

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF KANSAS

IN RE:)	
)	
FRANK MATTHEW WILLIAMS,)	Case No. 99-14089
SHIRLEY BELL WILLIAMS,)	Chapter 7
)	
Debtors.)	
_____)	
)	
J. MICHAEL MORRIS, Trustee,)	
)	
Plaintiff,)	
)	
v.)	Adversary No. 00-5062
)	
OMPAL S. CHAUHAN,)	
)	
Defendant.)	
_____)	

MEMORANDUM OPINION AND ORDER GRANTING TRUSTEE'S COMPLAINT TO AVOID
AND RECOVER PREFERENTIAL TRANSFER

This matter came before the Court for hearing on December 19, 2000 concerning the Trustee's Complaint To Avoid and Recover Preferential Transfer. J. Michael Morris, the Chapter 7 trustee (Trustee), seeks to avoid and recover monies garnished by defendant Ompal Chauhan (Chauhan) from the Debtors' wages during the 90 days preceding the filing of their Chapter 7 petition. Both parties appeared pro se and stipulated to the admission of the proffered exhibits.

Debtors Frank and Shirley Williams (Debtors) filed their case on October 29, 1999 and the parties stipulate that the 90-day preference period extends to, and includes, July 31, 1999. 11 U.S.C. §547(b)(4)(A).¹ Chauhan requested several garnishments prior to July 31 and garnishment orders were issued and served prior to that time. Garnishment orders were served within the 90-

¹All subsequent statutory references are to the Bankruptcy Code, 11 U.S.C. §101, et seq. unless otherwise noted.

day period as well. Being wage garnishments, the orders, once served, attached earnings of the Debtors for any pay period ending within the 30 days after service. See Kan. Stat. Ann. § 61-2005 (1999). Resolving this case requires the Court to consider: (1) whether the fact that certain of the garnishment orders were issued before the 90 days began insulates the wages earned and attached within the 90 days from avoidance; (2) whether the Debtors were solvent at the time of the transfers; and (3) whether Chauhan received more by his garnishments than he would have in a chapter 7 liquidation. In addition, defendant raises the §547(c)(8) affirmative defense that the case involves primarily consumer debt and that the transfers are for less than \$600. For the reasons set forth below, judgment should be entered for the Trustee, but only to extent set forth herein.

JURISDICTION

The Court has jurisdiction over this proceeding. 28 U.S.C. § 1334. This adversary proceeding is a core proceeding. 28 U.S.C. § 157 (b)(2)(K).

FACTS

On December 10, 1998, Chauhan obtained a judgment for unpaid rents against the Debtors for \$4902.00 in the District Court of Sedgwick County, Kansas. Beginning in April 1999, Chauhan requested garnishments of Frank Williams' wages to collect his judgment.² On May 5, 1999, an order of garnishment was served on Boeing. Boeing filed its answer on May 18, 1999 stating that Mr. Williams' employment was terminated on March 26, 1999.

Thereafter, on July 22, 1999, Chauhan requested garnishment of Frank Williams' wages from Apex Engineering (Apex).³ A garnishment order was served by certified mail to Apex on

²See Trustee's Exhibit 3.

³See Trustee's Exhibit 4.

July 30, 1999. Apex filed two answers on August 25, 1999 reporting that \$224.33 had been garnished from Mr. Williams' wages for the pay period from July 26, 1999 through August 8, 1999, and \$262.01 had been garnished for the pay period from August 9, 1999 through August 22, 1999. The court ordered these monies to be paid in on September 1, 1999 and September 22, 1999, respectively.

On August 30, 1999, another order of garnishment was served by certified mail on Apex.⁴ Apex filed its answer on September 9, 1999 reporting that \$135.86 had been garnished from Frank Williams' wages for the pay period August 23, 1999 through September 5, 1999. The court ordered this amount to be paid in on November 23, 1999.⁵

On September 15, 1999, the court issued a third order of garnishment which was served by certified mail dated on Apex.⁶ Apex filed its answer on September 17, 1999 reporting that Frank Williams' employment had been terminated on September 3, 1999.

