

1 Preferential Transfer

2 Grassmueck v. Golden West Homes 97-6010-fra
3 (In re T L Concepts 696-60684-fra7)

4 7/31/98 FRA Unpublished

5 The Debtor was a dealer in the sale of manufactured homes
6 and was the exclusive retailer for Golden West Manufactured Homes
7 in southwest Oregon. The Debtor and Deutsche Financial Services
8 entered into an agreement for wholesale financing, with Deutsche
9 retaining a security interest in each manufactured housing unit
10 financed by Deutsche as well a security interest in other
11 business assets. Subsequent to this, Golden West entered into an
12 agreement with the Debtor to provide a line of credit to the
13 Debtor to purchase manufactured housing units constructed and
14 sold by Golden West. Golden West retained a security interest in
15 the Debtor's inventory and other business assets.

16 Golden West then sold most of its assets to Lamplighter
17 Homes. From the sales proceeds, Deutsche was paid the amount of
18 its lien on each unit of manufactured housing sold (representing
19 the amount advanced by Deutsche for each specific unit). This,
20 however, still left Deutsche with a sizable unpaid claim. Golden
21 West was paid the total amount due it pursuant to its security
22 interest in the Debtor's assets. The Debtor then filed for
23 bankruptcy within 90 days of the sale.

24 The Chapter 7 trustee, the plaintiff in this case, filed an
25 adversary proceeding against Golden West, seeking to recover the
26 payment made to Golden West as preferential under § 547. The
27 Plaintiff filed a motion for partial summary judgment, asking the
28 court to rule that the Defendant received more pursuant to the
29 asset sale than it would have had the proceeds instead been
30 distributed pursuant to the distribution provisions of the Code
31 (the fifth element of a § 547 claim). The Defendant countered
32 with a motion for summary judgment of its own.

33 The Defendant argued that this court should adopt the
34 "Source Rule" articulated in a Texas bankruptcy case which holds
35 that there can be no preference when a creditor is paid entirely
36 from its own collateral because the creditor would receive the
37 same amount in or out of bankruptcy. The court, in rejecting
38 this argument, stated that this case is distinguishable because
39 here, unlike the Texas case, there are competing creditors for
40 the same collateral. The Defendant may not have received the
41 same amount in a Chapter 7 liquidation as it did from the sale.
42 However, there was insufficient evidence in the record to
43 determine whether the Defendant did receive more in the sale.
44 Because of that, both motions were denied.

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UNITED STATES BANKRUPTCY COURT
DISTRICT OF OREGON

IN RE)	
)	
T L CONCEPTS, INC.,)	Case No. 696-60684-fra7
)	
_____ Debtor.)	
)	
MICHAEL GRASSMUECK, INC.,)	Adv. Proc. No. 97-6010-fra
TRUSTEE,)	
)	
Plaintiff,)	
)	
v.)	
)	
GOLDEN WEST HOMES,)	
)	
_____ Defendant.)	MEMORANDUM OPINION

The Plaintiff filed a complaint to recover an alleged preferential transfer made to the Defendant. The Plaintiff filed a motion for partial summary judgment and the Defendant countered with its own motion for summary judgment. For the reasons that follow, both motions will be denied.

BACKGROUND

The Debtor was a dealer for the sale of manufactured homes and was the exclusive retailer for Golden West Manufactured Homes

1 in southwest Oregon. On April 2, 1993, ITT Commercial Finance
2 Corp. (predecessor to Deutsche Financial Services Corp. and
3 hereinafter referred to as "Deutsche") entered into an agreement
4 with the Debtor for wholesale financing (also known as a Flooring
5 Agreement). Deutche was granted a security interest in:

6 [A]ll of Dealer's inventory, equipment, fixtures,
7 accounts, contract rights, chattel paper, instruments,
8 reserves, documents, and general intangibles, whether
9 now owned or hereafter acquired, all attachments,
10 accessories, and substitutions and replacements thereto
11 and all proceeds thereof.

12 One provision of the Flooring Agreement required that the Debtor
13 pay to Deutsche the principal amount of indebtedness owed on each
14 item of collateral financed by Deutsche when such collateral is
15 sold. Over time, the Debtor paid down the amount it owed to
16 Deutsche on each item of stock manufactured housing units from
17 its ongoing sales so that there was a substantial equity in the
18 units it held in inventory.

