FILED
U.S. Bankruptcy Appellate Panel
of the Tenth Circuit
August 25, 2006
Barbara A. Schermerhorn
Clerk

NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE TENTH CIRCUIT

IN RE WESTERN INTEGRATED NETWORKS, LLC, CABLEXPRESS, INC., and WIN OF TEXAS GP LLC, Debtors.	BAP No. CO-06-021
TOM H. CONNOLLY, as liquidating trustee of the Consolidated WIN Liquidating Trust, Plaintiff – Appellant, v. FIBER INSTRUMENT SALES, INC., Defendant – Appellee.	Bankr. No. 02-13043-EEB Adv. No. 04-1065-MER Chapter 11 ORDER AND JUDGMENT*

Appeal from the United States Bankruptcy Court
for the District of Colorado

Before BOHANON, MICHAEL, and THURMAN, Bankruptcy Judges.[1]

MICHAEL, Bankruptcy Judge.

In this appeal, we are asked to decide whether a debtor who is presumed insolvent may also be presumed to not have the ability to pay its general

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* This order and judgment is not binding precedent, except under the doctrines of law of the case, res judicata, and collateral estoppel. 10th Cir. BAP L.R. 8018-6(a).

1 The parties did not request oral argument, and after examining the briefs and appellate record, the Court has determined unanimously that oral argument would not materially assist in the determination of this appeal. Fed. R. Bankr. P. 8012. The case is therefore ordered submitted without oral argument.

unsecured creditors 100 cents on the dollar. The appellant, the trustee of the bankruptcy estate presently before us, says yes. The appellee, who was paid in full as a result of the debtor's pre-petition largesse, contends that it does not necessarily follow from a presumption of insolvency that unsecured creditors will not be paid in full upon debtor's liquidation. The bankruptcy court agreed with the appellee, and sent the trustee home empty-handed. We rule in favor of the trustee, and reverse the decision of the bankruptcy court.

I. Factual Background

Western Integrated Networks of California Operating, LLC ("WIN CA") is a subsidiary of Western Integrated Networks, LLC ("WIN LLC"). On March 11, 2002, WIN CA, WIN LLC, and seven other related entities filed petitions for relief under Chapter 11 of the Bankruptcy Code. On June 21, 2002, two additional related entities filed Chapter 11 petitions. The cases were jointly administered.

On November 10, 2003, the bankruptcy court confirmed a liquidating plan of reorganization involving all of the debtors. Under the terms of the plan, all of the debtors were substantively consolidated into WIN LLC. A liquidating trust was created called the Consolidated WIN Liquidating Trust (the "Trust"). Tom H. Connolly ("Connolly") is the trustee of the Trust. Under the terms of the plan, all property of the consolidated debtors, including all causes of action, were transferred to the Trust.

In the 90 days prior to its bankruptcy filing, WIN CA made transfers totaling $72,902.97 to Fiber Instrument Sales, Inc. ("FIS") for goods purchased by WIN CA from FIS. These payments satisfied in full three outstanding invoices issued to WIN CA by FIS. These transfers were the subject of a preference action brought by Connolly against FIS.

Prior to trial of the preference action, the parties stipulated that FIS was entitled to a "new value" defense in the amount of $38,810.99, which reduced the

amount at issue to $34,091.98. In addition, the parties agreed that all of the elements of a preference were established except for the requirement under § 547(b)(5).[2] The only other matter remaining at issue was whether FIS was entitled to assert as a defense to the preference action that the payments which it had received from WIN CA were made in the ordinary course of business.

Trial of the adversary proceeding to the court was held on October 20, 2005. At trial, Connolly presented evidence to show that liquidation of the consolidated entity of WIN LLC would result in a distribution to unsecured creditors of approximately 21%. No such evidence was presented with respect to WIN CA as a separate entity. At the conclusion of presentation of evidence by Connolly, FIS moved for a directed verdict.[3] The bankruptcy court took the motion under advisement, and directed FIS to present its evidence as to all issues then before the court.[4]

On February 27, 2006, following the submission of post-trial briefs, the bankruptcy court found in favor of FIS on its motion. Specifically, the bankruptcy court found that Connolly failed to present evidence to establish that

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[2] Under § 547(b)(5), the transfers at issue must cause the creditor to receive more than it would have received if the debtor had been liquidated under Chapter 7 of the Bankruptcy Code. *See* 11 U.S.C. § 547(b)(5). Unless otherwise noted, all statutory references are to sections of the United States Bankruptcy Code, 11 U.S.C. § 101 *et seq.*

[3] Counsel for FIS made no reference to any statutory authority for such a motion. A motion for directed verdict is not a proper procedural vehicle in a bench trial. The correct procedural vehicle is a motion for judgment as a matter of law under Federal Rule of Civil Procedure 52(c), which is made applicable to adversary proceedings brought in bankruptcy cases by Federal Rule of Bankruptcy Procedure 7052. Motions for directed verdict are governed by Federal Rule of Civil Procedure 50. Under Federal Rule of Bankruptcy Procedure 9015, this rule applies in bankruptcy cases only if the matter at issue is tried to a jury. Notwithstanding the improper description of the remedy sought, the trial court apparently treated the motion for directed verdict as a motion for judgment under Federal Rule of Civil Procedure 52(c), and we shall do the same for purposes of appeal.

