UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF NEW YORK

BOOTH OIL SITE ADMINISTRATIVE GROUP,

Case No. 98-CV-0696A(Sr)

Plaintiff,

-vs-

GEORGE T. BOOTH, JR.
GEORGE T. BOOTH III
LONSDALE SLATER SCHOFIELD
JOSEPH CHALHOUB
AHSEN YELKIN
BOOTH OIL COMPANY, INC.
SCHOFIELD OIL LIMITED
118958 CANADA LIMITED
SPEEDY OIL SERVICES, INC.
BRESLUBE INDUSTRIES LIMITED
EC HOLDINGS CORP.
KATHERINE STREET PROPERTIES, INC. now known as Eventures Ltd.
SAFETY-KLEEN CORP.

Defendants.

REPLY MEMORANDUM OF LAW IN FURTHER SUPPORT OF PLAINTIFF'S MOTION FOR SUMMARY JUDGMENT AGAINST JOSEPH CHALHOUB

I. The Clear Terms of the Liquidating Plan Require Booth Oil Surplus to be Placed in a Contingency Fund for, Among Others, the Members of Plaintiff Who Are the PRPs Who Have Incurred Costs Cleaning Up the Site of Booth Oil's Production Facility in Tonawanda, New York

The Chalhoub defendants' position relative to the proper beneficiaries of the Contingency Fund appears at page 6 of their Reply Memo dated November 19, 2004 and refers to page 16 of their Reply Memo dated October 29, 2004:

> Chalhoub has previously identified (in his Reply Memorandum) parties which were contemplated by the Liquidating Plan of Reorganization as members of this Class (e.g., those parties to whom Booth Oil could become liable with regard to three other hazardous waste sites, as well as other liabilities that were then in dispute, all of which were identified in the class description.

Chalhoub Defendants' Memorandum dated November 19, 2004 (hereinafter 11/19/04 Chalhoub Memo) at 6 (emphasis added). The referenced October 29, 2004 Reply Memorandum states:

> To even suggest that Booth Oil created an express trust and designated these same PRPs as its beneficiaries is an extreme stretch of one's imagination since no one even thought anyone would incur any liability related to the Robinson Street Site. (It is more logical to conclude that the so-called "environmental creditor" beneficiaries would be those parties to whom Booth Oil could become liable with regard to the three other hazardous waste sites, as well as other liabilities that were then in dispute, all of which were identified in the class description.) Moreover, the "contingency fund" was not described as being established for "environmental creditors." The plan of reorganization clearly said that class 3 "shall consist of all environmental-related claims." This is a far broader scope of possible claimants than what Plaintiff wishes this Court to believe.

Chalhoub Defendants' Memorandum dated October 29, 2004 (hereinafter 10/29/04 Chalhoub Memo) at 16 - 17 (emphasis added). The 11/19/04 Chalhoub Memo continues:

> Regardless, Booth Oil's Liquidating Plan did not state that the fund would be created to pay environmental creditors, but stated only that, with respect to "environmental-related claims,"
>
> > [A] reserve must be established for expenses to be incurred by Booth [Oil] during the consummation of the Plan and the final dissolution of the Company. Expenditures will be required for an orderly transfer of the Company's business and operating assets to Speedy and dissolution of the Company. There are other matters such as proceedings under the federal "Superfund" law and other environmental issues, disputes over fees, property taxes, and questions related to pension plan contributions. These will require that a contingency be set up in an amount to allow for settlement of these matters and legal representation, if necessary. [Plan at 28-29.]
>
> Since neither Plaintiff nor any of its constituent members had an "environmental-related claim" in Booth Oil's bankruptcy, they were not members of this class. The contingency fund was to be set up to pay for costs related to claims by members of this class - - not Plaintiff. . . . . The language of the Liquidating Plan should not be construed to extend any rights to any environmental creditor of Booth Oil that may exist in the future, but only to those claimants who were recognized by the Plan.

11/19/04 Chalhoub Memo at 6-7 (emphasis added).

