

**UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF NEW YORK**

BOOTH OIL SITE ADMINISTRATIVE GROUP,

Plaintiff,

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

-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.**

**REPLY MEMORANDUM
OF LAW IN FURTHER
SUPPORT OF PLAINTIFF'S
MOTION FOR SUMMARY
JUDGMENT AGAINST
LONSDALE SCHOFIELD**

Defendants.

Preliminary Statement

The New York State Court of Appeals, in an action against certain directors and officers of a corporation for waste, found in favor of the defendants upon a finding that

the defendant directors of the corporate defendant had acted for [the corporation's] best interest . . . and . . . that none of the assets of the defendant corporation had been lost or wasted, and that none of the defendants had been guilty of such alleged waste.

Lonas v. Layman Pressed Rod Co., 269 N.Y. 529, 530, 199 N.E. 520, 521 (1935), aff'g Lonas v.

Layman Pressed Rod Co., 242 A.D. 444, 275 N.Y.S. 27 (1934))). The most obvious defense to

an allegation of misconduct by an officer or director of a corporation is that the officer or

director committed no misconduct.

Defendant Lonsdale Schofield, as well as Joseph Chalhoub, George T. Booth III, and Ahsen Yelkin, have adopted a different strategy. No defendant disputes that \$450,000 was transferred to EC Holdings Corp. between 1992 and 1993, that \$300,000 was transferred to Katherine Street Properties, Inc. in 1994, or that \$275,000 together with a general release was transferred to George T. Booth III on October 7, 1994. Defendants neither admit nor deny that Booth Oil had profits of approximately \$2.8 million between 1990 and 1992, as disclosed in tax returns produced by Booth Oil as a result of an Order of this Court. Defendants take the position that this fact is immaterial to this motion. Neither do Defendants dispute that the shareholders of Booth Oil, represented by George T. Booth III (who owned his shares individually), Joseph Chalhoub (who has had an indirect interest in Booth Oil through 118958 Canada Limited), and Lonsdale Schofield (who has had an indirect interest in Booth Oil through Schofield Oil Limited), made an agreement in principle on December 18, 1992 that \$500,000 would be placed in a "special fund" for "future claims and potential liabilities." Finally, Defendants do not dispute that a Disclosure Statement and Liquidating Plan were confirmed in this action, or that the interpretation of the provisions of that Plan affect the resolution of the issues in this action.

Instead of describing how they fulfilled their duties as directors and officers, Defendants complain that Plaintiff has not provided proper legal authority to support its claims. Defendants do not even seriously argue that such authority does not exist, but only that Plaintiff has failed to place it before the Court. Similarly, the Defendants complain not that the evidence is not compelling or suffers from some substantive defect that makes it misleading, but that it has not been properly placed before the Court.

While Plaintiff does not take these arguments lightly and has taken steps to address these

technical arguments, the result that Defendants urge this Court to compel is one that involves permitting Booth Oil to avoid approximately \$3.5 million out of \$4.5 million in secured debts and \$1.5 million in pre-petition unsecured debts through the operation of the Bankruptcy Code under the Liquidating Plan. At the same time, Defendants would have this Court allow them to walk off with at least \$2.8 million in post-confirmation profits, even in the face of additional liability of somewhere between \$4 and \$5 million associated with the Booth Oil production facility.

Plaintiff has moved for summary judgment against Lonsdale Schofield for breach of fiduciary duty and for violation of the Liquidating Plan. Based on the undisputed evidence, Lonsdale Schofield learned in the second half of 1994 that George T. Booth III and Ahsen Yelkin had removed at least \$750,000 of Booth Oil surplus and paid it over to corporations controlled by Ahsen Yelkin and George T. Booth III. Instead of making an effort to recover that surplus for the Contingency Fund beneficiaries, he took action with the approval of Joseph Chalhoub to prevent Booth Oil from recovering those amounts, by causing Booth Oil to execute a general release to George T. Booth III and Katherine Street Properties, Inc., and then paying an additional \$275,000 in Booth Oil surplus to George T. Booth III. This conduct constitutes a breach of Lonsdale Schofield's fiduciary duty to Booth Oil and the Contingency Fund beneficiaries, as well as a violation of the clear terms of the Liquidating Plan. Lonsdale Schofield has not raised a question of fact on any of the issues that form the foundation of this motion for summary judgment or the law that governs these issues. Plaintiff incorporates by reference the evidence and authority cited in Plaintiff's Reply Memoranda in Further Support of Summary Judgment Against Defendants Joseph Chalhoub, Ahsen Yelkin, and George T. Booth

