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IN THIS ISSUE

Misappropriation of Funds and Failure to List Transfers on Schedules Results in Denial of Discharge.

In Patti J. Sullivan v. Richard Jule Geckler, Jr. (*In re: Richard Jule Geckler, Jr.*), Adv. 10-3274 (Bankr. D. Minn., March 9, 2012), the debtor filed his Chapter 7 bankruptcy petition on June 18, 2010. His schedules omitted several transfers just prior to filing made by him to, or for the benefit of, family members and others.

The trustee commenced an adversary proceeding, claiming that some of the transfers were made with intent to hinder creditors from collecting a debt within the meaning of 11 U.S.C. § 727(a)(2), and that the debtor's failure to disclose the omitted transfers constituted a false statement within the meaning of 11 U.S.C. § 727(a)(4). The debtor denied any intent to hinder collections, claiming that he believed in good faith that some of the transfers did not need to be disclosed, and that the others were inadvertently omitted. A trial was held on January 30, 2012.

The evidence at trial established that the debtor was the president and a board member of Geckler Companies, Inc., a Minnesota corporation owned by the debtor's parents. Although the debtor owned no stock in the company, he was a personal guarantor of the company's debt to Sterling State Bank.

On February 7, 2011, the bank repossessed the assets of Geckler Companies and took control of its corporate headquarters. Another Geckler family corporation, Gallagher Top Ten Holdings, was located in the same building. Gallagher was owned by the debtor's sister and was managed primarily by the debtor's father. Although the debtor was not an employee, officer, or owner of Gallagher in 2009 or 2010, he did have access to Gallagher's finances.

The day after the repossession of Geckler Companies' assets, the debtor drove to Virginia, Minnesota, for the purpose of depleting $34,000 in Gallagher's account at Queen City Federal Savings Bank. The action was taken to keep Sterling Bank from seizing the funds. The debtor caused a check to be drawn, made payable to his attorney, in the amount of $15,000, and three checks of $5,000 each to himself and Geckler family members. He took the remaining $4,000 in the account in cash.

The court held that when the debtor withdrew the funds and exercised dominion and control over them, he acquired a cognizable interest in the funds, which – prior to the withdrawal – belonged to Gallagher. According to the court, the debtor's appropriation of the funds for the benefit of himself and his family members with intent to shield them from Sterling Bank constituted a transfer within the meaning of 11 U.S.C. § 727(a)(2), and therefore served as a basis to deny the debtor's general discharge.

Additionally, the court determined that the debtor was not entitled to a discharge pursuant to 11 U.S.C. § 727(a)(4) for his failure to list the $34,000 in transfers, as well as transfers used to pay his daughter's college tuition and his repayment of a loan to a booster club for which he was the treasurer, in his bankruptcy schedules.

The court did not find debtor's testimony that he believed the $34,000 belonged to his father credible as the funds were ultimately used for the debtor's bankruptcy and no evidence indicated that Gallagher received any benefit from the transfers. As for the transfers used to pay college tuition and repay a loan, the court did not believe they were unintentionally omitted as they were discovered by the trustee only after six months of searching, making requests, and holding three Section 341 sessions. Accordingly, the court determined that the debtor's intentional failure to disclose material information in his schedules constituted a false statement, thereby precluding his discharge.

Minnesota Court of Appeals Finds that When Marital Property is Impermissibly Liquidated, it Becomes Attachable by the Liquidating Party's Creditors.

In a non-bankruptcy case, CorePoint Capital Finance, LLC v. Hecker, 2012 WL 360413 (Minn. Ct. App. Feb. 6, 2012), the Minnesota Court of Appeals decided the extent to which an entity may garnish a debtor's funds held by the district court.

In April 2008, the appellant initiated marriage dissolution proceedings against her husband, during which the latter disclosed two retirement accounts held in his name. As the accounts were marital property, both parties were temporarily restrained from disposing of their contents due to the dissolution proceedings. Despite this prohibition, the appellant's husband liquidated and disposed of the contents of one account, which held $125,155.74. The family court subsequently held the husband to be in contempt and ordered that he restore the liquidated amount to the account. Unable to personally restore the account, the husband obtained the necessary funds from an acquaintance. However, as the account was closed upon liquidation, the family court ordered the husband to deposit the amount with the Hennepin County district court, after which a stipulation was entered awarding the appellant the funds in question.

