

In the United States Bankruptcy Court
for the
Southern District of Georgia
Savannah Division

In the matter of:)	
)	Adversary Proceeding
TOPGALLANT GROUP, INC.)	
(Chapter 7 Case <u>89-41997</u>))	Number <u>91-4044</u>
)	
<i>Debtor</i>)	
)	
)	
JAMES L. DRAKE, JR.,)	
TRUSTEE)	
)	
<i>Plaintiff</i>)	
)	
)	
v.)	
)	
AMBASSADOR FACTORS,)	
A Division of)	
Fleet Factors Corporation)	
)	
<i>Defendant</i>)	

MEMORANDUM AND ORDER

On April 23, 1991, the Trustee brought this adversary proceeding seeking turnover of funds collected post-petition by Defendant, Ambassador Factors ("Ambassador"). A hearing was held in this adversary proceeding and the related adversary proceeding, number 91-4043, on July 27, 1992. The record was supplemented by a letter with enclosures from the Plaintiff dated November 9, 1992. Upon consideration of the evidence adduced at the hearing, the documentation submitted by the parties and the applicable authorities, I make

the following Findings of Fact and Conclusions of Law.

FINDINGS OF FACT

The Trustee brought this adversary seeking turnover of funds collected by Ambassador Factors. The parties have stipulated that Ambassador "holds in (Topgallant Group) account number 957 a 'credit' in the amount of \$20,851.35, plus accrued interest." See Joint Pre-trial Stipulation filed December 20, 1991. The Trustee argues that Ambassador, post-petition, used the funds belonging to the Debtor to reduce the debt owed to Ambassador. The documents reveal that post-petition transfers totalling \$38,596.32 were made, resulting in the credit balance in Debtor's favor.

Ambassador argues that its security agreement with Debtor gives it the right to possess its security, accounts receivable, and to use the security to reduce any indebtedness owed.

CONCLUSIONS OF LAW

Section 549(a) of the Bankruptcy Code provides in relevant part:

. . . [T]he trustee may avoid a transfer of property of the estate--

- (1) that occurs after the commencement of the case;
and
- (B) that is not authorized under this title or by the court.

11 U.S.C. §549. Under Section 549 the court must determine:

- (1) Whether a transfer of property occurred;
- (2) Whether the property was property of the estate;
- (3) Whether the transfer occurred after the commencement of the case; and
- (4) Whether the transfer was authorized by the court or the Bankruptcy Code.

In re Watson, 65 B.R. 9, 11 (Bankr. C.D.Ill. 1986).

Ambassador argues that its valid perfected security interest which applies to the collected funds should prevent turnover. However, "[t]hat the post-petition payment might have been made from the proceeds of liquidation of the transferee's collateral is not a defense to the trustee's avoidance power under §549(a)." In re Ft. Dodge Creamery Co., 121 B.R. 831, 836 (Bankr. N.D.Iowa, 1990); *See also* In re Wilson, 52 B.R. 639, 641 (Bankr. E.D.Tenn. 1985) (holding that debtor's post-petition payment to savings and loan was avoidable under §549(a), notwithstanding that payment was applied to a secured note).

In Fort Dodge Creamery, *supra*, the secured creditor had an interest in debtor's accounts receivable and other items. The security interest provided for attachment to after-acquired property. 121 B.R. at 832. The debtor made a post-petition payment of \$17,791.66 to the creditor which represented the proceeds from liquidation of property and collection of accounts receivable. *Id.* at 834. The trustee brought a section 549 turnover

action. The creditor argued that it was entitled to payment from the fully encumbered property. Id. The court concluded that the property transferred, even though fully encumbered, was property of the estate under Section 549(a)(1) and subject to turnover. Id. *See also In re W. L. Mead, Inc.*, 42 B.R. 57, 59 (Bankr. N.D. Ohio 1984). I agree with this rationale and hold that the funds collected by Ambassador constituted property of the estate. There is no dispute that a post-petition transfer of these funds was made. Thus, the sole remaining issue is whether the transfer was authorized.

