

UNITED STATES BANKRUPTCY COURT  
DISTRICT OF MINNESOTA

In re:

James Bruce Preece,

Debtor.

Bankruptcy No. 03-44978  
Chapter 7

Central Boiler, Inc.,

Plaintiff,

Adversary No.

vs.

**COMPLAINT**

James Bruce Preece,

Defendant.

Plaintiff, Central Boiler, Inc., for its cause and claim against the defendant, James Bruce Preece, alleges to the Court as follows:

1. This court has jurisdiction over this adversary proceeding pursuant to 28 U.S.C. §§ 1334, 157.
2. This is a core proceeding pursuant to 28 U.S.C. § 157 (B)(2)(I).
3. That the debtor/defendant, James Bruce Preece (Preece), filed his petition for relief under the Bankruptcy Code on July 11, 2003, and this action is commenced prior to the bar date to commence such actions.
4. That Central Boiler, Inc. (Central) is a Minnesota corporation having its principal place of business in Greenbush, Minnesota.
5. That Helicopter Flight, Inc. (HFI) is upon information and belief a Minnesota corporation

- having its principal place of business in Crystal, Minnesota.
6. That Preece is and was the President of HFI, its alter ego, and is responsible for actions taken by HFI and his own actions, individually.
  7. That in 1994 Central, through the auspices of HFI as agent, purchased an R22 helicopter, serial number 2403, from Robinson Helicopter Company (RHC).
  8. That in early 2002 negotiations began whereby Central would purchase from HFI a new R44 Helicopter. Ultimately, the serial number assigned to this helicopter was 1203.
  9. That as negotiations continued, a \$25,000 down payment on the R44 helicopter was deposited by Central with HFI and forwarded by HFI to RHC.
  10. That in full payment for the helicopter, HFI agreed to accept the R22 helicopter at a trade in value of \$90,000, together with additional cash in the amount of \$181,414 for the purchase of the R44 helicopter.
  11. That the funds for the R22 trade were specifically agreed to and to be earmarked for the purchase of the R44 helicopter by Central.
  12. That thereafter all of the sums required by HFI to complete the purchase, together with the helicopter, were tendered by Central to HFI.
  13. That it appears that Central was deliberately misled in the transaction by HFI and Preece.
  14. That Central was unable to pick up the R44 helicopter due to the fact that funds (other than the \$25,000) were not tendered from HFI to RHC.
  15. That HFI was insolvent both before and after receipt of funds from Central.
  16. That HFI and Preece have deliberately misled Central by continually stating that the purchase was to be completed.

17. That despite the agreement to the contrary, HFI and Preece have apparently allowed the R22 or its proceeds to be commingled with other assets of HFI and may be subject to alleged claims by secured parties.
18. That the actions of Preece constitute conversion.
19. That Central commenced a lawsuit against HFI and Preece in Roseau County District Court in May of 2002.
20. That sufficient evidence was obtained during the course of litigation in Roseau County through written discovery and deposition which would indicate and demonstrate that Preece operated HFI as an alter ego, and is responsible for the debts of HFI. By way of example, attached as Exhibit A to the complaint is a copy of the affidavit (together with attachment) of Michelle Benton, CPA, dated June 6, 2003. This evidence, together with evidence to be submitted, will demonstrate that Preece is the alter ego of the corporation.
21. That a hearing on the plaintiff's motion for default judgment was to be held in Roseau County District Court on July 15, 2003, however, the defendant filed his bankruptcy petition on July 11, 2003, before a final judgment could be entered against him in the state court action.
22. That plaintiff suffered actual losses pursuant to the complaint in the amount of \$296,414.00, together with attorney's fees and other costs.

#### **COUNT I.**

23. Plaintiff incorporates and realleges all paragraphs preceding and following this Count herein.
24. Defendant obtained \$296,414.00 from plaintiff by fraud, false pretenses or actual fraud.
25. Defendant owes a debt to plaintiff in the amount of \$296,414.00 which is not dischargeable

in bankruptcy pursuant to 11 U.S.C. § 523 (a)(2)(A).

