

**UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF KENTUCKY
COVINGTON DIVISION**

IN RE:

EMERSON A. LEWIS

CASE NO. 10-21912

DEBTOR

LORI A. SCHLARMAN, TRUSTEE

PLAINTIFF

V.

ADV. CASE NO. 11-2007

HARRY JOHNS, ET AL.

DEFENDANTS

MEMORANDUM OPINION

The issue before the Court is whether the Plaintiff Trustee may avoid the liens held by the Defendants Harry Johns (“Johns”) and Harold Gaines (“Gaines”) (collectively the “Defendants”) on nine vehicles, titled in the name of Lewis Auto Sales and listed as personal property on Schedule B of the Debtor’s petition, pursuant to 11 U.S.C. §547(b). The Defendants do not dispute that if the vehicles are property of the Debtor’s estate then their liens may be avoided by the Trustee as a preferential transfer under §547(b). But the Defendants argue that the vehicles are not property of the estate because the vehicles are titled in the name of Lewis Auto Sales, which they assert is a partnership between the Debtor and the Defendants, and thus their interest is an ownership interest rather than a security interest subject to avoidance. The Trustee argues that Lewis Auto Sales is a sole proprietorship owned by the Debtor and thus the vehicles belong to the Debtor and may be avoided.

The Trustee moved for summary judgment against the Defendants and the Debtor. The Defendants objected but the Debtor did not respond. The Trustee and the Defendants have since stipulated to the relevant facts and submitted the matter on its record in lieu of trial. The

Court, after having reviewed the record and the parties' stipulations of fact, holds that Lewis Auto Sales is a sole proprietorship owned by the Debtor. Therefore, the nine vehicles, titled in the name of Lewis Auto Sales, are property of the Debtor's estate subject to the liens held by the Defendants as secured creditors. Those liens, noted on the certificates of title on April 15, 2010, or eighty-nine days prior to the filing of the Debtor's petition, are avoidable by the Trustee pursuant to 11 U.S.C. §547(b).

Facts

The following facts are undisputed. The Debtor, Emerson A. Lewis, operated Lewis Auto Sales, a used car lot located in Glencoe, Kentucky, jointly with his wife. Lewis Auto Sales was not incorporated nor did it have any partnership documents or a certificate of registration filed with any governmental entity.

The Debtor filed individually for Chapter 7 relief on July 13, 2010. The Plaintiff, Lori A. Schlarman, was appointed as Chapter 7 Trustee. On Schedule B of his petition, the Debtor listed nine automobiles held as inventory for resale at Lewis Auto Sales. The Debtor listed the Defendants on Schedule D of his petition as having a security interest in the nine vehicles (the "Vehicles"), identified more specifically as the following:

2009 Toyota Camry	Vin# 4T1BE46K39U315306
2004 Toyota Avalon	Vin# 4T1BF28B34U340584
2004 Toyota Highlander	Vin# JTEDP21A340007560
2004 Toyota Corolla	Vin# 2T1BR32EX4C294267
2002 Mercury Sable	Vin# 1MEPM50U62G635313
2000 Chevrolet Prism	Vin# 1Y1SK5283YZ409499
2001 Chevrolet Impala	Vin# 2G1WF52E919309416
2000 Ford Escort	Vin# 3FAKP1139YR123994
2004 Chevrolet Cavalier	Vin# 1G1JC52F947331904

The Defendants subsequently filed proofs of claim as secured creditors. Johns filed Proof of Claim #8 identifying a claim of \$46,110.89 based on a security interest in the following six vehicles: (1) the 2009 Toyota Camry; (2) the 2004 Toyota Avalon; (3) the 2004 Toyota Highlander; (4) the 2004 Toyota Corolla; (5) the 2002 Mercury Sable;

and (6) the 2000 Chevrolet Prism. Gaines also filed Proof of Claim #7 identifying a claim of \$12,778.00 based on a security interest in the following three Vehicles: (1) the 2001 Chevrolet Impala; (2) the 2000 Ford Escort; and (3) the 2004 Chevrolet Cavalier.

