

**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF KANSAS**

<b>In Re:</b>	)	
	)	
<b>SHIRLEY McQUEEN</b>	)	<b>Case No. 01-13746</b>
	)	<b>Chapter 7</b>
<b>Debtor.</b>	)	
_____	)	
	)	
<b>EDWARD J. NAZAR, Trustee</b>	)	
<b>Bankruptcy of Shirley McQueen</b>	)	
	)	
<b>Plaintiff,</b>	)	
	)	
<b>v.</b>	)	<b>Adversary No. 02-5017</b>
	)	
<b>FAIRBANKS CAPITAL CORP.,</b>	)	
	)	
<b>Defendant.</b>	)	
_____	)	

**MEMORANDUM AND ORDER**

This matter is before the court on the Trustee’s Complaint for Avoidance of Preferential Transfer (Doc. 1) and the Debtor’s cross-claim against Defendant Fairbanks Capital Corporation (Doc. 16). The Court has reviewed the arguments presented by the parties, the stipulated facts and the relevant law concerning this motion and is now prepared to rule. The Court has jurisdiction under 28 U.S.C. § 157(b).

**I. FINDINGS OF FACT**

The parties have submitted a Stipulated Statement of Facts (Doc. 19). Based on the Stipulated Statement of Facts, the Court makes the following findings of fact:

1. Fairbanks holds the second mortgage on the Debtors’ homestead.
2. The outstanding debt due Fairbanks at the time of the bankruptcy filing was \$34,187.18.

3. Fairbanks received a lump sum payment of \$2,518.62 in the 90 days prior to the filing of the bankruptcy petition.
4. The payment was not a regular monthly payment, which monthly payment is \$368.37.
5. The payment was made to bring the Debtor current on her payments prior to the bankruptcy filing.
6. The fair market value of the real estate is \$64,900.
7. The outstanding balance of the first mortgage is approximately \$43,356.92.
8. Thus, Fairbanks is undersecured by approximately \$12,500.

Additional facts will be discussed below, when necessary.

## **II. ANALYSIS**

The parties to this adversary proceeding, including the Debtor who was granted permission to intervene, have raised two issues. First, the Trustee contends, over objections by both Debtor and Fairbanks, that the transfer in the amount of \$2,518.62 was preferential under 11 U.S.C. § 547<sup>1</sup> and can be avoided by the Trustee. Second, Debtor contends in her cross-claim, over objection by Fairbanks only, that in the event the Trustee is successful in avoiding the transfer, Fairbanks should be precluded from charging the amount of the transfer back to Debtor's account.

### **A. The transfer of \$2,518.62 to Fairbanks was an avoidable transfer.**

The Trustee contends that the payment made to Fairbanks in the amount of \$2,518.62 within ninety days of bankruptcy constitutes a voidable preferential transfer pursuant to § 547(b). The Trustee can avoid this transfer, subject to certain exceptions, upon showing that the transfer of Debtor's property was:

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<sup>1</sup>Unless otherwise noted, all future statutory references are to the United States Bankruptcy Code, 11 U.S.C. § 101 et seq.

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

Both Debtor and Fairbanks admit that the first four elements under § 547(b) have been conclusively established. Therefore, the Court must only decide whether the fifth and final element under § 547(b) has been established in order to determine if the payment was a preferential transfer. Plaintiff, as Trustee, has the burden of proving the avoidability of the transfer. 11 U.S.C. § 547(g).

Pursuant to § 547(b), the Trustee must prove that the transfer to Fairbanks enabled Fairbanks to receive more than it would have received if the transfer had not been made and the Debtor liquidated her assets. On the date the bankruptcy was filed, Fairbanks was undersecured by approximately \$12,500.00. Generally, an undersecured creditor who receives payment during the preference period will receive more than it would have received in a Chapter 7 liquidation unless the payment releases a proportional amount

of secured collateral or all unsecured creditors will receive a 100% distribution. *In re Furley's Transport, Inc.*, 272 B.R. 161 (Bankr. D. Md. 2001). This issue is also discussed in *Collier on Bankruptcy* as follows:

Payments to a partially secured creditor from property not covered by its lien, however, have a preferential effect, because in a chapter 7 liquidation that creditor would receive a distribution for the full value of its secured claim, in addition to the payments already received. In other words, the payment would ordinarily be applied to the unsecured portion of the undersecured debt, but would not reduce the lien or increase the debtor's equity in the collateral.

*Collier on Bankruptcy*, § 547.03[7], at 547-46 (15<sup>th</sup> ed. rev. 2002). "Payments on an undersecured debt are conclusively attributable first to the unsecured portion of the debt." *In re Tax Reduction Institute*, 148 B.R. 63, 69 (Bankr. D. Colo. 1992).

The value of the home was approximately \$65,000, and the amount due on the first mortgage was approximately \$43,500. This left just over \$21,500 in equity to cover Fairbanks' \$34,000 mortgage on the property, leaving Fairbanks undersecured by approximately \$12,500. The Trustee claims that because Fairbanks is undersecured, the payment made by Debtor within 90 days of her filing the bankruptcy petition, under a hypothetical liquidation analysis, allowed Fairbanks to receive more than it would have received had the payment not been made. Conversely, Debtor's argument is that if she had liquidated under Chapter 7, Fairbanks would have received the \$21,500 in equity following the sale of the property, which, according to Debtor, is more than the \$2,500 transfer received by Fairbanks.

