UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA

In re: DANIEL S. MILLER, BKY 04-60106
Chapter 7

Debtor.

DAVID. G. VELDE, Trustee, ADV 06-6086

Plaintiff,

v.

ORDER GRANTING PARTIAL SUMMARY JUDGMENT

DAVID KIRSCH,

Defendant.

This matter came before the Court on the Chapter 7 Trustee's motion for partial summary judgment. Justin Weinberg appeared on behalf of the plaintiff, Chapter 7 Trustee David. G. Velde. David L. Johnson appeared on behalf of the defendant, David Kirsch. At the conclusion of the hearing, the Court took the matter under advisement. Based upon all of the files, records and proceedings herein, the Court being now fully advised, makes this Order pursuant to the Federal and Local Rules of Bankruptcy Procedure.

I. FACTS NOT IN DISPUTE

The facts central to this motion are not contested. In October 2003, the defendant David Kirsch sold approximately 6,994 bushels of soybeans to the debtor, Daniel Miller. At the time, Kirsch was indebted to his bank in an amount in excess of the value of the soybeans, and the bank held a security interest in the soybeans. Kirsch delivered the soybeans to Miller between October 10 and 14, 2003. Miller issued check # 22408 dated October 27, 2003, in the amount of $44,955.14, payable to Kirsch and the bank. Kirsch endorsed the check and presented it for payment, but check #22408 was refused due to insufficient funds. On November 10, 2003, Miller replaced bounced check #22408 by issuing check #185314, also in the amount of $44,955.14, also payable to Kirsch and the bank. The second check was honored; the funds were applied against Kirsch's debt; and the bank's security interest in the soybeans was released.

Less than ninety days following the issuance of check #185314, on February 3, 2004, an involuntary Chapter 7 petition was filed against Miller. On February 18, 2004, Miller converted the case to Chapter 11. On September 29, 2004, this case was

NOTICE OF ELECTRONIC ENTRY AND
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Filed and Docket Entry made on 08/29/06
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converted to Chapter 7 and David Velde was appointed Trustee. On January 19, 2006, Velde commenced this adversary proceeding seeking to avoid the November 10, 2003 payment from Miller to Kirsch of $44,955.14 as a preferential transfer. The complaint also seeks to avoid a separate transfer, but it was not included in the motion for summary judgment.

Kirsch asserts that the payment is excepted from avoidance as a contemporaneous exchange for new value because, under the Federal Food Security Act, Miller acquired the soybeans subject to the bank's security interest unless and until the security was either formally released or the bank was paid for the value of the soybeans. Velde, on the other hand, claims that no defenses to avoidance are available because the transfer at issue was payment to make good a bounced check.

II. SUMMARY JUDGMENT

The standard for determining a motion for summary judgment is well established. "Summary judgment is appropriate if the evidence, viewed in the light most favorable to the nonmoving party, shows that no genuine issue of material fact exists and that the moving party is entitled to judgment as a matter of law." See A & L Laboratories, Inc. v. Bou-Matic LLC, 429 F.3d 775, 778 (8th Cir. 2005), citing Krenik v. County of Le Sueur, 47 F.3d 953 (8th Cir. 1995); see also Fed. R. Civ. P. 56(c).

III. DISCUSSION

The trustee's complaint arises under 11 U.S.C. § 547(b), which provides, in pertinent part:

> (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--
>
> (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--
>
> (A) on or within 90 days before the date of the filing of the petition,
>
> (5) that enables such 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.

See 11 U.S.C. § 547(b).

The parties acknowledge that the requirements of § 547(b) are satisfied by the facts. The issue in this case is whether Kirsch can properly claim a defense under § 547(c)(1), or if the exceptions are barred as a matter of law because the transfer consisted of a payment made to cure a previously issued bad check. Section 547(c)(1) provides:

(c) The trustee may not avoid under this section a transfer--

(1) to the extent that such transfer was--

(A) intended by the debtor and the creditor to or for whose benefit such transfer was made to be a contemporaneous exchange for new value given to the debtor; and

(B) in fact a substantially contemporaneous exchange;

See 11 U.S.C. § 547(c)(1).

"Pursuant to 11 U.S.C. § 547(c)(1), an otherwise preferential transfer is not avoidable to the extent such transfer was intended by the debtor and the creditor to or for whose benefit such transfer was made to be a contemporaneous exchange for new value given to the debtor and was in fact a substantially contemporaneous exchange." See Stewart v. Barry County Livestock Auction, Inc. (In re Stewart), 282 B.R. 871, 874 (8th Cir. BAP 2002). "For purposes of 11 U.S.C. § 547, 'new value' is defined as money or money's worth in goods, services, or new credit, or release by a transferee of property previously transferred to such transferee in a transaction that is neither void nor voidable under any applicable law, including proceeds of such property, but does not include an obligation substituted for an existing obligation." Id., citing 11 U.S.C. § 547(a)(2).