[4] Such a procedure is expressly permitted under Federal Rule of Civil Procedure 52(c).

FIS received more as a result of the payments from WIN CA than it would have received had WIN CA been liquidated in a Chapter 7 case. The bankruptcy court rejected the notion that the unrebutted presumption of WIN CA's insolvency was sufficient to establish that FIS received more through payment in full of its invoices than it would have received in a Chapter 7 liquidation. Having found in favor of FIS on this issue, the bankruptcy court did not reach the issue of whether the payments by WIN CA to FIS were made in the ordinary course of business. This appeal followed.

II. Appellate Jurisdiction

This Court has jurisdiction to hear timely-filed appeals from "final judgments, orders, and decrees" of bankruptcy courts within the Tenth Circuit, unless one of the parties elects to have the district court hear the appeal.[5] Neither party elected to have this appeal heard by the United States District Court for the District of Colorado. The parties have thus consented to appellate review by this Court.

A decision is considered final "if it 'ends the litigation on the merits and leaves nothing for the court to do but execute the judgment.'"[6] In this case, the decision of the bankruptcy court terminated the adversary proceeding at issue. Nothing remains for the bankruptcy court's consideration. Thus, the decision is final for purposes of review.

III. Standard of Review

Resolution of this appeal hinges upon the interpretation of § 547(b)(5) and (f). Statutory construction is a matter of law which we review *de novo*.[7] When

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[5] 28 U.S.C. § 158(a)(1), (b)(1), and (c)(1); Fed. R. Bankr. P. 8002.

[6] *Quackenbush v. Allstate Ins. Co.*, 517 U.S. 706, 712 (1996) (quoting *Catlin v. United States*, 324 U.S. 229, 233 (1945)).

[7] *See In re Gledhill*, 164 F.3d 1338, 1340 (10th Cir. 1999) ("The district (continued...)

reviewing questions of law *de novo*, the appellate court is not constrained by the trial court's conclusions.[8]

IV. Discussion

This appeal deals with a rather routine preference claim. Under § 547(b),

> (b) Except as provided in subsections (c) and (i) 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;
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> (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
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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
> (C) such creditor received payment of such debt to the extent provided by the provisions of this title.[9]

Section 547(f) provides that "[f]or the purposes of this section, the debtor is presumed to have been insolvent on and during the 90 days immediately preceding the date of the filing of the petition." In addition, § 547(g) places the

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[7] (...continued)
court's interpretation of a statute is a question of law subject to de novo review by this court."); *see also In re Duncan*, 294 B.R. 339, 342 (10th Cir. BAP 2003) (citing *Gledhill*).

[8] *Wolfgang v. Mid-America Motorsports, Inc.*, 111 F.3d 1515, 1524 (10th Cir. 1997).

[9] § 547(b).

burden of proof of the prima facie elements of a preferential transfer on the trustee seeking to avoid the transfer.[10]

The term insolvent is defined in the Bankruptcy Code as a "financial condition such that the sum of such entity's debts is greater than all of such entity's property . . ." with adjustments for property that may be claimed as exempt and property that has been fraudulently secreted away.[11] It is a simple balance sheet test: does the debtor have more liabilities than assets? If so, the debtor is insolvent.

In the appeal before us, the focus is upon § 547(b)(5); the other elements of a preference are admittedly present. The question is whether the presumption of insolvency under § 547(f) is sufficient to establish that an unsecured creditor who was paid in full within the preference period received more than that creditor would have received in a Chapter 7 liquidation. The bankruptcy court ruled that a presumption of insolvency does not establish that unsecured creditors would not be paid in full in a hypothetical liquidation:

> Thus in this case, the Liquidating Trustee may rely on the § 547(f) insolvency presumption to satisfy his burden of proof on the requirement set forth in § 547(b)(3). However, he cannot do so with respect to the requirements set forth in the remaining elements of § 547(b). Specifically, the Liquidating Trustee must affirmatively establish facts to satisfy the requirements of § 547(b)(5). *See In re E&S Comfort, Inc.*, 92 B.R. 616, 620 (Bankr. E.D. Pa. 1988).[12]

Several cases have reached the opposite conclusion.

Consider the following ruling of the United States Court of Appeals for the Ninth Circuit:

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[10] *See* § 547(g) ("For the purposes of this section, the trustee has the burden of proving the avoidability of a transfer under subsection (b) of this section, and 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.").

[11] *See* § 101(32).

[12] *Order in* Appellant's Appendix at 179.