The Chalhoub defendants attempt to distinguish between claimants recognized in the

Plan and future environmental creditors. In support of this attempt, the Chalhoub defendants have cited the language of the Plan describing class 3 claims. The only sentence which they do not quote is the last sentence which states: "These matters are discussed in the Disclosure Statement." Liquidating Plan at 29 (attached as exhibit 4 to the July 30, 2004 Affirmation of R. William Stephens). The Disclosure Statement contains two and a half pages specifically describing class 3 claims. The claims of PRPs at the Booth Oil plant are specifically identified as well as a "potential State Superfund claim regarding the [Robinson Street North Tonawanda] Site:

> There are other matters such as proceedings under the federal "Superfund" law and other environmental issues . . . . These will require that a contingency be set up in an amount to allow for settlement of these matters and legal representation, if necessary. Booth has been . . . . cited as a PRP in two potential New York State Superfund sites . . . and the Booth Oil plant, also North Tonawanda, New York. All of these proceedings except, Wide Beach are in the initial stages of Remedial Investigation and Feasibility Study ("RI/FS"). PRPs which do not contribute to the costs of RI/FS preparation can be sued by either the government or participating PRPs for contribution and punitive damages . . . . Finally, the DEC requested Booth and other PRPs to perform an RI/FS with respect to the former production facility at North Tonawanda, New York. Various PRPs and Booth met with DEC in early 1988 but no additional action has been taken by the State. At the time of the meeting and during conferences thereafter none of the PRPs believed there was a strong basis for DEC's demanding an RI/FS of the Site.
>
> Recently the New York State Department of Law has demanded approximately $5,000 for clean-up costs associated with an oil spill in 1987 into the Little River, a tributary of the Niagara River. The spill occurred at a storm water outfall about (100) yards from the former Booth production facility. Booth cooperated with the DEC in the investigation of this incident but has consistently maintained that there is no basis for its liability because the oil found at the outfall cannot be traced to Booth. On June 30, 1989 the Department of Law advised that responsibility for collection was being transferred from its oil spill group to the solid waste group to be handled in conjunction with the potential State Superfund claim regarding the Site.
>
> . . .
>
> Another expense anticipated by Booth is related to storage expenses for corporate records after its dissolution. Booth estimates the expenses for such storage

to be $500 per year.

Estimates of these prospective expense amounts are set forth in exhibit 4. Amended Disclosure Statement at 14-16 (attached as exhibit 4 to the July 30, 2004 Affirmation of R. William Stephens) (emphasis added).

Exhibit 4 to the Amended Disclosure Statement details Administrative Expenses. Exhibit 7 to the Amended Disclosure Statement details Disputes and Contingencies. The amount for "Environmental Cleanup" is "unknown". See Amended Disclosure Statement and Liquidating Plan at exhibit 7 (exhibit 4 to the July 30, 2004 Affirmation of R. William Stephens).

Booth Oil intended through its Liquidating Plan to provide for "anticipated" and "prospective" expenses, including its liability associated with "its former production facility" to "participating PRPs for contribution." ADS at 14-16 (attached as exhibit 4 to the July 30, 2004 Affirmation of R. William Stephens).

On December 18, 1992 the shareholders of Booth Oil "agreed in principle that a special fund be set up in the amount of five hundred thousand U.S. dollars ($500,000) for the purpose of payment of any future claims or potential liabilities against Booth, and the associated legal fees that may result from the aforementioned." See Agreement (attached as exhibit 33 to the July 30, 2004 Affirmation of R. William Stephens) (emphasis added).

Booth Oil made a commitment to carry out the terms of the Liquidating Plan in exchange for protection from its creditors, including the members of Plaintiff. The Contingency Fund beneficiaries are owed a fiduciary duty whether or not they have established their right to the amounts in the Contingency Fund. That duty was established when the Plan was confirmed.

In the Consolidated Pioneer case, the appellate panel for bankruptcy appeals in the Ninth

Circuit explained:

> The bankruptcy Court determined that PLC was acting in a capacity akin to a liquidating trust, and, therefore, it had a fiduciary duty to the investors. . . . In a typical reorganization, once a plan is confirmed, a reorganized debtor no longer owes a fiduciary duty to the estate because the estate ceases to exist. If, on the other hand, the plan creates a trust or a vehicle for the exclusive benefit of the creditors, then the trust has a fiduciary duty to those for whose benefit it was created.

In re Consol. Pioneer Mortgage Entities, 248 B.R. 368, 375-76 (Bankr. App. Panel 9th Cir. 2000).

