IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

MICHAEL F. DIGIACOBBE,	)	
	)	
Plaintiff,	)	
	)	
v.	)	C. A. No. 14525
	)	
JOSEPH P. SESTAK and CHESAPEAKE CONSTRUCTION, LTD.	)	
	)	
	)	
Defendants.	)	

MASTER'S REPORT

Date Submitted: May 7, 2002
Draft Report: July 31, 2002
Final Report: March 3, 2003

Laraine A. Ryan, Esquire, Wihnington, Delaware; Attorney for Plaintiff.

Robert C. McDonald, Esquire, McDonald & Silverman, Wilmington, Delaware; Attorney for Defendants.

GLASSCOCK, Master

The plaintiff, Michael F. DiGiacobbe, and the defendant,' Joseph P. Sestak, were partners in a home construction business. DiGiacobbe seeks damages from Sestak for alleged breaches of fiduciary duty, and an accounting. The case has been tried, and the parties have submitted post trial briefs.[2] This is my report after trial.

I. FACTS

The plaintiff and the defendant were high-school friends who became reacquainted in the early 1980s. By that time, Mr. DiGiacobbe was working in the construction industry with his father, and Mr. Sestak was a draftsman for an architectural *firm. The two* men formed a *de facto* partnership and worked together on a number of houses between 1983 and 1985. In 1986, DiGiacobbe and

---

'Chesapeake Construction Co. ("Chesapeake") is one of two corporations formed by DiGiacobbe and Sestak as part of their construction business. Chesapeake is named as a defendant in this matter, which the plaintiff characterizes, in part, as a derivative suit. Chesapeake, however, was never served and was not represented at trial. The other corporation created by the parties under which they ran their construction business was Sestak and DiGiacobbe, Ltd. That corporation was not made a party to this action.

[2]This lawsuit was filed on September 8, 1995. It was tried before Master Richard Kiger, who issued a report after trial on January 15, 1998. The Master's report was affirmed by this Court on September 18, 1998, and an appeal was taken to the Supreme Court. The decision of this Court was reversed in part and remanded for further proceedings on December 17, 1999. The presiding Vice Chancellor ordered a trial *de novo*. The matter was then referred to me, resulting in this report.

Sestak decided to enter into the construction business on their own on a full-time basis. They incorporated their business as Sestak and DiGiacobbe, Ltd ("S&D"). From that point on, both Sestak and DiGiacobbe worked full time in their construction business. Sestak did the architectural work for the firm, as well as most of the office work and some of the field work. DiGiacobbe spent most of his time in the field, but he concedes that he also had a role in the financial affairs of the partnership. S&D is nominally a corporation but was not operated as such. Although the corporation is still in existence, it has never observed any corporate formalities. There have been no formal shareholders meetings and there is no board of directors. The ownership of S&D, like the partnership which it embodied, was 50 percent in Mr. DiGiacobbe (together with his wife) and 50 percent in Mr. Sestak (together with his wife).[3]

From the beginning, the business of Sestak and DiGiacobbe was run on a remarkably (and unfortunately) informal basis. The firm never produced a budget. It had no compensation scheme for its principals. Rather, the partners had an informal agreement under which they took "draws" from the business as they were available and needed. The partners each also borrowed money from the partnership to fund construction of their own homes. Mr. Sestak, on behalf of the

[3]Janet Sestak and Cheryl DiGiacobbe are not parties to this litigation.

business, made this loan to himself, without consulting DiGiacobbe. Once he discovered Sestak's loan to himself, Mr. DiGiacobbe was moved to express his disapproval of this practice by "grabbing [Sestak]" and "putting him up against the wall." Sestak repaid his personal debt to the partnership.

The business was also severely undercapitalized. Mr. Sestak's father-in-law made a loan of $36,000 to enable the business to proceed. It is unclear whether this amount was a loan by Mr. Sestak's father-in-law to the corporation, a loan to the partnership or a loan to Mr. Sestak (or to his wife, Janet Sestak) directly. This amount has not been repaid. Similarly, Mr. DiGiacobbe's father from time to time made thousands of dollars of loans to the business. The business was also forced to borrow thousands of dollars from a Mr. Auggie Fortunato at a very high rate of interest.[4] The latter loan was repaid.

