

**IN THE UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF ARKANSAS
TEXARKANA DIVISION**

IN RE: MEYER'S BAKERIES, INC., Debtor

**No. 4:05-bk-70837
Ch. 7**

RICHARD L. COX, Trustee

Plaintiff

vs.

4:07-ap-7152

**PROFESSIONAL PACKAGING SYSTEMS, INC.,
PROFESSIONAL PACKAGING SYSTEMS, LTD.,
PROFESSIONAL PACKAGING SYSTEMS, GP L.L.C.**

Defendants

ORDER

Before the Court is the Complaint to Avoid Preferential Transfer filed by the chapter 7 trustee, Richard L. Cox, on February 27, 2007, and the Defendants' Answer to Complaint to Avoid Preferential Transfer filed by the defendants [Professional Packaging] on March 26, 2007. The Court heard the complaint and answer on December 13, 2007, and allowed the parties an additional 20 days to submit post-trial briefs to the Court. For the reasons stated below, the Court grants the trustee's complaint in part and denies it in part.

The Court has jurisdiction over this matter under 28 U.S.C. § 1334 and 28 U.S.C. § 157, and it is a core proceeding under 28 U.S.C. § 157(b)(2)(F). The following order constitutes findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052.

At the beginning of trial, the parties stipulated to the following facts:

1. Debtor paid \$69,871.00 to Professional Packaging Systems, Ltd. on account of an antecedent debt within 90 days from the date the Debtor filed bankruptcy.
2. Debtor paid \$69,871.00 to Professional Packaging Systems, Ltd. while Debtor was insolvent.

3. The payment of \$69,871.00 to Professional Packaging Systems, Ltd. enabled Professional Packaging Systems, Ltd. to receive more than it would receive if the case were a case under chapter 7 of Title 11 and the payment of \$69,871.00 had not been made.
4. Transfer No. 1 - \$12,825.00 was paid on November 26, 2004 arising out of Invoice GP 10813 dated September 30, 2004--58 days after the invoice.
5. Transfer No. 2 - \$10,876.00 was paid on November 26, 2004 arising out of Invoice GP 11214 dated September 30, 2004--58 days after the invoice.
6. Transfer No. 3 - \$23,085.00 was paid on December 17, 2004 arising out of Invoice GP 11422 dated November 15, 2004--32 days after the invoice.
7. Transfer No. 4 - \$23,085.00 was paid on December 24, 2004 arising out of Invoice GP 11770 dated December 9, 2004--15 days after the invoice, and 25 days after shipment.
8. The average number of days in which Meyers Bakery's Inc. paid the Professional Packaging Systems, Ltd. pre-petition invoices was 53 days and median number of days was 58 days.
9. The average number of days for paying receivables in the food packaging industry average [sic] is 28 days.

Applicable Law

As a preliminary matter, the Court must determine the applicable bankruptcy law that controls this preference action. The debtor filed its voluntary chapter 11 bankruptcy petition on February 6, 2005, prior to the enactment of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 [BAPCPA], which took effect October 17, 2005.¹ According to the code, a voluntary case is commenced by the filing of the petition. 11 U.S.C. § 301(a). Further, commencement of a voluntary case constitutes an order for

¹ BAPCPA was signed by the President on April 20, 2005. Although some of the provisions took effect upon signing, most of them became effective on October 17, 2005, 180 days after BAPCPA was signed.

relief under the chapter in which the case was filed, in this case, chapter 11. 11 U.S.C. § 301(b). Later, on March 23, 2006, the case was converted to a chapter 7 liquidation case. Professional Packaging argues that the date of conversion constitutes a new order for relief and appears to suggest that because the conversion took place after the enactment of BAPCPA, BAPCPA would be the controlling law in the converted case.

Although Professional Packaging is correct that conversion of a case from one chapter to another constitutes an order for relief in the converted case, it is incorrect to conclude that conversion affects the date of filing or the date of the order for relief. Section 301 states that commencement of a case constitutes an order for relief under the chapter *in which the case was filed*. When a case is converted from one chapter to another, § 348 states that the conversion “constitutes an order for relief *under the chapter to which the case is converted . . .*” 11 U.S.C. § 348(a) (emphasis added). However, the code is also clear that conversion “does not effect a change in the *date* of the filing of the petition, the commencement of the case, or the order for relief.” *Id.* (emphasis added). In other words, in this case the date of filing the petition, the commencement of the case, and the date of the order for relief remains February 6, 2005. Because this date is prior to the enactment of BAPCPA, the Court finds that the bankruptcy code in effect prior to the enactment of BAPCPA is the applicable controlling law.