The certificates of title on all nine of the Vehicles are in the name of "Lewis Auto Sales". Furthermore, the titles of the 2001 Chevrolet Impala, the 2000 Ford Escort, and the 2004 Chevrolet Cavalier reflect a lien filed by Gaines on April 15, 2010 in Owen County, Kentucky consistent with the Debtor's Schedule D and Gaines' Proof of Claim. Likewise, the titles to the 2009 Toyota Camry, the 2004 Toyota Avalon, the 2004 Toyota Highlander, the 2004 Toyota Corolla, the 2002 Mercury Sable, and the 2000 Chevrolet Prism reflect liens filed by Johns on April 15, 2010 in Owen County, Kentucky consistent with his Proof of Claim and the Debtor's Schedule D.

On February 16, 2011, the Trustee filed this adversary proceeding seeking to avoid the liens held by the Defendants pursuant to 11 U.S.C. §547(b) as a preferential transfer made within ninety days of the filing of the Debtor's petition. The Defendants answered the Complaint on March 20, 2011, and filed a counterclaim against the Trustee and a cross-claim against the Debtor alleging that the Vehicles are not property of the Debtor's estate. The Defendants allege that they were partners with the Debtor in Lewis Auto Sales, which was purportedly operating as a partnership until the filing of the Debtor's individual bankruptcy. According to the Defendants, Lewis Auto Sales is not in bankruptcy and since the partnership owns the Vehicles, they are not assets of the Debtor's estate and are not subject to an avoidance action by the Trustee.

The details of the business arrangement between the Defendants and the Debtor, as opposed to its legal definition, are not in dispute. The Debtor had a long-standing business arrangement with the Defendants whereby the Debtor and the Defendants agreed that the Debtor would purchase certain vehicles to be titled in the

name of Lewis Auto Sales. After a particular vehicle was purchased at an auction, either Gaines or Johns would write a check to Lewis Auto Sales for the purchase price of the vehicle paid at the auction. The vehicle would then remain on the Lewis Auto Sales lot until purchased by a customer. Once the vehicle was sold, if either of the Defendants had written a check to Lewis Auto Sales, then Lewis Auto Sales would deduct expenses and pay either Gaines or Johns the original purchase price of the vehicle plus one-half the net profit over the purchase price and expenses for that particular car. The other half of the vehicle's net profit was retained by the Debtor.

During the course of this business arrangement with the Defendants, the Debtor sold vehicles at Lewis Auto Sales purchased by him that were not subject to this business arrangement with the Defendants. The Defendants did not share in the profits from these other vehicles; rather, the Defendants only received "profits" from sold vehicles for which they had written checks towards the purchase, repair and upkeep. Moreover, the business arrangement never involved the sharing of profits by all three parties for a single vehicle; either the Debtor would share the profits from the sale of a vehicle with Gaines or the Debtor would share the profits collected from a particular vehicle with Johns.

During the course of this business arrangement, the Defendants did not contribute towards the utility or the upkeep of the business operations of Lewis Auto Sales. Moreover, while the Debtor did pay for the cost of the Defendants' salesperson licenses, the Defendants did not receive K-1 or 1099 tax statements from Lewis Auto Sales or the Debtor.

Each of the Vehicles at issue in this adversary proceeding was purchased subject to this business arrangement. The Vehicles were purchased by the Debtor at an auction. The Debtor paid for the Vehicles by a check signed by the Debtor from a

checking account titled in the name of “Emerson or Ruth Ann Lewis d/b/a Lewis Auto Sales.” The Defendants in turn wrote a check to the Debtor or Lewis Auto Sales for the purchase price of the Vehicle. Each of the checks written by the Defendants reflects an amount that matches the purchase price paid at the auction for the Vehicles claimed by either Gaines or Johns. The Vehicles were parked at Lewis Auto Sales and offered for sale by Lewis Auto Sales. The Debtor or Lewis Auto Sales paid for the liability insurance covering the Vehicles.