Beginning on July 13, 1999, Chauhan sought to garnish Shirley Williams' wages from KSNW, Channel 3 (KSNW).⁷ On July 21, 1999, KSNW received by certified mail an order of garnishment. KSNW filed its answer on August 18, 1999 reporting that \$455.14 had been garnished from Mrs. Williams' wages for the pay period July 11, 1999 through August 7, 1999. The court ordered this amount to be paid in on September 9, 1999. Another garnishment order was served by certified mail on August 30, 1999 covering the pay period August 29, 1999 through

⁴See Trustee's Exhibit 5.

⁵See Trustee's Exhibit 7.

⁶See Trustee's Exhibit 8.

⁷See Trustee's Exhibit 9.

September 24, 1999 for \$455.14. The order to pay in to the court was filed on October 12, 1999. A third garnishment order was filed on September 13, 1999 covering September 19, 1999 through October 2, 1999 for \$227.57. No order to pay this garnishment in to the court was filed.

The Debtors filed their Chapter 7 petition on October 29, 1999. Chauhan released the last garnishment of Shirley Williams' wages on November 12, 1999.⁸

ANALYSIS

Under Kansas law, wage garnishment orders attach "...the non-exempt portion of the [debtor's] earnings for any pay period or periods which end during the 30-day period beginning the day the order is served." Kan. Stat. Ann. § 61-2005(c) (1999).⁹ At issue in this case is whether the lien of these garnishment orders serves to attach wages to be earned during the 90 day period before the debtor has actually earned them.

With respect to the garnishment orders served within the 90-day lookback period, the Court may easily find that preferential transfers were made. Assuming the Debtors were not solvent (as will be discussed infra), these orders and the transfers they effected meet all of the requirements of §547(b). To prevail in an action to avoid a preference, the Trustee must show that the transfer in question was (1) to or for the benefit of a creditor, (2) on account of an antecedent debt, (3) made while the debtor was insolvent, (4) made within 90 days of the commencement of the case, and (5) resulted in the creditor receiving more than it would have in a chapter 7 liquidation had the transfer not been made. §547(b). With respect to the August 30, 1999 garnishment of Frank Williams' wages and the August 30 and September 13, 1999 garnishments of Shirley Williams'

⁸See Trustee's Exhibit 12.

⁹The Court notes that, as a result of legislative activity in 2000, Kansas creditors may now obtain a form of continuing garnishment, see K.S.A. 61-3507(c) (2000).

wages, the Court can easily find that the transfers were made within 90 days of the commencement of the case.

Determining the preferential effect of the garnishment orders issued prior to the commencement of the preference period requires consideration of two competing schools of thought concerning wage garnishments in bankruptcy. A minority of courts holds that if a garnishment order is served prior to the commencement of the preference period, the lien of that order attaches not only to earnings accrued before the period, but also to those which accrue thereafter. Chauhan relies on Matter of Coppie, 728 F.2d 951 (7th Cir. 1984), in which the Seventh Circuit, relying on Indiana law, found that the lien of a continuing wage garnishment served prior to the commencement of the 90-day period constituted a lien on any wages earned thereafter which was superior to the Trustee's interest. There the court determined that, because the garnishee became accountable to the creditor for any wages earned by the debtor from the garnishee from the day the order was served, the debtor essentially lost any property interest in the garnished wages. Id. at 952-53. The court specifically held that the provisions of §547(e)(3)¹⁰ do not apply in this situation because, as to the debtor's future wages, the debtor will never acquire any rights. Id. at 953.

Another leading case for the minority position is In re Riddervold, 647 F.2d 342 (2nd Cir. 1981). Here, the court dealt with a New York continuing garnishment and held that the lien of the garnishment effected a novation of the contract between the debtor and his employer, replacing the debtor with the garnishing creditor and thereby preventing any transfer of property (wages) from debtor to the creditor. Id. at 345. Instead, the Second Circuit reasoned that the creditor now

¹⁰11 U.S.C. §547(e)(3) states: "For the purposes of this section, a transfer is not made until the debtor has acquired rights in the property transferred."

owned the garnished portion of the debtor's wages. Id.