The fact that the liabilities were future liabilities does not preclude the existence of a fiduciary duty to the Contingency Fund beneficiaries. In re Kensington Int'l Ltd., 368 F.3d 289, 321 (3d Cir. 2004) (stating in a dissenting opinion that a futures representative in an asbestos bankruptcy litigation has a duty "to promote the collective interest of those parties that will have future claims against the . . . post-confirmation trust"). If Booth Oil had no surplus, it would not be required to make any payment based on the terms of the Liquidating Plan. If events had transpired as Defendants had expected they would when the Plan was proposed, the Plan would provide protection from environmental creditors such as the members of Plaintiff.

Now that events have caused the Liquidating Plan to work in favor of environmental creditors, Defendants seek to avoid the burdens created by its clear terms.

II. THE TRANSACTIONS AT ISSUE VIOLATED THE LIQUIDATING PLAN AS A MATTER OF LAW

Defendant Chalhoub acknowledges that Booth Oil was required "to establish a contingency fund and to refrain from making any distribution of assets to its shareholders." 11/19/04 Chalhoub Memo at 7. Chalhoub contends that "Plaintiff does not dispute that Booth Oil fulfilled its first obligation, but only states that it distributed assets to equity holders in violation of the Plan." 11/19/04 Chalhoub Memo at 7. Plaintiff, however, does dispute that

Booth Oil fulfilled its obligation to establish a Contingency Fund and to place surplus, if any, in that fund. On December 18, 1992 the shareholders of Booth Oil agreed in principle that a "special fund" for future liabilities and potential claims should be established. See Agreement (attached as exhibit 33 to the July 30, 2004 Affirmation of R. William Stephens). While the shareholders acknowledged their responsibility in this regard, it is not at all clear that the fund was in fact established. A review of the Booth Oil tax returns reveals that $606,677 was placed in a Merrill Lynch account and $300,000 was loaned to EC Holdings in 1992. It is not clear that any of these funds were earmarked for the purpose of establishing the contingency or "special fund". These amounts do not account for the $2.8 million in profits Booth Oil realized between 1990 and 1992.

It is not correct to say that Plaintiff only alleges distributions to equity security holders in violation of the Liquidating Plan. Under the circumstances of this case, profits are surplus. Any transfer of surplus must be only to a Contingency Fund beneficiary; therefore, if a transfer is of surplus, and by that transfer the surplus is distributed to an entity that is not a Contingency Fund beneficiary, that transfer violates the Plan. If that transfer goes to an equity security holder, that constitutes a separate additional violation of the Plan. So Plaintiff alleges that at least $2.8 million (i.e., profits between 1990 and 1992) should have been placed in the Contingency Fund.

It is true that the Liquidating Plan does not bar every payment to an equity holder for any reason. George T. Booth III was entitled to draw a reasonable salary as an employee. It is hard to imagine any other payment to an equity security holder, whether it be surplus (i.e., profit) or even a return of capital (a payment that is not taken from profits but from operating capital), that would not violate the Liquidating Plan.

The payment to George T. Booth III of $275,000 violated the Liquidating Plan both because it was surplus, based on the $2.8 million in profits between 1990 and 1992, and because it represented a transfer to an equity security holder, based on George T. Booth III's status as an equity security holder and the fact that George T. Booth III would not have had a cause of action to challenge the actions of Booth Oil's directors and officers except as a shareholder.

George T. Booth III and G&H Oil Company would not have had standing to sue "[i]ndividually and as shareholders suing on behalf of Booth Oil Co., Inc. and on behalf of all other shareholders similarly situated." See Caption to Order to Show Cause in Booth III et al. v. Chalhoub et al., Index No. I994-9438 (attached as exhibit 10 to the Affirmation of R. Hugh Stephens filed herewith). That lawsuit was a shareholders' suit against Joseph Chalhoub and Lonsdale Schofield for committing what Booth III describes as "corporate suicide" by causing Booth Oil to plea to a felony, where that plea would cause Booth Oil to sacrifice (a corporation convicted of a felony cannot hold a permit under New York law) its valuable permit to operate its Katherine Street facility for the benefit of Safety-Kleen Oil Services, a corporation for whom both Mr. Chalhoub and Mr. Schofield worked and in whose shares Mr. Chalhoub and Mr. Schofield each had interests worth many millions of dollars.

