UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA
THIRD DIVISION

BKY 3-94-233
Chapter 7

Minnehaha Falls Garden Centers, Inc.,
Debtor.

John A. Hedback, Trustee,

Plaintiff, ADV 3-95-218

v.

Minnehaha Falls Nursery and Garden Stores, Inc.,

Defendant.

FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER

This matter was heard on August 20, 1996. Appearances were noted in the record. The Court, having received and considered all proper evidence, arguments, briefs of counsel, and being fully advised in the matter, now makes the following FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER pursuant to the Federal and Local Rules of Bankruptcy Procedure.

I. FACTS

This adversary proceeding was brought by Plaintiff, John A. Hedback, as Trustee of the Bankruptcy Estate of Minnehaha Falls Garden Centers, Inc. ("Debtor"), seeking to avoid an alleged preferential transfer to Defendant, Minnehaha Falls Nursery and Garden Stores, Inc., of business assets, including vehicles, equipment, inventory, supplies, and accounts receivable, pursuant to 11 U.S.C. Section 547(b). The Trustee seeks to recover such property pursuant to 11 U.S.C. Section 550.

The parties filed a stipulation of facts at trial. The stipulation contained these recitations of relevant undisputed facts:Œ

1. The Chapter 7 bankruptcy proceeding for Minnehaha Falls Garden Center[s], Inc. was commenced by the filing of a[n] involuntary petition on or about January 18, 1994. An Order for Relief was entered into on March 7, 1994. Plaintiff was appointed as Chapter 7 trustee for the case.

2. Defendant is a Minnesota Corporation. At all times relevant to these proceedings, Robert C. Lindgren was an officer and shareholder and Shirley A. Lindgren was a shareholder of Defendant.

3. At all times relevant to these proceedings, Debtor was a Minnesota Corporation. From April 1, 1988 to July 1, 1993, Debtor was engaged in a nursery and landscaping business. Keith Hittner was the principal officer and shareholder of Debtor. At all times relevant

to these proceedings, Keith Hittner was married to Monica Hittner, the daughter of Robert C. Lindgren and Shirley A. Lindgren. Monica Hittner had no active role in the conduct of Debtor's business.

4. On or about March 31, 1988, Defendant and Debtor entered into a series of agreements whereby Debtor agreed to purchase the assets of Defendant. In connection with those agreements, Debtor executed and delivered to Defendant two promissory notes, one in the original amount of $270,000 and one in the original amount of $161,000. Defendant did not retain a security interest in the assets sold to Debtor.

5. Debtor defaulted on the promissory notes in the spring of 1993. Defendant obtained a judgment against Debtor, in the amount of $393,772.18, which was entered and docketed in Dakota County District Court in case number 19-C2-93-8321 on June 25, 1993. A Writ of Execution was obtained, but was not served on Debtor.

6. In lieu of service of the Writ of Execution, after negotiations between counsel for Debtor and Defendant, on July 1, 1993, Debtor executed and delivered a Bill of Sale to Defendant, transferring to Defendant certain vehicles, equipment, office equipment, store equipment, inventory, supplies and accounts receivable. The Bill of Sale states that the transfer "is given in consideration of a partial satisfaction of judgment in theŒamount of $198,000." Defendant, on that date, executed a Partial Satisfaction of Judgment in the amount of $198,000.

7. Beginning approximately in the summer of 1992, Debtor began liquidating its inventory and other business assets located at its Apple Valley, Minnesota location. Debtor had closed the Apple Valley store prior to the commencement of the litigation described in paragraph 5 above. On or about July 1, 1993, Defendant took possession of the assets of Debtor. Defendant resumed business operations on that date at the one remaining business location of Debtor in Minneapolis, Minnesota. Defendant utilized the assets obtained from Debtor in that operation. At no time did Defendant have a liquidation sale of the assets of Debtor.

8. Debtor ceased all business operations on July 1, 1993. During the spring of 1993, Debtor was on a cash on delivery basis with its suppliers. When it filed its bankruptcy schedules on March 23, 1994, Debtor listed unsecured debts, not including the claim of Defendant, in the amount of $316,463.78.

9. In February, 1994, at the request of Defendant's counsel, Paul Tracy, an experienced personal property liquidator for Chapter 7 trustees, inspected the tangible assets used in the Defendant's business and prepared an itemized valuation report.

Stipulation of Facts (filed Aug. 14, 1996).

Before Debtor purchased Defendant's assets in 1988, Keith Hittner worked for Defendant as general manager from 1974 until the purchase in 1988. During the course of his employment, Hittner made many of the employment and management decisions, and was in control of the business when the Lindgrens were away from the stores.

