

I. INTRODUCTION

Presently before the Court is the Defendants' motion to dismiss certain counts of the Plaintiff's complaint pursuant to Fed. R. Bank. P. 7012 (hereafter, the "Motion"). Having now fully considered the Motion, and the Plaintiff's opposition thereto, the Court denies the Motion in its entirety for the reasons stated herein.

II. JURISDICTION

The United States District Court for the District of Connecticut has jurisdiction over the instant matter by virtue of 28 U.S.C. § 1334(b); and this Court derives its authority to hear and determine this matter on reference from the District Court pursuant to 28 U.S.C. § 157(a)(b)(1). This is a "core proceeding" pursuant to 28 U.S.C. §§ 157(b)(2)(A), (H), *inter alia*.

III. BACKGROUND

On April 22, 1998 (the "Petition Date"), the Debtors filed in this Court voluntary petitions for relief under Chapter 11 of Title 11, United States Code. On April 22, 1998, this Court entered an order approving the joint administration of the Debtors' estates. On January 19, 2000, Roberta Napolitano (heretofore and hereafter, "Plaintiff" or "Trustee") was appointed the Chapter 11 trustee of the Debtors' estates. On or about February 2, 2000, the Debtors ceased their business operations. On or about April 20, 2000, the Trustee filed the complaint herein (hereafter, the "Complaint") which commenced this adversary proceeding. The Complaint *alleges* the following facts, *inter alia*.¹

¹ Because the matter before the Court concerns a motion to dismiss, the relevant "facts" are those alleged in the Complaint. The Court's recitation of these "facts" shall in no way constitute *findings* of such "facts".

A. Organization and Operations of the Debtors.

Both of the Debtors are wholly-owned subsidiaries of the Defendant Anamet, Inc. (hereafter, "Anamet"). Until February 2, 2000, the Debtor Anamet Industrial, Inc. (hereafter, "Industrial") manufactured, *inter alia*, flexible metal hoses and vibration eliminators. The Debtor Glen Ellyn Realty, Inc. (hereafter, "Glen Ellyn") (i) owns the real estate where Industrial carried on its operations (hereafter, the "Real Estate"), and (ii) owned the machinery and equipment that Industrial used to manufacture its products (hereafter, the "Equipment"). Glen Ellyn leased the Real Estate and the Equipment to Industrial.

B. Promissory Note.

In the course of a 1993 corporate reorganization, valuable assets were transferred by Industrial and/or Glen Ellyn to Anamet, causing Anamet to make a non-interest bearing promissory note payable to Glen Ellyn (then known as Anamet Industrial, Inc.) in the amount of \$4,494,627.00, which was subsequently increased to \$4,683,111.00 (hereafter, the "Note"). On December 2, 1996, for no consideration, Glen Ellyn (still known as Anamet Industrial, Inc.) canceled the Note and returned it to Anamet (hereafter, the "Note Cancellation").

In the Complaint's first two Claims for Relief, the Trustee alleges that the Note Cancellation constituted a fraudulent conveyance under Connecticut law and the Bankruptcy Code.

C. Management Fees.

During the four years prior to the Petition Date, Industrial and/or Glen Ellyn paid

management fees to Anamet totaling \$639,578.78 (hereafter, the "Management Fees"). The Management Fees were inflated and excessive, and the services rendered were worth substantially less than the amounts paid for them.

The Complaint's third, fourth and fifth Claims for Relief allege that the Management Fees constituted fraudulent conveyances under Connecticut law and the Bankruptcy Code.

D. Unpaid Rent.

Anamet rented space from Industrial and/or Glen Ellyn from 1994 to on or about March 8, 2000, at a monthly rental of \$6,250.00. For the period January 1, 1997, through March 8, 2000, Anamet has not paid the rent due. The unpaid rent for this period totals approximately \$237,500.00 (hereafter, the "Unpaid Rent").

The sixth and seventh Claims for Relief allege breach of contract and unjust enrichment resulting from the Unpaid Rent.

E. Net Operating Losses.

Industrial and/or Glen Ellyn accrued approximately \$9,250,000.00 of net operating losses (hereafter, the "NOLs") prior to the Petition Date. A portion of the NOLs for tax years 1996, 1997, 1998 and 1999 were used by Anamet to offset its federal corporate income tax liability, resulting in a tax benefit to Anamet of approximately \$3,000,000.00 (hereafter, the "Tax Benefit").

The Complaint's eighth and ninth Claims for Relief allege that Anamet's utilization of the Tax Benefit constituted a fraudulent conveyance under Connecticut law and the Bankruptcy Code.

