

IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF: )  
)  
ADESTA COMMUNICATIONS, INC., )  
)  
Debtor(s). ) CASE NO. BK01-83236  
MICHAEL MAIDY, Trustee of the ) A03-8102  
Unsecured Creditors' Trust, )  
)  
Plaintiff, ) CH. 11  
)  
vs. )  
)  
AMERICAN DIRECTIONAL )  
BORING, INC., )  
)  
Defendant. )

MEMORANDUM

This matter is before the court on the defendant's motion for summary judgment (Fil. #25) and response by the plaintiff (Fil. #32), and on the plaintiff's objection to the second declaration of David Fischer submitted in support of the motion for summary judgment (Fil. #41). Anna Bednar represents the plaintiff, and Leanne Gifford represents the defendant. The motion was taken under advisement as submitted without oral arguments. This memorandum contains findings of fact and conclusions of law required by Federal Rule of Bankruptcy Procedure 7052 and Federal Rule of Civil Procedure 52. This is a core proceeding as defined by 28 U.S.C. § 157(b)(2)(F).

The motion for summary judgment is denied. The objection to the Fisher declaration is sustained.

This lawsuit was brought to recover preferential payments made by the debtor to the defendant. American Directional Boring, Inc. ("ADB"), is a vendor with whom Adesta Communications did business pre-petition. It is an unsecured creditor. Within 90 days prior to the petition date of November 2, 2001, Adesta transferred \$161,701.81 to ADB in two payments. The trustee of the unsecured creditors' trust asserts that those payments were for antecedent debt. ADB argues that it provided considerably more than that amount in new value, so the payments

are protected under § 547(c)(4). ADB also argues that the transfers are not avoidable because they were made in the ordinary course of business between the parties and therefore are covered under § 547(c)(2).

### I. Summary Judgment Standard

Summary judgment is appropriate only if the record, when viewed in the light most favorable to the non-moving party, shows there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law. Fed. R. Civ. P. 56(c) (made applicable to adversary proceedings in bankruptcy by Fed. R. Bankr. P. 7056); see, e.g., Celotex Corp. v. Catrett, 477 U.S. 317, 322-23 (1986); Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 249-50 (1986); Morgan v. Rabun, 128 F.3d 694, 696 (8th Cir. 1997), cert. denied, 523 U.S. 1124 (1998); Get Away Club, Inc. v. Coleman, 969 F.2d 664, 666 (8th Cir. 1992); St. Paul Fire & Marine Ins. Co. v. FDIC, 968 F.2d 695, 699 (8th Cir. 1992).

### II. Preferential Transfers

A payment or transfer is preferential and may be avoided by the trustee if it was made –

- (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;

\* \* \*

- (5) that enables such creditor to receive more than such creditor would receive if –
  - (A) the case were a case under chapter 7 of this title;
  - (B) the transfer had not been made; and
  - (C) such creditor received payment of such debt to the extent provided by the provisions of this title.

11 U.S.C. § 547(b).

ADB does not dispute that the payments were preferences. Instead, it focuses on two defenses to the trustee's ability to

recover preferential transfers.

### III. "Subsequent New Value" Exception

Section 547(c)(4) of the Bankruptcy Code excepts certain transfers from the trustee's avoidance power if such transfer was to or for the benefit of a creditor, to the extent that, after such a transfer, such creditor gave new value to or for the benefit of the debtor (A) not secured by an otherwise unavoidable security interest; and (B) on account of which new value the debtor did not make an otherwise unavoidable transfer to or for the benefit of such creditor. 11 U.S.C. § 547(c)(4).

The purpose of the defense is to encourage creditors to deal with financially distressed debtors with the goal of rehabilitation. Kroh Bros. Dev. Co. v. Continental Constr. Eng'rs, Inc. (In re Kroh Bros. Dev. Co.), 930 F.2d 648, 651 (8th Cir. 1991).

To prevail on a subsequent new value defense under § 547(c)(4), the creditor must establish by a preponderance of the evidence that (1) the creditor received a transfer that is otherwise avoidable as a preference under § 547(b); (2) after receiving the preferential transfer, the creditor advanced new value to the debtor on an unsecured basis; and (3) the debtor did not compensate the creditor with an "otherwise unavoidable" transfer for the new value as of the petition date. Shodeen v. Airline Software, Inc. (In re Access Air, Inc.), 314 B.R. 386, 395 (B.A.P. 8th Cir. 2004) (citing Kroh Bros. at 652).

