The ClawBack Report

A Preference and Fraudulent Conveyance Newsletter

Volume 3 Edition 7

JONES

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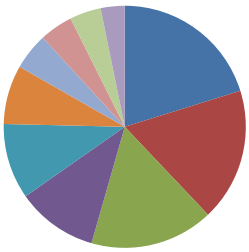
Groups of Adversary Proceedings Filed by the Debtor



- Kid Brands, Inc.
- Lamar Construction Company
- Pretty Girl, Inc.
- New Century Transportation, Inc.
- Licking River Mining, LLC
- Palm Drive Health Care District
- Gas-Mart USA, Inc.
- The Adoni Group, Inc.
- D.I.T., Inc.
- Oak Rock Financial, LLC

INTRODUCTION

Your monthly dispatch from the preference wars by Roland Gary Jones Esq., "The Preference Guy".

Trustees initiated more than 400 adversary proceedings nationwide during the month of June 2016. Most notable -

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- 82 clawback lawsuits initiated in the bankruptcy cases of **Kids Brand, Inc.**
- 72 preference actions were commenced in the **Lamar Construction Company bankruptcy.**

Rulings for June -

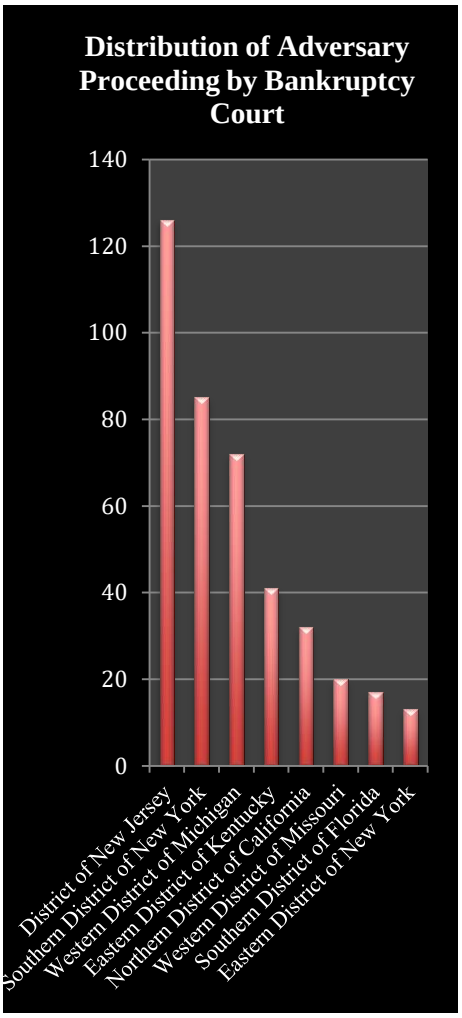
- The Court of Appeals for the Seventh Circuit elaborated on the application of the average lateness method for ordinary course defense. Reversing the bankruptcy and district court's decision, the Seventh Circuit held that the lower courts failed to establish the appropriate historical period for reflecting the parties' payment practices. The Court expanded the historical period range and held that all payments except two were made in the ordinary course of business between the parties.

- A Texas Bankruptcy Court concluded that a creditor can still establish an ordinary course of business defense to a preference action where a change in ownership of the creditor six months before the bankruptcy filing caused the debtor's ordinary course of the business with the subcontractor to change.

Warm Regards,
Roland

News

- Charles Bennett, a Former Corporate Lawyer at Skadden, Arps, Slate, Meagher & Flom, Disbarred From the Bar of the State of New York for Running a $5 million Ponzi scheme



- Clawback Actions Begin in the Bankruptcy Case of Lamar Construction Company
- Greenberg Traurig LLP To Face $2.2M Clawback Suit
- Preference Actions Filed in New Jersey in the Kid Brands Inc.'s Bankruptcy
- Hulk Hogan Wants to Keep Preference Actions
- Madoff Trustee Begins Seventh Pro Rata Interim Distribution of Recovered Funds to Madoff Claim Holders

Opinions

- Security Interest Perfected Beyond 30-Days After the Debtor Received Possession of Vehicle is a Preference
- Payments May be Ordinary, Even When the Payment Practices Differ in the Preference and the Base Period, If there Is a Change in the Defendant's Ownership
- Lack of Recognition of Constructive Trust in Louisiana Precludes Judgment in Favor of Defendant
- Seventh Circuit Refines the Standard for Calculating the Baseline of Payment History Between the Parties
- Puerto Rico Court Ruled for Defendant as the Trustee's Complaint Fails to Meet Plausibility Standards or State Sufficient Factual Information
- Utah Court Did Not Allow a Creditor to Retain the Funds He Invested With a Non-Debtor in a Ponzi Scheme, Even When the Non-Debtor was Operating the Debtor's Ponzi Scheme
- Issues of Material Facts Prevented the Court From Entering Summary Judgment in Favor of Debtor

Recent Preference and Fraudulent Conveyance News

Charles Bennett, a Former Corporate Lawyer at Skadden, Arps, Slate, Meagher & Flom, Disbarred From the Bar of the State of New York for Running a $5 million Ponzi scheme

June 2, 2016, New York - Charles E. Bennett, 57, a former corporate lawyer at Skadden, Arps, Slate, Meagher & Flom, who was sentenced to prison for running a $5 million Ponzi scheme, is now disbarred from the Bar of the State of New York.

Bennett's conviction stemmed from a Ponzi scheme wherein he solicited approximately $10 million from more than 30 investors under false pretenses. As per the complaint, the investment fraud came after Bennett launched his own law practice in 2001. As a part of the scheme, Bennett allegedly told investors that he had a relationship with various fund managers and could arrange for investments in his fund. But Bennett never allegedly invested the money and instead used it for his own benefit and to repay investors. He attempted to

commit suicide after investors began demanding repayment.