On July 25, 2011, the Trustee moved for summary judgment, arguing that the liens held by the Defendants should be avoided as preferential transfers pursuant to 11 U.S.C. §547(b). The Defendants objected on the basis that the Vehicles are not property of the Debtor’s estate, but belong to Lewis Auto Sales, a partnership in which they are partners. The Debtor did not respond. The Trustee and the Defendants stipulated to the facts as cited above and filed an agreed order deeming the matter submitted. This matter is therefore ripe for review and determination by this Court.

Analysis

This Court has jurisdiction to hear this matter pursuant to 28 U.S.C. §157 and §1334. This is a core proceeding under 28 U.S.C. §157(b)(2). Venue is appropriate pursuant to 28 U.S.C. §1409.

The Trustee moves to avoid the liens held by the Defendants in the Vehicles as preferential transfers. A trustee can avoid a transfer of an interest of the debtor in property:

- (1) to or for the benefit of a creditor;
- (2) for or on account of an antecedent debt owed by the debtor before such transfer was made;
- (3) made while the debtor was insolvent;
- (4) made –
 - (A) on or within 90 days before the date of the filing of the petition; or

- (B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and
- (5) that enables such creditor to receive more than such creditor would receive if –
 - (A) the case were a case under chapter 7 of this title 11 U.S.C. §§701 *et seq.*;
 - (B) the transfer had not been made; and
 - (C) such creditor received payment of such debt to the extent provided by the provisions of this title 11 U.S.C. §§101 *et seq.*

11 U.S.C. §547(b). A debtor is presumed insolvent on or during the ninety days preceding the date of the filing of the petition. 11 U.S.C. §547(f).

There is no dispute that the liens were conveyed to the benefit of the Defendants, who paid the Debtor an amount equal to the purchase price of the Vehicles following the Debtor's purchase of them at auction. There is also no dispute that the Defendants' liens were noted on the titles to the Vehicles eighty-nine days prior to the filing of the Debtor's petition. The Debtor is presumed insolvent ninety days before the filing of the bankruptcy petition, a presumption that the Defendants do not attempt to refute. Finally, the Defendants do not take issue with the fact that the liens on the Vehicles enable them to receive more as secured creditors than they would receive if the liens had not been noted on the titles.

Thus, the only dispute is whether the Vehicles are property of the estate as "an interest of the Debtor" that is subject to avoidance by the Trustee. The Defendants argue that the Vehicles are not, as they belong to Lewis Auto Sales, a partnership that has not filed bankruptcy. The Trustee contends that Lewis Auto Sales is a sole proprietorship and as such, its assets are property of the Debtor's estate. Thus, this matter boils down to the question of whether Lewis Auto Sales is a sole proprietorship or a partnership.

The definition of a partnership is governed by state law. A partnership is an “association of two (2) or more persons to carry on as co-owners of a business for profit.” K.R.S. §362.175. The rules for determining the existence of a partnership in Kentucky are set forth in K.R.S. §362.180:

- (1) Except as provided by KRS §362.225 persons who are not partners as to each other are not partners as to third persons.
- (2) Joint tenancy, tenancy in common, tenancy by the entireties, joint property, common property, or part ownership does not of itself establish a partnership, whether such co-owners do or do not share any profits made by the use of the property.
- (3) The sharing of gross returns does not of itself establish a partnership, whether or not the persons sharing them have a joint or common right or interest in any property from which the returns are derived.
- (4) The receipt by a person of a share of the profits of a business is prima facie evidence that he is a partner in the business, but no such inference shall be drawn if such profits were received in payment:
 - (a) As a debt by installments or otherwise,
 - (b) As wages of an employee or rent to a landlord,
 - (c) As an annuity to a widow, or widower or representative of a deceased partner,
 - (d) As interest on a loan, though the amount of payment vary with the profits of the business,
 - (e) As the consideration for the sale of a goodwill of a business or other property by installments or otherwise.