When Debtor purchased the Defendant's assets in 1988, no appraisal of Defendant's assets was made to determine an appropriate sales price. The Lindgrens had not formally planned to sell the business, and had not put the business on the market. Instead, Keith Hittner approached the Lindgrens with the idea to purchase the business. In addition to the two promissory notes entered into betweenŒDefendant and Debtor, Debtor also entered into a contract for deed with the Lindgrens personally for the land on which the Apple Valley and Minneapolis stores were located.

During the time that Debtor operated its business, Defendant continued to exist as a corporate entity solely for the purpose of collecting payments from Debtor on the debts owed by Debtor to Defendant and the Lindgrens. Debtor operated essentially the same business that the Defendant had operated, providing nursery and landscaping products and services. Debtor operated its business out of the same locations as Defendant until the closure of the Apple Valley location, at which time Debtor operated solely out of the Minneapolis location. Many of the Defendant's employees continued to work for Debtor. Although the assets Debtor purchased from Defendant included several vehicles used in the operation of the business, the vehicles remained titled in Defendant's name throughout Debtor's ownership of the assets.

Before the assets were transferred from Debtor back to Defendant on July 1, 1993, no one conducted an inspection or appraisal of the assets. Instead, Debtor transferred its assets in consideration of a Partial Satisfaction of Judgment in the amount of $198,000, a figure upon which Debtor and Defendant mutually agreed without conducting an independent appraisal. At trial, Keith Hittner testified that he thought the business was worth more than $198,000. In addition to executing the Partial Satisfaction of Judgment, Robert and Shirley Lindgren released Keith Hittner from all personal liability on the promissory notes.

When Debtor defaulted on the contract for deed in early 1993, the Lindgrens prepared a notice of cancellation and served it on Debtor in March, 1993. However, the Lindgrens agreed to let Keith Hittner and Debtor stay on the property until June 30, 1993. According to the Lindgrens' attorney, the fact that Keith Hittner was their son-in-law influenced the Lindgrens' decision to allow the Debtor to stay on the property until June 30, 1993.

On June 30, 1993, the day before the transfer of the assets from Debtor to Defendant was to occur, Keith Hittner worked at the remaining Minneapolis location until the end of the day, packed his personal belongings, gave his store keys to an employee, and left the store. OnŒJuly 1, 1993, the day the transfer of assets occurred, the

Minneapolis location was opened as usual. The locks were not changed. The employees were not fired. Physical inventory was not evaluated. Neither Robert nor Shirley Lindgren came to the Minneapolis store on July 1, 1993. Although the inventory of the store was lower than normal, the store had products to sell, and those products were sold in the ordinary course of business. In sum, the store operated on July 1, 1993 just as it had on June 30, 1993, except for the absence of Keith Hittner.

Many of the employees that had worked for Debtor continued to work for Defendant after Defendant resumed its business operations at the Minneapolis location. With the exception of the low inventory, nothing occurred out of the ordinary course of business throughout July. Although Shirley Lindgren eventually needed to loan Defendant money, beginning in October of 1993, the business ran through July, August, and September of 1993 as it had before the transfer on July 1, 1993. The first physical inventory of the store after the transfer back to Defendant occurred in December, when inventory was usually conducted for both Defendant and Debtor.

Plaintiff brought this adversary proceeding seeking to avoid an alleged preferential transfer from Defendant to Debtor. Plaintiff claims that the transfer of assets to Defendant from Debtor on July 1, 1993 was an avoidable preferential transfer under 11 U.S.C. Section 547(b), and that the Trustee is entitled to recover $198,000 as the value of the transferred assets under 11 U.S.C. Section 550. Defendant denies that the transfer from Debtor to Defendant on July 1, 1993 was an avoidable preferential transfer. Defendant further claims that even if the transfer was an avoidable preferential transfer under 11 U.S.C. Section 547(b), the value of the assets which the Trustee may recover under 11 U.S.C. Section 550 is only the liquidation value of the assets, which Defendant claims is $43,000, the amount at which a personal property liquidator valued the Defendant's tangible assets in February, 1994.

II. DISCUSSION

A. Preferential Transfer

11 U.S.C. Section 547(b) provides, in pertinentŒpart:

Except as provided in subsection (c) of this section, the trustee may avoid any 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 such transfer was made;

(3) made while the debtor was insolvent;

(4) made...

(B) between ninety days and one year before

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(5) that enables such creditor to receive more than

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(A) the case were a case under chapter 7 of

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(B) the transfer had not been made; and
(C) such creditor received payment of such
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The parties have stipulated to facts which establish most of the elements of a preferential transfer under 11 U.S.C. Section 547(b). The only disputed element of a preferential transfer in this matter is whether the creditor, in this case Defendant, is an insider as that term is defined by the Bankruptcy Code. The trustee has the burden of proving insider status. In re Orsa Assocs., 99 B.R. 609, 621 (Bankr. E.D. Pa. 1989).

