

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

In re

U.S. PRODUCTS, CORP.

Debtor

Case No. 95-13147
Chapter 11

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Hon. Robert E. Littlefield, U.S. Bankruptcy Judge

MEMORANDUM-DECISION AND ORDER

This matter is before the court on the motion on shortened notice by Order dated December 11, 1995 by Capital Resource Funding, Inc. ("CRF") seeking (1) reconsideration and reargument of a portion of the court's prior December 7, 1995 decision and (2) relief from the stay with regard to certain inventory and cash collateral. The court has subject matter jurisdiction over the instant matter pursuant to 28 U.S.C. §157(b)(2)(B), (K).

FACTS

As a result of CRF's prior motion seeking to prohibit the Debtor's use of cash collateral, the court entered its December 7, 1995 Memorandum, Decision and Order ("MD&O") wherein the court, *inter alia*, found that CRF possessed a first priority lien on the Debtor's assets and granted CRF's motion due to the Debtor's failure to provide adequate protection of CRF's interest. The court also denied without prejudice that portion of CRF's motion that pertained to the Debtor's so-called "non-Nomex" inventory because of an inadequate record to determine the competing rights of the three parties making claims against the non-Nomex inventory, to wit, CRF, the United States ("Gov't") and

Perfect Fit Glove Co., Inc. ("Perfect Fit"). Familiarity with the findings of fact and conclusions of law set forth in the court's December 7, 1995 MD&O are assumed and they are incorporated herein.

On December 11, 1995 CRF filed its instant motion (by way of order to show cause) seeking (1) relief from the automatic stay with regard to the collateral in which the court found it to possess a first priority security interest, and (2) reconsideration of that portion of its prior motion relating to property other than the Gov't non-Nomex inventory, which was denied without prejudice in the MD&O. A hearing on CRF's motion was conducted on December 13, 1995 ("hearing date") at which time the court granted CRF partial relief from the stay with regard to certain property of the Debtor.

On the hearing date the Debtor filed papers styled as a "response" to CRF's motion and "cross motion to reconsider prior orders and decisions of the court." The "cross motion" seeks that the court "vacate the prior Orders of August 30, 1995, October 4, 1995, October 10, 1995, and [the December 7, 1995 MD&O] and all other orders not made on adequate notice or hearing; and further that the court recuse itself from further proceeding in this matter...." The Debtor neither filed an affidavit of service, a notice of motion nor sought an order under Rule 9006(c) shortening notice regarding its cross motion. The court heard Debtor's argument seeking the court's recusal and denied the request from the bench. Because of the competing

claims against the Debtor's non-Nomex inventory, the court reserved on that issue and permitted parties to submit further memoranda.

The Debtor's non-Nomex inventory is divided into two subcategories of goods. Certain goods with a claimed aggregate value of approximately \$151,406 which are attributed to two contracts with the Gov't to produce "Unisex" and "cream shell" gloves are referred to herein as the "Gov't non-Nomex" inventory. Other goods located on the Debtor's premises consisting of materials used in Debtor's manufacturing process and goods in various stages of completion are referred to herein as the "non-Gov't, non-Nomex" inventory. The remaining property of the Debtor which is the subject of CRF's instant motion includes accounts receivable and equipment.

Subsequent to the hearing on CRF's motion, CRF conceded the Gov't's superior interest in the Gov't non-Nomex inventory and withdrew its motion with regard to same. See Declaration of George F. Carpinello dated January 5, 1996 at ¶5. No other party has clearly asserted any right to the Gov't non-Nomex inventory.¹

DISCUSSION

¹ While Perfect Fit continues to claim title to certain inventory located on the Debtor's premises it is not possible to discern from its documentation whether it claims an interest in the Gov't non-Nomex inventory.

In view of the absence of any clear competing claim against the Debtor's Gov't non-Nomex inventory, the court finds no impediment to declaring that the Gov't's interest therein is superior to the interest of any other party in interest. Similarly, insofar as CRF's proof of claim filed with the court evidences its properly perfected security interest (as of December 1994) in the Debtor's accounts receivable and equipment to which no substantive objection has been filed, the court must also conclude that CRF possesses a superior interest in the Debtor's accounts receivable and equipment.

Having determined the priority of interests as against the Debtor's equipment, accounts receivable and Gov't non-Nomex inventory, the remaining question concerns the priority of interests against the Debtor's non-Gov't non-Nomex inventory. The only parties claiming an interest therein are Perfect Fit and CRF.

Perfect Fit opposes CRF's instant motion but has not moved for or otherwise affirmatively requested any relief. It asserts that the issue of CRF's lien on the inventory in question is "strictly a matter of law." Perfect Fit's Response dated December 13, 1995 at ¶27. It contends, as it did in the context of CRF's prior motion which resulted in the court's December 7, 1995 MD&O, that the Debtor is in possession of Perfect Fit's goods with a value of \$113,538 by virtue of its "contractor and subcontractor" relationship with the Debtor. According to Perfect Fit, it previously shipped to Debtor certain materials

and partially completed gloves on which the Debtor was to perform additional labor and return to Perfect Fit.