Preference

Under § 547 of the bankruptcy code, an avoidable preference is a transfer of the debtor’s property to or for the benefit of a creditor, on account of an antecedent debt owed by the debtor before the transfer was made, on or within 90 days before the date of the filing of the debtor’s petition, while the debtor was insolvent, that enabled the creditor to receive more than the creditor would in a chapter 7 liquidation. 11 U.S.C. § 547(b). The burden of proof is on the trustee to prove the preferential transfer. *Bergquist v. Anderson-Greenwood Aviation Corp. (In re Bellanca Aircraft Corp.)*, 56 B.R. 339, 370 (Bankr. D. Minn. 1985). The parties have stipulated to all the elements of a preferential transfer, and the Court finds that the trustee has met his burden of proof as to the preferential transfer

from the debtor to Professional Packaging in the amount of \$69,871.00 consisting of four separate payments as set forth in the stipulations.

Professional Packaging may avoid preference liability if it can prove that it falls within one of the exceptions to a preferential transfer set forth in § 547(c); specifically, in this case, the ordinary course of business exception found in § 547(c)(2). To qualify for the ordinary course of business exception, Professional Packaging must prove that the 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 business terms.” 11 U.S.C. § 547(c)(2).² The parties did not specifically stipulate that the transfers were in payment of a debt incurred by the debtor in the ordinary course of business between the debtor and Professional Packaging. However, Defendant’s Exhibit 1 reflects a business relationship between the parties since at least January 31, 2004, and neither party suggested that the debts were not incurred in the ordinary course of the parties’ business. Accordingly, the Court finds that Professional Packaging meets the elements of subsection (c)(2)(A).

Subsection (c)(2)(B)--the second prong--deals with the way the parties actually conducted their business dealings and comprises a subjective component relating specifically to the debtor and the creditor. *Jones v. United Sav. and Loan Assoc. (In re U.S.A. Inns of Eureka Springs, Arkansas, Inc.)*, 9 F.3d 680, 684 (8th Cir. 1993). According to the Eighth Circuit

² This section was later amended by BAPCPA to read:
The trustee may not avoid under this section a transfer--

. . . .

(2) to the extent that such transfer was in payment of a debt incurred by the debtor in the ordinary course of business or financial affairs of the debtor and the transferee, and such transfer was--

(A) made in the ordinary course of business or financial affairs of the debtor and the transferee; *or*

(B) made according to ordinary business terms.

11 U.S.C. § 547(c) (emphasis added).

Court of Appeals, a court must engage in a “peculiarly factual analysis” to determine whether payments made by the debtor during the 90 day preference period were made in the ordinary course of business. *Lovett v. St. Johnsbury Trucking*, 931 F.2d 494, 497 (8th Cir. 1991). Specifically, the court must look at the “consistency of the transaction in question as compared to other, prior transactions between the parties.” *Concast Canada, Inc. v. Laclede Steel Co. (In re Laclede Steel Co.)*, 271 B.R. 127, 131 (B.A.P. 8th Cir. 2002) (citing *Lovett*, 931 F.2d at 497). Sufficient alteration of any one of four factors may be sufficient for a court to conclude that a payment was made outside the ordinary course of business. *Id.* at 132. The factors are,

- (1) the length of time the parties were engaged in the transactions at issue;
- (2) whether the amount or form of tender differed from past practices;
- (3) whether the debtor or the creditor engaged in any unusual collection or payment activity; and
- (4) whether the creditor took advantage of the debtor’s deteriorating financial condition.

Id. n.3. With regard to the third and fourth factors, Professional Packaging testified that it never engaged in any unusual collection or payment activities and that it was not aware that the debtor was experiencing any type of deteriorating financial conditions. The testimony was not rebutted or controverted. With regard to the first and second factors, the Eighth Circuit has found that the timing of the payments to the creditor to be of overriding importance, and stated that review of the 12 months preceding the 90 day preference period and the 90 day period itself was an appropriate standard for determining the ordinary course of business. *Lovett*, 931 F.2d at 498.

In this case, Professional Packaging introduced a spreadsheet showing the transactions between the debtor and Professional Packaging for the twelve months prior to the debtor filing its bankruptcy petition. Although the spreadsheet does not include the 12 months preceding the 90 day preference period, the parties stipulated that the average number of days in which the debtor paid Professional Packaging’s invoices was 53 days and the median number of days was 58 days. Only taking into account the payments made prior to the preference period, the average number of days in which the debtor paid Professional Packaging’s invoices was 59 days and the median number of days was 56 days. In

reviewing all of the payments made prior to the preference period, the two earliest payments were made 45 and 51 days after invoice, respectively.

Of the four transfers that occurred within the preference period, the first two--identified by the parties as Transfer No. 1 and Transfer No. 2--occurred 58 days after the transfer was invoiced. Because these payments were consistent with the payment history of the payments made prior to the preference period, the Court finds that the first two transfers were made in the ordinary course of business of the debtor and Professional Packaging.