F. Fiduciary Duties.

Defendant Joseph M. Cvengross ("Cvengross") was the Chairman of the Boards of Directors of the Debtors, and President of Anamet. Gerald A. Scutt ("Scutt") was President of the Debtors from April 1996 through December 1996. William Cady ("Cady") was President of the Debtors from January 1997 through April 21, 1998. Cvengross, Scutt and Cady owed fiduciary duties to the Debtors, which they each breached by: (i) overseeing, ratifying and/or permitting the Note Cancellation; and/or (ii) overseeing, ratifying and/or permitting the payment of the Management Fees; and/or (iii) overseeing, ratifying and/or permitting Industrial and/or Glen Ellyn to fail to collect the Unpaid Rent; and/or (iv) overseeing, ratifying and/or permitting Anamet to utilize the NOLs without any compensation to Industrial and/or Glen Ellyn; and/or (v) taking no action to avoid and/or recover the Note Cancellation, Management Fees, Unpaid Rent, and/or the benefit of the NOLs, all of which constituted property of the Debtors' estates.

The Complaint's eleventh, twelfth and thirteenth Claims for Relief allege that in connection with the foregoing, Cvengross, Cady and Scutt breached fiduciary duties to the Debtors.

IV. DISCUSSION

On or about August 16, 2000, the Defendants moved to dismiss 10 of the 13 Claims for Relief pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure, made applicable to these proceedings by Rule 7012(b) of the Federal Rules of Bankruptcy Procedure.

A. Dismissal Standards.

A motion to dismiss is designed to test the legal sufficiency of a Complaint, not to weigh the evidence which might be presented at trial. E.g., Goldman v. Belden, 754 F.2d 1059, 1067 (2d Cir. 1985). The motion should be granted where “it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations.” Hishon v. King & Spalding, 467 U.S. 69, 73 (1984). In considering a motion to dismiss, the court must read the complaint generously, accepting as true all well-pleaded factual allegations and viewing them in the light most favorable to the plaintiff. De Jesus v. Sears, Roebuck & Co., 87 F.3d 65, 69 (2d Cir. 1996), *cert. denied*, 117 S.Ct. 509 (1996). On a motion to dismiss, the Court’s purview is limited to “the facts alleged in the pleadings, documents attached as exhibits or incorporated by reference in the pleadings and matters of which judicial notice may be taken.” Samuels v. Industrial Transport Local 504, 992 F.2d 12, 15 (2d Cir. 1993).

B. Asserted Grounds for Dismissal.

The Defendants’ Motion presents five bases for the dismissal of certain counts of the Complaint. Those bases may be summarized as follows: (i) that the Plaintiff is not entitled to a monetary recovery in connection with avoidance of the alleged fraudulent transfers; (ii) that because the Debtors’ assets were subject to a security interest, they could not be the subject of a fraudulent conveyance; (iii) that the NOLs had no utility for the Debtors, and therefore could not be the subject of a fraudulent conveyance; (iv) that the breach of fiduciary duty claims should be dismissed to the extent that such claims relate to other, underlying claims which are dismissed; and (v) that given the timing of the tenure

of Defendant Cady with the Debtors, the breach of fiduciary duty claims against him should be dismissed as concerns the Note Cancellation.

1. Monetary recovery on fraudulent conveyance claims.

The Trustee's fraudulent conveyance claims are premised on Bankruptcy Code Section 544(b), see Complaint ¶ 2, which provides, *inter alia*, that the Trustee may avoid any transfer "that is voidable under applicable law by a creditor holding an unsecured claim that is allowable" Here, the "applicable law" on which the Trustee's fraudulent conveyance claims rests is Connecticut's version of the Uniform Fraudulent Transfer Act (hereafter, "UFTA"), C.G.S. § 52-552a, *et seq.* As a result, the Defendants contend that the Trustee's remedies are limited to those allowed by § 52-552h; remedies which do not *expressly* include a monetary recovery, to wit –

In an action against a transfer . . . under sections 52-552a to 52-552l, inclusive, a creditor . . . may obtain: (1) avoidance of the transfer to the extent necessary to satisfy the creditors claim; (2) an attachment or other provisional remedy against the asset transferred or other property of the transferee . . . (3) subject to applicable principles of equity and in accordance with applicable rules of civil procedure (A) an injunction against further disposition by the debtor or a transferee, or both, of the asset transferred or of other property, (B) appointment of a receiver to take charge of the asset transferred or of other property of the transferee, or (C) any other relief the circumstances may require.

C.G.S. § 52-552h(a) (1998).

The Defendants' argument fails for at least three reasons. First, as observed by the Trustee, the language of § 52-552h(a)(3)(C) - "any other relief the circumstances may require" - is itself broad enough to encompass a monetary judgment. Second, courts of local jurisdiction have construed the Connecticut fraudulent conveyance law to permit a

monetary recovery. Cf., e.g., Crepeau v. Gronanger, 41 Conn. App. 302, 316-17, 675 A.2d 1361,1368 (Conn. App. 1996) (expounding pre-UFTA law). Finally, and most fundamentally, the nature of the avoidance recovery available in this proceeding is governed by Bankruptcy Code Section 550, not C.G.S. § 52-552h(a). Section 550 provides that "to the extent . . . a transfer is avoided *under section 544* . . . , the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, *the value of such property* from [a] . . . transferee" (emphasis supplied). For claims premised on Code Section 544 (incorporating C.G.S. § 52-552a, *et seq.*), Bankruptcy Code Section 550(a) effectively preempts C.G.S. § 52-552h, and provides an explicit monetary recovery remedy measured by the value of the transferred property.