Sestak and DiGiacobbe were in the business of building custom and semi-custom single family homes. A substantial portion of the homes built by the partners were constructed on speculation; that is, the partners would borrow money to purchase land and build a home, pay interest on the construction loan until a buyer was located and the home sold, pay off the loan and retain the net

[4]According to Mr. DiGiacobbe the loan was for $35,000 at an interest rate of 50 percent.

amount as their profit.[5] During the economic boom years of the late 1980s, the business did well. It began to unravel, however, in the early 1990s. A number of factors are responsible for this decline in the business. First, the business became involved in litigation with a home buyer over a large construction contract, causing the income of the business to be disrupted and its credit-worthiness endangered. Ultimately, according to the plaintiff, the business ended up losing a "great deal of money" on the project. As a result, the business abandoned the corporate form S&D, although it did nothing to wind up the corporate affairs of that entity. Messrs. Sestak and DiGiacobbe simply formed a new corporation, Chesapeake Construction Co. ("Chesapeake") and proceeded to do business under the new name.[6] At about the same time, and even more problematically for the business, the economic downturn of the early 1990s caused significant difficulties. Interest rates were high, and the market for new housing slowed. The economic downturn came at a particularly bad time for the partnership. In July, 1989, the

[5]I refer to the "partnership" as being in the speculation home business although, in the conduct of their business, Sestak and DiGiacobbe used a number of different forms to bind themselves contractually. In some cases they dealt as Mr. Sestak and Mr. DiGiacobbe, in some cases as Sestak and his wife and DiGiacobbe and his wife, and other cases as either Sestak and DiGiacobbe, Ltd. or Chesapeake Construction Co. Therefore, I will refer generally to transactions of the partners as transactions of "the business".

[6]Like S&D, Chesapeake was a corporation in name only--it was not capitalized and was simply the alter ego of the partners, the parties here.

partners, using S&D as the contracting entity, entered into an agreement with two marketing agents (Duncan Patterson and John Teague, Jr.) to form a joint venture to develop a farm near Newark, Delaware (the "Stone Spring" venture). Under the joint venture agreement, S&D invested $5000 in Stone Spring. S&D was to be the exclusive home builder in the development, and Patterson and Teague were to be the exclusive marketing agents. S&D was to build houses for buyers found by Patterson and Teague, and on speculation. Upon sale of a home site and house to a buyer, S&D was to pay a minimum of $75,000 to Stone Spring, which was the cost of the lot.[7] The remainder of the purchase price was applied to the construction loan which S&D had obtained in connection with that particular house, and any net remaining was to be retained by S&D.

The Stone Spring development was a "high end semi-custom" development in which the houses were expected to sell for between $200,000 and $300,000. Unfortunately, the market for such houses became poor in the early 1990s. Home sales were slower than expected and the prices received were lower. The business, (now operating as "Chesapeake") experienced severe cash flow problems. As

[7]The plaintiff testified that a substantial portion of the $75,000/lot minimum was to be applied to pay down the loan by which the joint venture had obtained the Stone Spring acreage, and that once this obligation was satisfied, the lot purchase price would be lowered, resulting in a higher profit per house for S&D. Nothing in the agreement indicates that the lot price would ever drop below $75,000, however.

early as 1991 or 1992, the partners' bookkeeper warned them of the impending cash flow crises.[8] In late 1994, Sestak, unable to adequately support his family from the business, walked away from his duties as a partner and took a job selling automobiles.

By that time ten houses had been completed in Stone Spring, and one ("lot 8") was nearing completion. Construction on lot 8 was undertaken by the business on speculation, and the business had obtained a construction loan to build the house. Because of its financial condition, the business was unable to complete the construction without additional funds. Mr. DiGiacobbe attempted to borrow more money, but the bank refused further loans on the Lot 8 construction job. As a result, Messrs. Sestak and DiGiacobbe were forced to negotiate a buy-out with the two remaining Stone Spring Partners, by which the business forfeited its right as exclusive builder in Stone Spring and released all of its interest to the remaining partners, for $65,000. Mr. DiGiacobbe used the proceeds from this sale of his and Sestak's interest in Stone Spring to complete the house on Lot 8. The house was listed for sale for $285,000 but did not find a buyer at or near that price. It eventually sold for $215,000, which represented a net loss to the partnership. At

