UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

WILLIAM A. GESSLER
MARCIA A. GESSLER

CASE NO. 96-60189

Debtors

Chapter 7

MARY E. LEONARD, TRUSTEE

Plaintiff

vs.

ADV. PRO. NO. 96-70300A

WILLIAM A. GESSLER, MARCIA A. GESSLER and THE GESSLER FAMILY LIMITED PARTNERSHIP

Defendants

APPEARANCES:

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

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

Presently before the Court is an adversary proceeding commenced by the trustee in

bankruptcy, Mary E. Leonard ("Plaintiff"), against the defendants William and Marcia Gessler ("Debtors") who filed bankruptcy in January 1996, and the Gessler Family Limited Partnership ("Limited Partnership"). Pursuant to section 273 of the New York Debtor and Creditor Law ("NYDCL") and sections 542, 543 and 544(b) of the Bankruptcy Code (11 U.S.C. §§ 101-1330) ("Code"), the Plaintiff seeks to set aside property transfers made by the Debtors to the Limited Partnership in August 1994.

JURISDICTIONAL STATEMENT

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

FACTS

In the Spring of 1989 the Debtors acquired a window treatment business ("Better Shade Shop") located in Cicero, New York. Acting as officers of Gessler Enterprises, Inc. ("Gessler Enterprises" or "corporation"), the Debtors purchased the business from Elton Schoff ("Schoff") for approximately $130,000. In a separate transaction, the Debtors personally took title to the related business real property located at 5703 East Taft Road in Cicero, New York ("E.Taft Rd. property") for $180,000. Though these transactions were separate, the Debtors' down payments for the two transactions totaled $100,000. In order to finance the remaining portions of the transactions, the Debtors executed two mortgages in favor of Schoff. The mortgage on the

business real property totaled $146,640 and the chattel mortgage on the business itself totaled $64,130. *See* Plaintiff's exhibits 7-9.

The business, known to its customers as the "Better Shade Shop" and/or "Window Fashions of Central New York," continued under the Debtors' control for approximately six years until the Fall of 1995, at which time the business ceased operations. In August 1994, prior to the close of the business, the Debtors created the Limited Partnership establishing themselves as general partners and their three daughters as the limited partners. *See* Plaintiff's exhibit 4, at exhibit D. As a part of the agreement creating this entity, the Debtors transferred five privately held parcels of land[1] ("the transfer") to the Limited Partnership. *See id.* At trial, Mr. Gessler conceded that he did not receive any consideration for the transfer of the property to the Limited Partnership. Moreover, he admitted that none of the partners contributed any additional funds or property to the partnership. Mr. Gessler testified that approximately one year after this transfer, he and his wife closed the doors of the business and terminated its activities.

On January 17, 1996, the Debtors filed a voluntary chapter 7 bankruptcy petition. On October 16, 1996, the Plaintiff filed a complaint asserting that the transfer to the Limited Partnership is voidable pursuant to NYDCL § 273 and Code § 544. The Plaintiff seeks an order directing the defendants to turn over the Limited Partnership assets or their monetary equivalent, and in addition the Plaintiff seeks compensation for costs incurred during these proceedings. The defendants filed an answer to the complaint on November 12, 1996. A trial on this matter took

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[1] The properties consisted of a parcels of land in the following New York towns: Hastings ("Hastings property"), DeWitt ("DeWitt property"), Fleming ("Fleming property"), and Clay ("Clay property"). In addition, a parcel of land in Meridian, Arizona ("Arizona property") was transferred to the family limited partnership.

place on February 11, 1997 and was continued and concluded on February 24, 1997. The matter was submitted for decision on March 24, 1997.[2]

ARGUMENTS

The Plaintiff contends that the Debtors did not receive fair consideration in exchange for the conveyance of real property to the Limited Partnership. The Plaintiff supports this assertion by reference to Mr. Gessler's testimony during the trial when he conceded that neither he nor his wife received any consideration in exchange for the property transfer to the Limited Partnership.

The Plaintiff further contends that the transfer rendered the Debtors insolvent. Plaintiff asserts that there is a presumption of insolvency if a transfer is made without consideration at a time when the transferor has outstanding obligations. To support the presumption of insolvency, the Plaintiff argues that the Debtors had several outstanding obligations at the time of the transfer, including the fact that in August 1994 they were in default on the mortgages relating to the business,[3] that the Debtors had not paid their 1994 property taxes on a number of properties,

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[2] The Court allowed the parties to file post-trial memorandums of law by March 24, 1997. Memorandums were received from both parties and have been considered for this Decision.