Bennett was admitted to the practice of law in the State of New York by the First Judicial Department on June 2, 1986. On October 28, 2015, Bennett pleaded guilty in the United States District Court for the Southern District of New York to securities fraud in violation of 15 USC §§ 78j(b) and 78ff, 17 CFR § 240.10b-5 and 18 USC § 2, and wire fraud in violation of 18 USC §§ 1343 and 2, both felonies. On May 19, 2016, Bennett was sentenced to five years in prison and three years of supervised release.

Following the Departmental Disciplinary Committee's motion seeking an order striking Bennett's name from the roll of attorneys under Judiciary Law § 90(4)(b) upon the ground that he was automatically disbarred as a result of his conviction of a federal felony that would constitute a felony if committed under New York law (Judiciary Law § 90(4)(e), **the Court granted the Committee's petition and Bennett's name was stricken from the roll of attorneys and counselors-at-law in the State of New York effective nunc pro tunc to October 28, 2015.**

The case is *U.S. v. Bennett,* U.S. District Court, Southern District of New York, Case No. 15-00020 and Matter of Bennett 2016 NY Slip Op 04319 Decided on June 2, 2016 Appellate Division.

Clawback Actions Begin in the Bankruptcy Case of Lamar Construction Company

Michigan, June 2, 2016 - **Marcia Meoli, the Chapter 7 Trustee for the bankruptcy estate of Lamar Construction Company (Debtor) filed approximately 72 complaints during the month of June 2016**. The Trustee initiated the lawsuits in the U.S Bankruptcy Court for the Western District of Michigan and argued that the assets held by the defendants belonged to the Debtor and that the payments received by various defendants are avoidable and subject to recovery under 11 U.S.C. § 547 of the bankruptcy code.

The Debtor filed for protection under Chapter 7 of the Bankruptcy Code in the U.S. Bankruptcy Court for the Western District of Michigan on July 11, 2014. Prior to the petition date, the Debtor provided construction services. The Company offered general contracting, construction management, steel and pre-cast concrete erection, pre-engineered metal building erection, pre-construction, and facility maintenance services.

The Debtor's preference actions are pending before the Honorable Judge James W. Boyd. The Trustee is represented by the law firm Rhoades McKee PC. The Debtors cases are administered under Case no. 14-04719.

Greenberg Traurig LLP To Face $2.2M Clawback Suit

June 4, 2016, Delaware – **Elizabeth M. Guffy, the Plan Agent for the bankruptcy estate of a medical center management company, Brown Medical Centre (BMC) stated that Greenberg Traurig, LLP (GT) can't escape her lawsuit seeking to clawback transfers worth $2.2 million pursuant to 11 U.S.C. § 544, 548, 550 and Tex. Bus. & Com. Code Ann. § 24.008 and should return the funds to the estate.** The Plan Agent also sought to recover the attorney costs and fees pursuant to Tex. Bus. & Com. Code Ann. § 24.013.

The Complaint filed by BMC in the Texas Court contended that GT served as attorneys for Michael Brown (the owner and founder of BMC) and various business entities that he owned or controlled in the years 2012 and 2013. GT issued a number of invoices to BMC when the latter was insolvent and these invoices related to GT's representation of Brown personally or certain of Brown's wholly-owned entities. **The Plan Agent argued that the transfers and any agreement by BMC to make and/or allow such transfers within two years of the petition date were avoidable as fraudulent transfers under 11 U.S.C. § 548 because BMC received less than reasonably equivalent value in exchange for those transfers as GT did not provide any legal services for the benefit of BMC, and all value provided by GT was specifically for the benefit of Brown or Brown's wholly-owned entities unrelated to BMC.**

GT argued in its response that the Plan Agent cannot sue to take back $2.2 million as it cannot prove the money came from improper accounts. GT alleged that the Plan Agent's claims must be dismissed because the amended complaint failed to adequately plead specific and plausible allegations that any of the alleged transfers constituted property of BMC.

As of now, the Court has denied GT's motion to dismiss and have afforded an opportunity to the Plan Agent till July 11, 2016 to file an amended complaint. The Court also ordered that GT may file a motion to dismiss the amended complaint by August 1, 2016. The case is *Guffy v. Greenberg Traurig, LLP et al*; Case No. 4:16-cv-00536.

Preference Actions Filed in New Jersey in the Kid Brands Inc.'s Bankruptcy

New Jersey, June 16, 2016 - **On June 16, 2016, the Official Committee of Unsecured Creditors of Kid Brands Inc., et al. filed approximately 64 complaints seeking the avoidance and recovery of allegedly preferential and fraudulent transfers under Sections 547, 548 and 550 of the Bankruptcy Code.** The Committee also sought to disallow claims of such preference defendants under Sections 502(d) and (j) of the Bankruptcy Code.

The Debtors filed voluntary petitions for bankruptcy in the U.S. Bankruptcy Court for the District of New Jersey on June 18, 2014 under Chapter 11 of the Bankruptcy Code. On July 2, 2014, the Office of the United States Trustee for the District of New Jersey appointed the Committee. The law firms of ASK LLP and Gellert Scali Busenkell & Brown, LLC represent the Committee in these various preference cases. Honorable Judge Michael B Kaplan is presiding over the Debtor's bankruptcy case. The pretrial conference has not yet been scheduled.

Hulk Hogan Wants to Keep Preference Actions

New York, June 21, 2016 - **Gawker Media, a privately-held online media company has initiated an adversary case against a former pro-wrestling champ, Terry Gene Bollea, also known as Hulk Hogan, as part of an effort to hold back Hogan and potentially ward off a personal bankruptcy for Gawker's founder and owner Nick Denton.** The media company alleged that a $140 million final judgment in favor of Hulk Hogan in the invasion-of-privacy lawsuit would have a crippling effect on the Debtor's estates, prospects of reorganization, and distribution to creditors.