[8] As a result, the partners took a number of (ultimately futile) cost-cutting measures, notably including firing the bookkeeper.

this point, the business was defunct. The business was wound down in the same slovenly way that it had been conducted. The two corporations, which were never capitalized or active in any way, remain undissolved. The records of the business were left at its office condominium on the Kirkwood Highway by Mr. Sestak when he abandoned his post. Mr. DiGiacobbe also had access to these records. Subsequently, the office appears to have been ransacked and records and items removed and lost: both parties disclaim responsibility for this action. The mortgage on the office condominium, which was significantly in arrears, was foreclosed and the condominium disposed of by sheriffs sale.

Mr. DiGiacobbe was aware that Mr. Sestak had been taking draws larger than those take by Mr. DiGiacobbe. According to DiGiacobbe, however, it was not until Sestak left the partnership that he discovered the extent of that disparity, together with what he alleges are other irregularities in Sestak's performance of his duties, leading to this equitable action.

II. THE COMPLAINT AND THE NATURE OF THIS ACTION

Mr. DiGiacobbe alleges that Mr. Sestak "converted" funds of Chesapeake because he took draws from 1992 through 1994 which were larger than those

taken by Mr. DiGiacobbe. He also alleges that Sestak mismanaged Chesapeake in a way which caused the business to fail. He seeks damages for this mismanagement and conversion. Finally, he seeks an accounting of amounts due to Chesapeake.

The plaintiff characterizes this action as both a derivative action and as an individual action by Mr. DiGiacobbe as a shareholder of Chesapeake. There are a number of problems in proceeding with this matter as a derivative action on behalf of Chesapeake, however. First, that entity was never served and was not represented at trial. Second, a number of the acts for which DiGiacobbe seeks recovery had nothing to do with the Chesapeake corporate form. For instance, Mr. DiGiacobbe suggests that Mr. Sestak's conversion of assets led to an inability to pay the mortgage on the office condominium, leading in turn to a foreclosure and consequent loss of the equity which he and Sestak had built up in that property. The condominium was not an asset of Chesapeake, however, but was purchased in the name of S&D, with a loan and mortgage guaranteed by the individual parties and their wives. Similarly, he seeks damages for lost profits resulting from the Stone Spring Venture, but Chesapeake was not a party to the Stone Spring Venture. The entity which entered that venture was S&D, and the individual

parties and their wives were liable for the note used to secure the Stone Spring acreage.

In other words this is a morass, of the parties' own making. DiGiacobbe and Sestak became involved in a house building venture without a business plan, without a budget, without an agreement as to how they were to be compensated and with disregard for the corporate forms which they undertook and used inconsistently. As a result, in my view, it is inappropriate to differentiate the allegations of the complaint based upon whether the acts complained of involve property of the corporations or Sestak and DiGiacobbe individually. What is clear is that from the beginning the business has been run as a ***de facto*** 50-50 partnership. The corporations themselves were never active and it makes little sense to try to characterize this action as a derivative or individual corporate claim. At its heart, this is an action for an accounting of partnership assets, involving allegations of an unequal distribution of assets and breaches of fiduciary duty on the part of Mr. Sestak. I will treat it as such.

III. DISCUSSION

A) The Accounting Action

This action is, stated simply, one which seeks an accounting of the assets of the *de facto* partnership between the parties, which include both assets held by the principals of the partnership as well as the construction business carried on first as S&D and later as Chesapeake. An accounting is an equitable remedy by which a fiduciary is required to account to those to whom he owes his fidelity for the results of the exercise of his duty.

The defendant argues that the accounting action should be dismissed, because an accounting between partners, according to the defendant, will only be undertaken where the party seeking the accounting has been excluded from partnership records, while the evidence here indicates that the plaintiff himself has had access to the records of the partnership since the entity was formed. The defendant's view of the accounting remedy is far too narrow, however. "[E]quitable jurisdiction is . . . practically exclusive in procedures for an accounting and settlement of affairs between co-partners themselves. An accounting may be granted wherever a party alleges the wrongdoing of a fiduciary and asks his co-partner for an account and does not get it or is not satisfied with

it." Nero v. Littleton, Del.Ch., 1622, Jacobs, V.C. (April 30, 1998) (Mem. Op. at 4) (quotations omitted). See Pomeroy's Equity Jurisprudence § 142 1, at 1078 (1941). This Court will order an accounting between parties as required by equity. *Id.*

Here, the plaintiff has shown that the parties were partners, and as such stood in a fiduciary relationship to one another; and that the partners were to share on an equal basis in the expenses, profits and losses of the construction business which was the subject of the partnership, including profits of the two corporations formed to conduct the business. The plaintiff argues that the assets of the partnership have been distributed unequally, in favor of the defendant, and that the partnership has suffered from breaches of fiduciary duty by Sestak. Those claims, if substantiated, may be remedied by an accounting.