The lawsuit was not merely "brought against Booth Oil" as Defendants claim, but rather against Joseph Chalhoub and Lonsdale Schofield individually, among others. George T. Booth III was suing not because of something Booth Oil did, but because of what Joseph Chalhoub and Lonsdale Schofield were doing as directors and officers of Booth Oil, to the detriment of Booth Oil and for the benefit of Safety-Kleen. Under the circumstances, it is not reasonable to describe the payment to George T. Booth III in exchange for his shares of stock and in order to settle the

litigation as a payment to him unrelated to his status as a shareholder. If he did not hold shares, he would not have had a cause of action.

The Chalhoub defendants explain:

> If an unrelated party brought a lawsuit against Booth Oil and Booth Oil paid $275,000 to settle the suit, Plaintiff could not say that such a payment was in violation of the Plan. Plaintiff cannot claim that as a matter of law and undisputed fact, the payment to George T. Booth [III] violated the Plan since it clearly was a necessary and reasonable payment.

Plaintiff could indeed say that a payment of $275,000 to an unrelated party was in violation of the Plan. If the $275,000 was surplus, it was not Booth Oil's to spend on anything, no matter how "necessary and reasonable". If the payment was from surplus, the only unrelated party competent to receive such a payment would be a Contingency Fund beneficiary.

Neither was the payment at issue "necessary and reasonable". Booth Oil's proper response to a lawsuit by anyone other than a Contingency Fund beneficiary is: Booth is a bankrupt Corporation in liquidation pursuant to a Liquidating Plan of Reorganization and does not have assets to satisfy a judgment. All assets of Booth Oil are being liquidated and the terms of the Liquidation Plan require that the proceeds of the liquidation be used in accordance with the Liquidating Plan and any surplus be maintained in a contingency fund for certain creditors.

The $275,000 was not Booth Oil's to spend. It certainly was not Booth Oil's to use for the purpose of settling litigation, the target of which was not Booth Oil but its offending directors and officers, Joseph Chalhoub and Lonsdale Schofield.

III. CHALHOUB IS LIABLE FOR TRANSFERS OF $450,000 TO EC HOLDINGS AND $300,000 TO KATHERINE STREET PROPERTIES

While Chalhoub alleges he did not approve of the payments of $450,000 to EC Holdings in 1992 and 1993 and the payment of $300,000 to Katherine Street Properties in 1994, and

Plaintiff accepts that as a fact for the purposes of this motion, Chalhoub did agree to forgive George T. Booth III his liability for these transfers by voting "to authorize Booth Oil to enter into the Settlement Agreement with George T. Booth III" which involved Booth Oil releasing George T. Booth III from any liability to Booth Oil. See General Release (attached as exhibit 5 to the July 30, 2004 Affirmation of R. William Stephens).

Joseph Chalhoub and Lonsdale Schofield learned of the improper transfers and George T. Booth III's role in those transfers and, instead of attempting to retrieve the improperly diverted funds from the entities to which it was transferred, they decided to pay George T. Booth III $275,000 and forgive any liability he and Katherine Street Properties had to Booth Oil.

Mr. Chalhoub testified:

> Q. . . . at approximately this time, approximately August of 1994, did there come a time when you changed the banking resolutions of Booth Oil Company, Inc.?
> A. Yeah, I remember at that time the banking resolution was changed.
> Q. And did the change prevent George Booth [III] from writing checks against the Booth Oil Company, Inc. account without certain approval procedures.
> A. Yes
> . . .
> Q. And can you explain what occurred?
> A. At that time, we learned that significant funds were - - of Booth Oil were distributed, checks were written to the benefit of George Booth and Ahsen Yelkin, significant enough that it would have required discussions with the other shareholders of Booth Oil.
> Q. And who were the other shareholders of Booth Oil?
> A. The 118958 and Schofield Oil.
> Q. And what were the - - when you say significant funds, what - - do you remember what the checks were?
> A. Hundreds of thousands.
> Q. Okay. And how did you learn about these checks?
> A. It's a bit vague, but I do remember we learned about these - - this situation, the checks, while we were - - when we, this is Dale Schofield and I, were here during that period of time to execute documents relating to this 1994 incident.
>
> And exactly how it got to the surface I'm not clear, but it could have been a call that Mary, who is the office manager, initiated.
>
> And I was actually driving in the car with Dale Schofield when this