19 On March 1, 1994, the Debtor and Golden West entered into a
20 Secured Promissory Note with a principal balance of \$100,000 to
21 provide a line of credit to the Debtor in connection with the
22 purchase of manufactured homes constructed and sold by Golden
23 West which the Debtor intended to sell in the ordinary course of
24 business. To secure its Note, Golden West was granted a security
25 interest in

26 All of the following described goods and personal
property, distributions and proceeds thereto,
improvements, replacements, accessories and additions,
now owned or hereafter acquired, wherever located,
consisting of but not limited to, (i) manufactured
housing, mobile homes, and the like, including

1 accessories and all other equipment used in conjunction
2 with the foregoing acquired by Debtor from Golden West
3 Homes and all other furniture, equipment, accessories
4 and personal property acquired from other third parties
5 used in Debtor's business, all of which shall become a
6 component part hereof; (ii) accounts receivable,
7 accounts, deposit accounts, chattel papers, documents,
8 general intangibles or other rights to payment together
9 with all renewals, and (iii) Debtor's Golden West
10 Home's Dealer Bonus due from Secured Party relating to
11 its operations (collectively referred to hereinafter as
12 the "Collateral").

13 On May 8, 1995, the Debtor and Golden West entered into an
14 agreement to extend further credit to the Debtor. The Agreement
15 provided for a secured promissory note in the amount of \$140,000
16 dated March 31, 1995 and a Security Agreement granting a security
17 interest in the same items as the earlier agreement. In
18 addition, Larry Griffin, the President of the Debtor, personally
19 guaranteed the debt, with Golden West taking a trust deed on real
20 property owned by Mr. Griffin and his wife.

21 On November 9, 1995, the Debtor entered into an Asset
22 Purchase Agreement with Lamplighter Homes, which was attempting
23 to gain access to the manufactured home market in Oregon. Assets
24 to be sold included 1) office equipment, 2) office and display
25 furniture, 3) tools, equipment and office supplies, 4) the
26 manufactured housing unit used as the Debtor's office, and 5)
four stock manufactured housing units held in inventory. The
purchase price was \$140,000 to be paid in cash at closing, plus
the assumption of indebtedness payable by the Debtor to Deutsche
which was secured by the four stock manufactured housing units
and amounting to \$153,436, plus the assumption of the Debtor's

1 indebtedness to Key Bank secured by the manufactured housing unit
2 used as Debtor's office which amounted to \$32,214. In addition,
3 Lamplighter agreed to lend Mr. Griffin the sum of \$35,000, the
4 amount to be used to assist the Debtor in satisfying certain
5 liens against the property.

6 At closing, according to the affidavit of Mr. Griffin
7 (Golden West did not submit a copy of the closing statement with
8 its motion) Lamplighter wired funds to Jackson County Title in
9 the amount of \$361,538. The amount was earmarked to pay the
10 \$140,000 purchase price, fund the \$35,000 loan to Mr. Griffin,
11 and pay off Deutsche for the balances owing pursuant to the
12 Flooring Agreement on the four manufactured housing units
13 included in the sale. Jackson County Title issued a check to
14 Deutsche in the amount of \$150,635, representing the balance of
15 the indebtedness owed Deutsche on the four stock manufactured
16 housing units. The title company also issued a check to Golden
17 West on November 29, 1995 in the amount of \$109,928, representing
18 the net amount due Golden West on its promissory note. Golden
19 West thereupon released its security interest in the Debtor's
20 assets, including the four manufactured housing units, and its
21 security interest in the real property owned by Mr. Griffin and
22 his wife. There is an apparent dispute between the Plaintiff and
23 Defendant with regard to whether Deutsche released its security
24 interest in the four manufactured housing units after receiving
25 its payment out of closing. There is also an apparent dispute as
26 to whether the amount due Key Bank to pay off its lien against

1 the manufactured housing unit used as an office was paid from the
2 \$140,000 purchase price or from funds earmarked by Lamplighter
3 for that purpose.

4 The Debtor filed its bankruptcy petition on February 23,
5 1996 under Chapter 7.

6 SUMMARY JUDGMENT

7 Summary judgment is appropriate when the pleadings,
8 depositions, answers to interrogatories, admissions, and
9 affidavits, if any, show that there is no genuine issue of
10 material fact and the moving party is entitled to judgment as a
11 matter of law. Fed. R. Civ. P. 56, made applicable by Fed. R.
12 Bankr. P. 7056. The movant has the burden of establishing that
13 there is no genuine issue of material fact. Celotex Corp. v.
14 Catrett, 477 U.S. 317, 323 (1986). The primary inquiry is
15 whether the evidence presents a sufficient disagreement to
16 require a trial, or whether it is so one-sided that one party
17 must prevail as a matter of law. Anderson v. Liberty Lobby,
18 Inc., 477 U.S. 242, 247 (1986).