1. The Burden of Proof

The burden of proof in an accounting is generally stated simply as resting upon the party who is required to account. *E.g.* Pearson v. Rash (check), Del.Ch., 830-K, Berger, V.C. (Feb. 13, 1985) (Mem. Op.) at 1, citing 1 C.J.S. Accounting, § 39. The burden for establishing a basis for an accounting, however is on the plaintiff.

2. The Unequal "Draws "

Under the unique, informal practice of this partnership, each partner was entitled to "draw" from business funds. These payments were in lieu of salary. The draws to Sestak are represented in the record by checks drawn against the partnership's accounts to him; draws to DiGiacobbe are represented by checks drawn to DiGiacobbe's wife, Cheryl. Although on at least one occasion the plaintiff drafted the check which represented his draw, usually the checks representing a partner's draw were drafted by the defendant, the partner who was predominantly responsible for the partnership paperwork. The draws were made to the plaintiff as requested by the plaintiff or his wife, and to the defendant as the defendant chose to make them. By agreement of the partners, the draws of each partner were ultimately to be equal in total, although both parties agree that a substantial inequality in the running total of draws to each partner was tolerated throughout the existence of the partnership.[9] The plaintiff presented evidence, in the form of checks from the partnership's "Stone Spring" and "Chesapeake" accounts made to the plaintiffs wife and to defendant, which demonstrates that during the time the partnership was doing business under the Chesapeake name the defendant's draws were greater than those taken by the plaintiff, in the amount

[9]The parties disagree as to which of the partners was favored, however.

of $37,384. The defendant admits that his draws were greater than those taken by the DiGiacobbe's during this period. Sestak also concedes that his personal telephone bill was paid with partnership funds, in the amount of $2 19, for which he must also account.

DiGiacobbe also points to a number of checks drawn by Sestak on Chesapeake accounts made out to "cash." DiGiacobbe alleges that these actually represent additional "draws" or money taken by the defendant for his own use, and DiGiacobbe seeks an accounting of these sums. Sestak testified, however, that each of these checks to cash was an expenditure for partnership business. He demonstrated at trial that the larger checks to "cash" represent transfers from one partnership account to another. He testified that as the partnership experienced increased financial difficulties in the 1990s, the partnership checking accounts were occasionally overdrawn, and that obligations represented by "bounced" checks were then made good by cash payments. Finally, he testified that the balance of the "cash" checks were to independent contractors who wished to be paid in cash. This testimony was largely unrebutted.[10] I find that the defendant

[10] In post-trial briefing the plaintiff argues that some payments of checks made to "cash" are traceable to deposits in the defendant's personal bank accounts. The only testimony cited by the plaintiff is that of DiGiacobbe himself. DiGiacobbe, asked if the "cash" checks were traceable, responded: "They were cashed with [Sestak's] name on them, and I guess deposited into accounts that were not our accounts." After Sestak had rebutted this testimony in his direct examination, the plaintiff submitted no evidence to the contrary. In post-trial briefing, the

has adequately accounted for the funds represented by the checks to "cash" as expenditures of the business.

Against the $37,603 amount of inequality in draws and payments which the plaintiff has demonstrated, Sestak seeks to offset what he contends were thousands of dollars in unequal draws in the *plaintiff's* favor which defendant alleges had been made before 1992, when the partnership abandoned the S&D corporate structure. The plaintiff admits that an imbalance of several thousand dollars existed at that time, but argues that *he* was the one behind in draws from the business.

Neither party has produced any records, or any evidence other than their own disputed testimony, tending to indicate that an inequality in draws existed prior to the earliest records in evidence, dating from 1992." Therefore, I find that neither party has demonstrated entitlement to an offset or accounting for

---

plaintiff refers to summaries made by his counsel purporting to establish a link between "cash" checks and Sestak's deposits, but points to no record evidence.

