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Preferential transfer  
Contemporaneous exchange  
Loan refinance

Sticka v. U-Lane-O Credit Union  
In re Katherine McKay

98-6055-fra  
697-65404-fra7

2/1/99    FRA    Unpublished

The Debtor and her domestic partner purchased a vehicle and financed it through Key Bank. Approximately one year later, they obtained refinancing from the Defendant with interest of two percent less than they had been paying. The Debtor signed a promissory note and granted a security interest in the vehicle to the Defendant which, on that same day, issued a check to Key Bank for the balance of the loan. Key Bank did not process the payment for ten days and then it was an additional 12 days before the Certificate of Title was returned to the Defendant. When the Defendant received the Certificate, it was processed in the normal course and mailed to DMV. From the date of the initial exchange to the date of perfection of the security interest was 27 days.

The Trustee filed this adversary proceeding to avoid the Defendant's security interest as preferential under § 547. At trial, the Debtor argued that the transaction met the "contemporaneous exchange" exception of § 547(c)(1) which requires that the Defendant prove that the transaction was meant to and in fact constituted a contemporaneous exchange for new value. The trustee countered that the substitution of one obligation for that of another does not constitute new value as defined by § 547(a)(2).

The court first rejected the Trustee's argument that the Defendant's loan should be treated as an enabling loan since it was substituted for an existing enabling loan. It then held that under the test found in In re Marino and given the circumstances of this case, the exchange was meant to be and in fact was contemporaneous. Moreover, the court held, citing precedent from the Seventh and Eighth Circuits, that payment by a second creditor of an existing obligation of the debtor constitutes new value under § 547 and is not comparable to the "substituted value" cases which § 547(a)(2) meant to address. Judgment to the Defendant.

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UNITED STATES BANKRUPTCY COURT  
DISTRICT OF OREGON

IN RE	)	
	)	
KATHERINE MCKAY,	)	Case No. 697-65404-fra7
	)	
_____ Debtor.	)	
	)	
RONALD R. STICKA, TRUSTEE,	)	Adv. Proc. No. 98-6055-fra
	)	
Plaintiff,	)	
v.	)	
	)	
U-LANE-O CREDIT UNION,	)	
	)	MEMORANDUM OPINION
_____ Defendant.	)	

Plaintiff is the Trustee in the Chapter 7 bankruptcy of Katherine McKay. He commenced this action to avoid an alleged preferential transfer from the Debtor to the Defendant Credit Union. A trial was conducted and the matter was taken under advisement. For the reasons that follow, I find for the Defendant.

BACKGROUND

The Debtor owns, jointly with a domestic partner, a 1991 Ford Taurus purchased on or about July 23, 1996. The purchase

1 was financed by a loan from Key Bank USA and secured by a duly  
2 perfected lien in favor of Key Bank.

3 On June 18, 1997, Debtor and her partner made application to  
4 the Defendant for a loan to refinance the vehicle loan with Key  
5 Bank. The application was accepted and the loan approved. The  
6 principal balance was \$6,418.26 at an interest rate of 9.25%,  
7 exactly two points lower than the Key Bank rate.

8 Contemporaneously with the promissory note, Debtor and her  
9 partner signed a security agreement granting a security interest  
10 in the vehicle to the Defendant. That same day, June 26, 1997,  
11 Defendant sent to Key Bank the sum of \$6,418.26. The payment was  
12 processed by Key Bank on July 6, 1997. The following day, the  
13 Bank endorsed the Certificate of Title in the box labeled  
14 "signature of security interest holder or lessor releasing all  
15 interest."

16 It is not clear exactly when the Certificate of Title was  
17 returned to the Defendant. The records of the Motor Vehicle  
18 Division reflect that the application for a certificate of title  
19 was received by the Motor Vehicles Division on July 23, 1997. In  
20 Oregon, the lien is deemed to be perfected as of the date the  
21 application is received by the Division. Or. Rev. Stat. § 803.097  
22 (1997). The Defendant's title clerk testified that, while she  
23 had no specific recollection, she ordinarily processed 30 titles  
24 a day, and ordinarily held a title for processing no more than  
25 two days. Assuming three days for the mail, she infers from the  
26 date the document was received by the Motor Vehicles Division

1 that she received the Certificate of Title from Key Bank no  
2 earlier than July 18. Debtor filed her petition for relief on  
3 September 22, 1997.