Prior to the stipulation, and unbeknownst to the appellant, Chrysler Financial Services Americas, LLC served the district court with a garnishment summons for the funds held by the district court. Upon learning of the garnishment summons, the appellant petitioned the family court, which in turn referred the matter to the district court. The appellant primarily argued that the funds were marital property and beyond the reach of creditors, to which the district court held that the funds were a gift from the husband's acquaintance and received after dissolution. Therefore, they were properly attachable non-marital property. The appellant alternatively argued that the funds were held *in custodia legis*, and were not subject to garnishment. In response, the district court held that the funds were transferred to the district court in order to purge the husband's contempt charge rather than for protection against creditors. This appeal followed.

The court of appeals agreed with the district court that the funds were transferred as a means of purging the contempt charge rather than to protect them from the reach of creditors. Further, the court compared the power of a court-appointed receiver to that of the district court administrator, finding that the latter did not exercise sufficient control or dominion over the funds needed to find them *in custodia legis*. While a receiver must make substantive business decisions involving the liquidation, disposal, or investment of property, the administrator was merely tasked with holding the funds and distributing them as directed by the court.

The appellant then argued that the husband never had possession of funds, which therefore exempted them from garnishment. The court quickly dispensed with this argument, holding that the husband had constructive possession while the district court administrator merely had custody. The gift to the husband became his unencumbered property, which he then transferred to the district court administrator. When a property owner intentionally transfers physical control of property to another for the purposes of performing some act for the owner, the owner maintains constructive possession. In the current instance, the property owner intentionally transferred property for the purpose of purging the contempt charge levied by the family court.

Judicial Lien is Not Avoidable Under 11 U.S.C. 522(f) When State Law Requires Judgment Creditor to Satisfy Consensual Creditor Lien Before Sale of Attached Collateral.

In In re Carter, 466 B.R. 468 (B.A.P. 8th Cir. 2012), Iowa debtors pledged a vehicle as collateral for two bank loans. Prior to the bankruptcy filing, another creditor received a judgment against the debtors and writ of execution ordering the sale of the vehicle to satisfy the judgment. As required by Iowa law, the judgment creditor paid off the bank loans secured by the vehicle prior to the sheriff's sale of the vehicle. The debtors filed their bankruptcy petition and stopped the sale. The debtors claimed a portion of their interest in the vehicle was exempt under state exemption law and filed a motion under 11 U.S.C. 522(f)(1) to avoid the judgment lien.

The Bankruptcy Appellate Panel ruled that under Iowa law the debtors could not avoid the judgment lien. Although the judgment creditor satisfied the bank's lien by paying it off, when it did so, it merely "stepped into the shoes of the bank." The judgment creditor was now the effective holder of a consensual lien against the vehicle – which is not avoidable under 11 U.S.C. 522(f)(2). Because the judgment creditor stepped into the shoes of the bank, it was now holder of the consensual lien. Because the debtors could not avoid the lien under § 522(f)(1) when the bank was holder of the lien, they also could not avoid it when it was held by the judgment creditor.

Plaintiff Bringing a Nondischargeability Case Must Have a Good Faith Basis for Claim.

In In re Noreen, ADV 11-6009, BKY 10-61322 (Bankr. D. Minn. 2012) the personal representative of a deceased creditor sought a judgment of non-dischargeability under 11 U.S.C. § 523(a)(4) against the debtor, former power of attorney for the deceased. The complaint alleged defalcation by the defendant for making unauthorized gifts to herself and third parties from the deceased's assets. The evidence and corroborating statements by the deceased's attorney, accountant, and investment counselor show that the three gifts in question were made by the deceased with sound mind. Plaintiff's only evidence was testimony by several disgruntled relatives regarding the favoritism shown to a more distant relative.

The court found the claim frivolous. A creditor must have a good faith basis to bring a nondischargeability claim. Especially in a case where fraud is alleged, the creditor must investigate to make sure a dischargeability complaint is substantially justified. Two venues for such investigation include the 341 meeting and a Rule 2004 Examination. Given the Plaintiff's total lack of credible evidence, the court stated it will consider the awarding of attorney's fees and costs against both the plaintiff and her attorney on an appropriate motion.

Chapter 13 Plan Commitment Period Should Be Determined by Number of Payments Made, Not Number of Months Since Confirmation.