With specific reference to the Note Cancellation, the Trustee has prayed for a monetary judgment in the face amount of the Note - \$4,683,111.00 (hereafter, the "Face Amount"). While the Defendants claim that the Note is worth less than its Face Amount because it is non-interest bearing, and not due until 2004, those alleged facts (hereafter, the "Alleged Facts") are not pled in the Complaint and thus do not form a proper basis for dismissal. Yet even if the Alleged Facts were pled in the Complaint, this Court would not dismiss based thereon. Rather, the Court would simply discount the Note to arrive at a fair valuation for purposes of judgment. A plaintiff does not fail to state a claim upon which relief can be granted merely because the *extent* of the monetary relief requested is inappropriate.

2. Impact of security interest on fraudulent conveyance.

Next, the Defendants argue that the Trustee's fraudulent conveyance claims fail to state a valid claim for relief because "it is undisputed that all of the Debtor's [sic] assets at the time . . . were encumbered by the lien of the Bank of America." This contention is dependent upon the legal conclusion that property fully encumbered at the time of transfer is not an "asset" whose transfer is subject to avoidance under the UFTA. Even if that legal contention is correct - as it appears, see C.G.S. § 52-552b(2) - there are no grounds for dismissal here.

To determine that the subject property interests were fully encumbered at the time of transfer, this Court would need to find, at a minimum: (i) the existence of a debt owed by the relevant Debtor to a creditor, (ii) a valid security agreement in favor of that creditor; (iii) attachment of the resulting security interest to the subject property; (iv) due perfection of such a security interest; and (v) a debt chargeable² to such property in excess of the value of such property. Since these necessary findings are not pled or referenced in the Complaint, and are not fully susceptible of judicial notice, they cannot form a proper basis for a motion to dismiss.

3. Valuation of net operating losses.

As to the Claims for Relief relating to the transfer of the NOLs, the Defendants argue that the NOLs had no value because the Debtors could not use them. Ignoring for the moment that this assertion posits facts not pled in the Complaint, the argument proceeds

² This element may implicate marshaling and any other doctrine applicable to an analysis of the appropriate scope of a "blanket" lien.

on the faulty premise that an asset's lack of utility to one party - the owner - renders it valueless. Value is determined in a marketplace, even a very small one. If A has property he deems of no use, yet that property has utility for B, the property indeed has *value* to A since he can negotiate a sale to B at a price which approaches the value of the utility it provides to B. Accordingly, since the Trustee has alleged that the NOLs had utility for Anamet, there is no basis to dismiss based on lack of utility to the Debtors.

4. Fiduciary duty claims.

The Complaint's breach of fiduciary duty claims against the individual Defendants (hereafter, the "Fiduciary Claims") proceed on the factual predicate of its fraudulent transfer and other claims against the Defendant Anamet (hereafter, the "Direct Claims"), *i.e.* that the individuals breached a duty to prevent or rectify transfers and other benefits furnished by the Debtor(s) to Anamet. Conversely, the Defendants' argument for the dismissal of the Fiduciary Claims is based upon a presumption that the Direct Claims fail to state valid causes of action. Since this Court has determined not to dismiss the Direct Claims, the Fiduciary Claims must consequently stand.³

5. Defendant Cady.

In seeking to dismiss the claim against him for breach of fiduciary duty in connection with the Note Cancellation, Defendant Cady argues that the Note Cancellation occurred at a time that he was not in a position of fiduciary duty. Defendant Cady may well be correct in this respect, but it is unnecessary for this Court to dismiss any claim for relief

³ For this reason the Court need not reach the more interesting question of whether the Fiduciary Claims could stand despite the dismissal of the Direct Claims.

against him because the Complaint - generously read - does not attempt to plead a cause of action against Cady in connection with the Note Cancellation.⁴

V. CONCLUSION

For the foregoing reasons, the Motion shall be **DENIED** by separate order.

BY THE COURT

DATED: January 9, 2003


Hon. Albert S. Dabrowski 1/9/03
United States Bankruptcy Judge

⁴ The Trustee's opposition to the Motion takes a position consistent with the Court's reading of the Complaint, *i.e.* the Trustee does not seek relief from Cady in connection with the Note Cancellation.

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF CONNECTICUT**

In Re: Roberta Napolitano v. Anamet, Inc. et al.

Case No: 98 - 31608
Adversary No: 00 - 03069

CERTIFICATE OF MAILING

The undersigned Clerk in the Office of the United States Bankruptcy Court hereby certifies that a copy of the document attached hereto was mailed this date to:

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Office of the United States Trustee
Copy of Order placed in court mailbox

Dated: 01/14/03

By: pe