"Sestak points to a document, submitted by the plaintiff but never authenticated by either party, labeled "12/3 1/92 trial balance" and showing among other entries "loan-M. DiG. 22,500." This entry has been circled and modified in ink to read (perhaps) "77,501." Sestak argues that this represents proof that DiGiacobbe was "ahead" by $22,500 in 1992. I find the unauthenticated "trial balance" sheet of little or no evidentiary value, however. See Joint Ex. Volume II, Tab 6.

inequalities in draws other than those reflected by the 1992- 1995 checks as described above.

3. The Breach of Duty Claims

The plaintiffs claim here, stated succinctly, is that Sestak took more money out of the business for his own use than was permitted, that the extra draws which Sestak wrongfully took caused the business to fail, and that had the business been able to continue, it would have become highly profitable. The lost profits, according to the plaintiff, are the measure of the damages for which the defendant is liable. The plaintiff, however, is unable to demonstrate the validity of any of these propositions.

a) The Draws. No evidence has been presented indicating any agreement, formal or informal, regarding the timing or amount of draws to which each partner was entitled, other than that each partner was entitled to benefit equally from the business. Between 1992 and 1994, the DiGiacobbes removed $67,360 from the business, and Sestak took $104,744, resulting in the roughly $37,000 differential which I have already indicated must be addressed in an accounting. There is nothing in the record indicating that one amount is the "proper" amount of draws for the period, however.

b) The Failure of the Business and Resulting Damages. dssuming that the plaintiffs argument is that the defendant's draws were imprudently large, leading to the failure of the business, the evidence is contrary. The purpose of the business was to create income for DiGiacobbe and Sestak. The business failed because the economic downturn of the early 1990s reduced the market for their product, expensive custom and semi-custom homes. The business was severely undercapitalized, as demonstrated by the willingness of the partners to accept the ruinous interest rate of the Fortunato loan. It was evident from the testimony of both partners that for the last several years of operation, the business was struggling. Sales had slowed. This resulted in ever-increasing cash-flow problems. Subcontractors and suppliers were not being paid in a timely way, and the partnership began to bounce checks. The last house built by the business was on the market for a protracted period and sold at a loss. In the meantime, the business of a cotenant in the office condominium had failed, and Sestak and DiGiacobbe were forced to assume the entire responsibility for the loan on that unit, a space too large and expensive for their needs. While the plaintiff claims the he and the defendant had accumulated substantial equity in this property, the office condominium was on the market for nearly two years, and was eventually

foreclosed on and sold by the lender for an amount substantially below the amount of the mortgage.

In this climate, the business failed. It is neither supported by the evidence nor logical to believe that the amount of draws taken by DiGiacobbe was a "proper" and sustainable amount, that the few thousand more per year taken by Sestak was the cause of the business failure, and that Sestak should have or did recognize the impropriety of the size of his draws, but took them nevertheless, leading to the loss of the business. The evidence does not indicate that Sestak breached a duty to the partnership by taking the draws as he did.[12]

c) Negligent Mismanagement. DiGiacobbe also argues that Sestak is guilty of "negligent mismanagement" in conducting the business affairs of the partnership, amounting to a breach of fiduciary duty. DiGiacobbe points to bounced checks and cash flow problems as the result of Sestak's financial management, and alleges that this mismanagement led to the collapse of their business. These allegations are unsupported by the evidence, however. The cash

[12]The plaintiff indicated in his testimony that the partners' draws were to come from the "Chesapeake" account, along with overhead expenses, and that the "Stone Springs" account was to receive and disburse construction loans for the various projects in the Stone Springs development. DiGiacobbe implies that Sestak's use of this account to take draws for himself is what placed the partnership in a negative cash flow position. But DiGiacobbe must have been well aware that draws were being taken from the "Stone Spring" account; a substantial portion of his own draws came from that account..

flow problems and bounced checks were the result of, not the cause of, the failure of the business.[13] This is not to say that the business was well run. Record keeping and financial planning and oversight were, to be kind, haphazard. While Sestak was primarily responsible for the conduct of the financial affaires of the business, DiGiacobbe has conceded that he had access to and responsibility in this area as well. The evidence makes clear that, so long as business remained good, both parties were content to conduct the partnership with remarkably lax and informal oversight of their business affairs. In this context, I find no breach of fiduciary duty in Sestak's conduct of the business affairs, and no evidence that his conduct in that regard led to the failure of the business.

