

IN THE UNITED STATES BANKRUPTCY COURT

FOR THE

SOUTHERN DISTRICT OF GEORGIA
Savannah Division

IN RE:)	Chapter 7 Case
)	Number <u>89-41997</u>
TOPGALLANT GROUP, INC.,)	
)	
Debtor)	
)	
<hr/>		
IN RE:)	Chapter 7 Case
)	Number <u>89-41996</u>
TOPGALLANT LINES, INC.,)	
)	
Debtor)	
)	
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JAMES L. DRAKE, JR., Trustee for)	
the Chapter 7 Bankruptcy Estates)	
of TOPGALLANT GROUP, INC. and)	
TOPGALLANT LINES, INC.)	
)	
Plaintiff)	Consolidated
)	Adversary Proceeding
)	
vs.)	Number <u>92-04309A</u>
)	
BAX TIRE SERVICES, INC.,)	
)	
Defendant and)	
Third-Party Plaintiff)	
)	
vs.)	
)	
SOUTHEASTERN MARITIME CO.,)	
)	
Third-Party Defendant)	
)	

ORDER

By motion Bax Tire Services, Inc. (hereinafter "Bax"),

defendant in the main action, seeks partial summary judgment in the main action and by motion third-party defendant Southeastern Maritime Co. (hereinafter "SEMCO") seeks dismissal of the third party complaint. The main case is an action by the trustee against Bax to recover an allegedly preferential transfer. Bax brought the third party complaint against SEMCO, alleging that the payments sought to be recovered were made by the debtor on behalf of SEMCO and that SEMCO would be liable to Bax for any payments recovered by the trustee. SEMCO answered asserting that since it had acted as an agent for the debtor in the dealings at issue, primary liability for those dealings lay with the debtor as principal, not with SEMCO as agent. In that response and in the pending motion to dismiss, SEMCO requests that this court abstain from hearing the third party action in light of the proceedings styled Bax Tire Services, Inc. v. Southeastern Maritime Co., Civil Action No. 90-2592 pending in the State Court of Chatham County, Georgia, instituted by Bax for recovery on four unpaid invoices for goods supplied. SEMCO has requested a jury trial in the state court proceeding and contends that retention of jurisdiction by this court will deny it trial by jury of those issues. Bax opposes abstention, requesting instead that this court retain jurisdiction and resolve all related disputes between the three parties. Bax rests its motion for partial summary judgment in the main action on the "ordinary course of business"

exception to transfers avoidable under 11 U.S.C. § 547.

I. MOTION TO DISMISS THE THIRD PARTY COMPLAINT

Bax, in opposing abstention and encouraging retention and resolution of the third party complaint by this court asserts that if jurisdiction is not retained then two trials will be necessary, one in the state court and one again here by the loser making its claim against the debtor. In other words, Bax maintains that either Bax or SEMCO will seek to hold the debtor ultimately responsible in this court and therefore in the interest of efficiency this court should not abstain from deciding this case. Bax assumes that the trustee will object to any proof of claim filed by the loser of the contest between Bax and SEMCO. Bax also assumes that abstention is only a matter of judicial discretion. It is not and due to both SEMCO's request for a jury trial and the mandatory abstention provision of 28 U.S.C. § 1334, this court must abstain from hearing the third party complaint. Concerns for judicial economy are not relevant.

The jurisdiction of this court to resolve a case is conferred by 28 U.S.C. § 1334.¹ Under section 1334 there are four

¹28 U.S.C. § 1334 provides in relevant part:

(a) Except as provided in subsection (b) of this section, the district courts shall have original and exclusive jurisdiction of all cases under title 11.

(b) Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the

categories of matters over which the bankruptcy court exercises jurisdiction:

- (1) all cases under title 11;
- (2) all civil proceedings arising under title 11;
- (3) all civil proceedings arising in cases under title 11;
- (4) all civil proceedings related to cases under title 11.

Rentrak v. Cady v. Sapp (In re: Cady), Ch. 7 Case No. 93-50258, Adv. No. 93-05024 (Bankr. S.D. Ga. Walker, J. March 11, 1994); 28 U.S.C. § 1334(a) and (b). The issues raised in this case must fall within one of these four categories to sustain this court's jurisdiction. Rhodes v. Commercial Bank (In re: Rhodes), Ch. 13 Case No. 91-10488, Adv. No. 91-1050 (Bankr. S.D. Ga. Dalis, J. August 30, 1991).

The first category confers original and exclusive jurisdiction over the original bankruptcy petition itself in the

district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11 or arising in or related to cases under title 11.

(c)(1) Nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11.