**COUNT II.**

26. Plaintiff incorporates and realleges all paragraphs preceding and following this Count herein.
27. In the alternative, defendant obtained \$296,414.00 from plaintiff for the express purpose of acquiring the helicopter for his own use and deprive the plaintiff thereof.
28. Defendant obtained \$296,414.00 from plaintiff by embezzlement and/or larceny.
29. Defendant owes a debt to plaintiff in the amount of \$296,414.00 which is not dischargeable in bankruptcy pursuant to 11 U.S.C. § 523 (a)(4).

**COUNT III.**

30. Plaintiff incorporates and realleges all paragraphs preceding and following this Count herein.
31. In the alternative, defendant's conversion of plaintiff's \$296,414.00 constitutes a willful and malicious injury be defendant to another entity or the property of another entity.
32. Defendant is indebted to plaintiff in the amount of \$296,414.00 which is not dischargeable in bankruptcy pursuant to 11 U.S.C. § 523 (a)(6).

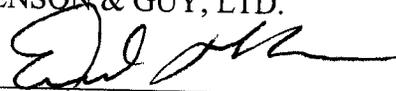
WHEREFORE, plaintiff prays the court enter its judgment as follows:

1. Entering judgment in favor of plaintiff and against defendant in the amount of \$296,414.00, together with prejudgment interest.
2. Declaring that such debt is not discharged by defendant's bankruptcy filing.
3. For costs, disbursements and reasonable attorney's fees.
4. Such other and further relief as the Court deems just and equitable.

Dated this 1<sup>st</sup> day of October, 2003.

GUNHUS, GRINNELL, KLINGER,  
SWENSON & GUY, LTD.

By



Edward F. Klinger

Attorneys for Central Boiler, Inc.

215 30th Street North

P.O.Box 1077

Moorhead, MN 56561-1077

(218) 236-6462

Attorney ID No. 56625

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STATE OF MINNESOTA  
COUNTY OF ROSEAU

IN DISTRICT COURT  
NINTH JUDICIAL DISTRICT

Central Boiler, Inc., )  
 )  
 Plaintiff, )  
 )  
 vs. )  
 )  
 Helicopter Flight, Inc. and J. Bruce Preece, )  
 )  
 Defendants. )

Civil No. C1-02-000369

**AFFIDAVIT OF MICHELLE BENTON**

STATE OF MINNESOTA )  
 ) : ss.  
COUNTY OF Pennington )

Michelle Benton, being duly sworn, states and deposes:

1. That she is a Certified Public Accountant.
2. That attached as Exhibit A to this affidavit is correspondence dated June 2, 2003 to the attorney for Central Boiler, Edward F. Klinger.
3. That this correspondence is based upon my professional experience, as well as generally accepted accounting principles.
4. That in my professional opinion, inadequate information has been provided by defendant J. Bruce Preece as had been requested in interrogatories as well as additional requests for information.
5. That in my professional opinion, corporate niceties and standards were violated by Mr. Preece, and based upon information provided to me by Edward F. Klinger, I believe that Mr. Preece was the alter ego of the corporation.

Further your affiant sayeth not.

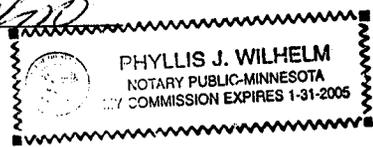


Dated this 6<sup>th</sup> day of June, 2003.

Michelle Benton, CPA  
Michelle Benton

Subscribed and sworn to before me  
this 6<sup>th</sup> day of June, 2003.

Phyllis J. Wilhelm  
Notary Public



# KAYS, BENTON, SAFRANSKI & Co. LLP



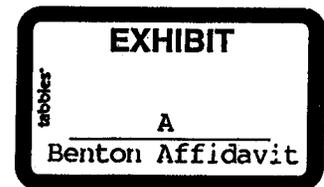
*Certified Public Accountants*

Thomas P. Kays, CPA  
Michelle M. Benton, CPA  
Raymond B. Safranski, CPA

116 West Third Street  
P.O. Box 637  
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June 2, 2003

Gunhus, Grinnell, Klinger, Swenson & Guy, Ltd.  
Attn: Mr. Edward F. Klinger  
215 30<sup>th</sup> Street North  
P.O. Box 1077  
Moorhead, MN 56561-1077



Dear Mr. Klinger:

I have reviewed the additional information received from Mr. Preece in response to the interrogatories for Civil Case No. C1-02-00369 Central Boiler, Inc. vs. Helicopter Flight, Inc. (HFI) and J. Bruce Preece. After reviewing this information, I noted the following:

1. Mr. Preece provided copies of the Form W-2's issued for the year 2001 in response to Interrogatory No. 15. The Form W-2's show that Mr. Preece took a salary of \$10,000 from HFI in the year 2001. This agrees with the amount Mr. Preece stated in his deposition taken August 13, 2002. Mr. Preece has not provided the detail for salaries and wages for the year 2000 as requested in Interrogatory No. 1 so we still have no idea of the amount of any salary received by Mr. Preece in that year. He should be able to provide the Form W-2's for the year 2000 but he has not provided that information, which indicates that he may not want us to see the amount of salary that he took in that year.
2. Mr. Preece provided copies of the depreciation schedules for the years 2000 and 2001 as requested in Interrogatory No. 11. The year 2000 depreciation schedule does not show an asset or assets with a cost basis of \$514,933 being removed from the schedule. However, a tie-out of the beginning of the year balance in buildings and other depreciable assets per the 2000 Form 1120S, Page 4, Schedule L, Column (a), Line 10a to the end of the year balance in buildings and other depreciable assets per the 2000 Form 1120S, Page 4, Schedule L, Column (c), Line 10a indicates that there is an unaccounted for decrease in buildings and other depreciable assets of \$514,933. See attached schedule for details. I would think that if \$514,933 of depreciable assets were removed from the books, the sole shareholder would have some idea what was removed!!

3. Mr. Preece provided some additional information regarding Interrogatories No. 16, 21 and 22, which he signed and had notarized. He did not provide a detailed breakdown as requested in the interrogatories, but made some very basic comments regarding what was included in repairs and maintenance expenses, telephone expenses and training and education expenses. His reluctance to provide detail regarding the repairs and maintenance, telephone expense and training and education expense leads me to conclude that he paid some of his own personal expenses through the corporation, and he does not want us to look at the detail included in these accounts. Mr. Preece should be able to produce the detailed accounting records (i.e. general ledger account detail) for these accounts (and other accounts, such as travel, bank charges, commissions, insurance, supplies and miscellaneous expenses as requested in the interrogatories) if he has maintained adequate accounting records for the corporation for tax purposes. If the Internal Revenue Service audited the corporation, they would request to see the detail in these accounts because they review expenses paid by the corporation to see if they are legitimate business expenses. I find it difficult to believe that Mr. Preece does not have adequate, detailed accounting records for the corporation which would include detailed general ledgers or detailed year to date account histories. His lack of compliance with the requests for account detail in the interrogatories leads me to conclude that he does not want these records reviewed because he has something to hide (i.e. possibly paying personal expenses through the corporation).
4. Mr. Preece signed and had notarized his responses to the interrogatories that he provided in a letter dated April 18, 2003. The signing and notarizing of his responses is meaningless, because as I pointed out in my letter dated May 13, 2003, Mr. Preece did not provide most of the information requested in the interrogatories and the information he did provide was vague, unclear, inaccurate and incomplete. Signing and notarizing incomplete and inaccurate information does not make it any more valid.

Helicopter Flight, Inc. is a closely held corporation with the sole shareholder being Mr. J. Bruce Preece. I believe Mr. Preece has failed to make the formal distinctions between corporate and individual property or funds. I believe that the corporate entity should be disregarded and that Mr. Preece should be held personally liable for Helicopter Flight, Inc.'s obligations for the following reasons:

1. The corporation was undercapitalized in the years 1999, 2000, and 2001 based on the balance sheets included in the 2000 and 2001 Form 1120S U. S. Income Tax Returns for an S Corporation. At December 31, 1999, 2000 and 2001 liabilities exceeded assets by \$156,752, \$352,083, and \$247,013, respectively. The company was in financial trouble a long time before their dealings with Central Boiler, Inc.
2. HFI has failed to observe the corporate formalities. The corporate minutes for the years 1996 through 2002 did not include the approval of any leases with Mr.