Hogan has filed an objection to Gawker's plan to sell itself to Ziff Davis or a higher bidder at a bankruptcy auction, on the grounds the sale will unfairly trade away potentially valuable rights. The objection focused on the inclusion of avoidance actions as part of the package of assets being sold. Hogan alleged that selling the avoidance actions could be particularly unfair in Gawker's case, because that money could be subject to reclamation by creditors and the sale of the lawsuit rights "frustrates the policy goals" behind avoidance actions.

Gawker filed for Chapter 11 bankruptcy, after the media house was ordered to pay up $140M to Hulk Hogan for publishing a report, commentary, and accompanying video excerpts involving Hogan's extramarital affair. Gawker Media and Denton was allegedly jointly and severally liable on $115 million of the judgment with an additional $10 million worth of punitive damages assessed against Denton separately. However, for now the media house has managed to get a temporary restraining order against Hogan from taking steps to enforce a judgment against Denton for the $10 million for which Denton was personally liable.

Madoff Trustee Begins Seventh Pro Rata Interim Distribution of Recovered Funds to Madoff Claim Holders

New York, June 30, 2016 - Irving H. Picard, Securities Investor Protection Act (SIPA) Trustee for the liquidation of Bernard L. Madoff Investment Securities LLC (BLMIS), commenced the seventh pro rata interim distribution from the customer fund to eligible BLMIS customers on June 30, 2016.

The SIPA Trustee is distributing approximately $190.247 million on a pro rata basis to BLMIS account holders with allowed claims, bringing the aggregate amount distributed to eligible claimants to approximately $9.47 billion, which includes approximately $836.6 million in committed advances from the Securities Investor Protection Corporation (SIPC). The seventh distribution represents 1.305 percent of each claim dollar and will be paid on claims relating to 972 BLMIS accounts to record holders of allowed claims as of June 15, 2016. When combined with the prior six distributions, in aggregate, at least 58.369 percent of each customer's allowed claim amount will be paid, unless that claim has been fully satisfied.

Currently, the SIPA Trustee has allowed 2,597 claims related to 2,249 BLMIS accounts. Of these, 1,296 accounts will now be fully satisfied following the seventh interim distribution. All allowed claims totaling $1,200,024.90 or less will be fully satisfied after the distribution.

To date, the SIPA Trustee has recovered or reached agreements to recover approximately $11.168 billion since his appointment in December 2008.

Recent Preference and Fraudulent Conveyance Opinions

Security Interest Perfected Beyond 30-Days After the Debtor Received Possession Of Vehicle is a Preference

Reynard v. Bank of Am., N.A. (In re Resler), Nos. 15-00477-TLM, 15-06052-TLM, 2016 Bankr. LEXIS 2187 (U.S. Bankr. D. Idaho June 3, 2016)

Debtor Timothy Resler and Peterson Autoplex entered into certain agreements to trade a 2010 Lexus for a 2015 Lexus. The series of events were like this: On December 29, 2014, Resler took physical possession of the vehicle. On the same date, Resler also granted a security interest in the Lexus 2015 to Peterson. On January 30, 2015, Peterson further assigned the security interest in the Lexus 2015 to the Defendant Bank of America. On February 2, 2015, the Defendant bank paid Peterson $89,524.94 as a purchase price of the contract. On April 16, 2015, the Debtor filed petition for relief

The security interest granted in the Lexus was perfected more than 30 days after Resler took possession of the Lexus. The actual application regarding the Lexus was date stamped February 5, 2015, and the title report issued by the Idaho Transportation Department showed February 9 as recorded date for the lien.

The Trustee brought an adversary proceeding alleging that the transfer of the security interest to the Defendant bank satisfied all the condition of Sec. 547(b) and hence was avoidable as preferential. The Trustee alleged that the transfer through the granting of a security interest in Lexus was not perfected within 30-day time frame and thus, it was a transfer of an interest of the Debtor in property and hence avoidable as preference. The Defendant alleged that the Trustee failed to prove when the transfer of the security interest took place. According to the Defendant bank, the transfer of security interest took place on January 30, 2015, which fit right within the 30-day time frame referenced in §547(e)(2)(A). The Defendant also argued that the transfer of the Lexus was not made on account of an antecedent debt because the contract between Peterson and the Debtor was conditioned upon the financing condition, which did not take place until January 30, 2015, when the transfer occurred and the debt was paid immediately thereon.

Rejecting both the arguments of the Defendant, **the Court stated that it need not determine which of the dates was the actual date of perfection, as all of them—January 30, February 5, February 9 fell beyond 30 days from December 29, 2014 i.e. when agreement was executed**. Thus, under § 547(e)(2)(A), the transfer through the granting of the security interest in the Lexus was deemed to have occurred for preference purposes on the date of perfection. As all these dates fell with the 90-day preference period, and the rest of the elements of Sec. 547(b) were already satisfied, the transfer was avoidable as preference.

The Court next stated that the Debtor became legally bound to pay the purchase price for the Lexus upon the execution of its contract with Peterson on December 29, 2014. The fact that Peterson assigned its rights to the Defendant bank through a new agreement did not create a new debt. **Upon the assignment, on January 30, the Defendant bank simply gained all the rights to collect and enforce the debt which the Debtor previously owed to Peterson.** Thus, the alleged transfer was not made pursuant to any new debt, rather was made on account of the pre-existing debt i.e. antecedent debt.

Thus, the Court concluded that the granting of a security interest is a transfer under 11 U.S.C.S. § 101(54) and in the present case, the security interest was perfected at least 32 days after the Debtor received possession of Lexus. Further, the new value defense at 11 U.S.C.S. §547(c)(3)(B) was unavailable. The Trustee established all the elements of 11 U.S.C.S. §547(b) and therefore the alleged transfer was avoidable as preference absent an applicable defense.