(2) Upon timely motion of a party in a proceeding based upon a State law claim or State law cause of action, related to a case under title 11 but not arising under title 11 or arising in a case under title 11, with respect to which an action could not have been commenced in a court of the United States absent jurisdiction under this section, the district court shall abstain from hearing such proceeding if an action is commenced, and can be timely adjudicated, in a State forum of appropriate jurisdiction.

district court. Id.; Matter of Wood, 825 F.2d 90, 92 (5th Cir. 1987). This category is inapplicable to the third-party complaint now before me. The second and third categories concern "core" proceedings under 28 U.S.C. § 157(b)(2). Rhodes, supra, at 4; Wood, supra, at 96-7. The phrase "arising under Title 11" describes proceedings "that involve a cause of action created or determined by the statutory provisions of Title 11." Rhodes, supra at 4; Wood, supra at 96. Such proceedings concern "administration of the estate in the sense that no adverse third party is involved (e.g., a dispute between the debtor and the trustee regarding a claim of exemptions)." Austin v. Tatum, et al. (In re Donald E. Austin) Chapter 11 case No. 85-40639 Adv. No. 89-4020, slip op. at 5 (Bankr. S.D. Ga. Dalis, J. Dec. 31, 1989) [quoting 1 Collier on Bankruptcy ¶3.01(c)(iii) (L. King 15th ed. 1989)]; Rhodes, supra at 5. "Arising in" proceedings are those "that are not based on any right expressly created by Title 11, but nevertheless, would have no existence outside of Bankruptcy." Wood, supra, at 97; Rhodes, supra, at 5; accord Austin, supra, at 5-6. The overriding test as to whether a proceeding is a "core proceeding" as "arising under" or "arising in" Title 11 is whether "it invokes a substantive right provided by Title 11 or if it is a proceeding that, by its nature, could arise only in the context of a bankruptcy case." Wood, supra, at 97; Rhodes, supra at 5. Thus, "if the proceeding does not

involve a substantive right created by the federal bankruptcy law and is one that could exist outside of bankruptcy it is not a core proceeding." In re: Davis, 899 F.2d 1136, 1141 (11th Cir. 1990), citing Wood, supra, at 97. Whether a payment is a preference and avoidable is a "core proceeding" arising under Title 11 of the United States Code and is appropriately decided in Bankruptcy Court. Wood, supra, at 97. The trustee's action against Bax is a core proceeding.

The matters at issue in both the third party action and the state court proceeding do not invoke a substantive right created by Title 11 or arising only in bankruptcy. These issues are at best "related to" Topgallant's bankruptcy case and fall into the fourth category of jurisdiction. The test for whether a proceeding is "related to" a bankruptcy case (and is therefore non-core) is "whether the outcome of that proceeding could conceivably have any effect on the estate being administered in bankruptcy." Askanse v. Fatjo, No. H-91-3140, 1993 WL 208682, at *2 (S.D. Tex. April 22, 1993), quoting Matter of Wood, supra at 93; Matter of Lemco Gypsum, Inc., 910 F.2d 784, 788 (11th Cir. 1990). If the trustee is successful in his preference action, the contest between Bax and SEMCO will resolve who holds the claim in the bankruptcy case for the payment recovered, i.e., who the estate owes. The issue of liability presented in the third party complaint is then "related

to" the bankruptcy proceeding and falls within the fourth category of jurisdiction under § 1334.

When a matter is merely "related to" a bankruptcy proceeding, it is subject to mandatory abstention when the other components for mandatory abstention are satisfied. See Harley Hotels, Inc. v Rain's Intern, 57 B.R. 773, 777-80 (M.D. Pa. 1985); In re: Wells Properties, Inc., 102 B.R. 685, 691-2 (Bankr. N.D. Ill. 1989). All requirements for mandatory abstention under 28 U.S.C. § 1334(c)(2), supra, are met in this case. There has been a timely motion by SEMCO, a party in the pending state court proceeding, for this court to abstain. The issues presented in the third party action are based on state law claims on open account and agency and are non-core issues "related to" Topgallant's bankruptcy. These claims could not have been brought in federal court absent 28 U.S.C. § 1334(b), supra. There is a clear congressional policy in favor of deciding state law claims within the courts of that state. Rhodes, supra.

Abstention from and dismissal of the third party action will not have a detrimental effect on the preference action for either party. The preference action by the trustee may be completely and fairly adjudicated without SEMCO's presence as a party. The elements of an avoidable preference under 11 U.S.C. § 547(b) are the transfer of an interest of the debtor in property:

- (1) to or for the benefit of a creditor;
- (2) for or on account of an antecedent debt owed by the debtor before the 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 filing of the petition, if such creditor at the time of such transfer was an insider; and
- (5) that enables the 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.