[3] During the trial the Plaintiff elicited testimony from Schoff regarding the status of the mortgage payments before the transfer. According to Schoff, the principal payments on the business real property mortgage stopped on August 1, 1993. Schoff claimed that over the course of the following nine months, the Debtors stopped paying the interest and principal on both the business real property mortgage and the chattel mortgage on the business itself. He stated that the Debtors resumed payments on the two obligations only after he agreed to reamortize the obligations, extending the repayment period to twenty years.

which the Plaintiff maintains the Debtors were personally obligated for since these taxes were levied prior to the transfer, and that the Debtors had several outstanding credit card obligations. The Plaintiff adds that the Debtors were also burdened with bank debt at the time of the transfer. Specifically, the Debtors' bankruptcy petition reflects obligations to Key Bank in the amount of $5,870.25 and to OnBank & Trust Company in the sum of $7,353.68.[4]

The Plaintiff claims that the transfer left the Debtors with few assets, which included a 1983 Mercedes automobile, a 1977 boat, household contents valued at $4,500, and an interest in Gessler Enterprises.[5] Regarding the Debtors' interest in Gessler Enterprises and their interest in debts owed to them by the corporation, the Plaintiff asserts that neither can be considered to have salable value. Plaintiff supports this contention in part by reference to Mr. Gessler's testimony concerning corporate-owned assets. He testified that the corporation possessed very few "hard" assets and that the majority of the purchase price of the business was attributed to "good will".[6] *See id.*

Plaintiff asserts that as of 1994, the Debtors' business was in decline. The Plaintiff also refers to Mr. Gessler's admissions regarding his inexperience in this business field. During the trial, Mr. Gessler conceded that the window treatment business was a new venture for the couple, and further that he and his wife only received a portion of the training that was promised. In

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[4] Mr. Gessler testified that these accounts were in existence at the time of the transfer.

[5] Plaintiff maintains that the value of items which would be exempt from creditors' claims pursuant to NYDCL § 270 must be subtracted from the total value of the assets. *See* Plaintiff's Post-trial Memorandum of Law, filed March 24, 1997, at 5.

[6] Defendant testified that the business purchase included a shade cutter, tools, and a company van. When asked to be more specific about the tools owned by the business, Defendant replied that they were "various tools that were used in the business." Later, Defendant testified that a portion of the purchase price was allocated to items such as current business and training.

addition, Plaintiff alleges that the Debtors' initiation of cost-cutting measures such as cleaning the building and removing trash themselves is an indication of the business' financial problems.

Plaintiff recognizes that at the time of the transfer, the Debtors were optimistic about the future of the business and anticipated an influx of new contracts. However, Plaintiff contends that such optimism was unfounded, characterizing the Debtors' anticipated contracts as "largely speculative". During the trial, Mr. Gessler admitted that many of these contracts were based solely on oral agreements, and the Plaintiff showed that much of the anticipated work did not materialize.

Finally, Plaintiff avers that the Debtors transferred the property to the Limited Partnership with fraudulent intent. Although Plaintiff recognizes that actual fraudulent intent is not essential to a fraudulent conveyance determination grounded upon constructive fraud, she asserts in this case that the property transfer was made in an effort to avoid the claims of creditors. To support this claim, the Plaintiff refers to Mr. Gessler's testimony that his definition of estate planning was "keeping assets in the family." The Plaintiff further asserts that the timing of the Limited Partnership creation is significant, in that the Debtors transferred the property within months of a threatened foreclosure on the E.Taft Rd. property. In addition, the Plaintiff questions the legitimacy of Debtors' proffered reason for the timing of the transfer, which was that it was the result of attending a Rotary Club meeting where family limited partnerships were mentioned as an estate planning instrument. Plaintiff maintains that this explanation is dubious in light of the Debtors' poor financial circumstances.

Debtors maintain that the transfer of property to the Limited Partnership does not constitute a fraudulent conveyance pursuant to NYDCL § 273. Although the Debtors concede

that a presumption of insolvency is raised in this particular instance, they contend that they have rebutted that presumption. Debtors maintain that NYDCL § 273 relies on the definition of insolvency incorporated in NYDCL § 271, which defines a person as insolvent "when the present fair salable value of his assets is less than the amount that will be required to pay his probable liability on his existing debts as they become absolute and matured." The Debtors assert that this definition necessitates the use of a "balance sheet test" to determine insolvency. *See* Defendants' Post-trial Memorandum of Law, filed March 18, 1997, at 3. The Debtors assert that despite the transfer of property to the Limited Partnership, their assets continued to significantly outweigh their liabilities.

The Debtors further assert that they did not intend to defraud their creditors by creating the Limited Partnership, but instead were simply engaging in estate planning as Mr. Gessler's father had done when some of these properties were initially transferred to Mr. Gessler.