III (filed herewith), as well as the Affirmation of R. Hugh Stephens (filed herewith), and Plaintiff's Reply Statement of Undisputed Facts Pursuant to Local Rule 56.1 (filed herewith).

I. INDIVIDUAL LIABILITY OF LONSDALE SCHOFIELD

A. Breach of Fiduciary Duty

There are legal grounds which form a basis for the personal individual liability of Lonsdale Schofield. The first is the trust created by the Liquidating Plan. As an officer and director of Booth Oil, Lonsdale Schofield was a trustee of the Contingency Fund with a fiduciary duty running to the Contingency Fund beneficiaries.

Booth Oil and its officers and directors are the trustees, Booth Oil surplus or surplus accounts receivable is the trust res, and the Contingency Fund beneficiaries are the trust beneficiaries. See Coleman v. Golkin, Bomback & Co., 562 F.2d 166 (2d Cir. 1977); Restatement (Second) of Trusts § 2 ("A trust . . . is a fiduciary relationship with respect to property, subjecting the person by whom the title to property is held to equitable duties to deal with the property for the benefit of another person, which arises as a result of a manifestation of an intention to create it"); Scott on Trusts, Vol. I, § 2.3 ("The notion of trust as has been developed in the Anglo-American law includes the following characteristics: (1) a trust is a relationship; (2) it is a relationship of a fiduciary character; (3) it is a relationship with respect to property; (3) it involves the existence of equitable duties imposed upon the holder of the title to the property to deal with it for the benefit of another; and (5) it arises as a result of a manifestation of an intention to create the relationship").

By using Booth Oil surplus to settle litigation in which he was named personally and to redeem the stock of George T. Booth III, in violation of the terms of the confirmed Liquidating

Plan, Lonsdale Schofield violated his fiduciary duty to the Contingency Fund beneficiaries and violated the terms of the confirmed Liquidating Plan. Both violations give rise to personal individual liability. An individual is not protected by the corporate veil from liability for breach of fiduciary duty or violation of a Liquidating Plan. See In re Krypton Broad., 181 B.R. 657 (Bankr. S.D. Fla. 1995).

Defendants raise no genuine issue of fact relative to the impropriety of the \$450,000 loan to EC Holdings or the \$300,000 payment to Katherine Street Properties. The suggestion that the loans to EC Holdings Corp. were “in the nature of a severance payment” or compensation for services does not make those payments proper. A liquidating corporation cannot simply loan \$450,000 to a corporation set up by one of its managing employees. A loan of \$450,000 on which a payment has never been made cannot be described as anything other than a transfer of surplus under the circumstances here. Defendant Schofield cannot attempt to provide a rationale for either the \$450,000 loan or the \$300,000 payment to Katherine Street Properties, Inc., except to dispute that “the referenced payments were necessarily improper.” Schofield Statement of Facts ¶ 8.

The \$275,000 paid to George T. Booth III can only be described as a payment of surplus. If Booth Oil could afford to pay George T. Booth III \$275,000, that amount cannot be described as anything other than surplus. Further, the payment can only be described as a payment to George T. Booth III based on his status as a shareholder, not a payment to him that was unrelated to his status as a shareholder. The question that sheds light on that issue is whether George T. Booth III could have brought the action if he had not been a shareholder. Had he not been a shareholder, George T. Booth III could simply have been voted out as a director and officer and

would not have had standing to bring his action on behalf of Booth Oil and its shareholders against Joseph Chalhoub, Lonsdale Schofield, and Booth Oil among others.