The issue of SEMCO's liability to Bax, if any, is unrelated to the issue of whether a preferential transfer has taken place according to the above requirements. Bax may defend the preference action in some part with evidence regarding Bax' relationship with SEMCO, but there is no need for SEMCO to be a party to the preference action. The preference action will have one of two results: Bax will win and keep the money the trustee seeks to recover, or Bax will lose and forfeit the money in exchange for a claim of the same amount against the estate. SEMCO is in no way involved or implicated in either scenario. If the latter situation results, Bax may choose to pursue SEMCO rather than Topgallant with the claim it receives as a result of recovery of the preference, but that issue is unrelated to the preference action itself.

SEMCO has also invoked its constitutional right to a jury trial. In an action at law where the value in controversy exceeds twenty dollars, the right to trial by jury is preserved. U.S. Const. Amendment VII.² The issues in the third-party complaint filed by Bax to recover on the invoices mirror those issues in the state court action. This court does not offer jury trial to litigants herein. See Stewart-Hall Marketing, Inc. v. Bob Maddox Dodge, Inc. v. WAGT Television, Inc., et al (In re: Stewart Hall Marketing, Inc.), Ch. 7 Case No. 89-10275, Adv. No. 89-1065, slip op. at 8-12 (Bankr. S.D. Ga. Dalis, J. Feb. 15, 1991). To retain jurisdiction over this matter would deny SEMCO its constitutional right to trial by jury. "If a jury trial has been requested but the case, although 'related', is based on state law, with no independent basis of federal jurisdiction, then the bankruptcy court ought to abstain." Rhodes, supra, at 10, quoting American Energy, Inc., 50 B.R. 175, 181 (Bankr. D.N.D. 1985). Accordingly, I find that it is appropriate and mandatory to abstain from the exercise of jurisdiction over the third party complaint. The matters presented

²United States Constitution Amendment VII provides:

In Suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact tried by a jury shall be otherwise re-examined in any Court of the United States, than according to the rules of the common law.

therein may be appropriately resolved and SEMCO's right to a jury trial preserved in the state court proceeding.

II. MOTION FOR PARTIAL SUMMARY JUDGMENT BY BAX

Bax bases its motion for partial summary judgment on the "ordinary course of business" exception to voidable preferences found in 11 U.S.C. § 547(c)³. Bax asserts on one hand that there existed no business relationship between itself and the debtor, but also that payments received by Bax from Topgallant on behalf of SEMCO were entirely ordinary.

Summary judgment shall be granted "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." Federal Rule of Civil Procedure

³11 U.S.C. § 547(c) provides:

- (c) The trustee may not avoid under this section a transfer-- . . .
- (2) to the extent that 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 course business terms;

56, made applicable in bankruptcy matters by Federal Rule of Bankruptcy Procedure 7056. The party moving for summary judgment bears the initial burden of showing there is no genuine issue of material fact. Velten v. Regis B. Lippert, Intercat, Inc., 985 F.2d 1515, 1523 (11th Cir. 1993). See also Celotex Corp. v. Catrett, 477 U.S. 317, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986). "To prevail on a motion for summary judgment, [the movant] must prove there is no dispute as to any material fact and that based on the material facts, to which the parties are in agreement, [the movant] is entitled to judgment as a matter of law." Haile v. Reynolds Tobacco Co., et al. (In re Haile), Ch. 11 case No. 88-40864 Adv. 90-4118 slip op. at 5 (Bankr. S.D. Ga. Dalis, J. Sept. 27, 1991). If the movant makes this showing, the burden then shifts to the non-moving party to demonstrate that there is indeed a material issue of fact. United States v. Four Parcels of Real Property, 941 F.2d 1428, 1438 (11th Cir. 1991). The evidence is reviewed in the light most favorable to the opponent of the motion, and all reasonable doubts and inferences should be resolved in favor of the opponent. Amey, Inc. v. Gulf Abstract & Title, Inc., 758 F.2d 1486, 1502 (11th Cir. 1985) (citation omitted), cert. denied 475 U.S. 1107, 106 S.Ct. 1513, 89 L.Ed.2d 912 (1986). Any reservations the court has concerning the evidence will preclude summary judgment. See International Shortstop, Inc. v. Rally's, Inc., 939 F.2d 1257 (5th

Cir. 1991). If reasonable minds might differ on the inferences arising from undisputed facts, then the court should deny summary judgment. Id.