4 Plaintiff filed a complaint to avoid the Defendant's  
5 perfected security interest in the collateral as preferential  
6 under 11 U.S.C. § 547(b). In its Answer, the Defendant claims  
7 that its security interest was properly perfected and that the  
8 debt created between it and the Debtor was not on account of an  
9 antecedent debt.

10 DISCUSSION

11 Preferential Transfer

12 A transfer is preferential under the Bankruptcy Code, and  
13 thus potentially avoidable by the Trustee, if the conditions at  
14 11 U.S.C. § 547(b) are met:

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

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

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

21 (3) made while the debtor was insolvent;

22 (4) made—

23 (A) on or within 90 days before the  
date of the filing of the petition; or

24 (B) between ninety days and one year  
25 before the date of the filing of the  
petition, if such creditor at the time  
26 of such transfer was an insider; and

1 (5) that enables such creditor to receive  
2 more than such creditor would receive if-

3 (A) the case were a case under chapter  
4 7 of this title;

5 (B) the transfer had not been made; and

6 (C) such creditor received payment of  
7 such debt to the extent provided by the  
8 provisions of this title.

9 The loan was consummated on June 26, 1997, the date the  
10 Defendant sent the funds to Key Bank, and was not perfected until  
11 July 23, 1997, the date the Certificate of Title was received by  
12 the Department of Motor Vehicles.

13 Section 547(e) (3) (A) provides that a transfer is made "at  
14 the time such transfer takes effect between the transferor and  
15 the transferee, if such transfer is perfected at, or within 10  
16 days after, such time . . . ." Thus, if perfection occurs within  
17 the 10 day period, the transfer would not be deemed to be on  
18 account of an antecedent debt and would not be preferential under  
19 the Code. That is clearly not the case here, however.

20 Because perfection of the security interest occurred within  
21 90 days of the petition date and the other requirements of §  
22 547(b) are present (or, at least, uncontested by the Defendant),  
23 a *prima facie* case under § 547(b) has been made by the Trustee.  
24 In order to prevent avoidance of its security interest, the  
25 Defendant must demonstrate that it meets one of the exceptions  
26 found at § 547(c).

Enabling Loan Exception

Section 547(c) (3) is the exception for so-called "enabling

1 loans," or loans which are earmarked to purchase specific  
2 property. That section reads as follows:

3 (c) The trustee may not avoid under this section a  
4 transfer- \* \* \*

5 (3) that creates a security  
6 interest in property acquired by  
7 the debtor-

8 (A) to the extent such security  
9 interest secures new value that was-

10 (i) given at or after the signing  
11 of a security agreement that  
12 contains a description of such  
13 property as collateral;

14 (ii) given by or on behalf of the  
15 secured party under such agreement;

16 (iii) given to enable the debtor to  
17 acquire such property; and

18 (iv) in fact used by the debtor to  
19 acquire such property; and

20 (B) that is perfected on or before  
21 20 days after the debtor receives  
22 possession of such property;

23 The Trustee argues that the loan made by the Defendant is an  
24 extension of the original enabling loan because it was used to  
25 replace the enabling loan from Key Bank. Because the Defendant's  
26 loan was not perfected within the 20 days allowed by § 547(c)(3),  
nor was Key Bank's lien assigned to the Defendant, perfection of  
the Defendant's security interest constitutes an avoidable  
preferential transfer according to the Trustee.

I do not agree. The Defendant was a new creditor, not the  
same creditor which made the original loan. New money was  
advanced with different and more beneficial terms. The loan was

1 not given to enable the Debtor to acquire the vehicle, nor was it  
2 used for that purpose; the loan was used to satisfy a pre-  
3 existing loan. The loan was therefore not an enabling loan  
4 subject to the 20 day deadline to perfect under § 547(c)(3).