The relevant inquiry is whether the new value replenishes the estate. Kroh Bros. at 652. To calculate the amount of new value provided, the majority of courts follow what is known as the "Garland Rule," which allows a given extension of new value to be applied against any preceding preference. Strauss v. Janesville Prods. (In re Acoustiseal, Inc.), 318 B.R. 521, 525 (Bankr. W.D. Mo. 2004) (citing Thomas W. Garland, Inc. v. Union Elec. Co. (In re Thomas W. Garland, Inc.), 19 B.R. 920 (Bankr. E.D. Mo. 1982)). The Acoustiseal court gives this example:

[I]f Acoustiseal made a payment to Janesville in the amount of \$1000.00 for no new value, then made another payment for \$1000.00 and Janesville then provided Acoustiseal with \$3000.00 worth of product, the trustee could not avoid either of the preferential payments. The subsequent new value would absorb both

payments. This is known as the Garland Rule.

318 B.R. at 525-26.

The Acoustiseal court also predicts the Eighth Circuit Court of Appeals, if given the opportunity, would endorse the Garland Rule because it best construes the plain language of § 547(c)(4) and comports with the instruction to determine whether the new value replenishes the estate. Id. at 526.

In the present case, ADB contends that it extended nearly \$390,000 of new value during the preference period for which it was not paid. The trustee disputes that, offering the declaration of the trustee's financial advisor, who states that the debtor's records regarding the amount owed to ADB are consistent with the amended proof of claim filed by ADB in the bankruptcy case in the amount of \$98,568.02. There was no supporting documentation attached to that declaration, however. By the same token, the evidence in support of ADB's allegation is unclear as to whether the work was actually performed. In that regard, the trustee objected to the second declaration of David Fischer, which purports to verify the unpaid invoices. The trustee is correct that, at a minimum, the entire declaration lacks foundation. For that reason, the objection is sustained and the declaration will not be considered. A trial will be necessary to adduce evidence on the issue of whether and how much new value was provided.

#### IV. "Ordinary Course of Business" Exception

Section 547(c)(2) of the Bankruptcy Code excepts certain transfers from the trustee's avoidance power to the extent such transfer was "(A) in payment of a debt incurred by the 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[.]" 11 U.S.C. § 547(c)(2). Because no precise legal test exists, resolution of the ordinary course of business question requires a peculiarly factual analysis. Harrah's Tunica Corp. v. Meeks (In re Armstrong), 291 F.3d 517, 527 (8th Cir. 2002). Its purpose is to encourage creditors to continue to deal with financially troubled debtors. Id. The exception is construed narrowly, however, because it places one creditor on better footing than all other creditors. Id.

Under § 547(c)(2)(B), the transferee must demonstrate by a preponderance of the evidence that the transfer was subjectively ordinary in that the debtor made the transfer in the ordinary course of the business or financial affairs of the debtor and the transferee. The transferee must also establish under § 547(c)(2)(C) that the transfer was objectively ordinary in that the debtor made the transfer according to ordinary business terms. Access Air, 314 B.R. at 392.

The transferee has to establish a "baseline" of pre-preference period transactions between it and the debtor to enable the court to compare the debtor's preference-period payment practice with its prior payment practices. Id. at 393. The controlling factor is whether the transactions between the debtor and the transferee were consistent both before and during the preference period. Stewart v. Barry County Livestock Auction, Inc. (In re Stewart), 282 B.R. 871, 875 (B.A.P. 8th Cir. 2002).

"The overriding factor as to whether the transfers in question were subjectively ordinary under § 547(c)(2)(B) is whether there is some consistency between the payments debtor made to the transferee prior to the preference period and the preference payments." Access Air, 314 B.R. at 393 (citing Lovett v. St. Johnsbury Trucking, 931 F.2d 494, 497-98 (8th Cir. 1991)). The appellate court noted that a late payment during the preference period may be subjectively ordinary if the debtor also made late payments during the pre-preference period. "A tardy preference payment, however, is not subjectively ordinary if it is substantially more tardy than the debtor's late payments during the pre-preference period." Access Air, 314 B.R. at 393 (citing Official Plan Comm. v. Gateway Pac. Corp. (In re Gateway Pac. Corp.), 153 F.3d 915, 918 (8th Cir. 1998)). In Access Air, the debtor's pattern was to pay late, both prior to and during the preference period. However, the lateness increased by 294 percent during the preference period, which the court ruled was not subjectively ordinary.