Payments May be Ordinary, Even When the Payment Practices Differ in the Preference and Base Period, If there Is a Change in the Defendant's Ownership

Satija v. C-T Plaster, Inc. (In re Sterry Indus.), Nos. 13-11818-TMD, 15-01108-TMD, 2016 Bankr. LEXIS 2268 (U.S. Bankr. W.D. Tex. June 9, 2016)

Debtor Sterry Industries, Inc. a pool installer had a long standing business relationship with a subcontractor **Defendant Hines/Harvey Interests, LLC dba Cen-Tex Plaster**, Inc to install the permanent liner in the pools constructed by the Debtor. The business was carried out in the following manner: The Debtor would fax a work order to Cen-Tex specifying where and when to install the liner. Cen-Tex would then install the liner and send an invoice to Sterry. As soon as the liner was installed, Sterry would fill the pool and then will look for payment from the owner. Payment terms were Net 30. About six months before Sterry's bankruptcy, Cen-Tex was sold to a new owner, and the business practice between Cen-Tex and Sterry changed: the invoice payment deadline changed from Net 30 to due upon receipt, instead of waiting for Sterry to mail the check, Cen-Tex would send a representative to pick up each check at Sterry's office. During the first three months after Cen-Tex changed owners, Sterry paid the invoices within 1, 4, 9, 17, and 7 days. During the preference period, the time gap between the invoice and payment dates lengthened to 22, 14, and 18 days.

The bankruptcy trustee sought to recover the payments made during the preference period as preference pursuant to Sec. 547(b). The Defendant contended that the alleged payments were made in the ordinary course of business and hence not avoidable pursuant to Sec. 547 (c) (3). The Trustee contended that changing the invoice to read due upon receipt instead of Net 30 took the payments on those invoices outside of the ordinary course. The Trustee also argued that sending someone to collect checks in person was a coercive practice that would take the payments outside of the ordinary course of business.

The Court found that the timing and manner of payments between Sterry and Cen-Tex in the three months prior to the preference period was substantially the same as during the preference period; someone would come in and pick up the check for Cen-Tex within a few weeks of the invoice date during both pre-preference and preference period, the payments were made in 30 days during the both periods. So, the alleged payments were made in the ordinary course of business. **The Court stated that the payments at issue might look preferential, if it had to look at the entire payment history between Cen-Tex and Sterry, without considering the ownership change, because Sterry began paying its invoices timely only three months before the preference period**. However, the Court concluded that it cannot ignore the ownership change which brought an agreed change in the business relationship between the two entities. **Since this new business relationship began three months prior**

to the preference period, that three-month period of time was the relevant baseline to compare to the preference period.

The Court further rejected the Trustee's collection pressure argument and reasoned that while sending someone to pick up a check in person is certainly more coercive than sending an invoice and demanding a check in the mail, this collection method was not so coercive here as to take these payments outside of the ordinary course of business. Since, this practice began with the ownership change three months before the preference period; it became ordinary to these parties.

The Court also rejected the Trustee's argument relating to the payment terms and held that according to witnesses for both parties, "Due upon Receipt" meant the same thing as "Net 30". Sterry had to pay the invoice within 30 days. Therefore, the language change did not alter, and so was not outside, the course of business between Cen-Tex and Sterry. **The Court concluded that the Trustee was not entitled to recover the alleged transfers as the Defendant has successfully established an ordinary course of business defense to the preference action.**

Lack of Recognition of Constructive Trust in Louisiana Precludes Judgment in Favor of Defendant

Rodney Tow Ch 7 Tr. v. Exxon Mobil Corp. (In re ATP Oil & Gas Corp.) Nos. 12-36187, 15-3174, 2016 Bankr. LEXIS 2249 (U.S. Bankr. S.D. Tex. June 6, 2016)

Debtor ATP Oil & Gas Corp. is a Texas corporation in the business of acquisition, development, and production of oil and gas. Being a developer in oil and natural gas properties, the Debtor's creditors consisted of oil and gas related vendors, including the **Defendant Exxon Mobil Corporation**. ATP and Exxon carried out business pursuant to an operating agreement executed between them. ATP was the operator while Exxon held a non-operating working interest. In compliance with the agreement, ATP sought advances from Exxon to cover Exxon's proportionate share of the estimated costs of decommissioning certain offshore wells and platforms. Exxon advanced those funds to ATP to cover its share of the costs under the agreement. Later on, the advanced funds significantly exceeded the actual costs of the decommissioning operations. Accordingly, ATP returned the overpayment to ExxonMobil. Subsequently, ATP filed a voluntary chapter 11 for relief. The case was converted to Chapter 7 and Rodney Tow was appointed as a Chapter 7 Trustee.

The Trustee commenced the adversary proceeding against Exxon to recover the overpayment amount worth $765,000.00 as a preferential transfer pursuant to 11 U.S.C. §§ 547. **Exxon filed a motion for summary judgment, alleging that the overpayment was held by ATP in a constructive trust for the benefit of Exxon, ATP had no equitable interest in the overpayment, and thus the alleged transfer was not a transfer of an interest of the Debtor in property and hence, was not avoidable as preferential. The Trustee for ATP argued that Louisiana law does not recognize constructive trusts. So, the alleged transfer was avoidable under 11 U.S.C.S. § 547 as the payment constituted property of the estate.** The Trustee further alleged that Exxon failed to adequately trace the funds, as

the overpayment was commingled. The Trustee argued that ATP exercised sufficient dominion and control over the overpayment such that the overpayment was ATP's property. Further, the operating agreement between the parties permitted commingling of funds. So, the Trustee contended that an agreement that permits commingling of funds and does not prohibit or condition a debtor's use of such funds creates a debtor-creditor relationship such that the funds are property of the debtor's bankruptcy estate.