DISCUSSION

The Plaintiff in this proceeding seeks to invalidate the Debtors' property transfer to the Limited Partnership. Pursuant to Code § 544(b), a trustee may avoid a prepetition transfer of a debtor's interest in property that is voidable under applicable state law by a creditor who has an allowable unsecured claim. *See* 11 U.S.C. § 544(b); *Pereira v. Goldberger (In re Stephen Douglas, Ltd.)*, 174 B.R. 16, 19 (Bankr. E.D.N.Y. 1994). In this instance, the Plaintiff asserts that the applicable state law is NYDCL § 273, which provides that "[e]very conveyance made and every obligation incurred by a person who is or will be thereby rendered insolvent is

fraudulent as to creditors without regard to his actual intent if the conveyance is made or the obligation is incurred without a fair consideration." N.Y. Debt. & Cred. Law § 273 (McKinney 1990). Under this section of the NYDCL, a transferor's transactions may be traced back over six years. *See Goscienski v. Larosa (In re Montclair Homes)*, 200 B.R. 84, 95 (Bankr. E.D.N.Y. 1996). Importantly, if the court finds that there was a lack of fair consideration and the test for insolvency is met, a transfer may be deemed a fraudulent conveyance regardless of the actual intent of the transferor. *See Babitt v. Schwartz (In re Lollipop, Inc.)*, 205 B.R. 682, 686 (Bankr. E.D.N.Y. 1997); *see also In re Stephen Douglas*, 174 B.R. at 20 ("Both insolvency and a lack of fair consideration are prerequisite to a finding of constructive fraud under [NYDCL] Section 273.").

As a general rule, the party challenging the conveyance bears the burden of proving the lack of fair consideration and insolvency. *See In re Lollipop, Inc.,* 205 B.R. at 686; *Pereira v. Private Brands, Inc. (In re Harvard Knitwear, Inc.),* 193 B.R. 389, 396 (Bankr. E.D.N.Y. 1996); *In re 375 Park Ave. Assocs., Inc.*, 182 B.R. 690, 695 (Bankr. S.D.N.Y. 1995); *In re Stephen Douglas*, 174 B.R. at 20; *American Inv. Bank, N.A. v. Marine Midland Bank, N.A.,* 191 A.D.2d 690, 595 N.Y.S.2d 537, 538 (App. Div. 1993). Where a conveyance involves family members, however, the transferee bears a heavier burden to establish that fair consideration was given for the transfer. *See Orbach v. Pappa*, 482 F.Supp. 117, 119 (S.D.N.Y. 1979) ("In an intrafamily transaction, it is well-settled that a heavier burden is placed on the grantee to establish fair consideration for the transfer"); *Tesmetges v. Herman*, 85 B.R. 683, 695 (Bankr. E.D.N.Y. 1988) ("Where a transfer involves a family transaction, the transferee bears the burden of proof that the transfer was made with fair consideration"); *see also Gross v. Russo(In re Russo)*, 1 B.R. at 373

(Bankr. E.D.N.Y. 1979) (indicating that intrafamily transactions are to be carefully scrutinized to detect possible fraud). In this case, the defendants do not dispute the fact that there was no consideration given in exchange for the transfer of various properties from the Debtors to the family Limited Partnership. Instead, the Debtors allege that at the time of the transfer[7] they were not insolvent.

"Insolvency" is defined in the NYDCL as "[w]hen the present fair salable value of assets is less than the amount that will be required to pay his probable liability on his existing debts as they become absolute and matured." N.Y. Debt. & Cred. Law § 271(1). Under the NYDCL, however, when a conveyance is made for no consideration at a time when the transferor has outstanding debts there is a presumption that the transferor was insolvent.[8] *See Commodity Futures Trading Comm'n v. Probber Intern. Equities Corp.,*504 F.Supp. 1154, 1161 (S.D.N.Y. 1981); *In re Stephen Douglas*, 174 B.R. at 21; *In re Tabala,* 11 B.R. 405, 408 (Bankr. S.D.N.Y. 1981); *In re Russo*, 1 B.R. at 379; *see also Feist v. Druckerman,* 70 F.2d 333, 334 (2d Cir. 1934) ("[I]f one indebted makes such a transfer, it is presumed, in the absence of some proof to the contrary, that he was then insolvent."). The Debtors in this case assert that they rebutted any presumption of fraud by coming forward with proof indicating that they were solvent on the date of the transfer. The proper test for determining solvency or insolvency under the NYDCL is the

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[7] For purposes of this Decision, the Court shall examine whether the transfer to the Limited Partnership rendered the Debtors insolvent.