Moreover, the damages that the plaintiff claims resulted from the loss of the business are purely speculative. DiGiacobbe testified that, but for Sestak's faithlessness or imprudence, "we would have struggled. However, we probably would not have failed." Despite this diffidence, DiGiacobbe asks me to speculate

---

[13] DiGiacobbe himself, the sole witness for the plaintiff, testified that

> "If Joe [Sestak] had not taken that money, we would have been able to continue the way we were and perhaps gotten over the hump. A lot had to do with the interest rates and the market in that particular time. It really hurt us. I don't think it was mismanagement, as far as what we were doing. We were building a good product. We were just having a difficult time selling at that time because the interest rates had gone up."

that the business could have weathered the recession, and would have turned a large profit on the rest of the construction in the Stone Spring community. This speculation is undermined by the evidence of the parlous state of the business described above, together with the fact that Sestak and DiGiacobbe sold their exclusive right to construct in Stone Spring for only $65,000. The plaintiff, in his post-trial briefing, bases his damage estimates on the supposition that the Stone Spring development would have "built out" over 24 months with 24 homes. The business, however, never built more than six homes even during its early, successful years. In fact, during four and one-half years the partners built only 11 homes in Stone Spring, some of those on speculation, and the build-out of Stone Spring has proved to take over eleven years. DiGiacobbe himself, the sole witness for the plaintiff, testified that, even had the business not failed, "[w]hether we would have made a great deal of money, I'm not sure." The plaintiff has failed to demonstrate that, but for the misconduct which he ascribes to Sestak, the business would have become profitable.[14]

[14]The plaintiff has operated another construction business since Sestak left the partnership, an opportunity which he would have missed if the partnership had remained in business and continued to require his full-time attention, as the partners had contemplated.

4. Conclusion.

The testimony at trial makes it clear that Sestak took draws larger than those taken by DiGiacobbe, without first consulting with his partner. Sestak also borrowed money from the partnership without DiGiacobbe's assent, a loan that was repaid only after a heated confrontation between the partners. It is abundantly clear that DiGiacobbe feels that Sestak's actions were a breach of trust between the two men, and that he blames the failure of the business on Sestak. The plaintiff has failed to show a breach of fiduciary duty on the part of the defendant, or demonstrate any damages which would have flowed from such a breach, however. Nevertheless, the plaintiff is correct that the assets which the defendant has retained from the partnership exceed the assets retained by the plaintiff in the amount of $37,384, contrary to the agreement of the parties that the assets were to be divided equally. This amount must be accounted for, and the partnership being defunct, distributed to the partners, unless this amount is reduced by the offset claims advanced by Sestak and discussed below.

B) Defendant's Offset Claims

Sestak claims to be entitled to offset against the amount for which he is required to account on two theories: that he invested disproportionately in the

partnership; and that he has paid debts of the partnership subsequent to its abandonment.

1) *Disproportionate investment.* Sestak alleges that his father-in-law provided $36,000 in start-up funds to the partnership shortly after its inception, an amount which has never been repaid. DiGiacobbe disputes that such a payment to the partnership remains outstanding. I need not resolve that dispute, however, because Sestak has failed to demonstrate that he, personally, has a claim against the partnership for the money which was advanced by his father-in-law. Therefore, this portion of the offset claim must fail.

2) Payment of the outstanding debts of the partnership. Sestak contends that in accounting to the partnership, he should be able to offset amounts which he alleges he paid to satisfy partnership debt after the business became defunct."

a) The condominium loan. The business operated by the parties was run out of a condominium unit (the "office condominium") which was purchased by

[15]DiGiacobbe sought to be reimbursed based on similar claims of debt payment, however, he failed to substantiate those claims at trial and, in fact, it became quite clear that he had not made a number of the payments which he claimed.