To demonstrate objective ordinariness in the business dealings, the transferee must produce objective evidence of the range of prevailing practices utilized within the debtor's industry involving transactions similar to the transfer in question and that the transfer fits into that range. Access Air, 314 B.R. at 394 (citing Jones v. United Sav. & Loan Assoc. (In re U.S.A. Inns), 9 F.3d 680, 684 (8th Cir. 1993)).

Other factors regarding the ordinary course of business between the parties may be considered, including the length of time the parties were engaged in the transactions at issue, whether the amount or form of payment differed from past practices, whether either party engaged in unusual collection or payment activity, and whether the creditor took advantage of the debtor's deteriorating financial condition. See Central Hardware Co. v. The Walker-Williams Lumber Co. (In re Spirit Holding Co., Inc.), 214 B.R. 891, 897 (E.D. Mo. 1997), aff'd, 153 F.3d 902 (8th Cir. 1998). These factors have more weight in the analysis if the issue of timing is a close one. Concast Canada, Inc. v. Laclede Steel Co. (In re Laclede Steel Co.), 271 B.R. 127, 132 (B.A.P. 8th Cir. 2002).

In this case, ADB submitted evidence that the average length of time to payment of the two invoices paid by Adesta during the pre-preference period was 92 days (ranging from 87 to 96 days), and that the average length of time to payment of the seven invoices paid during the preference period was 110 days (ranging from 82 to 161 days). The payment delay was 20 percent longer during the preference period. Much of the caselaw in this circuit deals with more significant disparities, such as the 237 percent increase in the "excruciating lateness" of the payments in Laclede Steel, the 294 percent increase in tardiness in Access Air, and the 54 percent increase in lateness in Gateway Pacific Corp. On the other hand, a 19 percent difference (10 days) was not considered significant enough to fall outside the ordinary course of business in Lovett v. St. Johnsbury Trucking, 931 F.2d at 498.

The trustee makes much of the fact that the debtor paid six of the preference period invoices at once, suggesting that such a lump-sum payment is not "ordinary course." The manner in which payments were made during the preference period may have something to do with Adesta's parent company, Bracknell, having control of Adesta's money, so Adesta could not write checks until Bracknell released the funds. Whether or not the transactions between Adesta and ADB were in the ordinary course is a question of fact which cannot be answered on the record presently before the court. Testimony as to the pre-preference-period course of dealings between Adesta and ADB would be helpful to give a fuller picture of the baseline against which to compare the preference-period transactions. In addition, the record contains no probative evidence of industry standards against which to compare these transactions. Such evidence is necessary to put these transactions into perspective.

V. Conclusion

There are significant issues of fact regarding elements of ADB's defenses to the trustee's preference action. A trial will be scheduled to permit the parties to provide the court with testimony on these issues. A separate order will be entered denying the defendant's motion for summary judgment.

DATED: May 2, 2005

BY THE COURT:

/s/ Timothy J. Mahoney  
Chief Judge

Notice given by the Court to:

Robert V. Ginn	Michael Becker
Anna Bednar	Raymond Aranza
Jeffrey Nolan	*Leanne Gifford
U.S. Trustee	

Movant (\*) is responsible for giving notice of this order to all other parties not listed above if required by rule or statute.

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ORDER

This matter is before the court on the defendant's motion for summary judgment (Fil. #25) and response by the plaintiff (Fil. #32), and on the plaintiff's objection to the second declaration of David Fischer submitted in support of the motion for summary judgment (Fil. #41). Anna Bednar represents the plaintiff, and Leanne Gifford represents the defendant. The motion was taken under advisement as submitted without oral arguments.

IT IS ORDERED: For the reasons stated in the Memorandum filed herewith, the defendant's motion for summary judgment (Fil. #25) is denied. The plaintiff's objection to the second declaration of David Fischer submitted in support of the motion for summary judgment (Fil. #41) is sustained. The case shall be scheduled for trial.

DATED: May 2, 2005

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