[8] Although Mr. Gessler testified that there was no fraudulent intent involved in the transfer of the properties to the family limited partnership, "actual intent to defraud need not be shown; constructive intent is established if the debtor was insolvent at the time of the transfer, or was rendered insolvent thereby." *In re Tabala*, 11 B.R. at 408; *see In re Montclair Homes*, 200 B.R. at 95.

"balance sheet" test. *See In re Tabala*, 11 B.R. at 408; *In re Russo,* 1 B.R. at 380; *see also In re Gordon Car and Truck Rental, Inc.*, 59 B.R. 956, 961 (Bankr. N.D.N.Y. 1985).

It is Mr. Gessler's undisputed testimony that the Debtors received no consideration for the transfer of property to the Limited Partnership. In order for the presumption of insolvency to apply in this case then, the Debtors must have had outstanding debts at the time of the transfer. *See, e.g., In re Stephen Douglas*, 174 B.R. at 21. Based upon the testimony elicited at trial, at the time of the transfer the Debtors had outstanding and past due obligations with Schoff, and in addition were personally indebted on various credit card accounts and were delinquent on real property taxes. Based on these facts the Court finds that there is a presumption that the Debtors were insolvent or made insolvent at the time of the transfer to the Limited Partnership. Therefore, the Debtors must shoulder the burden of coming forward with proof sufficient to rebut this presumption. Based on the evidence presented, the Court shall ascertain the liabilities and assets of the Debtors in order to determine the status of the Debtors' "balance sheet" at the time of the transfer.

A. Liabilities

1. Credit Card Accounts

At the time of the transfer of the Debtors' real property in August 1994, they were indebted on various credit card accounts. In an effort to identify these debts at trial, the Plaintiff referred Mr. Gessler to Schedule F of the Debtors' voluntary chapter 7 petition filed on January 17, 1996. *See* Plaintiff's exhibit 2. Mr. Gessler proceeded to identify the debts for which he and his wife were personally obligated and also identified debts for which Gessler Enterprises or Better Shade Shop is solely liable, despite the fact that these latter debts are listed on the Debtors'

personal bankruptcy petition. On cross-examination the Debtors' attorney made the observation that debts listed in the petition do not necessarily reflect the debts owed at the time of the transfer in 1994. The Plaintiff responded to this by referring to Debtors' exhibit G, which is entitled "Gessler Enterprises, Inc. (Better Shade Shop) Balance Sheet as of Sept. 6, 1994," and which contains balances for credit card debts near the time of the transfer in 1994 which Mr. Gessler identified as being personal obligations. The balances for debts identified as personal obligations include the following: Chase Visa, $4,922.77; Citibank Visa, $4,913.95; Discover, $2,463.36; First Card, $3,120.76; MBNA, $4,982.34; Marine Midland, $6,941.10.[9]

In addition to these amounts the Court also must consider other debts listed by the Debtors in their petition. Significantly, a number of these debts were incurred prior to the transfer, and there are others for which no date is provided. Unless it is clear from the petition, exhibits or testimony provided that these debts were incurred after the transfer or are debts for which the Debtors are not personally responsible, the Court shall include the obligations and amounts listed in the petition as liabilities of the Debtors at the time of the transfer. As discussed earlier, it is the Debtors' burden to show that they were not rendered insolvent by the transfer, and a failure to exclude or otherwise explain debts listed in the petition shall weigh in favor of a finding that these debts were due at the time of the transfer. Based on the foregoing, the following debts shall be included in the Court's calculations of the Debtors' liabilities as of the date of the transfer: Community General Hospital, $137.90; Costello, Cooney & Fearon,

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[9] The only other credit card debt listed in Defendants' exhibit G is a Chemical Bank obligation with an outstanding balance of $9,910.31 as of September 6, 1994. This obligation was identified by Mr. Gessler as owed solely by the Corporation, and therefore this account shall not be considered as a personal liability of the Debtors.

$3,981.15; Key Bank, $5,870.25; OnBank & Trust Co., $7,353.68; Onondaga Hill E.R. Phys., $140.00; Smith, Kline, Beacham, $336.28.[10]

Based on the above, the total of the credit card debt and other unsecured debt considered as owing at the time of the transfer is $45,163.54.

2. Taxes

The Debtors also had outstanding real property tax liabilities at the time of the transfer in the following amounts: Clay property, $1,295.30; Hastings property, $974.25; E. Taft Rd. property, $6,202.80.[11] *See* Plaintiff's ex. 1; N.Y. Real Prop. Tax Law §§ 902, 924 (McKinney 1989); *see also* Defendants' Post-trial Memorandum of Law, at 3. The total taxes due at the time of the transfer amount to $8,472.35.[12]

3. Mortgages

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[10] The Court notes that Schedule F of the Debtors' petition includes not only personal obligations but also those debts due on behalf of the Corporation and the Better Shade Shop. These latter debts were not included in the Court's calculations of additional liabilities.