Bax has failed to show that no genuine issue of material fact exists. In order to fall within the ordinary course of business exception, the burden is on the transferee asserting the defense to establish each of the elements of § 547(c)(2) by a preponderance of the evidence. 11 U.S.C. §547(g). Section 547(c)(2) provides that a debtor's otherwise preferential payment may not be avoided if the following conditions are satisfied:

1. the payment must be made on a debt incurred in the ordinary course of debtor's business;

(2) the payment must be made in the ordinary course of business of the debtor and of the transferee; and

(3) the payment must be made according to ordinary business terms.

The purpose of the §547(c)(2) preference exception is to protect normal and customary credit transactions paid in the ordinary course of business of the debtor and the transferee. In re Fulghum Constr. Corp., 872 F.2d 739 (6th Cir. 1989). This section encourages short-term credit dealings with troubled debtors in order to forestall bankruptcy. O'Neill v. Nestle-Libby's P.R., Inc., 729 F.2d 35 (1st Cir. 1984). The exceptions of §547(c) were enacted to allow normal financial relations to continue. James D. Walker, Jr.,

Trustee v. T.J.T. Axle, (Scott Housing Systems, Inc.) Chapter 7 case No. 86-50123 Adv. No. 88-5052 (Bankr. S.D. Ga. Davis, J. April 22, 1993).

The ordinary course exception requires a two-step analysis. Subsections (a) and (b) of § 547(c) (numbers 1 and 2 above) require a subjective analysis of the ordinary course of business of the debtor and of the transferee. Although in the vast majority of § 547 preference actions a debtor/creditor relationship exists between the debtor in the bankruptcy case and the defendant in the preference action and this subjective analysis usually analyzes the ordinary course of business between the debtor and the creditor as the transferee of the preferential transfer, see Marathon Oil Company v. Flatau (In re Craig Oil Company) 785 F.2d 1563, 1565 (11th Cir. 1986) (establishing as a condition under §547(c)(2) that the transfer was "made in the ordinary course of business between the debtor and the creditor"); James D. Walker, Jr., Trustee v. Waycross Paint and Wall Coverings (In re Scott Housing Systems, Inc.) Chapter 7 case No. 86-50123 Adv. No. 88-5066 slip op. at 10 (Bankr. S.D. Ga. Davis, J. May 24, 1991); James D. Walker, Jr., Trustee v. J.D. Moore Distributing Company (In re Concrete Products, Inc.) Chapter 11 case No. 88-20540 Adv. No. 90-2042 slip op. at 9 (Bankr. S.D. Ga. Davis, J. Sept. 24, 1992), § 547(c)(2)(A) and (B) does not require the existence of an ordinary

course of business between the debtor and the transferee. What is required is that the transfer be made in the ordinary course of debtor's business and in the ordinary course of the transferee's business.

In support of its motion for summary judgment Bax has submitted the affidavit of Mr. Anthony Del Ferguson. According to Mr. Ferguson Bax "had done business with steamship agents (sic) Southeastern Marine Company ("SEMCO") since approximately 1983, and it was ordinary and customary for SEMCO to act as an agent in purchasing goods on behalf of a principal." According to Mr. Ferguson, he entered into negotiations with an employee of SEMCO, Mr. Alvarez, for the sale of goods and for the terms of payment to allow 30 days for full payment by SEMCO. After being informed that the goods were intended for Topgallant, Mr. Ferguson would not agree to those terms for Topgallant and would only be willing contract with, and allow 30 days for a full payment by SEMCO. According to the affidavit, Bax received orders from Mr. Alvarez, delivered the goods ordered "to locations specified by Topgallant" and as payment "many of the checks tendered . . . were issued by Topgallant." The affidavit at best establishes the ordinary course of business dealings between Bax, the transferee, and SEMCO. Bax asserts that it had no business dealings with Topgallant. For summary judgment purposes, Bax has failed to establish that this triangular business

relationship it seeks to establish between Bax, SEMCO and Topgallant was in the ordinary course of Topgallant, the debtor's, business. Although Bax asserts that the payments received from Topgallant were in the ordinary course of Bax' business, Bax has failed to establish as a matter of fact that the payments were made in the ordinary course of Topgallant's business.

Bax having failed to establish that there is no genuine issue as to a crucial material fact, that the transactions between Bax, SEMCO and Topgallant were in the ordinary course of Topgallant's business, Bax is not entitled to judgment as a matter of law. I do not address whether the business dealings between Bax, SEMCO and Topgallant were conducted according to ordinary business terms, the second and objective analysis required for the ordinary business defense.

It is therefore ORDERED that the third party complaint is dismissed; and

Further ORDERED that partial summary judgment is denied.

JOHN S. DALIS
UNITED STATES BANKRUPTCY JUDGE

Dated at Augusta, Georgia
this 30th day of September, 1994.