Preece or the payment of any rent to Mr. Preece, even though the corporation was paying rent to Mr. Preece in the years 2000 and 2001 according to his responses to the interrogatories. Payments of rent to shareholders and any leases with shareholders or other related parties should be documented and approved in the corporate minutes. The last lease with Mr. Preece approved in the corporate minutes was for a term of January 1, 1995 to December 31, 1995. In addition, the corporate minutes did not include sufficient detail or the approval of sales, leases and leasebacks of equipment with HFI Aircraft Leasing Corporation or HFI Aviation Services, Inc., which would be related corporations because Mr. Preece is also a shareholder in those entities. The corporate minutes do not include any detail regarding salary or wages paid to Mr. Preece. The January 5, 2001 and the July 30, 2002 minutes both state, "The chairman reported because of cash flow needs for the corporation, the corporation was unable to pay the president a salary." Mr. Preece was in fact paid a salary of \$10,000 in the year 2001. Compensation paid to officers and shareholders should be documented and approved in the corporate minutes. The corporate minutes for the years 1999 through 2002 do not include any information regarding debts with financial institutions other than that the corporation entered into a loan for \$248,000 with Textron for the purchase of a Navajo Fixed Wing Twin Engine Aircraft. Debts owed to Security Bank USA were not discussed even though information provided by Mr. Preece as a part of the interrogatories indicates that new loans were obtained during this time period. The corporate minutes or resolutions should indicate the approval of any new debt. The corporate minutes do a poor job of documenting the corporation's activities and do not contain a lot of pertinent data that would normally be included in them especially in regards to related party transactions.

3. For the years 2000 and 2001, the corporation did not paid any dividends to Mr. Preece. However, I would not expect a corporation that was in such poor financial condition to pay dividends to its shareholder.
4. Helicopter Flight, Inc. was insolvent at the time the transaction for the trade-in of Central Boiler, Inc.'s helicopter and purchase of a helicopter by Central Boiler, Inc. was entered into. The corporate tax returns show that for the years 1999, 2000 and 2001 liabilities exceeded assets by \$156,752, \$352,083 and \$247,013, respectively. The corporate income tax returns showed a tax loss of \$157,993 and a book loss of \$195,331 for the year 2000 and a tax loss of \$299,040 and a book loss of \$324,982 for the year 2001. The corporation was experiencing financial difficulties long before the transaction with Central Boiler, Inc. and Mr. Preece had to be aware of it since he would have signed the income tax returns. The poor financial condition of the corporation cannot be blamed on September 11, 2001, as Mr. Preece would like us to believe.
5. Because Mr. Preece has failed to provide the information requested by the interrogatories, it is not possible to prove that Mr. Preece used the corporation to pay some of his personal expenses or to prove that he shifted money around

between his various corporations to hide assets and create confusion. However, his failure to provide the requested information and his vague, unclear, and inaccurate responses to the interrogatories leads me to believe that Mr. Preece is purposely withholding information that may be useful in Central Boiler Inc.'s lawsuit.