1. Statutory Definition of Insider

Although neither party argued as such, Defendant fits into the statutory definition of insider. According to 11 U.S.C. Section 101(31)(B)(vi), if the debtor is a corporation, an insider "includes" any "relative of a general partner, director, officer, or person in control of the debtor". 11 U.S.C. Section 101(45) defines "relative" as an "individual related by affinity or consanguinity within the third degree as determined by the common law, or individual in a step or adoptive relationship within such third degree". Affinity is "the connection existing in consequence of marriage between each of the married persons and the kindred of the other." In re Winn, 127 B.R. 697, 699 (Bankr. N.D. Fla. 1991). See also In re Busconi, 177 B.R. 153, 157 (Bankr. D. Mass.Œ1995); In re Ribcke, 64 B.R. 663, 666 (Bankr. D. Md. 1986); Black's Law Dictionary 59 (6th ed. 1990). The doctrine of affinity holds that from "the unity of marriage, one party to the marriage... [has] the same relation to the blood relatives of the other as the other stands toward them." Winn, 127 B.R. at 699. See also Busconi, 177 B.R. at 157; Ribcke, 64 B.R. at 666. Accordingly, Robert and Shirley Lindgren, by the doctrine of affinity, were the father and mother of Keith Hittner during Hittner's marriage to their daughter, Monica. By definition, the Lindgrens are relatives of an officer of the Debtor.

The matter is not complicated by the fact that the transfer was made between the Debtor and the Defendant as a corporation, instead of between the Debtor and the Lindgrens as individuals. Where the debtor and the defendant in a preferential transfer proceeding are both closely held corporations, and where an officer of the defendant corporation is an insider of the debtor by statutory definition, the defendant corporation is also an insider of the debtor. See In re Preferred Aluminum, Inc., 131 B.R. 889, 890-92 (Bankr. M.D. Fla. 1991) (holding that because the sole officer of the defendant corporation was an insider based on the statutory definition, the defendant corporation was also an insider). In this case, Robert and Shirley Lindgren are the sole officers and shareholders of Defendant. Accordingly, because the Lindgrens are Keith Hittner's relatives, and would therefore be insiders by statutory definition should the transfer have occurred between Debtor and the Lindgrens as individuals, the Defendant is an insider vis-a-vis Debtor as well. Defendant is an

insider by statutory definition in this transaction.

2. Insider by Relationship

A reading of 11 U.S.C. Section 101(31) clearly indicates that Congress intended to include more in the concept of insider than the specific examples set forth in the statute. See In re Schuman, 81 B.R. 583, 586 (Bankr. 9th Cir. 1987) ("Congress did not intend to limit the classification of insiders to the statutory definition."). In addition to the statutory examples, an insider is anyone "who has a sufficiently close relationship with a debtor that his conduct is made subject to closer scrutiny than those dealing at arms length with the debtor." S. Rep. No. 989, 95th Cong., 2d Sess. 25 (1978) and H.R. Rep.ŒNo. 595, 95th Cong., 1st Sess. 312 (1977), reprinted in 1978 U.S.C.C.A.N. 5787, 5810, 6269. Thus, if a party does not fit the specific examples of insider set forth in 11 U.S.C. Section 101(31), a party may still be an insider. To determine if a party is an insider, courts look to the closeness of the relationship between the parties and whether the transactions between the transferee and the debtor were conducted at arms length. See, e.g., In re Holloway, 955 F.2d 1008, 1011 (5th Cir. 1992); In re Babcock Dairy Co. of Ohio, Inc., 70 B.R. 685, 689 (Bankr. N.D. Ohio 1986) ("an insider may be any person or entity whose relationship with the debtor is sufficiently close so as to subject the relationship to careful scrutiny"); In re Montanino, 15 B.R. 307, 310 (Bankr. D.N.J. 1981) ("The true test of an 'insider' is one who has such a relationship with the debtor that their dealing with one another cannot be characterized as an arms-length transaction.").

Defendant is an insider applying this analysis as well. The relationship between Defendant and Debtor is very close. Debtor was formed for the sole purpose of purchasing Defendant's assets. When Debtor purchased the assets in 1988, it operated the same nursery and landscape business, used the same equipment, and employed the same individuals that Defendant did. The vehicles used for Debtor's business were never titled in Debtor's name, but remained titled in Defendant's name the entire time Debtor ran its business. Keith Hittner, who managed the stores when Defendant owned them, continued to run the stores after Debtor purchased the assets. During the five years that Debtor ran its business, Defendant existed as a corporate entity solely for the purpose of receiving payment from Debtor. When Debtor transferred the assets back to Defendant in 1993, Defendant operated the same business, used the same equipment, and employed the same individuals that Debtor did. These facts indicate not only that Defendant and Debtor were close, but that they essentially were the same business with different directors and shareholders.