Following receipt of the briefs, the Court applied the lowest intermediate balance test and found that Exxon had sufficiently satisfied its tracing burden. However, as regards to the recognition of constructive trusts, the Court said that it is the state law, which controls whether a constructive trust has been established or not. **The Louisiana Supreme Court has not explicitly ruled on whether Louisiana recognizes the concept of a constructive trust.** In the absence of guidance from the Louisiana Supreme Court, the Court stated that it must make an *Erie* guess and determine, to the best of its ability, how the Louisiana Supreme Court would rule if confronted by the issue. The Court further elucidated that when making an Erie guess, the Court looks to: (1) lower state court decisions and Supreme Court dicta, (2) the general rule on the issue, (3) the rule in other states looked to by Louisiana courts when they formulate the substantive law of Louisiana, and (4) other available legal sources, such as treatises and law review commentaries.

After review and analysis, the Court found that the lower appellate courts in Louisiana have been generally hostile to the concept of a constructive trust. **The Fifth Circuit has also consistently held that the equitable concept of a constructive trust does not have a place in Louisiana civil law and the Louisiana Trust Code is silent as to constructive trusts**. Thus, the Court concluded that given the lack of support for constructive trusts in both the Louisiana Civil Code and relevant case law, the Louisiana Supreme Court does not recognize constructive trusts. Hence, the Court denied the Defendant's Motion for summary judgment and held the alleged transfer constituted property of the estate and was liable to be returned to the bankruptcy estate pursuant to Sec. 547.

Seventh Circuit Refines the Standard for Calculating the Baseline of Payment History Between the Parties

Unsecured Creditors Comm. of Sparrer Sausage Co. v. Jason's Foods, Inc., No. 15-2356, 2016 U.S. App. LEXIS 10569 (7th Cir. June 10, 2016)

Debtor Sparrer Sausage manufactures sausage products. **Defendant Jason's Foods**, a wholesale meat supplier provided unprocessed meat products to the Debtor. During the relevant 90-day period, Sparrer paid 23 invoices to Jason's, totaling nearly $590,000, which Sparrer's creditors' committee (exercising trustee avoidance powers) sought to recover. Conceding that the payments were otherwise avoidable preferences, Jason's asserted that the payments had been made in the ordinary course of business between it and Sparrer.

The Bankruptcy Court determined that during the historical period, Sparrer generally paid invoices from Jason's within 16 to 28 days and that 12 of the 23 invoices in the preference period, totaling about $280,000, were ordinary and unavoidable because they fell within that range. The remaining 11 invoices, totaling nearly $310,000, were not made in the ordinary course because they were made either too early (14 days) or too late (29, 31, 37, and 38 days) after the invoice date. The District Court affirmed the bankruptcy court's decision. **On further appeal to the Seventh Circuit, Jason's challenged the bankruptcy court's determination that Sparrer typically paid invoices within 16 to 28 days**. The Defendant argued that bankruptcy court's calculation of 16 to 28 days range for the baseline period was too-narrow and it did not accurately reflect the companies' payment practices during that period.

The Seventh Circuit stated that the bankruptcy courts typically calculate the baseline payment practice between a creditor and debtor either by way of average-lateness method or the total-range method. In the case at bar, the bankruptcy judge used average lateness method (determining the average invoice date and adding some time to it in both directions) and his decision to use that method was within his discretion and there was no reason to disturb that. However, the Court pointed out that the problem was with the application of the method. **The Seventh Circuit concluded that the bankruptcy judge did not apply the average lateness method appropriately and that the application was "flawed."**

The Court found that the bankruptcy court erroneously applied *Quebecor World* and its so-called bucketing analysis to arrive at 16 to 28 days baseline period. It calculated the average invoice age during the historical period (22 days) and added 6 days on both sides of that average to arrive at 16 to 28 days range. However, neither the facts nor the bankruptcy court's analysis in that case had any resemblance to this case.

In re *Quebecor World*, the average invoice age during the historical period was 27.56 days, while the average invoice age during the preference period was 57.16 days - a difference of nearly 30 days. Given such a stark disparity, the bankruptcy court grouped historical-period invoices in buckets by age. That analysis revealed that the debtor paid 88% of invoices during the historical period within 11 to 40 days after the invoice date. Expanding this range by five days on the high end, the court determined that any invoices paid more than 45 days after the invoice date were outside the ordinary course.

However, in the case at bar, 16-to-28-day baseline range encompassed just 64% of the invoices that Sparrer paid during the historical period and the judge offered no explanation for the narrowness of this range. Thus, **the Seventh Circuit questioned the basis on which the bankruptcy court excluded the invoices that Sparrer paid within 14 days or 29 days when these payments were among the most common during the historical period. The Court expanded the baseline period and stated that by indeed adding just two days to either end of the range, the analysis would capture 88% of the invoices paid during the historical period, a percentage much more in line with the *Quebecor World* analysis. Thus, a 16-to-28-day baseline appeared not only excessively narrow but also arbitrary.**

Accordingly, the Seventh Circuit applied the broader range of baseline period and found that Sparrer paid 9 of the 11 alleged invoices within 14, 29, and 31 days of issuance and only two invoices were outside the 14-to-30 day expanded baseline. This limited Jason's preference liability to just $60,679.00. Jason's had also supplied new value worth $63,514.00 to Sparrer and Jason's was entitled to a reduction of its preference liability in this amount. After the revised analysis, the new value that Jason's supplied to Sparrer ($63,514.00) exceeded its remaining preference liability ($60,679.00). **Thus, the preference liability was entirely offset and the Committee was not entitled to recover anything from Jason's**.