The Debtor's president, Richard Denero, has filed an affidavit supporting Perfect Fit. Attached as an exhibit to Denero's affidavit is a handwritten list purporting to show "Perfect Fit's inventory in Debtor's possession" (at ¶5) post-petition during late September 1995 (the "list"). The list attached to Denero's affidavit is the same exhibit which Perfect Fit attached to its papers submitted in the context of CRF's previous motion to show its ownership of the listed materials. This court found previously that Perfect Fit's "bare listing of goods ... conveys little probative information" on the issue of ownership. MD&O at 6. The same list, now attached to Denero's affidavit, is no more probative the second time around.

In addition to having no probative value, the list appears to contradict Perfect Fit's contention that its property consists only of materials other than the Gov't Nomex inventory. See affidavit of Joseph Hoerner sworn to on December 19, 1995 at ¶2. Although the list purports to itemize materials *not* associated with the Gov't Nomex inventory, it contains items described as "black Nomex," "sage Nomex" and "black leather for Nomex". Moreover, the aggregate value of the items is \$72,084 - representing well over half of the entire alleged value (\$113,580) of the materials on Perfect Fit's list. Perfect Fit has offered no explanation (on either of the times that it has submitted the list) why Nomex materials appear on a list which

Perfect Fit itself asserts is an inventory of non-Nomex materials. Thus Perfect Fit's list is both non-probative on the issue of ownership and creates doubt as to the general reliability of Perfect Fit's efforts along these lines.

Although Perfect Fit argues that it purchased and owned the materials on its list and shipped them, as contractor, to the Debtor, as subcontractor, to have certain work performed, Perfect Fit has produced neither purchase invoices corresponding to the listed materials nor any other documents which would indicate its ownership of identified goods located on the Debtor's premises. Perfect Fit contends that, because it shipped cloth to the Debtor from its "general inventory", it is "impossible ... to ... trace the piece of cloth back to its purchase invoice." Hoerner affidavit at ¶10.

As for Perfect Fit's contract with the Debtor from which their alleged contractor - subcontractor relationship arises, reference is made only to its "relationship" with the Debtor. There is no written "contract" referenced or submitted to the court by any party. Thus, although the documents to which one would look to establish such relationships have not been produced, Perfect Fit nonetheless urges this court to find that it owns certain goods (notwithstanding the contradictions noted above) located on the Debtor's premises pursuant to its contractual relationship with the Debtor.

While secrecy and underdocumented transactions make for intriguing novels, they are generally antithetical to the conduct

of everyday commercial intercourse. Perfect Fit now seeks the benefits that flow from adequately documented commercial transactions without carrying the burdens. To make matters worse, Perfect Fit argues that its underdocumented, contradictory submissions warrant a finding that it possesses an interest in certain inventory superior to CRF. However, CRF was found by this court to possess a perfected, first priority security interest in the Debtor's inventory. On balance, the court must agree with CRF that, based upon the present record, a finding that Perfect Fit's interest is superior to CRF's would be to "elevate a secret lien over a duly perfected security interest." CRF's Reply Memo of Law dated October 27, 1995 at 7.

Perfect Fit has requested an evidentiary hearing on the issue of its ownership of goods in the possession of the Debtor. It has asserted that it has been unable to make an adequate showing due to the shortened notice of CRF's instant motion. While substantial doubt exists with respect to what further evidence, if any, Perfect Fit may offer to support its claim, the court must agree that it should be provided with a meaningful opportunity to be heard. Accordingly, the court shall schedule an evidentiary hearing at which Perfect Fit shall have the opportunity to establish (1) whether any of the items on its list match the non-Gov't, non-Nomex inventory, and (2) whether it is able to offer any additional further evidence of its ownership of the identified non-Gov't, non-Nomex inventory.

Based upon the foregoing reasons, it is hereby **ORDERED**,

that:

1. The Gov't possesses an interest in the "Unisex" and "cream shell" gloves located on the Debtor's premises superior to the other parties in interest;
2. CRF possesses a perfected security interest in the Debtor's equipment, accounts receivable, and other property as described in the November 17, 1994 Security Agreement located at the Debtor's premises (together the "remaining collateral");
3. CRF is granted relief from the automatic stay pursuant to Code §362(d) with regard to the remaining collateral based upon the reasons set forth in the court's December 7, 1995 Order; and
4. An evidentiary hearing shall be conducted on _____, 1996 at ___ for the purpose of permitting Perfect Fit an opportunity to establish its interest, if any, in the non-Gov't, non-Nomex inventory located on the Debtor's premises.

Dated: February , 1996
Albany, New York

Hon. Robert E. Littlefield, Jr.
U.S. Bankruptcy Judge