To succeed, Ambassador must show that the payments used to reduce debt were authorized either by this court or by the Bankruptcy Code. *See* 11 U.S.C. §549(a)(2)(B). Ambassador can show neither. First, Ambassador Factors was never authorized by this court to apply the freights collected to reduce the indebtedness owed by Debtor to it. On January 10, 1990, this court "ordered that Ambassador Factors shall sequester in a segregated interest-bearing account in the United States any and all monies received by Ambassador for the account of the Debtor" and "shall hold the funds pending further order of this court" Order Granting Ambassador Factor's Petitions for Temporary Restraining Orders, Adversary Proceeding Nos. 89-4124 and 89-4125, Chapter 11 Case No. 89-41996 (Bankr. S.D.Ga. January 10, 1990). Nowhere in that order did this court authorize Ambassador to apply the freights collected to reduce its debt.

Second, Ambassador cannot show that, pursuant to Section 1108, the debtor-in-possession's authority to operate its business authorizes such payments. The "Code does not permit payment, post-bankruptcy, out of property of the estate, of pre-bankruptcy debts." In re White Beauty View, Inc., 70 B.R. 90, 92-3 (Bankr. M.D.Pa. 1987) (citing In

re J.T.L., Inc., 36 B.R. 860, 862 (Bankr E.D.Mo. 1984); In re B & W Enterprises, Inc., 19 B.R. 421 (Bankr. D.Idaho 1982), *aff'd* 713 F.2d 534 (9th Cir. 1983); In re Leon Swartout, etc., 20 B.R. 102 (Bankr. S.D. Ohio 1982)).

Although pre-petition payment of the freights to Ambassador may have been in the ordinary course, the post-petition payments to reduce debt cannot be considered in the ordinary course. This court's prior order required payments into the sequestered fund of all post-petition monies received for the account of Debtor and application of the payments to reduce debt were made in violation of that order. When this court ordered the funds sequestered, they affirmatively changed their character to payments outside the ordinary course. *See e.g.*, In re Coco, 67 B.R. 365, 373 (Bankr. S.D.N.Y. 1986) (Debtor tenant's payment of rent to landlord's attorney, to be held in court-ordered escrow, was not made in the ordinary course of business, according to ordinary business terms). At the time of this court's order, and since that time, those funds have been subject to the conflicting claims of Ambassador as well as those of various maritime lien claimants. This court placed those funds in escrow to preserve the status quo pending a final determination of ownership. Ambassador Factors, by unilaterally using those funds to reduce its debt in violation of this court's order, gained an unfair advantage over those maritime lien claimants, and potentially others.

I hold that Ambassador's post-petition transfers were not authorized by the Code or by any court order and defeated the intent of the prior temporary restraining order issued by the court. The Trustee has made a *prima facie* showing that he is entitled to the relief requested pursuant to Section 549. No valid defenses to the Trustee's *prima facie* case

have been presented or argued by Ambassador.

In light of the foregoing, I conclude that Ambassador's post-petition transfers are avoidable under Section 549. Therefore, the Trustee's complaint for turnover is well founded, and Ambassador is hereby ordered to remit to the Trustee the sums at issue, which will be placed by the Trustee in an interest-bearing, sequestered account pending final determination of ownership and distribution in this case.

O R D E R

Pursuant to the foregoing Findings of Fact and Conclusions of Law, IT IS THE ORDER OF THIS COURT that, Defendant, Ambassador Factors, shall turnover to the Trustee all proceeds received post-petition of pre-petition collateral of the Debtor in the principal amount of \$38,596.32, plus interest from the date received by Ambassador.

Lamar W. Davis, Jr.
United States Bankruptcy Judge

Dated at Savannah, Georgia

This ___ day of February, 1993.