Kirsch offered a plausible and well supported argument that the payment for the soybeans, when it was honored, cashed and applied against his debt to the bank, resulted in the release of the bank's security interest in the soybeans, and that the release constituted new value. However, the prevailing law is clear that if the preferential transfer at issue was a payment to replace a bounced check, then the scope of the transfer is limited to that context --- a substitute payment of an antecedent debt arising out of an extension of

credit transaction — and the § 547(c) defenses are therefore not available.

"[A]ny payment to an unsecured creditor within the ninety-day preference period to make good a bounced check is an avoidable preference provided that the requirements for an avoidable preference are otherwise satisfied." See Endo Steel, Inc. v. Janas (In re JWJ Contracting Co., Inc.), 371 F.3d 1079, 1082 (9th Cir. 2004), citing Morrison v. Champion Credit Corp. (In re Barefoot), 952 F.2d 795, 797 (4th Cir. 1991). "[W]hen a check bounces, the date of delivery of the dishonored check no longer determines the time of transfer for the purpose of § 547(b)." See Pressman v. Rodemich (In re So Good Potato Chip Co.), 137 B.R. 330, 331 (Bankr. E.D.Mo. 1992), citing Barefoot, 952 F.2d at 798. "[T]o let a later good transfer relate back to a bad transfer would have the 'effect of giving operative legal significance to bad checks ... [and] would also undermine both of Congress' purposes for § 547(b)." Id.

"First, favoritism of certain creditors with payments making good the bad checks deals a serious blow to the fundamental bankruptcy policy of equality of distribution among members of the same class by enabling some unsecured creditors to receive more than their pro rata share of assets in the estate." Barefoot, 952 F.2d at 798. "Second, creditors may possess greater incentives to forsake cooperative arrangements involving financially troubled debtors if the delivery date of dishonored checks is to become the operative one under bankruptcy preference law." Id. "With the insufficiency of funds in a debtor's account less of an immediate constraint, creditors may be tempted to demand payment from a debtor on the edge of bankruptcy rather than negotiate a work-out plan on the grounds that even a bad check might later be made good without risking avoidance of the payment as a preference." Id. at 798-799.

"[W]hen a bounced check is given by the debtor in exchange for new value provided by a creditor, any subsequent payment to make good the bad check is not a contemporaneous exchange for new value." Barefoot, 952 F.2d at 800, citing Goger v. Cudahy Foods Co. (In re Standard Food Services, Inc.), 723 F.2d 820, 821 (11th Cir. 1984) (cashier's check making good a bounced check held not a contemporaneous exchange for new value). "The reason why an exchange involving a dishonored check is outside this exception to the avoidance power is [because] ... [t]he exception for a contemporaneous exchange does not ordinarily apply to credit transactions, and the dishonor of a check inevitably creates an antecedent debt owed by the debtor which any subsequent payments to make good the check, no matter how quickly made, would be satisfying." Id. *See also* Ewald Bros., Inc. v. Kraft, Inc. (In re Ewald Bros., Inc.), 45 B.R. 52, 57 (Bankr. D. Minn. 1984) (the result of a check being returned for nonsufficient funds is an extension of credit by the defendant); Reynolds v. Nissan (In re Car Renovators), 946 F.2d 780, 782 (11th Cir. 1991) (a payment for a dishonored check is a payment on account of an antecedent debt).

"The definition [of new value] expressly excludes 'an obligation substituted for an

existing obligation.'" Stewart, 282 B.R. at 875, citing 11 U.S.C. § 547(a)(2). Checks that were "replacement payments substituted for the earlier bounced checks ... are expressly excluded from the definition of 'new value' set forth in 11 U.S.C. § 547(a)(2)." Id. As in Stewart, the facts here are that both the debtor and Kirsch "intended the [second] check[] to satisfy the obligations arising out of the dishonored [] check[]." Stewart, 282 B.R. at 874-875. Accordingly, § 547(c)(1) is not a cognizable defense to a § 547(b) action involving a preferential transfer consisting of a payment made to cure a bounced check, and the trustee in this case must prevail.

IV. DISPOSITION

IT IS HEREBY ORDERED:

1. The transfer from the debtor Daniel Miller to the defendant David Kirsch, in the amount of $44,955.14, transferred as a result of the debtor's issuance of check #185314, constitutes an avoidable preferential transfer pursuant to 11 U.S.C. § 547(b);

2. The transfer above described in paragraph #1 of this Order does not satisfy an exception to § 547(b) as set forth in § 547(c)(1) as a contemporaneous exchange for new value; and

3. ENTRY OF JUDGMENT SHALL BE DEFERRED pending final adjudication, or other resolution, of the remaining claims in this adversary proceeding.

BY THE COURT:

DATED: August 29, 2006

/e/ Dennis D. O'Brien
United States Bankruptcy Judge