19 ANALYSIS

20 11 U.S.C. § 547

21 (b) Except as provided in subsection (c) of
22 this section, the trustee may avoid any
23 transfer of an interest of the debtor in
property—

24 (1) to or for the benefit of a
creditor;

25 (2) for or on account of an
26 antecedent debt owed by the debtor
before such transfer was made;

1 (3) made while the debtor was insolvent;

2 (4) made—

3 (A) on or within 90 days
4 before the date of the
5 filing of the petition;
6 or

7 (B) between ninety days
8 and one year before the
9 date of the filing of the
10 petition, if such
11 creditor at the time of
12 such transfer was an
13 insider; and

14 (5) that enables such creditor to
15 receive more than such creditor
16 would receive if—

17 (A) the case were a case
18 under chapter 7 of this
19 title;

20 (B) the transfer had not been
21 made; and

22 (C) such creditor
23 received payment of such
24 debt to the extent
25 provided by the
26 provisions of this title.

18 The Plaintiff, the Chapter 7 Trustee in Debtor's case, moved
19 for partial summary judgment on the fifth element of § 547,
20 contending that the payment made to Golden West out of closing
21 allowed Golden West to receive more than it would have had the
22 proceeds of the sale of assets been held by the Debtor until the
23 petition date rather than distributed. The Plaintiff contends
24 that he would have been required to distribute the proceeds to
25 Deutsche rather than Golden West with Golden West receiving
26 nothing pursuant to its security agreement.

1 The Defendant admits the first four elements of § 547 are
2 present, but, for a number of reasons, argues that Plaintiff is
3 wrong with respect to the fifth element and judgment should be
4 awarded to the Defendant.

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6 Relevant Transfer for § 547 Purposes

7 The Plaintiff contends that had the Debtor held onto the
8 proceeds of the asset sale rather than distributing them, at the
9 petition date they would have been property of the Debtor's
10 estate and the Plaintiff would have distributed them entirely to
11 Deutsche, pursuant to Deutsche's superior lien vis-a-viz Golden
12 West. It appears, however, that the funds were paid into escrow
13 rather than directly to the Debtor. All payments were made from
14 escrow to the recipients, presumably pursuant to binding escrow
15 instructions. While neither party has discussed the significance
16 of this matter, it would be helpful at this point to do so.

17 In Burch v. Bonded Adjusters, Inc. (In re Pelc), 34 B.R. 823
18 (Bankr. D. Or. 1983), the debtors, who had numerous judgment
19 creditors, sold their home. The seller/debtors and the buyers
20 desired that the judgment liens be satisfied from the proceeds of
21 the sale. Consequently, they delivered escrow instructions which
22 provided that the necessary money to clear liens against the
23 property was to be taken out of funds at closing. Certain of the
24 liens were paid off out of the down payment, but a number of them
25 remained. A promissory note from the buyers and a mortgage
26 securing it were delivered into escrow, as was a satisfaction of

1 mortgage executed by the sellers. The balance of the selling
2 price was to be paid in two annual installments. The first
3 annual payment was delivered to the escrow agent by the buyer who
4 thereupon made payments to the lienholders per the escrow
5 instructions. Two days later, the sellers filed bankruptcy. The
6 trustee sought avoidance of the payments made to the lienholders
7 out of escrow under 11 U.S.C. § 547.

8 The court held that property of the debtors, the right to
9 receive payment from the buyers, was transferred at the time of
10 delivery into escrow of the note, mortgage, and satisfaction of
11 mortgage. "The interest of the debtors after delivery was wholly
12 dependent on the terms of the escrow. Consequently, distribution
13 of the installment to the judgment creditors pursuant to the
14 instructions did not involve a transfer of property of the
15 debtors. Absent consent on the part of the [buyers] the escrow
16 instructions could not be modified and the [debtors] had a
17 property right only to the extent so provided in the escrow
18 instructions. . . . The property transferred to the escrow by the
19 [buyers] remains their property and not that of the debtors until
20 the terms of the escrow are met, and thus the funds in escrow
21 never became property to which the [debtors] were entitled." Pelc
22 at 826-827. See also Hasset v. Blue Cross and Blue Shield of
23 Greater New York, 46 B.R. 661 (Bankr. S.D.N.Y. 1985); Cedar
24 Rapids Meats, Inc. v. Hager (In re Cedar Rapids Meats, Inc.), 121
25 B.R. 562 (Bankr. N.D. Iowa 1990); Musso v. N.Y. Higher
26 Education Services Corp. (In re Royal Business School, Inc.), 157