Defendants describe the need to settle the litigation as a reasonable business decision designed in part to avoid litigation costs. Affidavit of Patrick Brown dated November 19, 2004 at ¶ 21. If there was a risk of significant litigation costs, that was a risk to Joseph Chalhoub and Lonsdale Schofield individually. If Booth Oil had assets to protect, they were the assets of the Contingency Fund, in which the Liquidating Plan prohibited George T. Booth III from sharing. Defendants suggest that one of the main benefits of the settlement was that certain individuals would not be prosecuted individually. Affidavit of Patrick Brown dated November 19, 2004 at ¶ 15. That is, of course, a compelling reason to settle litigation. It is not a compelling reason to use Contingency Fund assets to finance that settlement. The Settlement Agreement was beneficial to Joseph Chalhoub, Lonsdale Schofield, and George T. Booth III. It provided no real benefit to Booth Oil. In fact, it caused Booth Oil to plead guilty to a felony which it did not commit. The cost to Booth Oil of the Agreement was \$275,000 paid to George T. Booth III, \$100,000 paid as a fine in state court, plus a general release to George T. Booth III and Katherine Street Properties worth at least \$750,000, not to mention loss of Booth Oil's ability to operate the Katherine Street facility under its NYSDEC permit. See General Release from Booth Oil to Katherine Street Properties, Inc. (attached as exhibit 12 to the Affirmation of R. Hugh Stephens filed herewith).

Neither was George T. Booth III alleging that Booth Oil itself was liable for some damage but that Joseph Chalhoub and Lonsdale Schofield were acting for themselves and not for Booth Oil. That fact cannot be disputed, and yet Joseph Chalhoub and Lonsdale Schofield did

not participate in the cost of the settlement.

An order would lack proper force if a director or officer of a corporation could perform an act in violation of the order on behalf of the corporation with knowledge of the order and be spared from the enforcement of that order. The issue is not a technical or procedural one (i.e., whether the defendant can be held individually liable), but a substantive one (i.e., whether he should be).

The Schofield defendants have admitted that Booth Oil made payments totaling \$450,000 to EC Holdings Corp. and that a payment of \$300,000 was made to Katherine Street Properties, Inc. See Defendant Lonsdale Slater Schofield's Response to Plaintiff's Statement of Material Facts dated November 19, 2004 at ¶ 3 (admitting ¶¶ 66-75 (payments to EC Holdings Corp. totaling \$450,000 in exchange for promissory notes) and ¶ 80 (payment to Katherine Street Properties, Inc. of \$300,000)). Lonsdale Schofield also admits that he learned of certain payments by the company in October 1994 but disputes that the referenced payments were necessarily improper. See Schofield Statement of Facts at ¶ 8.

Mr. Schofield also admits that with knowledge of "certain payments by the company," Booth Oil entered into a settlement agreement with George T. Booth III which committed Booth Oil to paying George T. Booth III \$275,000 and accepting George T. Booth III's resignation as President and Director. See Schofield Statement of Facts at ¶¶ 8-9.

The questions are (1) whether the payments of \$450,000 and \$300,000 were improper payments of surplus, and (2) whether the payment to George T. booth III of \$275,000 and the forgiveness of his liability associated with the advances to Ahsen Yelkin, EC Holding Corp. and Katherine Street Properties were also payments of surplus as well as payments to an equity

security holder.

Mr. Schofield also admits that Booth Oil (1) filed for bankruptcy on June 6, 1985, (2) that its Liquidating Plan and Disclosure Statement were confirmed by the Bankruptcy Court on December 29, 1989, (3) that its equity security holders were to receive no distribution under the Plan and (4) that Booth Oil's shares were to be cancelled and the corporation was to be dissolved. Schofield Statement of Facts at ¶ 3 (admitting ¶¶ 38, 39, 42, and 43 of Plaintiff's Statement of Facts).

Mr. Schofield describes paragraphs 52-62 of Plaintiff's Statement of Facts as "not relevant to plaintiff's motion for partial summary judgment as it relates to Mr. Schofield." Schofield Statement of Facts at ¶ 1. On the contrary, these facts are relevant to Plaintiff's motion.

