

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA
THIRD DIVISION

In re: Chapter 11 Case
Youth Fair, Inc., BKY Case No. 3-89-3935
Debtor. ADV No. 3-90-191

Youth Fair, Inc.,
Plaintiff,

v. MEMORANDUM ORDER

The Schwab Company, a
Division of S. Schwab Company,
Inc., a Maryland Corporation,

Defendant.

This matter came before the Court on cross motions for summary judgment. Plaintiff Youth Fair, Inc. (Youth Fair) is represented by Darrell B. Johnson. Defendant Schwab Company (Schwab) is represented by William Douglas White. This is a core proceeding under 28 U.S.C. Sections 1334 and 157(a). The Court has jurisdiction to determine this matter under 28 U.S.C. Section 157(b)(2)(F). Based upon all the files and records in this case, being fully advised in the premises, the Court now makes the following Order pursuant to the Federal and Local Rules of Bankruptcy.

I.

FACTS

Swab
Youth Fair and Schwab have stipulated to the following facts. On October 10, 1989, Schwab shipped inventory to Youth Fair in the ordinary course of business. Youth Fair received the inventory items on October 13, 1989, accompanied by Invoice No. 3839 dated October 10, 1989 for \$724.55. Thereafter, Youth Fair filed for relief under Chapter 11 on October 17, 1989.(FN1) That same day, Schwab shipped additional inventory to Youth Fair, which received these inventory items on October 20, 1989, with Invoice Nos. 6710, 6711, and 6712, totalling \$3,819.54.

parties
When Schwab sent its reclamation demand on October 20, 1989, Youth Fair had Schwab's inventory(FN2) in its possession. The parties then negotiated an agreement under which Youth Fair would satisfy the demand by voluntarily making a cash payment to Schwab in lieu of returning its inventory. In accordance with their agreement, Schwab credited Youth Fair's account for \$4,544.09--the full amount due under Invoice Nos. 3839, 6710, 6711, and 6712. Schwab then re-billed the \$4,544.09 to Youth Fair for the same inventory items under Invoice Nos. 18985, 18986, 18987, and 18988. On October 30,

1989, Youth Fair returned \$792.00 worth of inventory to Schwab, and on October 31, 1989, paid Schwab \$3,752.12.(FN3) The check
memorandum

read "with this check, reclamation notice dated October 20, 1989 has been satisfied." Youth Fair marked, distributed, and sold the

(FN1) Youth Fair operated its business during its reorganization effort as a Debtor-In-Possession with authority to conduct its customary business affairs under 11 U.S.C. 1108.

(FN2) During the pendency of this case, it was undisputed that National City Bank had a properly perfected lien on all of Youth Fair's inventory to secure a debt of approximately \$2.6 million.

(FN3) The full amount due under Invoices 18985, 18986, 18987, and 18988, less the value of the returned goods.

remaining inventory in the ordinary course of business. On August 1, 1989, all of Youth Fair's inventory was sold as part of an asset sale pursuant to Court order, and National City Bank's security interest was satisfied in full from the proceeds of the sale.

The present dispute involves Youth Fair's contention that its payment to Schwab was an improper post-petition transfer under 11 U.S.C. Section 549(a).(FN4) Schwab argues that the payment was

proper

compensation for its agreement not to require return of its inventory under 11 U.S.C. Section 546(c).(FN5) Youth Fair seeks

return

of the \$3,752.12 to the estate, but would allow Schwab a claim in that amount as an administrative expense under 11 U.S.C.

Section507(a).

ISSUE

Is Youth Fair entitled to return of its cash payment to Schwab under 11 U.S.C. Section 549(a)?

DISCUSSION

Throughout the pendency of this case, Youth Fair operated as a debtor-in-possession with authority to conduct its customary business affairs in the ordinary course as a retail vendor of childrens' clothing. Ordering inventory, making arrangements with suppliers concerning inventory needs, and selling inventory in the ordinary course of its business are activities which the debtor might reasonably be expected to conduct without court supervision. See: 11 U.S.C. Section 1108. Under these circumstances, Schwab had every reason to believe that the debtor was dealing with it in good faith, and had the authority to resolve its reclamation claim.

Now, Youth Fair is attempting to use the "strongarm" power usually exercised by a bankruptcy trustee under 11 U.S.C. Section 549(a) to undo improper transactions concluded by the Debtor during the pendency of a case. Schwab opposes Youth Fair by asserting its rights as a reclaiming creditor under 11 U.S.C. Section 546(c).

While both parties supplied briefs which include statutory and

caselaw support for their respective positions, neither party fully

(FN4) 11 U.S.C. 549(a) reads in pertinent part: "...(a) Except as provided in subsection (b) or (c) of this section the trustee may avoid a transfer of property of the estate--

(1) that occurs after the commencement of the case; and

(A) that is authorized only under section 303(f) or 542(c) of this title; or

(B) that is not authorized under this title or by the court...."

(FN5) 11 U.S.C. Section 546(c) reads in pertinent part: "...(c) Except as provided in subsection (d) of this section, the rights and powers of a trustee under sections 544(a), 545, 547, and 549 of this title are subject to any statutory or common-law right of a seller of goods that has sold goods to the debtor, in the ordinary course of such seller's business, to claim such goods if the debtor has received such goods while insolvent, but--

(1) such a seller may not reclaim any such goods unless such seller demands in writing reclamation of such goods before ten days after receipt of such goods by the debtor; and

(2) the court may deny reclamation to a seller with such a right of reclamation that has made such a demand only if the court--

(A) grants the claim of such a seller priority as a claim of a kind specified in section 503(b) of this title;

or

(B) secures such claim by a lien...."

considered the effect of Youth Fair's willingness to grant Schwab an administrative expense priority under 11 U.S.C. Section 507(a). (FN6)

Section 507(a) does not contemplate administrative priority treatment for improper claims. Thus, Youth Fair's argument that its voluntary agreement to pay Schwab was an impermissible resolution of its inventory problem is inconsistent with its willingness to grant Schwab's claim priority treatment. Clearly, this was a post-petition transaction based on post-petition consideration. Specifically, consideration lies in the adjustment of the accounts of the parties in recognition of Schwab's reclamation rights. Accordingly, Youth Fair is not entitled to summary judgment that Schwab must return the \$3,752.12 and file an administrative expense claim.

NOW, THEREFORE, IT IS ORDERED:

1. Plaintiff's motion for summary judgment is denied.
2. Defendant's motion for summary judgment is granted consistent with grounds as stated in this opinion.

Dated:

Dennis D. O'Brien
U.S. Bankruptcy Judge

(FN6) 11 U.S.C. 507(a) reads in pertinent part: "Priorities.
(a) The following expenses and claims have priority in the
following order:

(1) First, administrative expenses allowed under section
503(b) of this title, and any fees and charges
assessed against the estate under chapter 123 of
title 28...."