[11] Counsel for the defendants stipulated to the admissibility of Plaintiff's exhibit 1 as well as to the tax amounts located therein. While the documents in Plaintiff's exhibit 1 (which were printed out on dates subsequent to August 22, 1994) do not indicate what amount of the tax liability, if any, comprises penalties for late or non-payment of taxes due, the Court shall accept the amounts as listed as due and owing at the time of the transfer since the defendants have failed to show otherwise.

[12] Although Plaintiff asserted at trial that as of January17, 1996, the Debtors were indebted for Federal Income taxes for tax year 1994, the Court shall not include this amount in its calculation of the Debtors' liabilities at the time of the transfer. *See Federal Deposit Ins. Corp. v. United States*, 654 F.Supp. 794, 806 (N.D. Ga. 1986) (stating that regardless of when federal taxes are actually assessed, "the taxes are considered due and owing, and constitute a liability as of the date the tax return for the particular period is required to be filed."); *see also In re White*, 168 B.R. 825, 831 (Bankr. D.Conn. 1994) (quoting *Federal Deposit Ins. Corp*., 654 F.2d at 806). The Court adopts the same rationale as a basis for omitting from consideration the Debtors' New York State Income tax liability for tax year 1994.

Owing at the time of the transfer was approximately $124,000 on the mortgage for the business property on E.Taft Rd. and a total of $80,000 on the first and second mortgages for the DeWitt property.[13] In addition, Mr. Gessler testified that he continued to be responsible for paying the mortgage on the Arizona property even after that property was transferred to the Limited Partnership, and therefore this mortgage in the amount of $25,000 shall be included as one of the Debtors' liabilities.[14] Thus, the total owing on mortgages at the time of the transfer was $229,000.

Based on the foregoing, the Court finds that the aggregate liabilities of the Debtors at the time of the transfer totaled $282,635.89.

B. Assets

1. Limited Partnership

At the time of the transfer in August 1994, the Debtors gave five properties to the Limited Partnership. Under the terms of the partnership agreement the Debtors retained a combined 10% interest in the assets of the Limited Partnership. At the trial, testimony was given regarding the value of that interest based upon assumed market values attributed to the individual parcels of real property. These values were determined by Mr. Gessler based on his opinion of what the market values would be, despite his admission that he has no professional training in the

[13] According to Mr. Gessler's testimony, the Debtors remained responsible for the mortgages on the DeWitt property despite the fact that it was transferred to the Limited Partnership. Therefore, these mortgages are included in the Debtors' post-transfer liabilities.

[14] The values of the DeWitt and Arizona properties have been correspondingly increased to reflect the full values of those properties. *See* section B.1., *infra*.

valuation of real property. The amounts ascribed to these properties can also be found in Plaintiff's exhibit 4, which is an affidavit signed by the Debtors in April 1996. The Court shall accept the values as listed in the aforementioned affidavit in light of a lack of evidence to the contrary or significant objection by the Plaintiff, with one exception. Mr. Gessler testified that had recently received a purchase offer from a non-relative in the amount of $39,900 for the Hastings property. Counsel for the Debtors argues that this is evidence that Mr. Gessler undervalued the property in the affidavit, since no substantial changes had been made to the property since it was initially transferred to the Limited Partnership in 1994. The Court will accept Mr. Gessler's contention that the higher value is appropriate for this property.

The Court rejects the Debtors' contention that the Arizona property should be valued at $90,000 instead of the $60,000 value ascribed to it in the affidavit. The basis for the Debtors' contention is that the property was eventually sold to their daughter for $90,000. Without a professional real estate appraisal, the Court is unwilling to accept the price paid by the Debtors' own daughter as the market value of this property.

Based on the above, the values of the real property transferred to the Limited Partnership are as follows: Hastings property, $39,900; Fleming property, $60,200; Clay property, $7,500; DeWitt property, $110,000; Arizona property, $60,000. The Debtors' 10% interest in these assets based upon the Limited Partnership agreement is valued at $27,760.