Section 547(b)(5) requires the Court to analyze what Fairbanks would have received had the \$2,500 payment not been made compared to what Fairbanks would receive if the payment is allowed to stand. Thus, if the house was liquidated, Fairbanks would have received approximately \$21,500 (the

equity over the first mortgage) from the sale proceeds if the transfer had not been made. However, it would have received approximately \$24,000 (\$21,500 + \$2,500) if the house was liquidated and the transfer not avoided. Similarly, if the house was not liquidated, Fairbanks would have received no sale proceeds, but it would receive the approximate \$2,500 payment as well as be entitled to retain its mortgage on the property, which has a secured value of \$21,500. Under either scenario, it is clear that Fairbanks will have received a larger portion of the bankruptcy estate if the payment is allowed to stand than it would have if the payment had not been made. Therefore, the Trustee has met his burden to prove the fifth element of § 547(b)(5).

The payment made by Debtor to Fairbanks constitutes a preference pursuant to § 547(b). Based on Fairbank's status as an undersecured creditor, the Court finds Fairbanks did receive a larger amount due to the payment than it would have received if the payment had not been made and the Debtor liquidated all her property. Therefore, the Trustee has established all the required elements of a preferential transfer, and Fairbanks is ordered to turn over \$2,518.62 to the Trustee for the benefit of the bankruptcy estate.

**B. Does Fairbanks have a claim against the Debtor in the amount of the preferential transfer that has been avoided?**

The Debtor has filed a cross claim in this action seeking an order from the Court that would bar Fairbanks from "charging back" to the Debtor's account the amount the Court has now held is a preference. The Debtor contends that if Fairbanks is required to turn over the amount of the preferential payment, Fairbanks should be required to take the loss on the transfer and never be able to assert a claim against the Debtor, or the subject property, to recover the amount of money returned to the Trustee.

Although the Code does not specifically grant a creditor the right to make a claim back against a debtor's estate following the disgorgement of funds based on the Trustee's avoiding powers, certain provisions in the Code make it clear that such a claim exists. A trustee has the authority, subject to certain restrictions, to recover property from the transferee of a voided transfer under § 550. Section 502(h) states that "[a] claim arising from the recovery of property under section 522, 550, or 533 of this title shall be allowed . . . or disallowed . . . the same as if such claim had arisen before the date of the filing of the petition." 11 U.S.C. § 502(h).

It is clear from reading § 550 and § 502(h) together that a creditor who is forced to disgorge funds based on the Trustee's avoidance powers has the authority to then make a claim against the estate to recover those funds. This is supported by *Colliers on Bankruptcy*, which states that "to the extent one becomes a claimant by reason of the recovery of property predicated upon an avoiding power, the claim, if allowable, has the status of a claim existing at the date of the filing of the petition." *Collier on Bankruptcy*, § 502.09[2], at 502-72 (15<sup>th</sup> ed. rev. 2002). See also *In re Dominion Corp.*, 199 B.R. 410, 413 (9<sup>th</sup> Cir. B.A.P. 1996) (holding that the recourse for a transferee who is forced to turn over money to the trustee under the trustee's avoidance powers is to file a claim with the bankruptcy estate).

In essence, § 502(h) and § 550 operate to unwind a transaction that was preferential in nature and put the parties back into the position they would have been had the transfer not taken place. The basis for the Trustee's power to avoid preferential transfers is to see that all creditors of the bankruptcy estate receive their proportionate share of the estate assets. By avoiding a transfer, the Trustee can assure that the creditor that received the preferential transfer is not treated any better than other similarly situated

creditors, by putting the creditor back in the same position it was in prior to the filing of the bankruptcy. Were the Court to require Fairbanks to return the transfer to the Trustee for the benefit of the estate, and then prohibit Fairbanks from debiting the Debtor's account the same amount it is returning and making a claim against the estate in that amount, Fairbanks would be placed in a worse position than other similarly situated creditors.

If Debtor's argument was correct, the remaining creditors of the bankruptcy estate would be treated preferentially to Fairbanks, which is no more appropriate than allowing Fairbanks to be treated preferentially to the other creditors. Therefore, Fairbanks does have the right to debit the Debtor's account in the amount it is ordered to return to the Trustee, and then make a claim against the bankruptcy estate equal to the amount of money it is required to turn over.

### **III. CONCLUSION**

The Court finds that Debtor's payment to Fairbanks in the amount of \$2,518.62 constitutes a preferential payment that can be avoided by the Trustee. The parties stipulated that the first four elements of § 547(b) have been met by the Trustee. Because of the undersecured status of Fairbanks and the effect that status has on the amount of money it stands to recover in a Chapter 7 liquidation, the Court finds that the Trustee has met the fifth requirement of § 547(b), as well. Therefore, the Court will enter judgment in favor of the Trustee and against Fairbanks in the amount of \$2,518.62, plus the costs associated with this action.

The Court also finds that Debtor's cross-claim against Fairbanks must be denied. Fairbanks is entitled to debit the Debtor's account in the same amount it is returning to the Trustee, and make a claim against the estate as a result of the Trustee's avoiding powers.

**IT IS, THEREFORE, BY THIS COURT ORDERED** that judgment is entered on the Complaint for Avoidance of Preferential Transfer (Doc. 1) in favor of the Plaintiff Trustee in the amount of \$2,518.62, together with the costs of this action.

**IT IS FURTHER ORDERED** that the judgment is entered on Debtor's Cross-Claim (Doc. 21) in favor of Fairbanks, plus costs associated with that cross-claim.

**IT IS SO ORDERED** this 13<sup>th</sup> day of June, 2003.

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JANICE MILLER KARLIN, Bankruptcy Judge  
United States Bankruptcy Court  
District of Kansas

#### CERTIFICATE OF MAILING

The undersigned certifies that a copy of the Memorandum and Order and Judgment on Decision were deposited in the United States mail, prepaid on this 13<sup>th</sup> day of June, 2003, to the following:

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Debra C. Goodrich  
Judicial Assistant to:

The Honorable Janice Miller Karlin  
Bankruptcy Judge