In the chapter 13 case of In re Zellmer, Case No. 10-30349 (Bankr. D. Minn. Feb. 23, 2012), the bankruptcy court denied the debtor's proposed modification of his Chapter 13 plan, finding that one of the proposed modifications failed to meet the good faith requirements for confirmation.

The debtor's original confirmed plan included income for plan payments from his non-filing spouse, and provided for a repayment term of 36 months. Post-confirmation, the debtor failed to make four monthly payments due to garnishment of his non-filing spouse's income and increased expenses. The debtor proposed a modified plan with a reduced monthly payment, to be made in the months remaining of the original 36 months. The trustee objected to the confirmation of the modified plan on the grounds that it would provide creditors with a total of only 31 payments, rather than 36. The debtor argued that the applicable commitment period should be measured by the number of months since plan confirmation, regardless of whether plan payments were made in all months.

After analyzing the relevant statutes and policy considerations, the court ultimately agreed with the trustee, holding that the commitment period is equivalent to the number of actual payments of disposable income, and that months of nonpayment should not be taken into account. The court further found that, although the debtor had an ongoing substantial change in circumstances that justified the reduced monthly payment amount, there was no such change that precluded the debtor from making 36 payments rather than 31 payments. Consequently, the court determined that the debtor was not making a sincere effort to repay creditors, therefore, the proposed modified plan did not comply with the good faith requirement of § 1325(a)(3). Because the debtor's good faith was "called into question by his willingness to enjoy the benefits of Chapter 13 without . . . making the full thirty-six payments of the commitment term," the court denied confirmation of the proposed modified plan.

Bankruptcy Court for the District of Minnesota Denies Employment and Fee Applications Based on Conflict of Interest.

In the case In re Kappy Investments, Inc., 10-61454 (Bankr. D. Minn. Feb. 2, 2012) (J. O'Brien), the U.S. Bankruptcy Court for the District of Minnesota denied applications to approve employment and an award of compensation. The In re Kappy bankruptcy petition and an employment application were filed by the Vogel Law Firm (the "Firm"). The U.S. Trustee objected to the Firm's employment on grounds that the firm had failed to disclose a number of potential conflicts in its employment application. Rather than setting the contested employment application on for hearing, the debtor obtained another attorney and the bankruptcy court approved such attorney's employment.

After a Chapter 11 plan was confirmed, the Firm filed an application seeking to be paid for legal fees and costs that accrued before their application for employment had been filed and before the debtor had obtained successor counsel. The U.S. Trustee objected again, this time on the basis that a professional cannot be paid from the estate until such professional's employment is first approved pursuant to 11 U.S.C. § 327. The Firm then filed a second employment application.

The bankruptcy court denied the Firm's employment and fee applications. In issuing its decision, the bankruptcy court explained that actual conflicts of interest prevented the bankruptcy court from approving the Firm's employment. Among other things, the court stated that the Firm's concurrent representation of an individual bankruptcy debtor with claims adverse to the corporate debtor's estate constituted an actual conflict of interest. The court further held that, because the Firm's employment could not be approved, the Firm could not be paid from the estate.

Minnesota Bankruptcy Court Confirms That Mortgagees Don't Need to Produce an Original Promissory Note to Foreclose Its Mortgage.

In In re Banks (Banks v. Kondaur Capital Corporation, LLC and Shapiro and Zielke, LLP), Adv. Case No. 10-3216, the bankruptcy court only allowed narrow discovery to determine a mortgagee's legal and equitable interest in a mortgage, even though a mortgagee's legal interest is the only interest relevant to a mortgagee's right to commence a foreclosure by advertisement of its mortgage under Minnesota law.

This case originated with a motion to compel discovery responses in an adversary case that was remanded by the 8th Circuit B.A.P. Originally, the debtor/plaintiff started the adversary case to avoid the mortgage against their homestead, or to at least establish that the defendant was not the mortgagee that had the power to foreclose the mortgage on their homestead property. The bankruptcy court granted summary judgment for the mortgagee/defendant. But on appeal, the B.A.P. remanded stating that there was only one fact at issue, and that was whether the mortgagee possessed the original signed promissory note secured by the mortgage on the debtor's homestead. Discovery on this narrow issue was allowed, but the debtor/plaintiff attempted a much broader breadth of discovery against the mortgagee, and inquired about the circumstances surrounding the acquisition of the note and mortgage, the defendant's full loan file, and the defendant's custodial procedures for handling promissory notes and locating lost promissory notes.