2. Gessler Enterprises / Better Shade Shop

During the trial, Mr. Gessler did not effectively distinguish between Gessler Enterprises and the Better Shade Shop, and in fact testified that Gessler Enterprises was doing business under the name Better Shade Shop. When asked what Gessler Enterprises owned in 1994, Mr. Gessler

responded that it owned the Better Shade Shop, its inventory and equipment. Mr. Gessler also testified that his wife and three daughters were the shareholders of Gessler Enterprises and that he also held a percentage of the stock prior to the transfer.[15]

The Debtors submit that the value of the common stock of Gessler Enterprises at the time of the transfer was $52,000. *See* Defendants' Post-trial Memorandum of Law, at 5, 8. Mr. Gessler testified without objection that this value was determined by his accountant. The defendants did not present any probative evidence other than the testimony of Mr. Gessler substantiating the value of the stock. Reference to the U.S. Corporation Income Tax Return for the tax year beginning 4/1/94 and ending 3/31/95 indicates the value of common stock to be $52,800. *See* Plaintiff's ex. 18.

The Court observes that the value of the common stock has not changed since 1989 according to the U.S. Corporation Income Tax Returns filed for tax years 1989 through 1994, despite the fact that gross receipts/sales and assets and liabilities varied significantly over those years. In fact, the value of the common stock does not appear to be tied to any economic indicator of how well or poorly the corporation is doing, and therefore it is unclear how the value of the common stock has been determined.[16] *See id.* at exhibits 13-18. Based on this observation,

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[15] The Court notes a discrepancy between Mr. Gessler's testimony regarding the ownership of the stock of Gessler Enterprises and the indication on the U.S. Corporation Income Tax Returns which show that Mrs. Gessler is the 100% owner of the stock. *See* Plaintiff's exhibits 14-18.

[16] Although the Debtors claim that the value of the common stock at the time of the transfer was "based on the balance sheet which was entered into evidence as Defendants Exhibit G. In addition, this was based on the sales of the Better Shade Shop in 1994 compared to the sales in 1989," *see* Defendants' Post-trial Memorandum of Law, at 5-6, the Court does not find this argument persuasive. For example, gross sales of Gessler Enterprises, Inc. (which was never sufficiently distinguished from the Better Shade Shop, as discussed above) in 1989 totaled

and the following discussion regarding the status of the Better Shade Shop at the time of the transfer, the Court cannot accept the Debtors' assertion that the value of the stock of Gessler Enterprises, Inc. was $52,000 in August 1994.

The Debtors claim that at the time of the transfer, Gessler Enterprises/Better Shade Shop owed Mr. Gessler approximately $128,000 and Mrs. Gessler $40,000 based upon loans made by them to the company. For the reasons set forth below, however, the Court does not find that the "fair salable value" of these assets at the time of the transfer was equivalent to the amount due on the loans. Since 1989, the year that Gessler Enterprises acquired the Better Shade Shop, Gessler Enterprises, consistently had a negative net income. *See id.* The Plaintiff also indicated that the total earnings of Gessler Enterprises as of September 6, 1994 showed a loss of over $300,000. Although Mr. Gessler indicated that this figure included all losses since the corporation was first incorporated in 1932, the corporate tax returns during the years that the Better Shade Shop was being operated by the Debtors demonstrate a consistent loss. Mr. Gessler also stated that from 1989 to 1994 he had not drawn a salary from the business on the advice of his accountant. When asked how he survived during these years and how the Debtors obtained the money to loan to the corporation, Mr. Gessler testified that funds came from a sale of real property, income from rental property in Syracuse, New York, a loan from Skaneateles Savings Bank, and some inheritance money.

According to the loan registers submitted by the Debtors, very little in the way of repayment occurred on either of the loans from the Debtors. *See* Debtors' exhibits D, E, F.

$264,492, and in 1994 gross sales diminished to $136,328. The stated value of the common stock was $52,800 during both of these reference points. The Court also notes that gross profit for 1989 was $81,180, while in 1994 profits were down to $34,299.

Despite this fact, Mr. Gessler testified that he believed the collectibility of the loans was excellent at the time of the transfer. Mr. Gessler stated that after 1989 sales decreased for various reasons, but that sales picked up in the Spring and Fall of 1994. Reference to the corporate tax returns covering the period from April 1, 1991 through March 31, 1995 indicate a steady decline in sales, however, and while Mr. Gessler believed sales were going to increase in the second half of 1994, he had no significant signed contracts or definite commitments for work prior to the transfer in August 1994.

Regarding the assets of the Better Shade Shop, Mr. Gessler admitted that there were few "hard" assets purchased in 1989 from Mr. Schoff, and in fact a substantial portion of the purchase price was attributable to a covenant not to compete, training to be received and goodwill. Only some limited tools and equipment, such as a shade cutter, were purchased along with the business. Furthermore, inventory was not a significant portion of the exchange since most of the supplies were special ordered. By the Fall of 1994 the Debtors were attempting to sell the business real property in order to reduce operating expenses, as "the cost of the building [was] a serious hardship." *See* Plaintiff's exhibit 12.