6. Even though the corporation was experiencing severe financial difficulties and incurring large financial losses for its size, Helicopter Flight, Inc. paid rent to Mr. Preece of \$52,335 in the year 2000 and \$30,000 in the year 2001 according to his response to the interrogatories and paid a salary to Mr. Preece of \$10,000 in 2001 according to the Form W-2's when he had not received a salary in the past according to his deposition. Normally, a corporate shareholder would not pay himself rent or other compensation when the corporation is experiencing large losses and financial difficulties. In addition during the year 2001, I believe that Helicopter Flight, Inc. loaned \$94,575 to HFI Aviation Services, Inc., which is a corporation owned by Mr. Preece that operates as the manager for the Moorhead airport. A note receivable listed as "N/R-Moorhead" is shown on the 2001 Form 1120S, Schedule L Balance Sheet, Line 6 Other Current Assets. This note receivable increased from \$138,130 to \$232,705 in the year 2001. Mr. Preece may have transferred money from HFI to HFI Aviation Services, Inc. as a way to get money out of HFI for his own personal use. Once the money was transferred to HFI Aviation Services, Inc. Mr. Preece could have taken it out of that corporation. Unfortunately I do not have copies of the tax returns for HFI Aviation Services, Inc. so I cannot see where the money went.
7. The corporate minutes indicate that on July 29, 1999 Al Ludwig was elected as vice president of Helicopter Flight, Inc. The minutes do not indicate if any compensation was paid to Mr. Ludwig. It appears that Mr. Ludwig served on the Board of Directors until Mr. Scott Schramm was elected to the office of vice president on January 5, 2001. The minutes do not indicate if any compensation was paid to Mr. Schramm. The minutes indicate that neither Mr. Ludwig nor Mr. Schramm presented any information at the Board meetings and Mr. Preece as president and chairman led all discussions. It appears that Mr. Schramm only served as vice president for one year and that at the July 30, 2002 Board meeting, that no vice president was elected and the Mr. Preece became the sole Board member.
8. The lack of information provided by Mr. Preece in response to the interrogatories indicates that there is an absence of adequate corporate records or that Mr. Preece is withholding information that may be useful to Central Boiler, Inc. in its lawsuit.
9. Mr. Preece has not explained the increase of \$430,052 in "additional paid in capital" that occurred during the year 2001. An increase in additional paid in capital indicates that the shareholder of the corporation, Mr. Preece, contributed money to the corporation, personally assumed some of the debts of the corporation, or loans from the shareholder to the corporation were converted to

equity. The balance sheet in the 2001 tax return indicated that there were no loans from the shareholder as of the beginning of the year that could have been converted to equity. Surely, Mr. Preece would remember if he contributed \$430,052 of his personal money to the corporation or if he personally assumed corporate debt of \$430,052 that he would become responsible for making payments on!! This is an unusual transaction, and as such, should be easily explained. Once again, this indicates a lack of adequate corporate records when the corporation is involved in transactions with related parties and Mr. Preece, its sole shareholder.

In conclusion, I believe that based on the review of Mr. Preece's responses to the interrogatories (which were vague, unclear and very often inaccurate), the lack of information provided by Mr. Preece in response to those interrogatories, the lack of corporate records provided by Mr. Preece, and the knowledge that Mr. Preece had regarding the financial condition of the corporation at the time it entered into the transaction with Central Boiler, Inc. that the corporate entity should be disregarded and that Mr. Preece should be held personally liable for Helicopter Flight, Inc.'s obligations.

If you have any questions or comments regarding this letter, please contact me at (218) 681-4287.

Sincerely,



Michelle M. Benton, CPA  
Partner

**Helicopter Flight, Inc.**  
**Schedule to Tie-Out 2000 Form 1120S, Page 4,**  
**Schedule L, Line 10a Buildings and Other**  
**Depreciable Assets to Depreciation Schedule**

Balance at Beginning of Year (January 1, 2000) Per  
 2000 Form 1120S, Page 4, Schedule L, Line 10a,  
 Column (a) \$1,143,448

Equipment Purchased in the Year 2000 Per  
 2000 Federal Depreciation Schedule and Per Form  
 1120S, Form 4562:

1. '94 Robinson R-22	85,000
2. Building Improvements	29,252
3. Cart	665
4. Equip. Metro	683

Equipment Sold in the Year 2000 Per 2000 Federal  
 Depreciation Schedule and Per Form 1120S, Form 4797:

1. Airplane-Moorhead	(52,000)
2. 97 Mitsubishi	(11,530)
	(63,530)

Balance at End of Year (December 31, 2000) Should  
 Be Based on Changes Reported on Federal  
 Depreciation Schedule and Tax Return 1,195,518

Balance at End of Year (December 31, 2000) Per  
 2000 Form 1120S, Page 4, Schedule L, Line 10a,  
 Column (c) 680,585

Net Decrease in Buildings and Other Depreciable  
 Assets Not Accounted For On 2000 Federal  
 Depreciation Schedule Provided or on Form 1120S,  
 Form 4797 \$514,933

**Note:** The beginning balance on the 2000 Federal Depreciation Schedule did not include the asset or assets with a cost basis of \$514,933 that was included in the figure reported on the beginning of the tax year balance per Form 1120S, Page 4, Schedule L, Line 10a. At some during 2000, an asset or assets with a cost basis of \$514,933 disappeared from buildings and other depreciable assets with no audit trail left on the depreciation schedule.