In this decision, the bankruptcy court only "nominally" granted the plaintiff's motion to compel discovery responses, but only to make it "absolutely clear to both parties" that the only discovery allowed pertains to the chain of title to the promissory note and the chain of interest in the mortgage. Generally, the plaintiff's motion to compel response to its broad discovery requests regarding the circumstances of the loan, the full loan file, and the defendant's custodial procedures were denied. And since these broad demands were not reasonably calculated to lead to the discovery of admissible evidence based on the limited scope of the B.A.P.'s remand, defendant was awarded attorneys' fees under Fed. R. Civ. P. 37(a)(5)(B), as incorporated by Fed. R. Bankr. P. 7037.

Further, the bankruptcy court noted that under the Minnesota Supreme Court's decision in Jackson v. Mortgage Electronic Registration Systems, Inc., 770 N.W.2d 487 (2009), that the location of the original promissory note, the one fact at issue for the B.A.P. on remand, might not even be relevant to the plaintiff's request for relief. In Stein v. Chase Home Fin., LLC, the 8th Circuit recently applied the Jackson case and held that under Minnesota law, the right to foreclose a property by advertisement "lies with the legal, rather than equitable, holder of the mortgage." 662 F.3d 976, 980 (8th Cir. 2011). A mortgagee with a legal interest is the mortgagee identified in the original mortgage document and subsequent assignments. A mortgagee with just an equitable interest is the holder of a right to payment under the underlying note. So under Stein, if a mortgagee has documentation that it has the proper chain of interest in the mortgage and assignments of the mortgage, and not possession of the original promissory note, then it is the party entitled to commence a foreclosure by advertisement.

A Debtor's Additional Disposable Income Cannot Be Used to Make Voluntary Contributions to a Pension Plan at a Level Greater than Pre-Petition Contributions.

In In re Swanson, Bankr. Case No. 11-45600, the bankruptcy court for the District of Minnesota denied the confirmation of a chapter 13 plan under which the debtor proposed to increase his voluntary contributions to his 401(k) plan. The bankruptcy court held that the debtor cannot use additional disposable income to increase his voluntary contributions to his 401(k) plan above the contribution level at the time of filing for bankruptcy protection.

Prior to filing for bankruptcy, the debtor has voluntarily contributing 1% of his annual income to his 401(k) and making mandatory repayments of the loans from his 401(k). In the debtor's proposed Chapter 13 plan, the debtor would continue to make voluntary contributions of 1% of his annual salary and the monthly required loan payments. After 21 months of loan payments of $477 each, the loans from his 401(k) would be paid in full, and the debtor would have $477 additional each month which was proposed that a part of that money would be used to increase the voluntary contributions to 6% of his annual salary. Under this proposed chapter 13 plan, 67% of the unsecured creditor's claims would be paid. However, if all the $477 of additional money went toward the chapter 13 plan once the loans from the debtor's 401(k) were repaid, then 85%

of the unsecured creditor's claims would be paid. The bankruptcy trustee argued, and the bankruptcy court agreed, that by increasing his voluntary contributions to his 401(k) the debtor does not meet the "best efforts" test of 11 U.S.C. § 1325(b) because the additional $477 is additional disposable income that needs to be contributed to the chapter 13 plan when unsecured creditors are not being paid in full.

The bankruptcy first determined that the additional $477 a month was "projected disposable income" under § 1325(b)(2) and that definition would include voluntary contributions to pension plans. The bankruptcy court then adopted the Supreme Court's "forward-looking approach" to define projected disposable income to include changes in the debtor's income that are known or virtually certain at the time of confirmation of the plan. Since the repayment of the 401(k) loans is known or "virtually certain," the court knows that there will be an additional $477 a month available to the debtor and that under § 1325(b) that projected disposable income must be paid to the creditors.