S&D[16] with a loan and mortgage from Wilmington Trust Co. Sestak and DiGiacobbe and their wives were guarantors on the loan and, therefore, personally liable for its repayment. Initially, the partners shared the space with another business, but that entity failed and the partners became solely responsible for the mortgage payments. As the parties' business began to fail in the early 1990s, they were unable to make mortgage payments, and Wilmington Trust had the property sold at a sheriffs sale in early 1995. The proceeds of the sale were insufficient to pay off the loan on the property. Wilmington Trust offered to settle the remaining obligation for $25,000, which was less than the outstanding amount of the loan. Sestak accepted this offer and paid Wilmington Trust $25,000, in return for which the obligations of Sestak, his wife, DiGiacobbe, his wife, and the business were satisfied.

The condominium was a partnership asset, used in conducting the business of the partners. The loan was guaranteed by the parties for the convenience and benefit of the partnership. The balance of the loan outstanding after the sheriffs sale was a debt legally collectable from the guarantors, and was an obligation actively being pursued by Wilmington Trust. The satisfaction of the obligation by Sestak worked a direct benefit to the partnership and the partners individually, and

[16]Some evidence indicates that the office condominium was owned by Chesapeake.

he is entitled to offset the amount paid against the amount for which he is required to account.

The plaintiff points out that Wilmington Trust had insisted on payment from Sestak before it would cooperate in another financial transaction which Sestak was pursuing shortly after the sheriffs sale." It is clear that Sestak felt compelled, for reasons of his own, to settle this debt. The payment, nevertheless, directly benefitted the partnership and the partners individually, and equity requires that it be offset against the amount to be accounted for.

b) Sestak's payment of judgments against him on behalf of the partnership. In contracting for services or materials on behalf of the business, the partners frequently were required to personally guarantee payment. Some of these creditors who had not been paid sought and received personal judgments against Sestak, totaling $7360." These judgments represent debts on behalf of the partnership, and Sestak's personal obligation was created for the convenience and benefit of the partnership. The judgments against him were equitably judgments

---

"This transaction involved the sale of the Sestak family home.

[18]These included Lempers Landscaping, Woodmill Condominium Association and Hillcrest Associates.

against the partnership, and Sestak's payment of these judgments must be set off against the amount for which he is required to account.

c) Other payments by Sestak to claimants. Sestak seeks to be permitted to offset payments he made to other claimants against or creditors of the business. According to Sestak these were mostly small amounts owed to various providers of services to the business. DiGiacobbe disputes Sestak's characterization of some of these payments as for business purposes, but I need not resolve this dispute, because I find that, even if these payments were made to individuals who had provided services to the business, Sestak has failed to show that the payments worked a benefit to the partnership. Therefore, no offset is appropriate.

Sestak testified that his reason for making these payments was a personal sense of obligation. "I felt . . . obligated because . . . . I worked with these people . . . and we owe them money and not all these guys are big companies and they . . . count on their funds." If true, Sestak's expression of personal responsibility is admirable. It is his burden, however, to demonstrate that any payment which he seeks to impose on the partnership actually worked a benefit for the partnership. Sestak failed to consult with DiGiacobbe before making the payments. The record is silent as to wether these were enforceable obligations and as to whether enforcement, in fact, would have been sought. Without denigrating Sestak's

apparent impulse to do the right thing by these claimants, he has simply failed to demonstrate that the payments worked any financial benefit to the partnership or that he was legally compelled to make them on behalf of the partnership. No offset is therefore appropriate.

C) Net Accounting

Sestak has retained excess draws of $37,603, less all allowable off-sets of $32,360, and must therefore account to the partnership for $5,243.

IV. SESTAK'S EXCEPTIONS

Sestak takes exception to the draft report on two grounds.[19] He does not contest my finding that an accounting of the post- 1992 "Chesapeake Construction" phase of the partnership indicates that Sestak is "ahead" of the DiGiacobbe in the amount of $5,243. However, he argues that I erred in not off-setting against this amount the sum of two separate transactions occurring during the pre-1992 ("S & D") phase of the partnership. First, Sestak argues that I should

[19] A third exception involving a proposed off-set (for money allegedly retained by DiGiacobbe from the sale of Lot 8 in Stone Spring) has been waived by the defendant.

have given him credit for $36,000 in funds made available to the partnership by Sestak's father-in-law, a sum which was never repaid. Second, Sestak argues that I should off-set a draw or loan of $22,500 taken by DiGiacobbe in connection with DiGiacobbe's construction of his family home.