> This analysis [under § 547(b)(5)] requires that in determining the amount that the transfer "enables [the] creditor to receive," 11 U.S.C. § 547(b)(5) (1982), such creditor must be charged with the value of what was transferred *plus* any additional amount that he would be entitled to receive from a Chapter 7 liquidation. The net result is that, as long as the distribution in bankruptcy is less than one-hundred percent, *any* payment "on account" to an unsecured creditor during the preference period will enable that creditor to receive more than he would have received in liquidation had the payment not been made.[13]

In *Still v. Rossville Bank (In re Chattanooga Wholesale Antiques, Inc.*),[14] the Sixth Circuit Court of Appeals stated that "[u]nless the estate is sufficient to provide a 100% distribution, any unsecured creditor . . . who receives a payment during the preference period is in a position to receive more than it would have received under a Chapter 7 liquidation."[15] In *Ossen v. Bernatovich (In re National Safe Northeast, Inc.)*,[16] the court determined that when the estate is found to be insolvent on the petition date, such a finding is sufficient to satisfy the preferential treatment standard of § 547(b)(5) where general unsecured creditors are involved.[17] Each of these cases supports the position advanced by

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[13] *Elliott v. Frontier Props. (In re Lewis W. Shurtleff, Inc.)*, 778 F.2d 1416, 1421 (9th Cir. 1986) (italicized emphasis in original; underlined emphasis added); *accord Jacobs v. Matrix Capital Bank (In re Apponline.com, Inc.*) 315 B.R. 259, 281 (Bankr. E.D.N.Y. 2004) (quoting *Elliott*); *see also Levine v. Custom Carpet Shop, Inc. (In re Flooring Am., Inc.)*, 302 B.R. 394, 402-03 (Bankr. N.D. Ga. 2003) (quoting 1 David G. Epstein, Steve H. Nickles, & James J. White, *Bankruptcy*, § 6-20 (1992) "Fortunately, the courts have recognized certain shorthand tests for deciding if a transfer had a preferential effect. The most commonly used test is as follows: In the case of a payment to an unsecured, nonpriority (general) creditor, the preferential effect requirement is satisfied unless general, unsecured creditors would have received 100% of their claims in the hypothesized Chapter 7 distribution.").

[14] 930 F.2d 458 (6th Cir. 1991).

[15] *Id.* at 465.

[16] 76 B.R. 896, 907 (Bankr. D. Conn. 1987).

[17] *Id.* (citing *Elliott*, 778 F.2d at 1421); *accord, Clark v. A.B. Hirchfeld Press, Inc. (In re Buyer's Club Mkts., Inc.)* 123 B.R. 895, 898 (Bankr. D. Colo. 1991) (quoting *Monzack v. ADB Investors (In re EMB Assocs., Inc.)*, 100 B.R. 629, 633 (Bankr. D. R.I. 1989)).

Connolly.

In the present case, WIN CA was presumed insolvent when it made the transfers to FIS and when it filed for bankruptcy relief. Connolly was entitled to rely upon the presumption at trial. Under the presumption, WIN CA had fewer assets than liabilities. It is axiomatic that a debtor with fewer assets than liabilities does not have the ability to pay all of its unsecured creditors in full in liquidation. There simply is not enough money to go around; it is a matter of mathematics. Accordingly, the requirements under § 547(b)(5) were met, and the decision of the bankruptcy court was in error.[18]

The bankruptcy court relied upon *In re E&S Comfort, Inc.*[19] for the proposition that Connolly may not rely on the presumption of insolvency arising under § 547(f), but must affirmatively establish facts to satisfy the requirements of § 547(b)(5). However, the facts of *E&S Comfort* are significantly different from the facts of this case. In *E&S Comfort*, the transferees were not unsecured creditors but federal and state governments with priority tax claims. It is possible that where an estate is insolvent, a priority creditor could be paid in full. The same cannot be said about a general unsecured claim.

FIS argues that reversal of the bankruptcy court's decision would render § 547(b)(5) a nullity because the presumption of insolvency would render the hypothetical liquidation test meaningless. We disagree. While the presumption may eliminate further inquiry on the hypothetical liquidation issue where unsecured creditors are involved, the test remains vital where priority or partially secured creditors are involved. Our ruling does no violence to the framework of

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[18] Connolly also argues that he presented sufficient evidence of the insolvency of WIN CA. Given the basis of our ruling today, we do not reach that issue.

[19] *Baehr v. IRS* (*In re E&S Comfort, Inc.*), 92 B.R. 616, 620 (Bankr. E.D. Pa. 1988).

the Bankruptcy Code.

V. Conclusion

The bankruptcy court erred when it failed to find that a presumptively insolvent debtor did not have the ability to pay unsecured creditors in full in a hypothetical Chapter 7 liquidation. The decision of the bankruptcy court is reversed. This adversary proceeding is remanded for further proceedings consistent with this Order and Judgment.