Next, the bankruptcy court analyzed the debtor's ability to maintain or increase voluntary contributions to a pension plan. The court noted that a minority of cases in the 9th Circuit may not allow a debtor to make post-petition voluntary contributions as a part of a plan. Another minority of cases take the other extreme and allow debtors to make post-petition voluntary contributions to a pension plan up to the maximum allowed to be contributed under the pension plan, regardless of whether or not the debtor made such contributions pre-petition. Instead, the bankruptcy court in this case followed a third line of interpretation set forth by the 6th Circuit that allows a debtor to make post-petition contributions only at the level the debtor was contributing pre-petition. This reasoning is also in line with its decision that the additional $477 a month in projected disposable income must be paid to the creditors under the plan. This decision also allows a debtor to continue making voluntary contributions without diverting newly available funds away from creditors. The balance struck by the bankruptcy court protects a debtor's retirement assets while also ensuring that debtors pay creditors the maximum they can afford.

BAP Affirms Bankruptcy Court's Rulings on Allowance/Disallowance of Claims; No Evidentiary Hearing Was Required.

In Sears v. Sears *(In re AFY, Inc.)*, No. 11-6042 (B.A.P. 8th Cir. Jan. 23, 2012), the BAP affirmed an order of the bankruptcy court for the District of Nebraska: 1) overruling Robert and Korley Sears' objection to claims filed by Sears family members; 2) allowing the family's claims; and 3) disallowing Korley's claim.

Pre-petition, the debtor and Korley acquired the family's interests in the debtor through a stock sale agreement. Only Korley executed the promissory notes; the debtor did not. Shortly afterward, the debtor's shareholders issued a resolution requiring the debtor to redeem all stock under the agreement and to make all required payments to the family. Robert and Korley, and then the debtor, filed bankruptcy petitions.

The family filed claims in the debtor's case for amounts owed under the agreement. Robert and Korley objected to the family's claims on the basis that the debtor was not directly liable to the family under the agreement, and asserted various defenses. Korley filed a claim in the case for approximately $5.3 million, which was the aggregate amount of the family's claims. The chapter 7 trustee and the family objected to Korley's claim. Robert and Korley requested a continuance, discovery, and an evidentiary hearing. The bankruptcy court denied their requests, allowed the family's claims over the objections, and disallowed Korley's claim.

The BAP affirmed the disallowance of Korley's claim. Although Bankruptcy Rule 3001(f) provides that a properly filed claim is "prima facie evidence of the validity and amount of the claim," Korley's claim provided no legal basis for liability.

The BAP affirmed the allowance of the family's claims. It agreed with the bankruptcy court that Robert and Korley had failed to rebut the presumption that the family's properly filed claims were valid. The agreement unambiguously provided that the debtor was liable to the family, so there was no need to consider the promissory notes as extrinsic evidence regarding the intent of the parties. The BAP rejected Robert and Korley's argument that the family's claims should be disallowed due to an alleged post-petition breach of duty of good faith and fair dealing, noting that the alleged misconduct consisted only of assisting the trustee and enforcing their claims. The BAP also rejected Robert and Korley's argument that since the debtor's business had failed, the agreement was unenforceable under the "supervening frustration" theory. *See* Restatement (Second) of Contracts § 265 (1981).

The BAP held that the family's argument that Korley lacked standing to challenge the allowance of their claims due to the disallowance of Korley's claim was immaterial since the BAP affirmed the bankruptcy court on the allowance of the family's claims as well. Finally, the BAP found that the bankruptcy court did not err in refusing to allow testimony or additional time for discovery since the claims had been filed a year prior to the determination and Robert and Korley had not identified any issue that would have required testimony or cross-examination.

Limited Partnership Units Awarded as Compensation do not Qualify as Exempt Employee Benefits under Minnesota Law.

The bankruptcy court held that a debtor's limited partnership units did not qualify as exempt employee benefits under Minnesota Statute § 550.37, subd. 24(a). In re Foellmi, BKY 11-30939 (Bankr. D. Minn. Jan. 11, 2012). The debtor received limited partnership units in a real estate investment partnership as compensation for her employment at a Kwik Trip store. The partnership invested in real estate which it would develop and lease to Kwik Trip, Inc. The partnership agreement provided for the sharing of profits and losses from operations, net sale gains and losses, tax allocations and distributions among partners in proportion of their respective partnership interests. The partnership would redeem any partnership interest upon termination of employment, unless termination occurred by death or retirement. Mandatory redemption also applied if the employee intended to compete with Kwik Trip after retirement. Otherwise, the partnership could refuse any redemption request. Another disclosure document prepared by Kwik Trip referred to the limited partnership as an employee benefit plan.