5 Contemporaneous Exchange Exception

6 At trial, the Defendant argued, and presented evidence to  
7 support its position, that the contemporaneous exchange exception  
8 found at § 547(c)(1) is applicable. Even though that defense was  
9 not specifically included in Defendant's Answer<sup>1</sup>, it was  
10 presented without opposition from the Plaintiff and will be  
11 considered by this court. See Fed.R.Civ.P. 15(b), made applicable  
12 by Fed.R.Bankr.P. 7015. The exception states that the transfer  
13 may not be avoided to the extent it was

14 (A) intended by the debtor and the creditor to or for  
15 whose benefit such transfer was made to be a  
16 contemporaneous exchange for new value given to the  
17 debtor; and

18 (B) in fact a substantially contemporaneous exchange;

19 The Defendant has the burden of proof with respect to  
20 showing that the exchange was intended to be contemporaneous for  
21 new value and that the exchange was in fact contemporaneous. The

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22 <sup>1</sup> It could be argued that Defendant's affirmative defense  
23 that the transfer was not on account of an antecedent debt  
24 encompasses the contemporaneous exchange exception. It has been  
25 stated that "[t]he underlying rationale behind the  
26 contemporaneous exchange exception 'is a simple one, excepting a  
transfer that is really not on account of an antecedent debt,'  
but is instead a substantially contemporaneous exchange for new  
value." In re Marino, 193 B.R. 907, 915 (BAP 9th Cir. 1996),  
aff'd 117 F.3d 1425 (9th Cir. 1997) (internal citations omitted).

1 Code does not define "contemporaneous," so it has been left to  
2 case law to make the determination. In this Circuit, the leading  
3 case in this area is In re Marino, 193 B.R. 907 (BAP 9th Cir.  
4 1996), aff'd 117 F.3d 1425 (9th Cir. 1997). That court stated:

5 While there will be litigation involving what is  
6 substantially contemporaneous in fact, a court need  
7 only look to the facts and circumstances of the case  
8 and determine whether the delay in perfection was  
reasonable. The concern over lack of an objective  
standard is illusory, given that facts and  
circumstances will differ with each particular case.

9 193 B.R. at 915. The court adopted the "facts and circumstances"  
10 standard over another line of cases which hold that  
11 contemporaneity in fact is present only when perfection occurs  
12 within 10 days of the underlying transfer as provided by §  
13 547(e) (3) (A). The contemporaneous exchange exception is not  
14 available if the security interest relates to an enabling loan.  
15 In re Vance, 721 F.2d 259 (9th Cir. 1983).

16 I find from the evidence presented that the exchange was  
17 intended to be contemporaneous. The Debtor and her partner  
18 signed a security agreement at the same time that they signed the  
19 promissory note. Both the Debtor and the Defendant clearly  
20 intended that the security interest and the loan be  
21 contemporaneous. I also find from the evidence that the transfer  
22 was contemporaneous in fact. There was a ten day delay between  
23 the time that the Defendant sent the money to Key Bank and the  
24 date that Key Bank processed the payment. It appears there was a  
25 further delay by Key Bank in returning the Certificate of Title  
26 showing its release of lien. Once received by the Defendant, it



1 appears that the Certificate was processed in the normal course  
2 and sent to DMV for filing and perfection of Defendant's security  
3 interest. Given these circumstances, the transfer was in fact  
4 contemporaneous.

5 The Trustee argues that even if the exchange was  
6 contemporaneous, it was not of "new value" as required by §  
7 547(c) (1) (A). New value for purposes of § 547 is defined at §  
8 547(a) (2) :

9 "new value" means money or money's worth in goods,  
10 services, or new credit, or release by a transferee of  
11 property previously transferred to such transferee in a  
12 transaction that is neither void nor voidable by the  
13 debtor or the trustee under any applicable law,  
14 including proceeds of such property, but does not  
15 include an obligation substituted for an existing  
16 obligation.

17 The Trustee's argument points to the last part of the definition  
18 which states that new value does "not include an obligation  
19 substituted for an existing obligation." He asserts that a  
20 refinancing necessarily substitutes the second loan for the first  
21 obligation.

