Mitchell v. Phipps, et al., Adversary No. 89-3267
In re Brookfields, Inc., Case No. 388-11451-ELP7

4/2/90 CEL Unpublished

The trustee initiated this action for recovery of an avoidable preferential transfer made to a creditor and the creditor's attorney within 90 days of filing. After a default was taken against the creditor, the trustee pursued his claim against the creditor's attorney as the "initial transferee" under § 550(a)(1). The creditor's attorney argued that he was a mere conduit and not the recipient of a preferential transfer.

Unlike most of the cases, this case did not involve a transfer within the extended insider period but rather within the 90-day period. Nor did this case involve an unbenefited transferee. The payment to creditor's attorney was not a mere pass through of a payment because the creditor's attorney retained a beneficial, non-passed through portion of the preferential payment as his fee. Thus the creditor's attorney cannot escape a literal application of § 550(a)(1) which requires recovery from an initial transferee.

UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF OREGON

In Re:	)	Case No. 388-01451-P7
BROOKFIELDS, INC., an Oregon corporation,	)	
Debtor.	)	
JOHN MITCHELL, Trustee in Bankruptcy,	)	Adversary No. 89-3267
Plaintiff,	)	
v.	)	MEMORANDUM OPINION
SCOTT and KRISTI PHIPPS and TERRY SUNDKVIST,	)	
Defendants.	)	

Plaintiff trustee has filed a complaint seeking recovery of an alleged pre-bankruptcy preferential transfer within 90 days to a creditor of the debtor and the creditor's attorney. The transfer by the debtor of $6,500 was by checks made payable to the creditor and his attorney. Default has been taken by the plaintiff trustee against the creditor. Trustee

seeks recovery from the attorney who had placed all the proceeds in his trust account and thereafter paid himself his fee of $2,164.50 and remitted the balance to his client, the creditor, for the amount retained. Trustee seeks recovery from the attorney as the "initial transferee" under the language of 11 U.S.C. § 550(a)(1). The defendant urges that he was not a creditor of the debtor, but that he was a mere conduit and a joint payee of the check without his demand therefor and received from the debtor no preferential transfer.

The parties have submitted the proceedings after oral argument and memoranda for determination on the record.

The courts have struggled with the literal application of 11 U.S.C. § 550(a)(1) where equitable considerations seem to make its application harsh to unbenefitted transferees. Most of such cases involve the enlarged preferential period in guarantor situations in which the trustee is seeking recovery of a transfer after 90 days to a creditor who holds an insider's guarantee of the debtor's obligation. The cases are split and a number are collected in Matter of Installation Services, Inc., 101 B.R. 282 (Bankr. N.D. Ala. 1989). The court has not found a case apposite on its facts to this case in which the transfer was made within the 90 day period before bankruptcy.

The broad policy appears to support the position of the trustee. The defendant Sundkvist was not a creditor of the

trustee. He therefore in receiving and exercising dominion over and obtaining benefit from the transfer received at best as to the debtor a transfer without consideration, and it is no more inequitable to require its repayment than it is to require an ordinary innocent preferred creditor to do the same.

As the court notes in Matter of Installation Services, Inc., 101 B.R. at 284:

> The literal reading of § 550(a) is adopted here because it is believed to express Congressional policy favoring equality in distribution, a desirable goal in the management of debtors' estates.

Also in Insider Guaranties and the Law of Preferences, 55 Am. Bankr. L.J. 343, 347 (1981) author, Thomas E. Pitts, Jr., notes:

> As hard as one searches, one is unable to uncover any material evidence in the Code or its legislative history that Congress intended paragraph 550(a)(1) to operate less than literally merely because only one of the potential defendants designated in that paragraph supplies the factual predicate for avoiding a transfer.

It is troublesome to apply the preferential transfer concept to a transfer to a non-creditor. But see In re C-L Cartage, Inc., 70 B.R. 928 (Bankr. E.D. Tenn. 1987) (wherein the court found an avoidable transfer relating to transfers to a correspondent, not creditor, bank beneficial to an insider of the debtor). Therein the court in allowing recovery against the bank

for transfers within the 90 day period, but not within the extended insider period stated:

> Thus, the court rejects a literal reading of § 550(a)(1) on this point but adopts a literal reading on the issue of whether the bank is liable as an initial transferee despite not being a creditor.

C-L Cartage, 70 B.R. at 934.

Protection of transfers to non-creditor initial or mediate transferees from recovery by trustees could lead to a practice of such transfers until the 90 day period has passed, thus frustrating the policy of vulnerability of preferential transfers.

This court concludes that it cannot deviate from the expressed congressional language. See In re Coastal Petroleum Corp., 91 B.R. 35, 38 (Bankr. N.D. Ohio 1988). There the court held:

> The language of § 550 is clear to state that recovery may be had from the initial transferee . . . or the entity for whose benefit the transfer was made . . . . That language is not only unambiguous but is also unconditional. To the extent avoided, the trustee may seek recovery under § 550(a)(1) against the creditor or against the insider but is limited to a single recovery.
>
> Courts which have chosen to ignore the letter of § 550(a)(1) have done so on equitable grounds. (citations omitted). The inescapable conclusion remains, however, that courts must apply the law as enacted by the Congress. The legislative history of § 550(a)(1) is silent to indicate a meaning

> different from the statutory language. Since the enactment of the Bankruptcy Code in 1978, Congress has twice amended the Code, in 1984 and 1986, respectively. On neither occasion did the Congress deem it necessary to alter or amend the language of § 550(a)(1). Thusly, we are constrained to an application of the literal provisions of the statute which clearly expresses congressional intent. Where, as here, the statutory language expresses congressional intent, a court may not read another meaning into the statute to arrive at a more preferable result. See, U. S. v. Turkette, 452 U.S. 576, 580, 101 S.Ct. 2524, 69 L.Ed.2d 246 (1981), ("Where the language of the statute is unambiguous, in the absence of a clearly expressed legislative intent to the contrary, that language must ordinarily be regarded as conclusive."); (citations omitted).

Reference is made to a case relied on by the defendant in oral argument. In that case, In re Fabric Buys of Jericho, Inc., 33 B.R. 334 (Bankr. S.D.N.Y. 1983), the avoidable preferential transfer was made to settle a disputed account with a third party. The payment was made into the attorney's escrow and then transferred to the client. The court stated:

> The Hopgood firm acted as a mere conduit of funds from Fabric Buys to Unitrac . . . . That such amount was funneled through the escrow account does not make Unitrac's lawyer an initial transferee.

Fabric Buys, 33 B.R. at 337.

In the case at bar, however, the representations are not of a mere pass through of the payment, but a beneficial, non-passed through sum of $2,164.50.

The payment in this case was preferential to the

client. By taking beneficial dominion over a portion of that preferential payment delivered to him, within 90 days of the bankruptcy, Sundkvist did not fall within classes of entities which have escaped literal application of § 550(a). See also Matter of Milwaukee County Conservation, 47 B.R. 846 (Bankr. E.D. Wis. 1985).

This Memorandum Opinion contains the court's Findings of Fact and Conclusions of Law and pursuant to Bankruptcy Rule 7052 they will not be separately stated.

Separate Judgment consistent herewith will be entered.

DATED this _____ day of March, 1990.

_____
C. E. LUCKEY
Bankruptcy Judge