If the facts stated in paragraphs 52-62 are correct, and Defendants have not disputed that they are, Booth Oil had profits of more than \$500,000 in 1990, \$1.2 million in 1991, and almost \$1.1 million in 1992, for a total over the three years of more than \$2.8 million. Of that amount \$300,000 was loaned to EC Holdings Corp. and \$606,677 was placed in a Merrill Lynch investment account in 1992. See Booth Oil tax return for year 1992 (attached at tab 3 of the Tax Returns for 1990-1995, filed under seal with Plaintiff's Motion pursuant to this Court's order) at page 17, Supporting Statements, Statement 5, Form 1120, Schedule L, Other Current Assets.

In 1993, an additional \$150,000 was loaned to EC Holdings, bringing the total owed to Booth Oil by EC Holdings to \$450,000, and an additional \$17,403 was placed in the Booth Oil Merrill Lynch investment account bringing the balance of that account to \$624,090. See Booth Oil tax return for year 1993 (attached at tab 4 of the Tax Returns for 1990-1995, filed under seal

with Plaintiff's Motion pursuant to this Court's order) at page 10, Supporting Statements, Statement 5, Form 1120, Schedule L, Other Current Assets.

In 1994, the Merrill Lynch account was depleted by \$399,677. See Booth Oil tax return for year 1994 (attached at tab 5 of the Tax Returns for 1990-1995, filed under seal with Plaintiff's Motion pursuant to this Court's order) at page 11, Supporting Statements, Statement 5, Form 1120, Schedule L, Other Current Assets (Total Other Current Assets went from \$1,557,629 to \$819,868 for a total depletion of \$737,761).

In 1995, the loan to EC Holdings Corp. remained at \$450,000 and the amount in the Merrill Lynch investment account was \$241,266. See Booth Oil tax return for 1995 (attached at tab 6 of the Tax Returns for 1990-1995, filed under seal with Plaintiff's Motion pursuant to this Court's order) at page 11, Supporting Statements, Statement 6, Form 1120, Schedule L, Other Current Assets.

The payments to EC Holdings Corp. of \$450,000 and to Katherine Street Properties, Inc. of \$300,000 were payments of surplus accounts receivable. These were violations of the Liquidating Plan whether or not they were paid to or for the benefit of equity security holders. Surplus was required to be maintained for the Contingency Fund beneficiaries. Instead of maintaining surplus in the Contingency Fund or "special fund", Defendants paid EC Holdings Corp. \$450,000 and Katherine Street Properties, Inc. \$300,000.

With respect to the \$275,000 paid to George T. Booth III, the issue is not whether Booth Oil paid appropriate consideration to George T. Booth III in order to settle his lawsuit against Joseph Chalhoub, Lonsdale Schofield, Booth Oil and others, but whether the funds used to pay that settlement were the property of Booth Oil and whether those funds could be used for that

purpose under the Liquidating Plan. The inescapable conclusion is that the settlement was financed with Booth Oil profits – Booth Oil surplus – which the Liquidating Plan required be held in a Contingency Fund for the Contingency Fund beneficiaries.

On December 18, 1992, the majority shareholders of Booth Oil, George T. Booth III, 118958 Canada Limited, and Schofield Oil Limited, signed an agreement that states:

We the undersigned majority shareholders of Booth Oil Co., Inc. (hereinafter referred to as “Booth”) have agreed in principle that a special fund be set up in the amount of Five Hundred Thousand U.S. Dollars (\$500,000.00) 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).

While the majority shareholders agreed that the special fund should be set up, it is not clear whether any such fund was in fact set up. The Agreement is compelling, uncontroverted, contemporaneous evidence both that the shareholders of Booth Oil believed that they were required to place surplus in a contingency fund for future claims and that by the end of 1992, there was a significant surplus.

Conclusion

For the reasons set forth above as well as in the affirmations, affidavits, and statements of facts before the Court and the authorities contained in the Reply Memoranda submitted herewith and the other memoranda before the Court on this motion, this Court should grant Plaintiff summary judgment against Lonsdale Schofield on its causes of action for breach of fiduciary duty and violation of the Liquidating Plan in connection with the transfers of surplus from Booth Oil of \$450,000, \$300,000, and \$275,000.

Dated: December 3, 2004
Buffalo, New York

s/ R. William Stephens
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