The transactions between Defendant and Debtor also were not conducted at arms length. When Keith Hittner originally purchased Defendant's assets, the Lindgrens were not planning to sell the business. Neither party conducted any independent appraisal of the assets, but instead mutually agreed on a selling price. When DebtorŒdefaulted on the promissory notes, Defendant obtained a judgment against Debtor. Instead of executing on their

judgment, the Lindgrens agreed to take the assets to satisfy $198,000 of the judgment. No appraisal was conducted to reach this figure. In addition, Defendant agreed to release Hittner on his personal liability on the debts. When Debtor defaulted on its obligation under the contract for deed with the Lindgrens, the Lindgrens agreed to allow Hittner and Debtor to remain on the property for several months, in part, according to the Lindgrens' attorney for the transaction, because Hittner was married to their daughter. When the assets were transferred back to Defendant on July 1, 1993, the locks were not changed and Debtor's employees were not fired. The Lindgrens did not even find it necessary to come to the Minneapolis store that day to verify that the transfer had actually occurred. They did not come to see the store that they had, in essence, just purchased in consideration of the partial satisfaction of judgment. This sequence of events does not indicate that the Defendant and Debtor conducted the transaction at arms length.

After looking at the relationship between Debtor and Defendant and at the transfer, it is readily apparent that Defendant is an insider. Accordingly, the transfer of assets from Debtor to Defendant on July 1, 1993 was an avoidable preferential transfer under 11 U.S.C. Section 547(b).

B. Trustee's Right to Recover Under Section 550

To the extent that a transfer is avoided as a preferential transfer under 11 U.S.C. Section 547(b), the trustee "may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property". 11 U.S.C. Section 550(a). It is "within the court's discretion to determine whether a return of the value of the property or return of the actual property is the appropriate remedy." In re First Software Corp., 107 B.R. 417, 423 (D. Mass. 1989).

Where the parties have agreed to the value of the property transferred, that agreement shows a prima facie case of value, and the person attempting to show otherwise must present evidence to show that the value of the transferred property is not the value placed on it by the parties. See In re Clemons, 42 B.R. 796, 799 (Bankr. S.D. Ohio 1984). In this case, Debtor and Defendant agreed upon the value of the transferred assets. The partiesŒboth agreed that the property would be transferred in consideration of a partial satisfaction of judgment in the amount of $198,000. This agreement establishes a prima facie case of value.

Defendant has failed to make a showing of evidence sufficient to defeat the prima facie case of value established by the Trustee. The only evidence Defendant has offered as to value was an appraisal of some of the assets conducted in February, 1994 by a personal property liquidator. Although the appraisal valued Defendant's assets at significantly lower than $198,000, the liquidator was merely appraising the tangible assets of Defendant as of February 1994. He was not appraising Defendant as an on-going business at the time of transfer, six months earlier.

The Bill of Sale entered into by the parties that transferred the assets to Defendant on July 1, 1993 in

consideration of the partial satisfaction of judgment did not explicitly state that Debtor was transferring the business as a going concern. However, that is precisely what was transferred. The facts surrounding this transfer indicate that more than just the physical assets such as vehicles and equipment transferred. The business continued as a going concern after July 1, 1993 just as it had before the assets were transferred. The locks were not changed, the employees were not fired, and the Lindgrens did not come to the store on July 1, 1993 to verify that the transfer had taken place. Everything continued just as it had when Debtor was operating its business. Although Shirley Lindgren needed to put money into the business in late 1993 to keep the business running, the business functioned through July, August, and September of 1993 just as it had prior to the July 1, 1993 transfer. Nothing changed in the way the business was run. These facts indicate that the business was transferred to Defendant as a going concern on July 1, 1993. Accordingly, valuation of only tangible assets is insufficient to rebut the prima facie showing by the agreed upon valuation of $198,000.

III.

Based on the foregoing, it is hereby ORDERED: that Plaintiff is entitled to judgment against Defendant for $198,000, as a preferential transfer received by Defendant, and avoidable and recoverable by Plaintiff pursuant to 11 U.S.C. Sections 547(b) and 550.Œ™LET JUDGMENT BE ENTERED ACCORDINGLY.

Dated: October 30, 1996

By The Court:

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DENNIS D. O'BRIEN
CHIEF BANKRUPTCY JUDGE