Puerto Rico Court Ruled for Defendant as Trustee's Complaint Fails to Meet Plausibility Standards or State Sufficient Factual Information

In re Editorial Flash, Nos. 13-08014 BKT, 14-00224 BKT, 2016 Bankr. LEXIS 2435 (U.S. Bankr. D.P.R. June 29, 2016)

Defendant Heriberto Olavarria was an employee of Debtor Editorial Flash, Inc. The Debtor made certain transfers in amount of $11,751.60 to the Defendant during the period of January 13, 2012 and December 15, 2012. The Debtor filed a Chapter 7 petition on September 28, 2013. The Trustee brought an adversary proceeding against the Defendant, alleging fraudulent transfer, pursuant 11 U.S.C. § 548 or, in the alternative, preferential transfer, pursuant 11 U.S.C. § 547, alleging that the Debtor made a transfer of funds to the Defendant while he was his accountant. The Trustee merely stated language of §§ 548 and 547, without providing any supporting facts as to each element of the specific claims, to allege that the transfer of funds were either a fraudulent or a preferential transfer. The Defendant moved for the dismissal of the claim on grounds of failure to state a claim upon which relief can be granted, pursuant Fed. R. Bank. P. 7012(b). The Defendant admitted that he received the alleged payment from the Debtor, but clarified that the said amount of money was provided to him as monthly salary payments for rendering services related to graphic design. Furthermore, the Defendant elucidated that he was employed by the Debtor as a graphic designer and not as an accountant. However, in an attempt to prove the Defendant's insider status, the Trustee asserted that the Defendant received the alleged transfer in controversy while being the Debtor's accountant.

On preference argument, the Court found that although the transfer at issue occurred within the reach-back period contained in § 547(b)(4)(B) i.e. one year in case of insiders, **the Trustee failed to provide evidence as to the closeness of the relationship between the Defendant and the Debtor. The Trustee did not provide any evidence as to whether the transaction between the Defendant and the Debtor was conducted at arm's length. The Court said that the only alleged fact that the Defendant was the Debtor's accountant, when he received the transfer, was not sufficient to determine the Defendant's insider status**. The Court thus, concluded that the Trustee neither provided sufficient facts as to the elements the cause of action nor stated a claim to relief that was plausible on its face. Thus, the alleged transfer was not preferential pursuant to Sec. 547 (b).

On the next argument, the Court emphasized that the onus to show that the purpose of the alleged transfer was to hinder, delay or defraud creditors is on the party alleging actual fraud or it could be

inferred from the badges of fraud on circumstantial evidence. . **However, in the case at bar, the Trustee did not provide any facts or evidence to show that the transfer was made to prevent creditors from obtaining what was rightfully theirs or to prove the Debtor's intent to hinder, delay or defraud any creditor.** The Trustee cannot meet § 548 burden of proof by merely alleging that the Defendant was the Debtor's accountant at the moment the transfer took place; the transfer was for the amount of $11,751.60; and the transfer occurred within one year of the fling the bankruptcy petition. There has to be substantial evidence to prove that there was indeed a fraudulent intent.

The Court held that since the Trustee failed to provide any facts or the indicia or badges of fraud from where fraudulent intent could be inferred, the alleged transfer cannot be held as a fraudulent and the Trustee has failed to state a claim upon which relief can be granted under § 548(a)(1)(A).

Utah Court Did Not Allow a Creditor to Retain the Funds He Invested With a Non-Debtor in a Ponzi Scheme, Even When the Non-Debtor was Operating the Debtor's Ponzi Scheme

Gillman v. Russell (In re Twin Peaks Fin. Servs.) No. 2:15-cv-00167-DN, 2016 U.S. Dist. LEXIS 73550 (D. Utah June 6, 2016)

Debtor Twin Peaks Financial Services, Inc. and MNK Investments, a real estate development company was allegedly operated by Kenneth C. Tebbs. Defendant Christopher Russell was introduced to Tebbs who represented himself as the owner and principal of the Debtor. In reality, Tebbs operated the Debtor as a Ponzi scheme. In reliance on Tebbs' representations and assurances, Russell provided a significant amount of short term financing to the Debtor and/or Tebb and also received returns from the Debtor later on. The Defendant provided transfers to the Debtor totaling $520,000.00.

In return for the $520,000.00 total investment, Russell was paid a total of $961,008.97 by the Debtor, thus allowing him to receive $441,008.97 more than he had invested with the Debtor. A year later, involuntary Chapter 11 petitions were filed and the Court entered an order for substantively consolidation all of the Debtor’s cases. However, Tebbs case was not consolidated with the Debtor’s other cases. The Trustee brought an adversary proceeding against Russell alleging that the funds Russell received were fraudulent transfers pursuant to Sec. 548. **The Bankruptcy Court ruled that the excess of funds specifically deposited directly into the Debtor's account (totaling $441,008.97) constituted Ponzi scheme profits and were therefore avoidable as fraudulent transfers.**

Russell argued that the transfers were not made with the subjective intent to hinder, delay, and defraud creditors; that the Debtor was part of Tebb's fraudulent scheme and that Russell had a fraud claim against the Debtor and all payments that he received from the Debtor was received for value under §548(c); that the bankruptcy court erred in only considering what he invested with the Debtor and disregarded his investments with Tebbs which totaled $1,725,635.48; and finally by separating and

isolating the Debtor from the broader Ponzi scheme, the bankruptcy court ignored the underlying public policy that allows for clawbacks.