The Defendants rely on K.R.S. §362.180(4) and argue that their receipt in a share of the profits in the Vehicles is *prima facie* evidence that they are partners in Lewis Auto Sales. This reliance on K.R.S. §362.180(4) is misplaced. While the Defendants certainly received a share of the profits for the sale of particular vehicles, and would have received a share of any profits for the sale of the Vehicles herein, the Defendants did not share in the overall profits of Lewis Auto Sales. Rather, their select share of the profits was tied to their initiative to provide the Debtor financing with which to purchase the Vehicles for resale by paying the Debtor for the purchase price of the Vehicles at the auction. The Defendants did not share in the profits “of a business” but rather financed

the purchase of particular vehicles for a portion of the profits upon resale. Thus, the business arrangement between the Debtor and the Defendants more closely resembles the exception set forth in K.R.S. §362.180(4)(d), or profits received in payment “as interest on a loan.” “One who makes a loan of money or credit to the owner of a business in consideration of a share of its profits in repayment of such loan does not thereby become a partner in business.” See *Dowdey v. Henry (In re Washington Communications Group, Inc.)*, 18 B.R. 437 (Bankr. D.C. 1982).

Lewis Auto Sales was not incorporated and no partnership documents or certificate of registration was filed with any governmental entity. The Debtor testified that Auto Sales was a sole proprietorship. The Debtor, in filing his petition as Emerson A. Lewis, did not distinguish between his personal assets and those of Lewis Auto Sales, but rather listed the Vehicles as his personal property on Schedule B of the petition. In paragraph 18 of the Debtor's Statement of Financial Affairs, he listed no business partners and treated the Defendants as secured creditors on Schedule D of the petition. Likewise, the Defendants acted as secured creditors by filing proofs of claims as secured creditors asserting their liens on the Vehicles.

Finally, the Debtor paid for all the expenses associated with Lewis Auto Sales, including the insurance covering the Vehicles; the Defendants shared none of this burden. The select sharing of profits on a few select vehicles paid for by the Defendants without the sharing of profits and expenses of Lewis Auto Sales as a whole is not “an association of two (2) or more persons to carry on as co-owners of a business for profit...” K.R.S. §362.175. This business arrangement is nothing more than a creative arrangement to finance the purchase of certain vehicles owned and sold by the Debtor in exchange for a portion of the profits from those selective vehicles.

Lewis Auto Sales is not a partnership but a sole proprietorship. As a sole proprietorship, Lewis Auto Sales is not a separate legal entity and the inventory of Lewis Auto Sales belongs to the Debtor as property of his estate. 11 U.S.C. §541; *In re Doris A. Christenberry*, 336 B.R. 353 (2005) (quoting *Gilliam v. Speier (In re KRSM Props, LLC)*, 318 B.R. 712 (B.A.P. 9th Cir. 2004)) (holding that a sole proprietorship cannot file for bankruptcy without its proprietor so filing). Thus, the Vehicles titled in the name of Lewis Auto Sales are assets of the Debtor's estate and subject to the Trustee's avoidance powers pursuant to 11 U.S.C. §547(b).

Conclusion

Lewis Auto Sales is a sole proprietorship owned by the Debtor and not a partnership with the Defendants. Therefore, the Vehicles titled in the name of Lewis Auto Sales are property of the Debtor's estate. The Trustee having met the elements of 11 U.S.C. §547(b), the Defendants' liens on the Vehicles are subject to avoidance as a preferential transfer. The Defendants' counterclaim against the Chapter 7 Trustee and cross-claim against the Debtor shall be dismissed.

The foregoing constitutes the Court's findings of fact and conclusions of law. A separate order shall be entered accordingly.

Copies To:

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Michael D. Triplett, Esq.

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***The affixing of this Court's electronic seal below is proof this document has been signed by the Judge and electronically entered by the Clerk in the official record of this case.***



**Signed By:**  
**Tracey N. Wise**  
**Bankruptcy Judge**  
**Dated: Wednesday, November 02, 2011**  
**(tnw)**