One of the most significant factors weighing against a finding that these loans merit a valuation at their face amounts at the time of the transfer is that just over one year later the Better Shade Shop ceased operation, and less than 18 months after the transfer, the Debtors considered these loans to be valueless to the extent that they were not even listed as assets in the Debtors' schedules. In addition, it does not appear that the Debtors listed the alleged value of the common stock of Gessler Enterprises as an asset either.

Based on the evidence presented, the Court has serious doubts that the fair salable value

of the loans or the common stock was anywhere near the values asserted by the Debtors. More than likely, the true values were only a fraction of the values on paper.

3. Other Assets

The Debtors submitted evidence of a lease that was to commence on September 1, 1994 for a period of one year at a rent of $520 per month. At the time of the transfer, this lease agreement was allegedly in existence. Therefore the Court shall consider the total payments due under the lease, $6,280, as an asset of the Debtors at that time.[17] Mr. Gessler also owned a van with an approximate value of $13,000. Furthermore, the Court shall accept the Debtors' contention that the value of the E.Taft Rd. property was $180,000, despite the fact that even after August 1994 the Debtors were unable to sell that property for less than this amount.

The Debtors also owned a 1983 Mercedes automobile and a 1977 Crestliner boat in August 1994. The automobile was purchased in 1992 for approximately $12,500, and the boat was purchased in 1991 for $8,000. According to Schedule B of their petition, as of January 1996 the Debtors valued the automobile at $8,000 and the boat at $1,500. The Debtors assert that the values of these items at the time of the transfer were $12,000 and $4,000, respectively. Based on the purchase prices of these items compared to the values attributed to them at the time of bankruptcy, the Court finds the value of the automobile to be $10,000 and the boat $3,350 at the time of the transfer.

Excluding the value, if any, of the common stock and the outstanding loans due to the Debtors, the assets of the Debtors at the time of the transfer totaled $240,390. Even if the Court

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[17] The Court notes that this lease was subsequently transferred to the Limited Partnership less than three weeks after the initial transfer of property.

were to find the fair salable value of the common stock and the loans to be $40,000, two assets which the Court has noted were considered to be valueless less than 18 months after the transfer, the Debtors would still be found to be insolvent as a result of the transfer of property to the Limited Partnership. Based upon the evidence presented to the Court, and taking into consideration the economic status and financial health of Gessler Enterprises and the Better Shade Shop, the Debtors have not rebutted the presumption that they were rendered insolvent by the transfer of property to the Limited Partnership.[18]

While the circumstances and motivation behind the transfer are less than clear, the Court does not find sufficient evidence to charge the Debtors with the actual intent to defraud their creditors. As noted earlier, such a finding is not essential to a claim of fraudulent conveyance within the meaning of NYDCL § 273. *See HBE Leasing Corp. v. Frank*, 48 F.3d 623, 633 (2d Cir. 1995); *Elgin Sweeper Co. v. Melson, Inc.*, 884 F.Supp. 641, 649 (N.D.N.Y. 1995). Since there is no finding of actual intent to defraud on the part of the Debtors, however, the Plaintiff may not recover attorney's fees. *See Orbach v. Pappa*, 482 F.Supp. at 121; *Harvard Knitwear,* 193 B.R. at 399; *Marine Midland Bank v. Murkoff*, 120 A.D.2d 122, 508 N.Y.S.2d 17 (2d Dept. 1986), *appeal dismissed*, 69 N.Y.2d 875, 514 N.Y.S.2d 1029 (1987). Regarding the Plaintiff's request for the costs of this action, reimbursement for such expenses shall be denied, as there is no basis posited by the Plaintiff for charging the Debtors with these costs. *See Harvard*

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[18] Pursuant to NYDCL § 270, assets of a debtor means property which is not exempt from liability for his debts. Exempt assets are not properly viewed as assets under the NYDCL §§ 271 and 273 insolvency test. *See In re Russo*, 1 B.R. at 380. The Court does not need to specifically address the items and amounts that are exempt, however, since the Court finds that the Debtors were insolvent at the time of the transfer regardless of any deductions from the value of assets based upon NYDCL § 270.

Knitwear, 193 B.R. at 400.

Since the Debtors have failed to present evidence sufficient to prove that they were not rendered insolvent by the transfer to the Limited Partnership for no consideration at a time when they had outstanding debts, the Plaintiff may set aside the Debtors' voluntary transfer of property as a fraudulent transfer within the meaning of NYDCL § 273. *See In re Tabala*, 11 B.R. at 409; *see also In re Russo*, 1 B.R. at 383.