22 I agree that a new loan with the same or similar terms  
23 substituted for an earlier loan from the same creditor may not  
24 constitute new value under § 547(c).<sup>2</sup> That is not the case here,  
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26 <sup>2</sup>The Third Circuit has stated with respect to substituted  
obligations: "In principal, a bankruptcy statute's section on  
voidable preferences should basically read as follows: 'If a  
creditor tries to change his position after this extension of  
credit in order to improve his lot in an anticipated bankruptcy  
(or other collective) proceeding, or if the debtor at the behest  
of such creditor so tries to change the position for such  
creditor in order to improve such creditor's lot in an  
anticipated bankruptcy . . . the creditor must return any

1 however. Here, a new creditor provided new money on more  
2 favorable terms to the Debtor in order to pay off an earlier  
3 obligation to another creditor.

4 The Eighth Circuit had to determine whether new value was  
5 advanced by a creditor when the creditor made payments to other  
6 creditors of the debtor. The creditor argued that this met the  
7 "new value" exception found at § 547(c)(4).<sup>3</sup> The trustee argued  
8 that it was not new value because it merely substituted the later  
9 obligation for the earlier obligations. In holding that the  
10 payments constituted new value, the court stated:

11 we are convinced that the trustee misconstrues section  
12 547(a)(2) when he argues that [the creditor's] payment  
13 of [the debtor's] debts to third parties constituted  
14 'an obligation substituted for an existing obligation.'  
15 What [the creditor] contributed for [the debtor's]  
16 benefit was money, albeit paid to creditors rather than  
17 directly to [the debtor]. [The creditor's]  
18 contribution therefore falls squarely within the  
19 definition of new value, and is in no way comparable to  
20 'substituted obligation' cases, in which creditors  
21 postpone collecting debts by substituting a new  
22 obligation of the debtor's for the old one.

23 In re Bellanca Aircraft Corp., 850 F.2d 1275, 1280-1281 (8th Cir.  
24 1988).

25 In a case from the Seventh Circuit, a creditor retained a  
26 security interest in iron mines that the debtor had purchased  
from another party. As part of the deal, the creditor agreed to

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27 advantage so obtained'." In re Spada, 903 F.2d 971 (3d Cir.  
28 1990) (internal citation omitted).

29 <sup>3</sup>§ 547(c)(4) generally denies avoidance of a preferential  
30 transfer to the extent that the creditor subsequently advances  
unsecured new value.

1 guarantee a \$6 million debt that the debtor owed to a second  
2 creditor which also had a lien on the mines. The second debt  
3 came due, and the debtor asked the first creditor for help. The  
4 first creditor paid off the debt to the second creditor and was  
5 given iron pellets from the debtor in exchange. The debtor then  
6 filed bankruptcy less than 90 days later. The trustee sought to  
7 avoid the payment to the creditor from the debtor as a  
8 preferential transfer. In response to the creditor's claim that  
9 the transaction met the contemporaneous exchange exception at §  
10 547(c)(1), the trustee argued that new value was not given by the  
11 creditor because it merely paid off another creditor. In  
12 rejecting that view and holding that new value was given, the  
13 court cited with approval the holding in Bellanca Aircraft Corp.  
14 that a creditor who pays off another creditor is contributing new  
15 value to the debtor. "A payment of cash that gets an importunate  
16 secured creditor off the debtor's back is a boon to the debtor .  
17 . . ." Matter of EDC, Inc., 930 F.2d 1275, 1282 (7th Cir. 1991).

18 The only real difference in facts between Matter of EDC and  
19 the present case, is that in the present case the Debtor granted  
20 the Defendant a security interest in the collateral rather than  
21 give the collateral to the creditor. The difference is not  
22 significant for purposes of determining whether new value was  
23 given. The security interest was granted in exchange for new  
24 value just as the payment of iron pellets was made in exchange  
25 for new value.

26 CONCLUSION

1           The transaction between the Debtor and the Defendant in  
2 which the Defendant received a perfected security interest in  
3 Debtor's vehicle in exchange for a payment in cash to Debtor's  
4 creditor Key Bank constituted a contemporaneous exchange under §  
5 547(c)(1). The Defendant's lien is therefore not avoidable as a  
6 preferential transfer under § 547(b). Judgment will be entered  
7 consistent with this Memorandum Opinion.

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11                           FRANK R. ALLEY, III  
12                           Bankruptcy Judge  
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