Riddervold does not mention §547(e)(3) and Coppie finds it inapplicable, stating that the section “does not come into play in this case simply because after a garnishment order providing for a continuing lien is entered..., a debtor will never acquire rights in the portion of his or her wages to be garnished in the future...” 728 F.2d at 953. This Court notes that the garnishments in issue here are not of a continuing nature, making these cases distinguishable.

The more logically attractive view is that garnished wages are “transferred” for preference purposes only when they have been earned and are due. Even before the Bankruptcy Code was enacted, the Supreme Court had made it clear that a debtor has no rights in the property interest which is his right to collect wages until they have been earned. Local Loan Co. v. Hunt, 292 U.S. 234, 54 S.Ct. 695, 78 L.Ed 1230 (1934). Typically, “[i]n the absence of any controlling federal law, ‘property ‘ and ‘interests in property’ are creatures of state law.” Barnhill v. Johnson, 503 U.S. 393, 112 S.Ct. 1386, 118 L.Ed.2d 39 (1992), citing Butner v. United States, 440 U.S. 48, 99 S.Ct. 914, 59 L.Ed2d 136 (1979). “What constitutes a transfer and when it is complete” is a matter of federal law. Barnhill, 112 L.Ed 2d at 1386. The Bankruptcy Code defines a transfer as “every mode...of disposing of or parting with property or an interest in property....” §101(54). Later, §547(e)(3) provides that for preference purposes, “... a transfer is not made until the debtor has acquired rights in the property transferred.” Section 547(e)(3) is the sort of “controlling federal law” to which the Barnhill Court refers. Because the debtor can acquire no rights in his wages until they are earned, the garnishment cannot be said to have effected a transfer of those wages to the creditor until that time.

Among the numerous cases so holding is a recent case in this Circuit, In re Chavez, 257 B.R. 341 (Bankr. D.N.M. 2001), which holds that wages can only be transferred via garnishment

when they are earned. See also In re Wade, 219 B.R. 815 (8th Cir. BAP 1998); In re Mays, 256 B.R. 555 (Bankr. D.N.J. 2000). Plainly, § 547 (e)(3) provides that the Debtors could not transfer their wages until they were earned. Thus, those portions of the Debtors' wages attached by the pre-preference period orders, but earned by them after July 30, 1999, are recoverable by the Trustee.

Based on the forgoing, the Trustee may recover a ratable share of the Frank Williams garnishment served on July 30, 1999. With respect to the pay period of July 26 through August 8, 1999, for which some \$224.33 was garnished, the nine days' share of the wages earned on and after July 31, 1999 are subject to recovery in the amount of \$144.21 (9/14 of \$224.33). All of the \$262.01 earned from August 9 to August 22, 1999 (all within the 90 day period) is recoverable as well.

The Trustee similarly may recover a ratable share of the Shirley Williams garnishments, too. The order served on July 21, 1999 attached wages for the period of July 11, 1999 through August 9, 1999 in the amount of \$455.14. Some 20 days of this period occurred prior to July 31, 1999, rendering 10/30 of \$455.14, or \$151.71, recoverable.

As to the garnishment orders served after July 31, 1999, the Court finds that all of the attached wages are recoverable. This includes \$262.01 attached from Frank Williams' wages by the garnishment served August 9, 1999 and \$135.86 attached by the garnishment served on August 23, 1999. The \$455.14 attached by the garnishment of Shirley Williams' wages served on August 29, 1999 is also recoverable. The garnishment of \$227.57 attached by the September 19, 1999 garnishment (well after the case was filed) appears to have been released by Chauhan as of December 13, 2000, but it is unclear whether those funds were released to Mrs. Williams. In any case, those funds are a part of the property of the estate.

Chauhan asserts that the Debtors were solvent at the time of the otherwise preferential transfers. Section 547(f) provides that a debtor is presumed insolvent on and during the 90 days preceding the date of filing. This presumption is rebuttable by the preferred creditor, but the burden of proof of insolvency remains on the trustee. To rebut this presumption, Chauhan had to come forward with some evidence of the Debtors' solvency. This he failed to do. A review of the Debtors' schedules and statement of affairs, admitted into evidence by agreement, suggests that the Debtors were hopelessly insolvent at the time of filing. Even assuming that the Debtors overstated some of their debts and failed to schedule a bank account (approximately \$25), their reported assets only amount to \$11,500 and their debts \$33,511.¹¹ The Trustee has met his burden to show that the Debtors were insolvent at the time of the transfers.