Section 550.37, Subd. 24, of the Minnesota Statutes govern whether an asset is exempt as an employee benefit. The two elements of the statute at issue in *Foellmi* were whether the debtor had the "right to receive payments under a stock bonus, pension, profit sharing, annuity, individual retirement account, Roth IRA, individual retirement annuity, simplified employee pension or similar plan," and whether such right to payment was on account of "illness, disability, death, age or length of service."

The court held that the partnership units did not meet either element required to establish that they constituted exempt employee benefits. First, the court observed Minnesota law generally did not recognize partnerships as exempt. The purported "employee benefit plan" here was a partnership notwithstanding the title given by Kwik Trip. Further, the court concluded that the partnership was not a type of plan similar to those listed in Section 550.37, Subd. 24. While partners shared in profits and losses, the units themselves did not increase in value. Further, upon certain conditions the partnership could automatically redeem the interests, another distinguishing characteristic from the types of plans listed as exempt.

Second, the court held that payments made by the partnership were not on account of illness, disability, death, age, or length of service. Rather, payments were made on account of the profits of the partnership. The only connection between the partnership and the qualifying events for payment in the statute was that if the employee discontinued employment due to retirement or death, such an event would not require a mandatory redemption of the units. This connection, however, was not sufficient to demonstrate that payments by the partnership were on account of retirement or death.

Estate Planning Re-Conveyance of Property from Son to Surviving Mother Deemed a Fraudulent Transfer.

The bankruptcy court avoided a transfer of real property from a son to his mother where the transfer was a re-conveyance of a transfer of the property previously made to him without consideration. Ries v. Lee *(In re Lee)*, Adv. 11-3123, (Bankr. D. Minn. Jan. 9, 2012).

In May, 2006, as an estate planning device, parents transferred real property to their son and recorded the conveyance. Contemporaneously, the son executed and delivered a deed for the property back to his parents, but the deed went unrecorded, and the parties understood that the parents would only record the deed at their discretion in the future. Approximately two months later, the son mortgaged the property, which had a tax assessed value of $121,000, to secure a loan of $35,000. In October, 2007, the father deceased and the mother requested a deed returning the property. In November, 2007, the son executed and delivered a new deed to his mother but she did not record the deed until

September 2008. No parties gave any consideration for any of the transactions.

The son filed bankruptcy in December 2009. His trustee sought to avoid the transfer of the real property to his mother. The bankruptcy court avoided the transfer under Section 548(a)(1)(B) of the bankruptcy code as a constructive fraudulent transfer. The court found that the transfer occurred in September, 2008, when the son recorded the deed, which transfer occurred within two years of the petition date and enabled the trustee to avoid the transfer under the code. The court found that notwithstanding the parents' discretion to recover the property at any time, they nonetheless intended to have the son remain record title holder. Otherwise the transfers would have had no purpose and the mother conceded that these transfers were an estate planning device. The intent for the son to hold ownership was further evidenced by the mortgage granted by the son to a third-party lender.

The court further found that the son did not transfer the property until it was recorded. In making this determination the court relied on the principle that state law defines property interests. The court cited Section 513.46 of Minnesota's fraudulent transfer act which deems a transfer of real property as occurring for fraudulent transfer purposes when "the transfer is so far perfected that a good faith purchaser of the asset from the debtor against whom applicable law permits the transfer to be perfected cannot acquire an interest in the asset that is superior to the interest of the transferee."

The court concluded the transfer occurred in the two-year period prior to the bankruptcy, that the debtor gave no consideration for the transfer, and that the debtor was insolvent. Thus, the trustee established a constructive fraudulent transfer and the court avoided the transfer to the mother.

Bank's Perfection of its Security Interest in Debtor's Property on the 90th Day Before the Bankruptcy Filing and its Subsequent Receipt of Payment on the Secured Debt Constituted a Voidable Preference.

In the case of In Re: HovdeBray Enterprises; David Velde vs. Border State Bank, Adv. 11-6007, (Dist. of Minn.) the trustee plaintiff brought a preference action against Border State Bank ("Bank") who received a payment from the debtor in the 90 days prior to its bankruptcy filing.

