no such lease existed, then it is conceivable that the Trustee will be able to prove a lack of fair consideration by BFG's payment of interest from its own assets to the Defendant and that either BFG was insolvent or perhaps about to incur debts beyond its ability to pay at the time the payments were made to the Defendants. Accordingly, at this stage of the proceeding, it would be inappropriate to dismiss the Complaint insofar as it asserts a claim for constructive fraud.

With respect to the Trustee's claim for actual fraud pursuant to NYD&CL § 276, it is the state of mind of the transferor (and not the actions or intent of the transferee) that are relevant. Assuming that the Trustee's allegations are true for purposes of this motion, including the allegation that the Defendant's lease did not exist, then the Trustee should have an opportunity to establish that the payments were made by BFG with the intent to defraud its creditors. Therefore, the Court will also deny Defendant's request for dismissal of the Complaint insofar as it alleges a cause of action based on actual fraud pursuant to NYD&CL § 276.

In the context of the Dismissal Motion, the Defendant also requests that the Court impose sanctions against the Trustee. Defendant argues that in claiming that the Debtors "pledged" the lease to the Defendant, the Trustee was well aware of the position taken by the Securities Exchange Commission that what was offered to investors such as the Defendant were "lease

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[7] As noted above, according to the documents presented by the Defendant, the lessee was the State of New Jersey.

assignments." Therefore, the Trustee had no legal basis for filing a Complaint against the Defendant alleging that the lease was "pledged" to him.

Having found that the Trustee's second cause of action in his Complaint states a claim for which the possibility of relief exists, the Court must deny Plaintiff's request for sanctions. Whether the transaction between BFG and the Defendant involved a pledge or an assignment of leases is of no import if the Trustee is able to establish that the lease did not exist, as suggested in his Complaint and more specifically set forth in the affidavit of Frank T. Halligan, sworn to October 4, 2001.

Based on the foregoing, it is hereby

ORDERED that the Defendant's motion seeking vacatur of the Stay Order of November 13, 1998, as applicable to former investor defendants who have not agreed to the settlement offered by the Trustee, including the Defendant herein, is granted; it is further

ORDERED that the Defendant's motion seeking dismissal of the Trustee's Complaint is granted with respect to the First Cause of Action, which is based on Code § 548; it is further

ORDERED that the Defendant's motion seeking dismissal of the Trustee's Complaint is denied with respect to the Second Cause of Action, which is based on Code § 544(b) and NYD&CL § 271-276, and it is finally

ORDERED that the Defendant's motion requesting sanctions pursuant to Fed.R.Bankr.P. 9011 is denied.

Dated at Utica, New York

this 22nd day of February 2002

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STEPHEN D. GERLING

Chief U.S. Bankruptcy Judge