The District Court concluded that the bankruptcy court did not err when it found that Russell received funds in excess of his undertaking. The Court pointed out that **Section 548(c) specifically limits the affirmative defense to the value given to the debtor**. In the present case, the Debtor was Twin Peaks Financial Services, Inc. and MNK Investments. **Although Russell invested with Tebbs in amount of $1,725,635.48 (apart from the amount he gave to the Debtor), this amount cannot be considered as principal investment with the Debtor as Tebbs had his own bankruptcy case which was not substantially consolidated into the Debtor's bankruptcy case.** The fact that Tebb's fraudulent scheme may have extended beyond the Debtor's business operations did not automatically permit the Court to ignore Tebbs's and the Debtor's separateness**.** The District Court also affirmed the determination of the lower court that the transfers were not given in exchange for satisfaction of the Defendant's alleged fraud claim. The Court said that the transfers were made pursuant to certain investment contracts promoted by the Debtor and not in exchange for satisfaction of his alleged fraud claim.

The Court concluded that **although Russell lost a significant amount of money through his investments with the Debtor and non-Debtor parties, Russell cannot be given credit for the value that he provided to the third parties**, because if he is allowed to keep the money he received from the Debtor in excess of his investments with the Debtor, then the money invested by other investors in the Debtor's Ponzi scheme will be used to compensate Russell for investment losses that he suffered with investments which he made with other entities that never benefitted the Debtor. This will be against the public policy behind clawback. **The District Court affirmed the ruling of the Bankruptcy Court in its entirety and ordered Russell to remit $441,008.97 as those were fraudulent transfers pursuant to 11 U.S.C. § 548.**

Issues of Material Fact Prevented the Court From Entering Summary Judgment in Favor of Debtor

Correa v. P.R. Treasury Dep't (In re Correa) Nos. 13-02615 (EAG), 15-00075, 2016 Bankr. LEXIS 2383 (U.S. Bankr. D.P.R. June 24, 2016)

Debtors Julio Antonio Torres Correa, Amparo Colon Gonzalez brought a complaint against the Defendant Puerto Rico Treasury Department to avoid a preferential transfer of funds garnished pre-petition by the Defendant. On March 26, 2013, the Defendant sent the Debtors a notice of garnishment to secure the collection of outstanding tax debts. On the same day, the Defendant sent another notice of garnishment, informing that by order of the Treasury Department the amount of $6,010.02 was being garnished from their bank account. The day after, on March 27, 2013, Treasury made a partial release of the preventive garnished funds in favor of the Debtors in the amount of $800.00. On April 5, 2013, the Debtors filed a voluntary petition under chapter 13 of the Bankruptcy Code.

The Debtors (Plaintiff) brought an action against the Defendant alleging that they had an interest in property, namely $6,010.02 in their bank account. The Debtors argued that the garnished funds complied with the definition of transfer; garnishment was made for the benefit of the Defendant and on account of an antecedent tax debt; was made within 90 days before the filing of the petition; the transfer was presumed to have occurred while the Debtors were insolvent by operation of §547(f), since it occurred within 90 days before the filing of the petition and finally the garnishment enabled the Defendant to receive the totality of the $6,010.02 in the Debtor's bank account, instead of having to receive just a portion of these funds. Thus, all the elements of an avoidance action were present in the case and hence the alleged transfer was avoidable as preference under Sec. 547 (b). The Defendant alleged that there existed genuine issues of material facts and the Debtors/Plaintiffs were not entitled to judgment as a matter of law.

The Court found that the Debtors filed voluntary petition for relief under Chapter 13 on April 5, 2013. For the transfer to fall within the preferential period under section 547, the transfer had to be made on or after January 5, 2013. Although, the uncontested facts established that the alleged garnishment was made on March 26, 2013 and was made for the benefit of the Defendant and on account of an antecedent tax debt owed by the Debtors, **the Court held that there existed issues of material fact that prevent the court from entering summary judgment in the Debtor's favor. The Court reasoned that the Debtors' standing for an avoidance action under section 547(b) is subject to the provisions of section 522(h).** Section 522(h) allows the debtor to utilize the trustee's traditional avoiding powers, but again only to the extent the property would be exempt, the trustee has not acted to avoid the transfer, and the transfer was involuntary.

However, in the case at bar, the Court found that the Debtors failed to meet their burden to show that there was no genuine issue of material fact that warranted the entry of summary judgment. While Puerto Rico law allowed for the exemption of three-fourths of the earnings of a judgment debtor for personal services rendered at any time within thirty days next preceding the levy of execution, the Debtors in the present case did not put the court in a position to determine whether the garnished funds by the Defendant could have been exempted under state law. Further, there was also an issue of fact as to the actual amount that was garnished by the Defendant. The Court denied the Debtors' motion for summary judgment.

Snapshot of Clawback Cases Filed

Groups of Adversary Proceedings filed by the Debtors	Total cases filed	Name of Judge	Largest Case in the group	Claim Amount of the Largest Case	Petition Date	District
Kid Brands, Inc.	82	Michael B. Kaplan	Beene Garter LLP	$1,825,669.89	6/18/2014	District of New Jersey
Lamar Construction Company	72	James W. Boyd	Quality Air Heating & Cooling, Inc.	$544,139.40	7/11/2014	Western District of Michigan

Pretty Girl, Inc.	67	Sean H. Lane	Victor Lavy	$499,916.66	7/2/2014	Southern District of New York
New Century Transportation, Inc.	44	Michael B. Kaplan	Comdata Inc.	$1,673,440.24	6/11/2014	District of New Jersey
Licking River Mining, LLC	41	Tracey N. Wise	Wrigley's 7-711, Inc.	$2,104,620.65	5/22/2014	Eastern District of Kentucky
Palm Drive Health Care District	32	Alan Jaroslovsky	Western Health Advantage	$299,920.80	4/7/2014	Northern District of California
Gas-Mart USA, Inc.	20	Arthur B. Federman	Kansas City Power & Light Company	$95,063.89	7/2/2015	Western District of Missouri
The Adoni Group, Inc.	18	Mary Kay Vyskocil	Express Trade Capital, Inc.	$188,994.33	6/19/2014	Southern District of New York
D.I.T., Inc.	17	Erik P. Kimball	Select Portfolio Servicing, Inc.	$464,364.24	6/6/2014	Southern District of Florida
Oak Rock Financial, LLC	13	Robert E. Grossman	na	na	4/29/2013	Eastern District of New York

BIO

About Roland Jones

Mr. Jones has practiced bankruptcy law for over two decades. His primary focus is representing corporate defendants in preference and fraudulent conveyance litigation. Mr. Jones has a national client base and has also represented corporate clients based in Europe and the Far East.