Chauhan's suggestion that he received no more by the garnishments than he would have in an ordinary chapter 7 liquidation is also without merit. The Trustee demonstrated that he has \$868.38 on hand according to his interim reports and that filed claims exceed \$14,400. Chauhan received \$1148.93 in preferential garnishment payments on account of his \$4902 judgment, a "dividend" of approximately 23 per cent. If Chauhan's \$1148.93 is added back into the funds on hand in the estate, \$2017.31 would be available to address \$14,400 in claims, yielding a dividend of approximately 14 per cent.¹² Chauhan received more as a result of his garnishments than he

¹¹The Court denied Chauhan's objection to the Debtors' discharge based on their alleged failure to keep records and making false oaths in an unreported decision. In so doing, the Court considered and rejected Chauhan's assertion that a stove and refrigerator were undervalued and should have been worth \$500. See Ompal Chauhan v. Frank Matthews Williams, et al., Case no. 99-10489, Adversary No. 99-5047 (Bankr. D. Kan. March 6, 2001). Even were this to be true, the significant shortfall between the Debtors' assets and debts demonstrates their insolvency.

¹²The Court recognizes that the trustee has a turnover order requiring debtor Frank Williams to surrender a sizeable federal tax refund. However, the IRS has filed a claim exceeding \$8900 and the un rebutted evidence of the trustee was that the IRS would likely set off the refund

would have in a chapter 7 distribution. One of the purposes of bankruptcy is the fair and ratable distribution of the debtor's assets among his creditors and §547 is one of the means a trustee has of fulfilling that purpose.

The Trustee having carried his burden of proof on all of the elements of §547, the Court must now briefly address the affirmative defense of “de minimus” raised by Chauhan in his answer. Section §547(c)(8) affords creditors in consumer cases a “de minimus” exception to the preference rule by providing that–

The trustee may not avoid under this section [§547]a transfer...(8) if, in a case filed by an individual debtor whose debts are primarily consumer debts, the aggregate value of all property that constitutes or is affected by such transfer is less than \$600.

Chauhan argues that, because each of his garnished amounts were for less than \$600, each of them is excepted from §547(b). To sustain this affirmative defense, the Court must find that each garnishment is a separate transfer to which this statute applies. The Court declines to do so. Although the statute speaks of “transfer” in the singular, §102(7) offers a rule of construction which provides that “the singular includes the plural.” Thus the Court may read §547(c)(8) to require an aggregation of all of the garnishments in determining whether the \$600 threshold has been met or passed. Clearly, the threshold has been surpassed here.

A majority of courts considering the issue agree that by not aggregating de minimus transfers, courts would essentially approve preferences provided they were taken in amounts smaller than \$600. In In re Hailes, 77 F.3d 873(5th Cir. 1996), the Fifth Circuit held that the use of the terms “aggregate” and “all” in the statute imply that individual transfers should be totaled in

against its claim rendering the refund unavailable to the unsecured creditors.

determining whether the \$600 mark is reached. See also In re Djerf, 188 B.R. 586, 588 (D. Minn. 1995); In re Bunner, 145 B.R. 266, 267 (Bankr. C.D. Ill. 1992). Sustaining Chauhan's affirmative defense on these facts would effectively swallow the preference rule.

Therefore, judgment should be entered for the Trustee and against Chauhan avoiding the preferential transfers listed herein in the amount of \$1148.93 and finding that the \$227.57 garnished in September but not paid in to Chauhan is property of the estate which the Trustee may recover in separate proceedings. A Judgment on Decision will issue this day.

IT IS SO ORDERED.

Dated at Wichita, Kansas, this 19th day of March, 2001.

ROBERT E. NUGENT, BANKRUPTCY JUDGE
UNITED STATES BANKRUPTCY COURT
DISTRICT OF KANSAS

CERTIFICATE OF SERVICE

The undersigned certifies that copies of the MEMORANDUM OPINION AND ORDER were deposited in the United States mail, postage prepaid on this 19th day of March, 2001, to the following:

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