1 B.R. 932 (Bankr. E.D.N.Y. 1993).

2 In a case with facts similar to those in Pelc, it would be
3 the debtor's transfer into escrow of the right to payment that
4 would be legally significant for purposes of § 547, not the
5 payment to lienholders out of escrow. Moreover, the money paid
6 into escrow by the buyers would not become property of the
7 debtor's estate, except to the extent that the terms of the
8 escrow agreement were met and required payments had been made to
9 third parties. In the case at bar, the court was not provided
10 with the closing statement or escrow instructions or an affidavit
11 detailing their terms and is thus not in a position to determine
12 their significance with regard to time of transfer or whether the
13 subsequent payment was property of the estate.

14 Hypothetical Liquidation in Chapter 7

15 For purposes of this analysis, the court must determine
16 whether the Defendant received more as part of the asset sale
17 than it would have had the relevant transfer not been made and
18 the Defendant instead received payment on its debt pursuant to
19 the distribution provisions of the Bankruptcy Code. I must
20 assume for that purpose that the asset sale took place at the
21 petition date and the proceeds were paid into the bankruptcy
22 estate rather than into escrow. The Trustee would then
23 distribute the proceeds according to the applicable provisions of
24 the Bankruptcy Code.

25 The Defendant cites to the "Source Rule" articulated by
26 Judge Clark in Krafsur v. Scurlock Permian Corp. (In re El Paso

1 Refinery), 178 B.R. 426 (Bankr. W.D. Texas 1995) which states
2 that no preference results if an undersecured creditor is paid
3 out of its own collateral, even if the payment is applied to an
4 unsecured claim of the undersecured creditor. See Id. at 434.
5 The problem with applying this rule in the present situation is
6 that there are two creditors secured in the same, or nearly the
7 same, collateral. The "Source Rule" is premised on the
8 supposition that a creditor who is paid out of its own collateral
9 pre-petition would be paid the same amount by the bankruptcy
10 trustee due to the creditor's entitlement to its collateral.
11 When there is a second secured creditor, however, that
12 supposition may not prove to be correct. Given this, the record
13 presented does not foreclose the possibility of a preferential
14 transfer.

15 What would the Trustee have distributed to the Defendant in
16 the hypothetical sale? The short answer is, there is not enough
17 information in the record at this point to tell. Both Deutsche's
18 and Golden West's security interests extended to most of the rest
19 of the Debtor's property with a considerable amount of overlap.
20 The record does not disclose dollar values of assets of the
21 Debtor which were not part of the sale and which would also be
22 subject to the security interest of one or both of the two
23 creditors. It is conceivable that Golden West would have been
24 paid part or all of the amount of its claim from the proceeds of
25 other assets. This could occur in one of two ways: 1) Deutsche's
26 claim would be paid in full from the sale of the manufactured

1 housing units¹ and other assets; proceeds of remaining assets
2 could be applied to Golden West's claim, or 2) Golden West's
3 security interest covers assets that Deutsche's does not and
4 Golden West would be paid from the proceeds of those assets ahead
5 of Deutsche.

6 Because the record is unclear as to the value of assets
7 remaining after the relevant sale which would be available to pay
8 Deutsche's and Golden West's claims, I cannot find in the context
9 of the Plaintiff's motion that Golden West received more than it
10 would have in a hypothetical sale by the trustee. For the same
11 reason, I also cannot find that it did not.

12 CONCLUSION

13 There are material facts missing from the record regarding
14 the dollar amount of assets subject to the security interests of
15 Deutsche and Golden West which are necessary to make a
16 determination under 11 U.S.C. § 547. Also missing is information
17 regarding the terms of the escrow for the Lamplighter sale, which
18 may or may not be material. For this reason, Plaintiff's motion
19 for partial summary judgment is denied and Defendant's cross-
20 motion for summary judgment is likewise denied. An order
21 consistent with this opinion will be entered.

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24 ¹ It is clear from the record that the security interest of both
25 Deutsche and Golden West extended to the manufactured housing units which were
26 the subject of the sale to Lamplighter. Presumably, the Trustee would
distribute the proceeds of a hypothetical liquidation of these assets to
Deutsche because of the seniority of its lien.

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FRANK R. ALLEY, III
Bankruptcy Judge