The last two transfers--identified by the parties as Transfer No. 3 and Transfer No. 4--present a different time frame. Transfer No. 3 was paid 32 days after the transfer was invoiced and Transfer No. 4 was paid 15 days after the transfer was invoiced, and 25 days after shipment.³ In other words, these two payments were made approximately four and five weeks earlier than the average payments made in the ordinary course of business between the parties, and at least two weeks earlier than the earliest payment made prior to the preference period. Because of this, the Court finds that these two payments--Transfer No. 3 and Transfer No. 4--were not made in the ordinary course of business of the debtor and Professional Packaging.⁴ Because pre-BAPCPA law requires all three prongs of the

³ The difference in the invoice date and the shipment date for Transfer No. 4 was explained by Professional Packaging as the result of Professional Packaging's computer system crashing. The crash resulted in data from an approximate nine day period having to be reentered into the system. Professional Packaging also testified that the debtor was aware of the charges on or about December 1 and would have been invoiced shortly thereafter, but because of the computer system crash, was not invoiced until December 9.

⁴ While one may ordinarily think of a preferential payment being made *later* than in the ordinary course of business between the parties, a payment made earlier likewise meets the criteria of not being made in the ordinary course. Such an analysis is consistent with the policy against preferences, which is to "discourage unusual action by either the debtor or his creditors during the debtor's slide into bankruptcy." H.R. Rep. No. 595, 95th Cong., 1st Sess. 373 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 6329. In this case, by the time the average payment period--59 days--would have passed, Transfer Nos. 3 and 4 could not have been made because the debtor would have already been in bankruptcy.

ordinary course of business exception to be met, and Professional Packaging has failed to meet its burden with regard to the second prong for Transfer Nos. 3 and 4, the Court finds that Transfer No. 3 in the amount of \$23,085.00 and Transfer No. 4 in the amount of \$23,085.00 were preferential transfers in favor of Professional Packaging and not excepted under § 547(c)(2). By separate order, the Court will enter its judgment in favor of the chapter 7 trustee and against Professional Packaging Systems, Ltd. in the amount of \$46,170.00.

Subsection (c)(2)(C)--the third prong--requires that the transfers be made according to ordinary business terms and comprises the objective component of the analysis. *U.S.A. Inns of Eureka Springs*, 9 F.3d at 684. In other words, the Court must determine “whether the transaction was ordinary pursuant to terms in the industry.” *Laclede Steel Co.*, 271 B.R. at 133. To make this determination, the Court must compare the payment record of the debtor with the general practice in the industry regarding time of payment. *Lovett*, 931 F.2d at 499. Because the Court has already found that Transfer Nos. 3 and 4 were preferential transfers not subject to an exception, it will only review Transfer Nos. 1 and 2 under subsection (c)(2)(C).

The parties stipulated that the average number of days for paying receivables in the food packaging industry is 28 days. In support of this stipulation, Professional Packaging introduced Defendant’s Exhibit 2, a table from the Almanac of Business in Industrial and Financial Ratio (Grocery and Related Product). In addition to the stipulation, an official from Professional Packaging testified that in his opinion, the four alleged preference payments were all made in accordance with the general industry, and later testified that from an industry standard, it is not unusual to be paid 58 days from invoice. Although the stipulation and testimony appear to contradict each other, it is possible to have an average that does not comport with specific testimony with regard to the industry at issue. In this particular instance, even though the average in the industry is 28 days, the uncontroverted testimony of the official from Professional Packaging was that payment 58 days from invoice was not unusual in the industry. Stated another way, “average time of payment” is

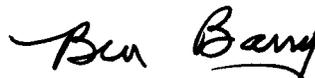
not the same as “made according to ordinary business terms,” but is merely one factor in the analysis. In the absence of any contrary evidence, this is sufficient to carry Professional Packaging’s burden on the third prong. *See U.S.A. Inns of Eureka Springs, Arkansas, Inc.*, 9 F.3d at 685 (finding that testimony of creditor’s President/C.E.O. was sufficient to satisfy burden of proving industry-wide practice under § 547(c)(2)(C)); *Lovett*, 931 F.2d at 499 (finding that unrefuted testimony by two of the defendant’s officials was sufficient to satisfy § 547(c)(2)(C) burden). Accordingly, the Court finds that the first two transfers were made according to ordinary business terms within the industry and, because all three prongs of the ordinary course of business exception have been met, are excepted from preferential transfer liability.

For the reasons stated above, the Court finds that Transfer Nos. 1 and 2 were preferential transfers by definition, but are excepted from liability under § 547(c)(2). The Court further finds that Transfer Nos. 3 and 4 were preferential transfers as well, and are not excepted from liability under § 547(c)(2). By separate order, the Court will enter its judgment in favor of the chapter 7 trustee and against Professional Packaging Systems, Ltd. for Transfer Nos. 3 and 4 in the amount of \$46,170.00.

IT IS SO ORDERED.

January 15, 2008

DATE



BEN T. BARRY

UNITED STATES BANKRUPTCY JUDGE

cc: William Siegel, attorney for Professional Packaging
Thomas S. Streetman, attorney for the chapter 7 trustee
Richard L. Cox, chapter 7 trustee

EOD 1/15/2008
by T Wilkins