The testimony with respect to these two proposed off-sets is either unclear or disputed in the record. I have addressed the loan from Mr. Sestak's father-in-law to the partnership adequately above: there is simply no evidence that this infusion of cash to the partnership from a third party represents an obligation undertaken by Sestak himself for the benefit of the corporation, or that the funds provided by his father-in-law should otherwise be credited to him in this accounting action.[20]

With respect to the draw or loan taken by Mr. DiGiacobbe for construction of his home, DiGiacobbe acknowledges that he drew out this amount, but asserts that the resulting imbalance in draws was compensated in favor of Sestak. Sestak denies that this is so.[21] Mr. DiGiacobbe, in fact, points out quite reasonably that if

---

[20]See Transcript, at 154-55.

[21]Sestak points to the testimony of DiGiacobbe that "[Sestak] had been reimbursed--in fact, I believe that was part of the money he used towards his house." Transcript, at 299-300. Sestak points out that the amount he "loaned" to himself from partnership funds to build his home was repaid, and argues that DiGiacobbe's testimony erroneously conflates the ***unrepaid*** DiGiacobbe draws for personal home construction with the similar but ***repaid*** draws of Sestak. I do not read Mr. DiGiacobbe's testimony to be referring to Sestak's $20,000 "self-help" draw,

he had been ahead $22,500 due to his taking a draw for personal home construction, DiGiacobbe would have been unlikely to angrily confront Sestak about a $20,000 draw Sestak had taken for similar purposes (which in fact DiGiacobbe did); and Sestak would have been unlikely to borrow $20,000 from a commercial lender to replace the draw (a process which Sestak testified that he had begun even before the confrontation).[22]

My decision that Sestak is not entitled to off-set either the loan from his father-in-law or the DiGiacobbe draw does not rest on the evidentiary grounds stated above, however. The problem is more fundamental. The proposed off-set is a part, but only a part, of transactions between the partners over a period of years before 1992, in the "S & D" phase of the partnership. While the record is clear that unequal draws were not unusual throughout the partnership up to its dissolution, neither the testimony nor partnership records are sufficient to support an accounting before 1992. Although DiGiacobbe had access to these partnership records, it is undisputed that Sestak was the partner primarily responsible for the inadequate state of the financial record keeping. To off-set the two proposed amounts, favorable to Sestak, without any proof of the other transactions between

---

however, but to other funds which Sestak applied to the construction of his home.

"Transcript, at 162.

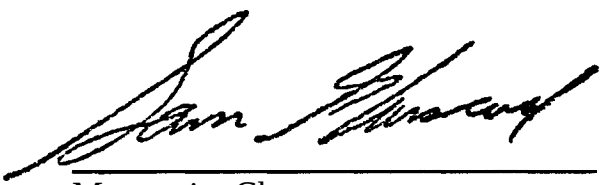
the partners, would be unfair. This is true particularly in light of the fact that it would allow Sestak what may be a benefit for his own slovenly record keeping. This is sufficient reason to disallow the proposed off-sets; a decision bolstered by the unclear and disputed evidence relied upon by Sestak to demonstrate the proposed off-sets, as described above.

Stated simply, it is clear that an accurate accounting of the early partnership years is not possible. While this is unfortunate, it is fair that the consequences of the inadequate state of the records fall upon the party responsible for that portion of partnership operations, Mr. Sestak. Sestak has failed to meet his burden to establish entitlement to the two off-sets he seeks in his exceptions to the draft version of the report. For that reason, the exceptions must be denied.

V. CONCLUSION

The amount of excess draws and personal telephone payments retained by Sestak is $37,603. Offset against this amount must be the payments made by Sestak on behalf of the partnership in relief of the office condominium loan ($25,000) and to satisfy personal judgments for partnership debt ($7360), totaling $32,360. Therefore, Sestak must account to the partnership in the amount of

$37603 less $32,360, or $5243. This amount represents the sole remaining asset of the partnership. It should be distributed equally between the parties. Therefore, Sestak may retain $2,621 SO and must pay $2,621 SO to DiGiacobbe, on behalf of the partnership. Once this report becomes final, the plaintiff should submit a consistent form of order.



Master in Chancery

oc: Register in Chancery (NC)