In addition to his law practice, Mr. Jones has authored professional articles on bankruptcy issues for the *New York Law Journal*, *The Environmental Claims Journal*, *The Mergers and Acquisitions Report*, and other scholarly publications.

Mr. Jones also edits and writes the ***Clawback Report***, a monthly publication on preference and fraudulent conveyance litigation.

Mr. Jones was the founding member and former Chair of the Federal Bar Association Empire State Chapter Bankruptcy Committee. The Bankruptcy Committee has hosted experts to speak on topics important to both bankruptcy and non-bankruptcy practitioners. Guest speakers have included The Honorable Jerrold Nadler on new bankruptcy legislation, Wilbur L. Ross, Jr. of Rothschild Inc. on the distressed bond market, and Professor Edward Altman of New York University on bankruptcy investing.

Mr. Jones is the founding member and current President of the National Association of Bankruptcy Litigators. The NABL is a new organization focusing exclusively on clawback issues consisting of 110 bankruptcy lawyers from throughout the country.

Mr. Jones' introduction to bankruptcy practice began by serving as a judicial law clerk to Chief U.S. Bankruptcy Judge Conrad B. Duberstein of the Eastern District of New York during law school. He continued his training after graduation by clerking for U.S. Bankruptcy Judge Cecilia H. Goetz of the Eastern District of New York from 1990 to 1991.

Mr. Jones attended the Horace Mann School, Columbia University (B.A. Ancient Studies) and Brooklyn Law School (J.D. 1990) He is admitted to practice law before the United States District Courts for the Southern and Eastern Districts of New York, as well as the United States Court of Appeals for the Second Circuit.

Mr. Jones was born in New York City.

Bar Admissions
New York State Bar Admission - 1990

United States District Court Southern District of New York - 1991
United States District Court Eastern District of New York - 1991

Professional Memberships
President: National Association of Bankruptcy Litigators
Member: New York State Bar Association
Member: Association of Bar City of New York
Member: Turnaround Management Association
Member: American Bankruptcy Institute

Education
1972 – 1977: The Horace Mann School
1977 – 1979: Vassar College
1985 – 1987: Columbia University; top 10% of the graduating class
1988 – 1990: Brooklyn Law School; top 10% of the graduating class

Writings
"Are repos exempt from automatic stay?"; Bankruptcy Law - New York Law Journal; Pg. 31, (col. 6); Vol. 213, 2586 words

"Bankruptcy's conflict of Interest Rule"; Outside Counsel - New York Law Journal; Pg. 35, (col. 3); Vol. 212, 2117 words

"Bankruptcy and Environmental Law", The Environmental Claims Journal

"Mergers and Acquisitions in Bankruptcy", The Mergers and Acquisitions Report

The Clawback Report, A Quarterly Publication on Preference and Fraudulent Conveyance Litigation Issues.

"Introduction to Preference Law", National Association of Bankruptcy Litigators Journal

Bankruptcy Bulletin: "Wellness International Network, Ltd. v. Sharif, 135 S. Ct. 1932 (2015)", National Association of Bankruptcy Litigators Journal

Majority Report: "Redefining the Circuit Split Over the § 547(c)(4) Subsequent New Value Defense" by Roland Jones, Esq. and Solomon Rotstein, National Association of Bankruptcy Litigators Journal

Videos

Please feel free to watch our video, Basic Preference Law, on YouTube.

Below is a list of other clawback related videos that we have uploaded to YouTube. For an in-depth review of the preference laws, please see our five-part video series. CLE credit is currently available for New Jersey and Texas. We are expecting to be approved in more states shortly.

Introduction to the Bankruptcy Preference Laws - Part 1/5

Introduction to the Bankruptcy Preference Laws - Part 2/5

Introduction to the Bankruptcy Preference Laws - Part 3/5

Introduction to the Bankruptcy Preference Laws - Part 4/5

Introduction to the Bankruptcy Preference Laws - Part 5/5

For other videos on special topics regarding clawback law, please see the following:

Adversary Complaint – Who Bears the Burden of Proof of Service of Process?

Can Summary Judgment Be Granted If Factual Issues Exist?

Agriculture Preference Issues - Part 1

Agriculture Preference Issues - Part 2

Transfer of a Security Interest in Property During the Preference Period–Is it Preferential?

Preference Issues in the Construction Industry

Non-Filing of the Creditor's Claim Against the Debtor – How Does It Affect Court's Jurisdiction?

Sudden Change In the Mode of Payment During the Preference Period-Is It Out of the Ordinary Course?

Is an Express Trust Constituted During the Preference Period Preferential?

The Preference Period Payments Match the Base Period Timing of Payments - Are they Preferential?

Payments Received By a Conduit During the Preference Period - Are they Preferential?

Change in the Scope of Work- Does the Industry Standard Defense Still Apply?

Internal E-mail Listing the Assets and Liabilities - Is It Sufficient To Prove Debtor's Insolvency?

Creation of a Judgment Lien - Is It a Preferential Transfer?

The Source of Preferential Payments - Is It Relevant To the Preference Analysis?

What Is the Purpose Behind the New Value Exception?

Baseline of Dealings For the Ordinary Course Defense - Who Bears the Burden To Establish It?