Although the debtor granted a security interest in its property to the Bank in 2007, the Bank did not perfect its security interest in the property until July 13, 2010 which was on the 90th day prior to the debtor's bankruptcy filing (the bank did however file the financing statement with the County Recorder's Office, which was not the correct place to do so). The debtor then retained a liquidation service and held a going out of business sale in the following months from which its gross sale proceeds totaled $426,571.79. Of that, $256,422.02 was paid to the bank and satisfied the bank's note in full, while the remaining was used by the debtor to pay expenses and other obligations. All sale proceeds were deposited into the debtor's bank account at the bank and the bank had exercised its right to setoff as to the account, prior to the debtor's liquidation, in the amount of $13,579.98.

The preference action went to trial, at which the remaining issues to be litigated were:

(1) Whether the liquidation payments made to the bank during the preference period were ordinary course payments;

(2) Whether the bank's release of approximately $164,000 from the debtor's account to pay third party bills and expenses constituted new value;

(3) Whether $26,480 of the liquidation proceeds was from the sale of fixtures which security interest was perfected by the 2007 financing statements filed with the appropriate counties; and,

(4) Whether the bank has a set off defense against the plaintiff in the amount of $13,579.98.

With regard to the first issue, the court held that the liquidation of the debtor's business did not fall under the "ordinary course" of business exception to a voidable preference listed in Section 547(c)(2). The court found that none of the characteristics of a transfer in the ordinary course of business as laid out in case law applied to this transaction. The court found for the trustee on the first issue.

On the second issue, the court held that there was no new value defense under Section 547 because the Bank did not have the right to exercise a setoff against the $256,422.02 that was used to pay off the bank's note. Rather, the court held that payment constituted a transfer to the bank during the preference period while the debtor was insolvent for the purpose of satisfying an antecedent debt to the defendant. The court held for the trustee on this issue as well.

The court held that the property claimed by the bank to be fixtures, which were the subject of the third issue, were shelves that were easily dismantled and sold without doing any damage to the premises, and therefore, were not fixtures, but were personal property of the debtor. Thus, the court held for the trustee on the third issue.

Lastly, on the fourth issue, the court held that the $13,579.68 worth of funds which were in the debtor's account prior to the liquidation of the debtor's business were subject to the bank's setoff rights under 11 U.S.C. § 553(a). As such, the court held in the bank's favor on the fourth and final issue.

The Bankruptcy Appellate Panel Enforces a Wavier Against Co-Debtors and Affords the Bankruptcy Court Great Deference in Interpreting its Own Order.

In Boyher v. Stuart J. Radloff, Trustee, No. 11-6077 (B.A.P. 8th Cir. March 9, 2012) (J. Federman, J. Venters, and J. Nail), the Bankruptcy Appellate Panel for the Eighth Circuit Court of Appeals affirmed an order approving a Chapter 7 trustee's "Amended Final Report, Proposed Distribution, and Motion for Abandonment."

During their bankruptcy, two co-debtors entered an agreement with their chapter

7 trustee to split evenly the proceeds of a class action settlement. The agreement between the co-debtors and the trustee was memorialized in an order of the bankruptcy court stating, among other things, that "the debtors, upon accepting said share of the Settlement Proceeds are deemed to have waived all claim to any part of Trustee's portion of the Settlement Proceeds. …"

After obtaining the settlement proceeds, the chapter 7 trustee deducted and paid "estimated" taxes to state and federal authorities, and distributed half of the remaining funds to the co-debtors. The trustee then filed a final report and account reflecting these actions. The co-debtors did not object to the trustee's final report and said report was approved by the bankruptcy court.

Several months later, federal taxing authorities refunded $1,972.35 of the "estimated" taxes paid by the trustee in connection with the class action settlement. After reopening the case, the trustee filed an amended final report seeking to distribute the refund to creditors. One of the co-debtors filed a late objection to the trustee's amended final report. The bankruptcy court overruled the objection based on the language contained in its earlier order waiving any interest held by the co-debtors in the trustee's portion of the settlement proceeds.

On appeal, the Bankruptcy Appellate Panel for the Eighth Circuit Court of Appeals affirmed the bankruptcy court's decision. In so doing, the B.A.P. noted that bankruptcy courts are entitled to great deference when interpreting their own orders, and stated that the co-debtors had clearly waived any claim to receive – or to direct distribution of – additional funds from the settlement.