> conversation went on relating to these approvals or the issuing of these checks.
> Q. And do you remember who the checks were issued to?
> A. I'm not sure. My understanding is these funds were issued to the benefit of George Booth III, Ahsen Yelkin, or to a corporation that they had put together. I remember vaguely that they were looking at going into partnership.
> Q. And how was this situation resolved?
> A. It really didn't get - - it really didn't get resolved. We clearly decided at the time that with everything that was happening, including - - including this investigation that went on and the government requesting in order to resolve the issue that there were going to be management changes and checks were issued out to significant amounts of money without other shareholders approval, we, Schofield and I, thought that 118958 and Schofield Oil should find a solution to the Structure of Booth Oil and the ownership in it.
>
> And at the end of this and after the transaction went on with the government authorities, George Booth III resigned and the shares in Booth Oil were either redeemed or - - I can't recall the exact transaction and it was really essentially the end of his ownership in Booth Oil.
> Q. All right. And were - - did Ahsen Yelkin or George Booth III ever repay any of these amounts?
> A. No, absolutely not.
> Q. And did you or Lonsdale Schofield take any action to attempt to collect any of these amounts?
> A. No.

Chalhoub Deposition at 132-35 (attached as exhibit 31 to the July 30, 2004 Affirmation of R. William Stephens).

The payment to George T. Booth III was not simply the $275,000, but the release associated with the $750,000, as well as the $80,000 paid to Ahsen Yelkin. Whether Schofield and Chalhoub were aware that they were breaching their fiduciary duty in connection with this payment to George T. Booth III and the release associated with all additional amounts improperly transferred by Booth III is not determinative of their liability. Even a negligent breach of fiduciary duty gives rise to individual liability. Further, it appears that there was some awareness of the implications associated with the transfers. The Settlement Agreement states:

> 1. Yelkin Note Booth Oil hereby releases GTB [George T. Booth III] from any obligation associated with the $80,000 advance made by Booth Oil in December,

> 1991 to Ahsen Yelkin ("Yelkin") evidenced by a promissory note dated December 20, 1991 ("Yelkin Note") and hereby assigns the Yelkin Note to GTB without representation or recourse.

Settlement Agreement at 2. It appears that the parties to the Settlement Agreement understood that liability associated with the $80,000 "advance" was of a character that required a release. We recently learned that this amount was used by Ahsen Yelkin to secure the assignment of the mortgage on George T. Booth III's residence. That mortgage was discharged by Ahsen Yelkin on or about September 30, 1998 in a transaction that involved the mutual exchange of general releases by George T. Booth III and Ahsen Yelkin.

It appears that Joseph Chalhoub and Lonsdale Schofield were more concerned with their duty of disclosure to shareholders than they were with their duty to creditors. If they were ignorant of their duties and the requirement that they act not simply in their own best interest but in the interest of the Contingency Fund beneficiaries, that ignorance is no defense to their individual liability.

While the Chalhoub defendants claim that "Booth Oil (and its officers, directors and shareholders) had no duty to the universe of parties that could someday, potentially become a creditor" (11/19/04 Chalhoub Memo at 12), the Booth Oil shareholders, when they agreed in principle to set up a "special fund . . . for the purpose of payment of any future claims or potential liabilities" (see Agreement (attached as exhibit 33 to the July 30, 2004 Affirmation of R. William Stephens)), acknowledged as much. Now that it appears that Booth Oil and its officers and directors may be required to fulfill the obligations under the Liquidating Plan, Defendants are searching for an interpretation of the Plan (1) that departs from the clear terms of the Plan and (2) under which they are free to simply keep the $2.8 million in Booth Oil profits

which Booth Oil earned subsequent to confirmation of the Plan. The terms of the Plan are clear and require Booth Oil to maintain surplus (i.e., profit) in a contingency fund for environmental creditors, including the members of BOSAG.

Conclusion

For the reasons set forth above and in Plaintiff's affirmations and memoranda served herewith, on September 30, 2004, and on July 30, 2004, as well as the statements of facts filed in connection with this motion, this Court should grant summary judgment against Joseph Chalhoub for breach of fiduciary duty and violation of the Liquidating Plan in connection with the three transfers of $450,000, $300,000, and $275,000 from Booth Oil.

Dated: December 3, 2004
Buffalo, New York

s/ R. William Stephens
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