Since the Court has found that the transfer is avoidable under Code § 544, the Court shall address the Plaintiff's request that the defendants be required to turn over the property transferred to the Limited Partnership. *See Brown v. Harris (In re Auxano, Inc.)*, 96 B.R. 957, 964 (Bankr. W.D.Mo. 1989) (stating that once court has found that transfer is avoidable, Code § 550 is applied to determine from whom transfer can be recovered). Code § 550(a) allows a trustee to recover a fraudulent transfer of the Debtors' property from (1) the initial transferee of the transfer or the entity for whose benefit the transfer was made, or (2) any immediate or mediate transferee of such initial transferee, after the transfer has been avoided. *See* 11 U.S.C. § 550(a); *Security First Nat'l Bank v. Brunson (In re Coutee)*, 984 F.2d 138, 140 (5th Cir. 1993); *CCEC Asset Management Corp. v. Chemical Bank (In re Consolidated Capital Equities Corp.)*, 175 B.R. 629, 635 (Bankr. N.D.Tex. 1994); *Hooker Atlanta (7) Corp. v. Hocker (In re Hooker Invs., Inc.)*, 155 B.R. 332, 337 (Bankr. S.D.N.Y. 1993).

Although the term "initial transferee" is not defined in the Bankruptcy Code, courts have applied a "dominion and control" test to ascertain whether a party is considered to be an initial transferee. *See In re Coutee*, 984 F.2d at 141; *In re Consolidated Capital Equities Corp*., 175 B.R. at 635; *In re Hooker Invs*., 155 B.R. at 338. Under this test, an initial transferee is a party

who receives a transfer from the debtor and who exercises dominion and control over the property to the extent that he is able to use it for his own purposes. *See In re Coutee*, 984 F.2d at 141; *Bonded Fin. Servs., Inc. v. European American Bank*, 838 F.2d 890, 893-95 (7th Cir. 1988); *In re Hooker Invs*., 155 B.R at 338.

Upon review of the facts and the Limited Partnership agreement, it is clear that the Limited Partnership is an "initial transferee" within the definition set forth above. The Debtors transferred the five parcels of real property directly to the Limited Partnership, and the Limited Partnership had full control over the assets transferred to it.[19] Therefore, pursuant to Code § 550(a) the Plaintiff may recover the avoided transfers of the four parcels of real property located in New York State.

The subsequent transfer of the Arizona property from the Limited Partnership to one of the Debtors' daughters requires a separate analysis. Code § 550(b) circumscribes the trustee's power to recover property transferred from an initial transferee to a subsequent immediate or mediate transferee if certain statutory conditions are met. Specifically, "[a] trustee may not recover from a § 550(a)(2) transferee that 'takes for value, including satisfaction or securing of a present or antecedent debt, in good faith, and without knowledge of the avoidability of the transfer avoided,'" *In re Consolidated Capital Equities Corp*., 175 B.R. at 637 (quoting 11 U.S.C. § 550(b)(1)), or any immediate or mediate good faith transferee of such transferee. *See* 11 U.S.C. § 550(b)(2). The immediate or mediate transferee bears the burden of proving the requirements of Code § 550(b). *See Internal Revenue Serv. v. Nordic Village, Inc. (In re Nordic*

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[19] In this case it was actually the Debtors in their capacities as the two general partners of the Limited Partnership who had full authority to "grant, assign, transfer, lease or let any of the property of the Limited Partners, whether real or personal . . . ." *See* Plaintiff's ex. 3, at 7-8.

Village, Inc.), 915 B.R. F.2d 1049, 1055 (6th Cir. 1990), *rev'd on other grounds*, 503 U.S. 30, 112 S.Ct. 1011, 117 L.Ed.2d 181 (1992); *In re Consolidated Capital Equities Corp*., 175 B.R. at 637; *In re Hooker Invs*., 175 B.R. at 337.

At this time the Court shall make no finding as to the ability of the Plaintiff to recover the Arizona property. The immediate transferee of the property, the Debtors' daughter, is not a party to this adversary proceeding in her individual capacity. Furthermore, no arguments addressing the applicability of Code § 550(b) regarding the Arizona property have been made by the parties in this case.

Based on the foregoing, its is

ORDERED that the Plaintiff is entitled to an order declaring that the Debtors' fraudulent conveyance of the five parcels of real property to the Gessler Family Limited Partnership is null and void as against the Plaintiff, and that the property transferred, with the exception of the Arizona property, may be recovered for the benefit of the Debtors' estate; and it is

ORDERED that the Debtors and the Limited Partnership shall cooperate with the Plaintiff in recovering said real property to include the execution and delivery of any and all deeds and other documentation necessary to effect transfer of title; and it is finally

ORDERED that the Plaintiff's request for the costs of this action is DENIED.

Dated at Utica, New York

this 18th day of September 1997

STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge