UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF INDIANA
HAMMOND DIVISION

IN RE:	)	
	)	
LSF TRANSPORTATION, INC.,	)	Case No. 01-63512 JPK
	)	Chapter 7
Debtor.	)	
*******************************		
KENNETH A. MANNING, Trustee,	)	
	)	
Plaintiff,	)	
	)	
v.	)	Adversary No. 03-6189
	)	
AMY J. FAURE, and	)	
FAURE BROTHERS CORP.,	)	
	)	
Defendants.	)	

AMENDED FINDINGS OF FACT AND CONCLUSIONS OF LAW AND ORDER

This adversary proceeding was commenced by a Complaint, seeking to avoid and recover certain preferential transfers pursuant to sections 544(b), 547, 548 and 550 of the U.S. Bankruptcy Code ("Code") and § 32-1-7-1[1] *et. seq*. of the Indiana Code, filed on June 17, 2003 by the plaintiff, who is the Trustee of the Chapter 7 Bankruptcy estate of LSF Transportation Inc. ("Trustee").[2] A joint answer to the Complaint was filed by Amy Faure ("Amy") and Faure Brothers Corp. ("Faure Brothers"), together defendants ("Defendants") on August 7, 2003. By an order dated February 25, 2004, the Court ordered the parties to file a joint stipulation of facts. The parties have complied with the Court's order by their filing of a Stipulation of Uncontested Facts, together with attached exhibits, on April 8, 2004. In its May 6, 2004 Order Scheduling Trial, the Court ordered the parties to jointly prepare a final pre-trial order. Each party was also ordered to file a trial brief. Both parties complied with said order. A trial to the

[1] Perhaps § 32-**1**-7-1 is a typo, as Indiana Uniform Fraudulent Transfer Act was embodied in § 32-2-7-1 *et. seq*. Now it is embodied in I.C. § 32-18-2-1 *et. seq*.

[2]By and through a Final Pretrial Order, the plaintiff has voluntarily withdrawn all claims related to AIM National Lease and all claims alleging fraudulent transfers or conveyances.

bench of this adversary proceeding was held on October 29, 2004, at which point the Court entertained the testimony of Jerry Helton ("Helton"), an accountant/controller for Faure Brothers.

In its November 10, 2004 Order Establishing Briefing Schedule, the Court ordered the parties to submit their limited initial post-trial briefs by December 31, 2004.[3] Each party was also permitted to submit, by January 31, 2005, one brief in reply to the other's initial brief. Both parties have taken advantage of that opportunity. This matter was submitted for decision on February 1, 2005.

JURISDICTIONAL STATEMENT

The Court has subject matter jurisdiction with respect to this adversary proceeding by operation of 28 U.S.C. § 1334(b), 28 U.S.C. § 157(a) and N.D.Ind.L.R. 200.1. This adversary proceeding constitutes a core proceeding under 28 U.S.C. § 157(b)(2)(F) and thus this Court has jurisdiction to enter a final judgment on the complaint.

FACTS

LSF Transportation Inc., ("Debtor") filed a voluntary petition ("Petition") seeking relief pursuant to Chapter 7 of the Code on August 20, 2001. The facts in this case are largely not in dispute and are for the most part embodied in a Stipulation of Uncontested Facts filed by the parties. In pertinent part, the stipulation states that Amy was the sole shareholder, officer and director of the Debtor, as well as of Faure Brothers. Faure Brothers was a holding company of the Debtor. Both of the corporations conducted their business from a common location. The Debtor was in the trucking business as a contract carrier for hire. The Debtor ceased

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[3]The briefs were to be limited to the discussion of the concept of "constructive trust" under Indiana law, and whether that concept encompasses a transaction originating from a mistake or error or whether that doctrine is limited to transactions origination from some form of fraudulent conduct.

operations by July 26, 2001. The Debtor was also insolvent during the ninety (90) days immediately prior to the petition date. [Stipulation, ¶ 4]. Both Faure Brothers and Amy are 'insiders' as defined by 11 U.S.C. §101(31). The facts are herein set out as they relate to each claim.

Claim I: Trustee's Requested Recovery of $11,474.39

The facts upon which this first claim is based are not extraordinary. In order to obtain credit from Comdata ("Comdata") to purchase fuel for its trucks, the Debtor was required to post an irrevocable standby letter of credit in its favor. The Debtor sought to obtain the letter of credit from the Mercantile National Bank of Indiana ("Bank"); as a condition of providing it, the Bank required Amy, as a director/shareholder of the Debtor, to personally guarantee payment of the credit extended by the letter of credit. Amy would not be implicated in this matter, provided the Debtor had remained current on its obligations to Comdata. All our wishes aside, the Debtor defaulted on its obligation to Comdata by August 10, 2001 and Comdata exercised its rights against the letter of credit. The Bank, as the issuer of the letter of credit, as well as the holder of various accounts maintained by the Debtor, subsequently honored Comdata's request by paying Comdata the default amount, $11,474.39. Contemporaneously with its payment to Comdata, the Bank charged the Debtor's checking account maintained with the Bank for the same amount.

Claim II: Trustee's Requested Recovery of $66,092.01

Faure Brothers was also a holder of a separate checking account at the Bank. On or about July 6, 1999, Pat Duke ("Duke"), an employee of Faure Brothers, was in possession of thirty (30) checks totaling $109,856.20. Those checks had been endorsed to the order of Faure Brothers. In order to deposit those 30 checks into Faure Brothers' bank account, Duke utilized two (2) deposit tickets. [Plaintiff's Exh. 2].

Also on or about July 6, 1999, Duke was in receipt of twenty (20) checks totaling

$43,764.19, checks which have been made payable to the Debtor. Like with the 30 checks payable to Faure Brothers, it was the responsibility of Duke to deposit the 20 checks payable to the Debtor to the Debtor's checking account. On or about July 6 or 7, 1999, the employee of Faure Brothers brought both groups of checks (20 payable to the Debtor and 30 payable to Faure Brothers) to the Bank.

On July 7, 1999, the Bank issued a receipt properly showing that a deposit of $43,746.19 had been made to the Debtor's account. [Plaintiff's Exh. 4]. Also on July 7, 1999, the Bank issued a receipt showing that a deposit of $109,856.20 had been made to the account of Faure Brothers. [Plaintiff's Exh. 5]. The Debtor's bank statement issued on July 30, 1999, however, indicates that a deposit of $109,856.20 had been made into its account. Likewise, on July 30, 1999, a bank statement issued to Faure Brothers indicates that a deposit of $43,764.19 had been made into its account. Thus, the Debtor's account was credited for an excess amount of $66,092.01[4] while the account of Faure Brothers was credited for $66,092.01 less. Subsequent to July 30, 1999, on several occasions the Debtor's checking account into which the over credit had been made had a balance of less than $66,000.00.

Both of the errors were brought to the Bank's attention by Mr. Helton nearly two years later, on June 7, 2001. Also on June 7, 2001, the Bank issued a document entitled "advice of charge," a document which was signed by Mr. Helton, indicating that the sum of $66,092.01 had been debited from the Debtor's account and that the same amount had been credited to the account of Faure Brothers. [Plaintiff's Exh. 8].

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[4] In various documents filed with the Court, the parties at times state that the differential in the amounts of the two deposits to have been $66,092.01, while at other times they state the differential to have been $66,292.01. The difference between $109,856.20 and $43,764.19 is $66,092.01, which correlates precisely to the Bank's ultimate debit/credit reversal which reconciled the two accounts.

Claim III: Trustee's Requested Recovery of $83,698.49

On January 22, 2001, Faure Brothers was in receipt of a number of checks totaling $83,698.49. Those checks were made payable to Faure Brothers. Those checks were entrusted to the employee of Faure Brothers Billiejo Cripe ("Cripe"), an accounts receivable clerk, who bore the responsibility of depositing checks into Faure Brothers' account. Everything would be okay so far, if not for what had actually transpired. Instead of depositing the subject checks to the Faure Brothers' account, Mr. Cripe mistakenly entered the checks on the Debtor's bank deposit tickets. [Plaintiff's Exh. 9]. As a result, a deposit of $83,698.49 was made to the Debtor's account. Shortly thereafter, on February 13, 2001, Mr. Helton advised the Bank of this error made by the Faure Brothers' employee, and that the $83,698.49 should be instead credited to the Faure Brothers' account. A statement issued by the Bank on February 28, 2001, as it relates to Faure Brothers' account, indicates that such credit of $83,698.49 was entered on February 13, 2001. [Plaintiff's Exh. 10]. A debit for the same amount from the Debtor's account, however, was not made until June 6, 2001, as reflected on the Debtor's Bank statement of June 29, 2001. [Plaintiff's Exh. 11].

DISCUSSION

The Trustee seeks to recover three (3) alleged preferential transfers from the Defendants:

1. From Amy, as a "creditor" of the Debtor (due to her contingent right to recover from the Debtor any amount she would have had to pay on her personal guarantee of the letter of credit), whom the Trustee asserts received a benefit from the transfer made by the set-off of the Debtor's account by the Bank in the amount of $11,474.39;

2. From Faure Brothers, the amount of the over credit of $66,092.01 derived from drafts payable to Faure Brothers erroneously credited by the Bank to the Debtor's

account, which the Trustee alleges were the subject of an avoidable preference when the credits were reversed by the Bank into the proper account; and

3. From Faure Brothers, the amount of the over credit of $83,698.49 derived from drafts payable to Faure Brothers erroneously deposited by an employee of Faure Brothers into the Debtor's account, which the Trustee alleges were the subject of an avoidable preference when the credits were reversed by the Bank into the proper account.

In response, the Defendants argue that not only are these transactions not transfers, but if they were, they were not transfers of property of the estate, or of property in which the estate had an interest. In addition, with respect to the latter two transactions, the Defendants argue for the imposition of a constructive trust due to mistake. Each claim will be addressed in turn.

A. The $11,474.39 Claim

The Trustee asserts that he is entitled to recover from Amy the sum of $11,474.39, stemming from a payment made by the Bank to Comdata and the Bank's subsequent draw on the Debtor's account for a debt which Amy, an insider, personally guaranteed. The Bank's payment to Comdata, and its subsequent debit from the Debtor's account, *ipso facto* discharged Amy's obligation to the Bank based on her personal guarantee. This is where the Trustee finds his potential for recovery under 11 U.S.C. §§ 547 and 550, and seeks to recover the benefit Amy received. Amy, on the other hand, vigorously contends that no such recovery is allowed, as setoffs are not transfers avoidable by § 547(b).

The heart and soul of Amy's argument is that the Trustee cannot seek recovery from her, without first pursing the Bank, thereby implicating 11 U.S.C. § 553.[5]

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[5] § 553. Setoff
(a) Except as otherwise provided in this section and in sections 362 and 363 of this title, this title does not affect any right of a creditor to offset a mutual debt owing by such creditor to the Debtor that arose before the commencement of the case under this title against a claim of such creditor against the Debtor that arose before the commencement of the case, except to the extent that – . . .

At the outset, the Court will note that neither have the parties presented to the Court, nor has the Court itself been able to unearth, any authority with similar issues presented in the realm of the facts of the case at bar. The issue at the heart of the Trustee's claim is whether a § 547(b) action can be sustained against a person who was a beneficiary of a transaction when no recovery could be sustained against an entity that was the direct recipient of the funds due to the application of setoff. The issue, being framed as such, appears to be one of first impression, at least in this Court's jurisdiction.

In order to avoid a preferential transfer, the Trustee must establish each element of § 547(b) by preponderance of the evidence as it relates to a particular creditor. *In re Golfview Developmental, Center Inc.,* 309 B.R. 758, 766 (Bankr. N.D.Ill. 2004); *In re Midwest Mobile Technologies, Inc.*, 304 B.R. 787 (Bankr. S.D.Ohio 2003); *In re M2Direct, Inc.*, 282 B.R. 60 (Bankr. N.D.Ga. 2002). Section 547(b) provides that:

> (b) Except as provided in subsection (c) of this section, the trustee may avoid any transfer of an interest of the debtor in property –
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> (1) to or for the benefit of a creditor;
>
> (2) for or on account of an antecedent debt owed by the debtor before such transfer was made;
>
> (3) made while the debtor was insolvent;
>
> (4) made –
>
> (A) on or within 90 days before the date of the filing of the petition; or
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> (5) that enables such creditor to receive more than such creditor would receive if –
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> (A) the case were a case under chapter 7 of this title;
>
> (B) the transfer had not been made; and
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> (C) such creditor received payment of such debt to the extent provided by the provisions of this title.

Amy's argument that the Trustee must first seek to avoid a transfer from the initial transferee – the Bank in this case – is unavailing. The case law is clear that § 547(b) provides the Trustee with two options: the Trustee may seek to avoid and recover preferential transfers from either the creditor to whom the transfer was made, or from the creditor who benefitted by the transfer: *In re Broad Street Associates*, 163 B.R. 68, 73 (Bankr. E.D.Va. 1993); *In re Helen Gallagher Enters., Inc.*, 126 B.R. 997, 1001 (Bankr. C.D.Ill. 1991); *In re C-L Cortage Co.*, 899 F.2d 1490, 1493 (6th Cir. 1990); *Midwest Mobile,* 304 B.R. 787; *Levit v. Ingersoll Rand Financial Corp.*, 874 F.2d 1186, 1190 (7th Cir. 1989). *See* also *In re International Admin. Services, Inc.*, 408 F.3d 689, 703-08 (11th Cir. 2005). In the case at bar, the Trustee chose to pursue the creditor who benefitted from the transfer, i.e. Amy, and seeks to recover the alleged preference from her under section 550(a).[6]

The rub for the Trustee in this case is that the "transfer" may be recovered from Amy under § 550(a) only to the extent it is avoidable under § 547(b). *Levit*, supra., 874 F.2d at 1186.

As one might imagine, the Trustee had a valid reason not to pursue the Bank. Generally, courts have held bank accounts are eligible for setoff in bankruptcy; See, *New York County Nat'l Bank v. Massey*, 192 U.S. 138, 146 (1904) [setoff should be allowed as between a bank and a depositor becoming bankrupt]; *In re Bennett Funding Group, Inc.*, 146 F.3d 136, 139-40 (2nd Cir. 1998); *In re Almacenes Gigante, Inc.*, 159 B.R. 638, 643 (Bankr. D.Puerto Rico 1993) ["[A] bank may setoff the monies deposited against the amount owed to it by the depositor if the deposit was a general one and the monies were withdrawable at will."]. [7] As the

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[6] § 550. Liability of transferee of avoided transfer

(a) Except as otherwise provided in this section, to the extent that a transfer is avoided under section 544, 545, 547, 548, 549, 553(b), or 724(a) of this title, the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from –

(1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or

(2) any immediate or mediate transferee of such initial transferee.

[7] In fact, given the first sentence of 11 U.S.C. §553(a) – that except as provided in sections 553, 362 and 363, Title 11 of the United States Code does not affect a creditor's right to setoff – it can be pretty persuasively argued that apart from the conditions imposed by the three designated sections, a creditor's right to setoff provided by nonbankruptcy law is absolute.

stipulation of the parties indicates, and the testimony at trial confirmed, the Debtor's bank account held at the Bank was a general checking account with the monies withdrawable at will. In addition, both parties, the Bank and the Debtor, held the position of creditor vis-a-vis each other, a position that arose pre-bankruptcy. Although in certain instances, perhaps, the allowance of a setoff is a decision that lies within the sound discretion of the bankruptcy court, generally setoffs are freely allowed; *Meyer Medical Physicians Group, Ltd. v. Health Care*, 385 F.3d 1039, 1041 (7th Cir. 2004) [discussing the mutuality requirement of § 553(a)].

The Trustee has not pursued the Bank, and even if he had, the application of § 553 would prevent the Trustee's recovery from the Bank. Moreover, there is ample authority that setoffs are not transfers. A reasonably recent decision elaborated on this principle:

> . . . (I)t is well settled that offsets are not transfers avoidable pursuant to § 547(b). *Braunstein v. Branch Group, Inc. (In re Massachusetts Gas & Electric Light Supply Co., Inc.)*, 200 B.R. 471, 473 (Bankr.D.Mass.1996); *Belford v. Union Trust Company (In re Wild Bills, Inc.)*, 206 B.R. 8, 12-13 (Bankr.D.Conn.1997); *Eckles v. Petco Inc., Interstate (In re Balducci Oil Co., Inc.)*, 33 B.R. 847, 852 (Bankr.D.Colo.1983).
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> 11 U.S.C. 101(54) defines the term "transfer" as follows: "transfer" means every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property or with an interest in property, including retention of title as a security interest and foreclosure of the debtor's equity of redemption 11 U.S.C. § 101(54). Conspicuously missing from that definition is the term "setoff." The omission was no accident.
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> The legislative history of the definition of § 101(54) clearly illustrates that Congress intended to exclude setoff from the "transfer" definition in order to assure that setoff would be treated exclusively under the provisions of § 553. *In re Massachusetts Gas & Electric Light Supply Co., Inc.*, 200 B.R. 471, 473 (Bankr.D.Mass.1996); *In re Wild Bills, Inc.*, 206 B.R. 8, 12- 13 (Bankr.D.Conn.1997); *In re Balducci Oil Co., Inc.*, 33 B.R. 847, 852 (Bankr.D.Colo.1983). That legislative history is captured in the following identical statements by Representative Edwards and Senator DeConcini, the House and Senate sponsors of the bills:
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> Section 101(40) defines "transfer" as in the Senate amendment. The definition contained in H.R. 8200 as passed by the House

> included "setoff" in the definition of "transfer." Inclusion of "setoff" is deleted. The effect is that a "setoff" is not subject to being set aside as a preferential "transfer" but will be subject to special rules.
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> *In re Massachusetts Gas & Electric Light Supply Co., Inc.* at 473 (footnotes and citations omitted).
>
> Indeed, § 553(a) provides:
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> Except as otherwise provided in this section and in sections 362 and 363 of this title, this title does not affect any right of a creditor to offset a mutual debt owing by such creditor to the debtor that arose before the commencement of the case under this title against a claim of such creditor against the debtor that arose before the commencement of the case. . . . 11 U.S.C. § 553(a) (emphasis supplied).
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> By preserving the right of setoff, and restricting its application under Title 11 only as noted in sections 553(b), 362 and 363 of the Bankruptcy Code, it is clear that Congress did not intend that setoffs be recoverable as voidable transfers under § 547(b). *See Lee v. Schweiker*, 739 F.2d 870, 873 n. 4 (3rd Cir.1984)(citing *F.D.I.C. v. Bank of America*, 701 F.2d 831, 836 (9th Cir.1983)); *In re Wild Bills, Inc*. at 13 (holding that the failure of § 553 to reference § 547 precludes an analysis of setoff under the latter provision).

In re Holyoke Nursing Home, Inc., 273 B.R. 305, 309-10 (Bankr. D.Mass. 2002) *aff'd,* 372 F.3d 1 (1st Cir. 2004). See also *In re Jenkins Enterprises, Inc.*, 289 B.R. 702 (Bankr. C.D.Ill. 2003). Amy has grabbed onto this proposition here, and rightfully so, by stating that because there is no transfer avoidable under § 547(b), no recovery under § 550(a) can be sustained against her. See *In re H & S Transp. Co., Inc.*, 939 F.2d 355 (6th Cir. 1991) [involving new value].

In order to prevail, the Trustee here would reinstate a proposition that has long been rejected. Mainly, whenever a transaction benefits third parties, such as the guarantor here, said transaction could be viewed as two transfers; one transfer to the lender and the other to the guarantor. Only in such case could a recovery be obtained against the so called second transferee even though transfer number one is missing.

The Seventh Circuit Court of Appeals in *Levit*, supra., 874 F.2d at 1186, rejected the two-transfer approach. The Trustee would like the Court to hold that because Amy received a benefit from the Bank's setoff, a benefit which no one here denies, that benefit was a transfer to her as far as she is concerned. Because, viewing it from the Debtor's perspective, there can only be one possible transfer resulting in more than one beneficiary, the Court rejects the Trustee's assertion. The *Levit* decision is instructive:

> [t]he Code, however, equates "transfer" with payments made. Section 101(50) . . . says that a transfer is a disposition of property. Sections 547 and 550 both speak of a transfer being avoided; avoidability is an attribute of the transfer rather than of the creditor. While lenders want to define transfer from the recipients' perspectives, the Code consistently defines it from the debtor's. A single payment therefore is one "transfer", no matter how many persons gain thereby.

Levit, 874 F.2d at 1195-96. Taking that logic a step further, the Court must conclude that because the Bank's setoff was not a transfer to the Bank as defined by section 101(50), it cannot be deemed a transfer to a beneficiary thereof.[8] Accordingly, as in *Holyoke Nursing Home*, 273 B.R. 305, the Trustee failed to establish a necessary element of section 547(b), mainly, that a transfer took place.

The Trustee's demand for recovery of $11,474.39 from Amy J. Faure is therefore denied.

B. The $66,092.01 and $83,698.49 Claims:

Because the analysis of both of these alleged preferential transfers is largely the same, the two transfers will be primarily addressed together.

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[8] The Court's conclusion would perhaps be different if instead of the Bank's exercise of its setoff right, the debtor made a payment, *via* a check or otherwise, which would eviscerate any further obligation on the part of the guarantor. A check payment, for example, would make it a transfer, and thus subject to the trustee avoidance powers pursuant to §§ 574(b) and 550. See *In re Herman Cantor Corp.,* 15 B.R. 747 (Bankr. Va. 1981); *In re Aerco Metals, Inc.*, 60 B.R. 77 (Bankr. N.D.Tex.1986). A transfer must be first avoided as a preference under § 547, then, and only then, may actual recovery be had under § 550. *In re DLC, Ltd.*, 295 B.R. 593 (8th Cir. BAP 2003), *aff'd*, 376 F.3d 819 (8th Cir. 2004).

The Trustee asserts that both of these transactions meet the requirements of 11 U.S.C. §547(b). In opposition, Faure Brothers argues that no transfers took place within the purview of section 547(b) between the Debtor and Faure Brothers, but that the Bank merely corrected errors. Alternatively, Faure Brothers contends that if those transactions were transfers, they were not transfers of property of the Debtor or of property in which the debtor had an interest. Faure Brothers also argues that if there was a transfer, the transfer was not "for or on account of an antecedent debt owed by the Debtor before such transfer was made" as required by § 547(b)(2). These are the only issues of contention here in the application of § 547(b).

In order to succeed, the Trustee must establish the elements of 11 U.S.C. §547(b), which are stated on page 7 above.

The focus of attention in this case is whether there was a "transfer of an interest of the debtor in property" "for or on account of an antecedent debt owed by the debtor before such transfer was made".

The term "debt" is defined by 11 U.S.C. §101(12) as "liability on a claim". The term claim, as relevant to this case, is defined in 11 U.S.C. §101(5) as follows:

> **(5)** "claim" means –
> **(A)** right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured...

This case does not involve performance under a contract, and thus 11 U.S.C. §101(5)(B) is not implicated.

The term "transfer" is defined by 11 U.S.C. 101(54) as follows:

> **(54)** "transfer" means every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with <u>property or with an interest in property</u>, including retention of title as a security interest and foreclosure of the debtor's equity of redemption. (Emphasis supplied).

The concept of "property or with an interest in property" which triggers the application of the definition of “transfer” under 11 U.S.C. §101(54) is to be distinguished from the form of “transfer” which triggers the potential application of 11 U.S.C. §547(b) – the former definitional provision is totally neutral as to the whose interest was “transferred” : section 101(54) merely describes what a “transfer” is, no matter who has interests in the object of the “transfer”. On the other hand, 11 U.S.C. §547(b) requires that the object of the transfer have been “an interest of the debtor in property”. For the purpose of the following analysis, the distinction between the concept of “property or an interest in property” within §101(54)’s definition of “transfer”, and the fact that 11 U.S.C. §547(b) allows recovery only if the “transfer” was of “an interest of the debtor in property” – must be constantly borne in mind.

Faure Brothers' contends that no “transfer” was made: this asserted construction of the term “transfer” is too restrictive. The Supreme Court, in determining the construction of the term 'transfer' as defined by § 101(54) of the Code, stated that "what constitutes a transfer and when it is complete is a matter of federal law." *Barnhill v. Johnson*, 503 U.S. 393, 112 S.Ct. 1386, 1389 (1992). The Fifth Circuit Court of Appeals stated:

> "the definition of 'transfer' under the Bankruptcy Code is comprehensive and includes every conceivable mode of alienating property, whether directly or indirectly, voluntarily or involuntarily. Given this broad meaning of ‘transfer’, the fixing of a non-statutory, judicial lien – such as the one created by Cullen's filing of its abstract of judgment – is avoidable as a preferential ‘transfer’ provided § 547(b)'s other requirements are satisfied."

Matter of Criswell, 102 F.3d 1411, 1415 (5th Cir. 1997). The Seventh Circuit Court of Appeals also relied on *Barnhill* when it stated that "the Bankruptcy Code's definition of a transfer is 'expansive'." *Warsco v. Preferred Technical Group*, 258 F.3d 557, 564 (7th Cir. 2001).

The record before this Court does not require the Court to take giant leaps in order to determine that each of the two transactions constitute a transfer within the purview of § 101(54). The Faure Brothers' argument that no transfer took place when the Bank corrected its error with respect to the $66,092.01 is clearly not supported by the facts. An Advice of

Charge, a document resulting from Mr. Helton's request to the Bank to correct the mistake, a document signed by Mr. Helton, has the following marking: **Transfer** From 11-47005 into 11-05469.[9] [emphasis supplied] [Plaintiff's Exh. 8]. In addition, the same Advice of Charge includes the following notation: Debits - 06/07/01. *Id.* Further, the Debtor's bank statement dated June 29, 2001, under the heading of Other Debits, has the following entry: Advices, Date 06/07, Amount 66,092.01.

The second of the alleged non-transfers requires the same conclusion; It was indeed a transfer. A monthly bank statement issued to the Debtor on June 29, 2001 bears the following description under the heading of Other Debits: "To Correct Debit Not Posted to This Acct For **TRF** 2-13-01, Date 06/06, Amount 83,698.49;" [emphasis supplied]. A monthly Bank statement issued to Faure Brothers on February 28, 2001 indicates that a deposit for the same amount had been made on February 22, 2001. [Plaintiff's Exh. 10; Defendant's Exh. 1]. In addition, Faure Brothers' bank statement dated June 29, 2001, under the heading of Other Credits, has the following notation: "To Reverse Debit of 2-13-01, Date 06/06, amount 83,698.46;" [Defendant's Exh. 2]. The trial testimony of Mr. Helton confirmed the same. The second of the transfers (involving $83,698.49) was made not to correct a mistake made by the Bank, but to correct a mistake made by the employee of Faure Brothers.

Given what is perhaps a limitless definition of a transfer, and the fact that it is difficult to conceive how something can be in one bank account and end up in the bank account of another without being "transferred" thereto, the Court concludes that the transactions involving both of the amounts, $66,092.01 and $83,698.49, were "transfers" from the Debtor's account into the account of Faure Brothers within the meaning of 11 U.S.C. §101(54). However, the fact

[9]The former account belongs to the Debtor while the latter account belongs to Faure Brothers.

that something was “transferred” does not speak to whether the object of the transfer was or was not “an interest of the debtor in property” under 11 U.S.C. §547(b).

While the United States Supreme Court and other authorities have decreed and emphasized the expansive and all inclusive manner in which a transfer constituting “disposing or parting with” property or an interest in property may be effected, it is up to State law to determine whether or not the object of the transfer was an “interest of the debtor in property” as required by 11 U.S.C. §5474(b); *In the Matter of Smith*, 966 F.2d 1527, 1530 (7th Cir. 1992). It is this concept of property law that in part causes this case to be so complex.

The case is also made complex by the issue of whether or not there was a “debt” between the Debtor and Faure Brothers.

This is a case in which there are no precedents, in essence a case of first impression. This is a case in which the sterile mechanical application of a few legal principles leads nowhere, because there has been no other reported case like this. This is a case in which the Court has determined that there is a correct result – totally in accordance with principles of the Bankruptcy Code. But the extrapolation of a decision in this case is one which the Court must “cut from whole cloth”, a phrase which the attorneys involved in this litigation will understand, having suffered through the same litany of hoary cases I did when learning the ABC’s of the law in law school.

In arriving at its decision, the Court must be cognizant of the fact that federal bankruptcy courts are not, as is commonly incanted, “courts of equity”. Bankruptcy courts are required to adhere to the dictates of the statutory law and of precedentially binding caselaw which govern the cases that come before them. Bankruptcy courts are not courts of equity; rather, they are courts which apply the law as it has been laid out.

Given the foregoing, be forewarned: this is not a decision in which extensive incantations to statutory or caselaw authority will be made. Those authorities just don’t exist with respect to the unique facts of this case, at least as those authorities are reflected in reported decisions which the parties have cited, or which the Court has otherwise discovered.

We start with the proposition that in order to succeed, the Trustee must establish that the Debtor made a "transfer" of "an interest in property of the debtor", "for or on account of an antecedent debt owed by the debtor before such transfer was made."

The focus of this case is <u>not</u> upon whether or not a "transfer" was made. Clearly, something was transferred from a deposit account of which the Debtor was the owner, to Faure Brothers. But 11 U.S.C. §547(b) requires that the object of the passing or exchanging between one party and another be "an interest <u>of the debtor</u> in property".

The Court is of the opinion that much of the confusion in this case has arisen because the "transfer" involves credits and debits in deposit accounts, a confusion the Court has facilitated by focusing a sequence of briefs on the issue of "constructive trusts". This case would be perhaps much more fundamentally comprehensible if the object of the exchange had been baseballs, delivered erroneously to side-by-side bins rented by different entities in a warehouse.

So, let's perceptually begin with the thought that what is involved here are two shipments of baseballs, one ordered by an entity doing business as "Cubs Crafts" and the other ordered by an entity doing business as "Yankees Yippies". The shipment ordered by "Cubs Crafts" (an order placed late in the 2004 season for use in the 2005 season) is destined to be imprinted with the "autograph" of Sammy Sosa, and the shipment ordered by "Yankees Yippies" is destined to be imprinted with the "autograph" of Alex Rodriguez. Each order is of an identical product, from the same supplier, but Cubs Crafts ordered only 43,764 balls, while Yankees Yippies ordered 109,856 balls. Both Cubs and Yankees rent warehouse space in the same building, and as luck would have it the storage areas for their respective balls are immediately adjacent to each other. Well, as is true with a number of things involving the Cubs, there is an error, and the 109,856 balls destined for Yankees ends up in the Cubs bin, and the 43,764 balls destined for Cubs ends up in the Yankees bin, due to a delivery error by the shipping company, which simply failed to correctly read the bills of lading and as a result put each shipment in the wrong adjacent bin. The error is quickly discovered when each of the companies is billed for the shipments, and each has an employee spend hours counting out the number of balls received and compare that number to the amount ordered.[10] When the error is known to both, Cubs Crafts could have simply transferred 66,092 balls from its bin to the adjacent Yankees Yippies' bin. Under this scenario, clearly no one would contend that Cubs Crafts had any property interest in the 66,092 extra balls delivered to it, and no one would contend that Cubs Crafts' transfer of the 66,092 balls to Yankees Yippies was in relation to any debt owed by Cubs to Yankees.

However, Cubs Crafts, having failed to anticipate that Derrick Lee would replace Sammy Sosa, doesn't have enough balls for the 2005 season to imprint with the autograph of Derrick Lee, and rather than return the extra balls immediately to Yankees, keeps them and actually diminishes its store of warehoused balls several times below 66,092. This retention and use is done with the knowledge and consent of Yankees Yippies, which doesn't care because both companies are owned by the same ownership group, and Yankees knows Cubs will get other balls later that can replace the ones it allows Cubs to keep and use in its business. Finally, after A-Rod knocks in 10 runs in one game and reestablishes himself as a premium player in the eyes of Yankees' fans, Yankees needs more balls for A-Rod appreciation night, and at that point demands that Cubs Crafts turn over the 66,092 extra balls that should have delivered to it, to it. Clearly, Yankees' acquiescence in Cubs' retention and use of the extra baseballs gave rise

[10] The Yankees were suspicious from the git-go because, accustomed to lots of scoring, they seemed to be far short of the number of balls they ordered; the Cubs were a little slower, being accustomed to losing track of the count.

to a property interest in the extra balls in Cubs, a loan if you will – one clearly intended by Yankees – and the transfer of the balls later satisfied the debt owed by Cubs to Yankees for the use and sale of the 66,092 extra balls.

The 2005 season progresses, and Yankees Yippies orders another shipment of baseballs. A similar mixup occurs, but this time the error is caused when a new employee shared by both companies to submit orders states the wrong warehouse bin for a shipment of 83,968 baseballs ordered by Yankees Yippies. This error is easily discovered – even the Cubs employees notice that their pile is a lot larger. Yankees needs the balls immediately, so it requires Cubs to transfer 83,698 balls from Cubs' bin to Yankees', which is done promptly, and without Cubs Crafts using any of the 83,698 over shipment. As was true with the first instance, the initial misdelivery didn't give Cubs any property interest in the 83,698 balls. However, unlike the first instance, because the balls were never used by Cubs in any way, there was no creation of a property interest in Cubs due to its retention of possession of, and use of, the entire shipment *en masse*.

We next go to the proposition that negotiable instruments payable to the order of a designated payee are "property" or an "interest in property" of the designated payee, just as baseballs ordered from a supplier create a property interest in the purchaser and in no one else. Thus, checks payable to the Debtor were the property of the debtor, to the exclusion of anyone else, and checks payable to Faure Brothers were the property of Faure Brothers to the exclusion of anyone else.

When negotiable instruments are endorsed, the character of the ownership interests in them is determined by the nature of the endorsement. Thus, a check payable to "X" as the payee, which the payee "X" endorses as "Pay to the order of 'Y'" becomes a right to payment owned by "Y" by presentment of the check to the payor (usually a bank). In this case, the endorsement of the checks respectively payable to the Debtor and to Faure Brothers did not change the ownership right to payment of those drafts, i.e., the checks were still payable solely to the payee designated on the face of the instruments.

The drafts were then delivered to Mercantile, as an intermediary bank, for presentment to, and payment by, the respective drawee/payor banks who maintained the accounts held by the drawers of each of the respective drafts. As the initial transferee, Mercantile was obligated to handle these checks in accordance with the directions from its immediate transferee, and to deposit the drafts as directed by its contract with its depositor. In the first instance, Mercantile did not handle the transactions as directed, and it thus credited the wrong accounts for the proceeds it received as an intermediary/presentor bank, contrary to its contractual arrangements with its customers and contrary to the ownership interests of the payees of the checks. Did this mistaken crediting of accounts effect a transfer of ownership of the right to receive payment stated in the original drafts? Of course not. A bank and its customer have a debtor/creditor relationship with respect to demand deposits held by a bank for its depositing customer, with the bank being the debtor and the customer being the creditor. No matter where the bank put the deposits in its customer account system, its obligation to its depositing customer as an intermediary bank remained the same: Faure Brothers was still the owner of the funds transferred to Mercantile by the drawee banks on checks payable to Faure Brothers, and the Debtor was still the owner of funds transferred to Mercantile by the drawee banks on checks payable to the Debtor. Nothing Mercantile did in miscrediting these respective funds to the wrong accounts changed the fact that the funds realized by the honoring of checks by drawee banks belonged to the payees of the honored drafts, and not to anyone else; See, *Castano v. Wells Fargo Bank*, N.A., 82 S.W. 3d 40 (Tex.App., 2002); *Hicks v. State of Indiana*, Ind. App., 635 N.E. 2d 1151 (1994); *trans. denied. 1994.* Thus, in the first transaction, **absent more**, the funds misapplied by Mercantile did not change the ownership interest in the funds derived from the checks payable to the respective payees and retained their quality as property of the original payee. More on this transaction later.

What of the second transaction, in which the application of the deposit of funds was directed by a person having at least apparent authority to direct the deposit of those funds? The drafts were all properly endorsed for negotiation, and the evidence does not establish that any transferee endorsement was used on any of the drafts. Thus, by the payees' respective endorsements, the checks all became "bearer" paper, and as such "live" substitutes for cash upon presentment to, and honor by, the drawee banks. As the intermediary bank, and ultimate depository bank, Mercantile was obligated to handle the drafts as directed by the entity which negotiated the drafts through it and with whom it had contractual relationships as debtor/creditor with respect to deposit accounts maintained with it by both Faure Brothers and by the Debtor. Mercantile in this instance did exactly what it was directed to do: It deposited the proceeds of the drafts to the accounts to which it had been directed to deposit them. Did this effect a transfer of ownership interests of the credits created by the honoring of the negotiated drafts by the banks on which the checks had been drawn. The answer here depends on whether the direction of deposit *by mistake* was effective to transfer ownership of the deposit credits. One who owns property can choose to transfer ownership of that property, or of an interest in ownership of that property, by various means. Transfer can be effected by sale, by gift, by devise, by bequest, by involuntary means such as eminent domain, or by a consensual transfer motivated by fraud. Apart from eminent domain or similar involuntary takings, all of these mechanisms for potentially transferring ownership depend on the intent of the transferor – however motivated – to make a transfer of ownership or ownership interests to another. The parties have stipulated that the erroneous deposit tickets which caused the miscrediting of accounts in the second instance were not intended to transfer ownership of the rights to receive payment on the negotiated drafts to the party to whose credit those rights were effected on the books of Mercantile. The record makes clear– and the parties' stipulation makes conclusive – the fact that the erroneous preparation of deposit tickets was not intended to affect the ownership interests in the funds to be transferred to Mercantile as a result of the processing of the checks made payable to the respective payees of those drafts.

A great deal of time has been spent by the parties and by the Court on issues relating to whether the principle of "constructive trust" is applicable to the issues. The doctrine of "constructive trust" is a doctrine of remedy, not of determination of property rights; See, *In re Nova Tool & Engineering, Inc.*, 228 B.R. 678 (Bankr. N.D. Ind. 1998); *In re Omegas Group, Inc.*, 16 F.3d 1443 (6th Cir. 1994).[11] Moreover, because the account credits to which this case relates had already been "reversed" by the time the Debtor had filed its case, the doctrine has no relevance at all to any issue of determination of ownership by the application of a possible remedial doctrine on the date of the filing of the debtor's petition. In order to apply the doctrine of constructive trust in this case, one would be required to hypothesize what a court in Indiana applying the Indiana law of constructive trusts would have decreed as to the property rights of the Debtor and Faure Brothers with respect to the reversal of the credits if the reversal had been challenged at the time of the reversal of credits by a party adversely affected by the reversals. This is a totally speculative exercise, one in which the Court declines to engage, and one which has nothing to do with the concept of "property " or an "interest in property" within the scope of 11 U.S.C. 101(54).[12]

[11] These cases are cited for the proposition stated by the Court, and not necessarily for the Court's approval of the application of that proposition under the factual circumstances of the cited cases.

[12] If the Court deemed the constructive issue relevant, the Court notes the following. If the imposition of a constructive trust was warranted, the Debtor would have lacked the equitable title necessary for the funds to ever become property of the Debtor or property in which the Debtor had an interest, to the extent the "transfers" would have been challenged within a reasonable period of time after the transfers had been made, and without consideration of the nearly two year authorized use of the transferred funds in the $66,092.01 transaction.

The trustee would then be unable to use his §547(b) powers because the debtor did not transfer anything that belonged to it. *Belisle v. Plunkett,* 877 F.2d 512, 513 (7th Cir. 1989) ["A constructive trust ordinarily survives bankruptcy: the property may not be used to satisfy the Debtor's obligations to other creditors, and the debts to the victims of the fraud may not be discharged"]. See also *In re Marrs-Winn Co., Inc.*, 103 F.3d 584, 589 (7th Cir. 1996) ["From the plain language of the Code, one can easily conclude that the debtor's bankruptcy estate does not include property held in trust for another"]. In *In re Brown*, 227 B.R. 875, 878 (Bankr.S.D.Ind. 1998) in FN4 the court wrote:

> The Dissolution Court found that the Debtor and his former spouse held title to the 7 Acre Lot as "constructive trustees" for the Debtor's Parents.
>
> The United States Supreme Court held in *Begier v. I.R.S.*, 496 U.S. 53, 110 S.Ct. 2258, 110 L.Ed.2d 46 (1990), that property held in trust is neither property of the estate, nor property of the debtor. Because the debtor does not own an equitable interest in property he holds in trust for another, that interest is not 'property of the estate'. Nor is such an equitable interest 'property of the debtor' for purposes of [Section] 547(b). *Begier*, 110 S.Ct. at 2263. *See also In re Unicom Computer Corp.*, 13 F.3d 321 (9th Cir.1994) (deposit of funds into the debtor's account by mistake and subsequent repayment to the client is not a preference if applicable state law would have imposed a constructive trust on the funds).

There are no Indiana cases which expressly impose a constructive trust on funds transferred due to mistake. The Second Circuit Court of Appeals, however, recognized the application of a constructive trust in a similar setting. See, *In re Berry*, 147 Fed. 208, 211 (2nd Cir. 1906) ["When the money was paid under a plain mistake of fact equity impressed upon it a constructive trust which followed it through the bank and into the hands of the trustees"]. The lack of express Indiana case law, however, does not mean that mistake cannot be a ground for the imposition of a constructive trust. There is no question here, and no one suggests otherwise, that both transfers were prompted by someone's mistake, in one case the mistake of the Bank for not depositing the funds into the correct account of the respective parties, while in the other the mistake of an employee of Faure Brothers who utilized a wrong deposit ticket. There are in fact numerous Indiana cases which, as a general rule, state that:

> A constructive trust is imposed where a person holding title to property is subject to an equitable duty to convey it to another on the ground that he would be unjustly enriched if he were permitted to retain it. The duty to convey the property may rise because it was acquired through fraud, duress, undue influence or **mistake**, or through a breach of a fiduciary duty, or through the wrongful disposition of another's property. The basis of the constructive trust is the unjust enrichment which would result if the person having the property were permitted to retain it. 5 Scott on Trusts § 404.2. [emphasis supplied].

Melloh v. Gladis, 261 Ind. 647, 309 N.E.2d 433 (1974); Kalwitz v. Estate of Kalwitz, 822 N.E.2d 274 (Ind.Ct.App. 2005); *Strong v. Jackson*, 777 N.E.2d 1141, 1151 (Ind.Ct.App. 2002); *Koenig v. Leas*, 165 N.E.2d 134, 136-37 (Ind. 1960); *Brown v. Brown*, 135 N.E.2d 614, 616 (Ind. 1956) ["such breach of duty may include mistake, undue influence, or duress"]; *Jefferson School Tp. of Greene County v. School Town*, 32 N.E. 807, 809 (Ind.App. 1892) [". . . where a person has obtained money belonging to another through accident or mistake as well as through fraud, in such cases the person thus wrongfully profiting by the advantage gained will be treated as the trustee of the other"]; *American United Life Ins. Co. v. Douglas*, 808 N.E.2d 690, 697 (Ind.Ct.App. 2004).

A constructive trust arises by operation of law from a course of conduct, which, if sanctioned by law, would secure an unconscionable advantage, irrespective of the actual intent to defraud. *Jackson*, 777 N.E.2d at 1146. The Trustee argues that constructive trust is not appropriate in this case, as no fraud has been established, either actual or constructive. The Indiana case law, however, does not require the establishment of fraud. As noted earlier, the Indiana Supreme Court has stated that a mistake may warrant the imposition of a constructive trust. This reading is further supported by *Hicks v. State*, 635 N.E.2d 1151 (Ind.Ct.App. 1994) where the court held that "a constructive trust may be imposed appropriately where property is wrongfully gained or held. Fraud is but one means by which property may be wrongfully gained; robbery is certainly another." Thus, mistake is merely another means by which property is wrongfully gained.

Indiana courts, once faced with a case such as this one, would impose a constructive trust based on mistake. Although there are cases which state that fraud is an essential ingredient in a constrictive trust, that assertion is a mere gloss and it does not fully conform with other Indiana judicial statements which list mistake as a ground for a constrictive trust. <u>All</u> of the case law cited by the Trustee involved a set of circumstances where the showing of fraud was an integral element with respect to the facts of the case. In no case, however, was a constructive trust alleged based on mistake. Clearly, a mistake is not equivalent to fraud. Fraud may require some degree of ill motive, while mistake can be innocent. Because the two operative words are separate and distinct in their meaning and application, the Court must conclude that one does not encompass the other and each may be a ground for a constructive trust. The court in *F.T.C. v. Think Achievement Corp.*, 144 F. Supp.2d 1013, 1020-21 (N.D.Ind. 2000) wrote the following:

> . . . courts may employ the doctrines of constructive trust and unjust enrichment "where, rightfully or wrongfully, a party has obtained property that unjustly enriches him." *Id.* (internal quotation marks and citation omitted). *See also Rollins v. Metropolitan Life Ins. Co.*, 912 F.2d 911, 914 (7th Cir. 1990)(under Indiana law, courts have imposed a constructive trust where a duty has been breached and "a third party unjustly enriched as a result of that breach, even absent wrongdoing by the party unjustly enriched," and "equity may collect proceeds from an innocent party in order to protect the equitable rights of those who have suffered the wrong"); *Egan*, 856 F. Supp. at 402 ("To be sure, Relief Defendants may not have been directly culpable in the . . . violations, but what the [Commission] seeks to have them disgorge are the benefits that they derived from the violations by the culpable defendants. And those benefits – the unjust

Viewed as it must initially be viewed – from the intent of the transferor to create an interest in the transferee in property of the transferor – at the time that the original miscrediting of each of the accounts was made, did Faure Brothers intend to transfer its rights to payment of drafts made payable to it to the Debtor? Based upon the parties' stipulations, the answer is "No", and thus at the time of the initial miscrediting of accounts, no transfer of an interest to receive payment on checks processed through Mercantile was intended, and the monies of Faure Brothers erroneously designated as deposit credits in the Debtor's account remained property of Faure Brothers. The Court thus finds that *at the time of the initial miscrediting of accounts*, there was no transfer of a property interest by Faure Brothers to the Debtor, and that thus merely as a result of transfer back to Faure to Brothers of account credits there was no "transfer of an interest of the debtor in property" under 11 U.S.C. §547(b).

But the analysis doesn't stop here. The record establishes that with respect to the first transaction ($66,092.01) erroneously handled solely by Mercantile, the erroneous handling of the deposits was made known to both the Debtor and Faure Brothers at a very early stage of the erroneous process. If it had "called its chits" at the first notice to it of the erroneous recording of the transactions, Faure Brothers would be immune from the Trustee's action. But Faure Brothers didn't do that. Knowing from very early on that its property had been

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> enrichment – are what trigger the application of the doctrine of constructive trust as a 'device for preventing unjust enrichment.' ") (quoting *American Nat'l Bank & Trust Co. v. United States*, 832 F.2d 1032, 1035 (7th Cir. 1987).

Hindsight isn't 20/20 when the object of hindsight is a hypothetical exercise. However, utilizing hypothetical hindsight, the Court has no difficulty in stating that upon the basis of Indiana caselaw, particularly *Hicks,* supra., if challenged before the Bank's reversal of account credits, an Indiana court would have imposed a constructive in the circumstances of the second "erroneous deposit" transaction ($83,698.49). However, there is no even remotely applicable Indiana decision which allows the Court to derive in any manner what an Indiana court would have done with respect to the first "erroneous deposit" transaction if that transaction had been challenged immediately prior to its reversal by a party affected by it.

erroneously “assigned” to the credit of another entity, Faure Brothers did nothing about correcting the misapplication until shortly before the Debtor filed its bankruptcy petition. The Debtor and Faure are related entities, so closely related that the same individual was charged by each with the responsibility for making bank deposits for both. What happened here, the Court is confident in pronouncing, is that what was originally a mistake by the Bank was taken by both Faure Brothers and the Debtor as a convenient mechanism for Faure Brothers to advance funds to its closely held buddy without the formalities and bother – and potential tax consequences – of making a formal loan from Faure Brothers to the Debtor. What the two year delay in rectifying the Banks’ error caused to happen was to convert the excess of erroneously deposited funds owned by Faure Brothers in the Debtor’s account to an acquiesced-in retention of those funds for the use of the Debtor, i.e., essentially a loan of those excess funds from Faure Brothers to the debtor. Thus, with the knowledge and consent of Faure Brothers, the Debtor acquired an “interest in property” with respect to the over credit, i.e., a consented to right to use those funds. What resulted from the consented-to use of Faure Brothers’s check deposit credits by the Debtor was a loan from Faure Brothers to the Debtor, a simple debt for the authorized use of funds. This conclusion is more than amply supported by the record’s establishment of the fact that the Debtor’s account dipped below the excess deposit amount on several occasions – a circumstance known to Faure Brothers – and that Faure Brothers did nothing to seek to rectify the deposit error until essentially the eve of the Debtor’s bankruptcy filing. By its clear acquiescence, and indeed nearly endorsement, of the Debtor’s use of the funds from the first erroneously- credited transaction, Faure Brothers created an “interest in property” of the Debtor in those funds and a “debt” as defined by 11 U.S.C. §101(12) with respect to the Debtor’s use of those funds – just as the proceeds of a loan given by a bank to an individual deposited in the individual’s account becomes the individual’s property, with the bank becoming a creditor of the individual with respect to the funds advanced. When the “erroneous” credit was reversed by the Bank, and funds from the Debtor’s account were debited to the Debtor and transferred and credited to Faure Brothers’ account, that action constituted a “transfer” as defined by 11 U.S.C. §101(54), of “an interest of the debtor in property”, “for or account of an antecedent debt”.

In the *Begier* case, the United States Supreme Court was first confronted with the determination of what is 'property of the debtor’ pursuant to § 547(b). In pertinent part, the Court wrote:

> The Bankruptcy Code does not define "property of the debtor." Because the purpose of the avoidance provision is to preserve the property includeable within the bankruptcy estate – the property available for distribution to creditors – "property of the debtor" subject to the preferential transfer provision is best understood as that **property that would have been part of the estate had it not been transferred before the commencement of bankruptcy proceedings**. For guidance, then, we must turn to § 541, which delineates the scope of "property of the estate" and serves as the postpetition analog to § 547(b)'s "property of the debtor." [FN3]
>
> Section 541(a)(1) provides that the "property of the estate" includes "all legal or equitable interests of the debtor in property as of the commencement of the case." Section 541(d) provides:
>
> "Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest . . . becomes property of the estate under subsection (a) of this section only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold." Because the debtor does not own an equitable interest in property he holds in trust for another, that interest is not "property of the estate."
>
> Nor is such an equitable interest "property of the debtor" for purposes of § 547(b). As the parties agree, then, the issue in this case is whether the money AIA transferred from its general operating accounts to the IRS was property that AIA had held in trust for the IRS.

Begier v. I.R.S., 496 U.S. 53, 58-9, 110 S.Ct. 2258, 2263 (1990).

Indiana, like many other states, emphasizes control of disposition in defining the contours of property rights. *In the Matter of Smith*, 966 F.2d 1527, 1530 (7th Cir. 1992), citing *State v. Ensley*, 240 Ind. 472, 487, 164 N.E.2d 342, 348-49 (1960) ["Property in its legal sense means a valuable right or interest in something rather than the thing itself, and is the right to possess, use and dispose of that something in such a manner as is not inconsistent with law." (emphasis supplied)]. The facts of the case at bar indicate, and the trial testimony confirmed, that the subject funds were in the account of the Debtor for nearly two years and that the account was being utilized by the Debtor with the consent of Faure Brothers.[13] The court in *Smith* has noted that one's "interest in property" depends not on his *statutory right* to withdraw . . . the credited funds, but the real focus is whether the Debtor was actually able to exercise sufficient dominion and control over the funds. *Smith*, 966 F.2d at 1531. As in *Smith*, the Debtor here exercised dominion and control over the funds for almost two years. More importantly, the Debtor used said funds on many occasions making payments to various creditors. The balance of its checking account dropped below the amount of this disputed transfer, further evidencing that the Debtor had, and indeed exercised, dominion and control over the funds. The dominion and control was exercised with the knowledge and consent of Faure Brothers.

All of the other elements necessary for recovery of a preference by the Trustee have been stipulated to.

Although the doctrine of constructive trust is not directly applicable to the Court's

[13] The record clearly indicates that Faure Brothers was aware of the erroneous deposit in July of 1999. Even the exhibit provided by Faure Brothers indicates that fact, as its own reconciliation statements beginning in August of 1999 have the following marking: 66,092.01 Deposit Error, due from LSF. [Defendant's Exh. 2]. In addition to Faure Brothers' knowledge of this mistaken deposit, the Debtor was also fully aware. Its own account reconciliation statement dated August 1999 has the following marking: July bank error: 66,092.00. This error was brought to the Bank's attention nearly two years later, shortly before the Debtor's bankruptcy filing. The fact that the proponent of the constructive trust here cannot and did not explain the reason for this prolonged delay, further convinces the Court that this transaction, albeit prompted by the Bank's mistake, was acquiesced to or ratified by both parties.

decision, the Trustee also asserts that even if the remedy of a constructive trust could be imposed, it is nonetheless inappropriate as this equitable remedy is "cut-off" by the statuses which the Trustee holds under § 544(a)(1) and (3) of the Code. This effort by the Trustee misses its mark. Section 544(a)(3) refers to a *bona fide* purchaser of real property; no real property is at issue here. Section 544(a)(1) is likewise unavailing as it allows the Trustee to step into the shoes of a fictitious creditor "who extends credit to the debtor at the time of the commencement of the case". The issues in this case do not involve a conflict with the rights of a creditor described in §544(a)(1), as the transactions which the Trustee seeks to avoid were completed prior to the filing of the Debtor's petition, and the Trustee has not chosen to pursue claims based on fraudulent transfers or conveyances.

Lastly, at various points in its briefs, Faure Brothers states that "even if there were a transfer from LSF [Debtor] to Faure Brothers . . . that transfer was made in the ordinary course of the business or financial affairs of both companies." Such a defense is embodied in §547(c)(2), which states:

> (c) The Trustee may not avoid under this section a transfer -
> (2) to the extent that such transfer was -
> (A) in payment of a debt incurred by a debtor in the ordinary course of business or financial affairs of the debtor and the transferee;
> (B) made in the ordinary course of business or financial affairs of the debtor and the transferee; and
> (C) made according to ordinary business terms;

Further, section 547(g) states in pertinent part that:

> (g) For the purposes of this section [547] . . . the creditor or party in interest against whom recovery or avoidance is sought has the burden of proving the nonavoidability of a transfer under subsection (c) of this section.

Because Faure Brothers failed to present any evidence concerning its ordinary course of business defense, other than mere conclusory assertions, it failed to carry its burden of proof on this defense. *See*, *Kleven v. Household Bank F.S.B.*, 334 F.3d 638 (7th Cir. 2003); *In re Energy Co-op. Inc.*, 832 F.2d 997, 1004 (7th Cir. 1987) ["a creditor asserting § 547(c)(2) must show that the Debtor incurred its debt and paid the creditor in ways similar to other transactions"]. *See also In re Economy Milling*, 37 B.R. 914, 922 (D.S.C.1983) [debt not incurred and payment not made in the ordinary course of business because creditor did not show that he or other creditors had conducted similar transactions with the debtor before]; *Matter of Excello Press, Inc.*, 967 F.2d 1109 (7th Cir. 1992); *Matter of Tolona Pizza Products Corp.*, 3 F.3d 1029 (7th Cir. 1993).

The Court finds that the transaction involving adjustment of credits in the amount of $83,698.49, while a "transfer" as defined by 11 U.S.C. §101(54), did not involve "an interest of the debtor in property" and was not made with respect to an antecedent debt, and that the Trustee cannot recover with respect to that transaction under 11 U.S.C. §547(b).

The Court finds that the transaction involving adjustment of credits in the amount of $66,092.01 is a "transfer" as defined by 11 U.S.C. §101(54), involved "an interest of the debtor in property", and was made "with respect to an antecedent debt", and that the Trustee can avoid that transaction with respect to Faure Brothers and recover from Faure Brothers with respect to that transaction under 11 U.S.C. §547(b) in the amount of $66,092.01.

The Trustee's complaint requests an award of pre-judgment interest, a request which the Court deems appropriate to grant; See, *Matter of P.A. Bergner & Co.*, 140 F.3d 1111, 1123 (7th Cir.1998); *In re Industrial & Mun. Engineering, Inc.*, 127 B.R. 848, 851 (Bankr. C.D.Ill. 1990) from June 17, 2003, the date of filing of adversary complaint to the date of entry of judgment.

IT IS ORDERED, ADJUDGED AND DECREED that the Trustee shall have judgment against, and is entitled to recover $66,092.01 from, the defendant Faure Brothers Corporation pursuant to 11 U.S.C. §547(b), together with prejudgment interest from June 17, 2003 to the date of entry of this judgment at the rate of **6% per annum simple interest,** said total judgment amount to accrue interest pursuant to 28 U.S.C. §1961 at the rate of 3.89% until paid in full.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that Faure Brothers Corporation shall have judgment against the Trustee with respect to all claims asserted against it by the Trustee with the exception of the judgment awarded hereby.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that Amy J. Faure shall have judgment against the Trustee with respect to all claims asserted by the Trustee against her, and that the Trustee shall recover nothing on his complaint against the said defendant.

Dated at Hammond, Indiana on September 9, 2005.

J. Philip Klingeberger

J. Philip Klingeberger
United States Bankruptcy Court

Distribution:
Attorneys of Record