IN THE UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF ARKANSAS
FAYETTEVILLE DIVISION

IN RE: JON AND JUDY ZIMMER	**No. 5:09-bk-74621** **[Consolidated case]**
BATH JUNKIE, INC., Debtor	**No. 5:09-bk-74992** **Ch. 11**
BATH JUNKIE, INC.	**PLAINTIFF**
vs.	**No. 5:09-ap-7212**
BATH JUNKIE BRANSON L.L.C. and GLORIA R. ARNEY	**DEFENDANTS**

ORDER

Before the Court is the Complaint to Avoid Preferential Transfer filed by the debtor, Bath Junkie, Inc. (Bath Junkie) on November 30, 2009, and the Answer to Complaint to Avoid Preferential Transfer filed by the defendants, Bath Junkie Branson, LLC, and Gloria Arney (Bath Junkie Branson) on December 17, 2009. 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 opinion constitutes findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052. For the reasons stated below, the Court grants Bath Junkie's Complaint to Avoid Preferential Transfer.

Background

Bath Junkie Branson obtained a judgment against Bath Junkie in the United States District Court for the Western District of Missouri on August 1, 2007, and registered the judgment in the United States District Court for the Western District of Arkansas on May 8, 2008. (Pl's. Ex. 1.) On September 9, 2009, Bath Junkie Branson obtained and served a Writ of Garnishment on the Bank of Fayetteville related to the Missouri judgment. (Pl's. Ex. 2.) Two days later, on September 11, 2009, Bath Junkie Branson obtained and

served additional Writs of Garnishment on Arvest Bank and Metropolitan National Bank, also related to the Missouri judgment. (Pl's. Ex. 2.) Bath Junkie filed its bankruptcy petition on October 1, 2009.

The transfer at issue is the lien that arose as a result of Bath Junkie Branson's writ of garnishment and subsequent execution lien that it obtained on Bath Junkie's Bank of Fayetteville account, elevating Bath Junkie Branson to the status of a secured creditor of Bath Junkie. *See, e.g., In re Klingbeil*, 119 B.R. 178, 181-82 (Bankr. D. Minn. 1990) ("the combination of the fixing and/or perfection of a garnishment lien on all wages earned during that period, and the levy on the garnished wages, enabled [the creditor] to advance its position in contravention of the policy of equality of treatment which underlies 11 U.S.C. § 547"). According to the debtor's schedules, at the time the debtor filed its bankruptcy case, the debtor had a Bank of Fayetteville "gift card" account with a balance of $92,252.60 and a payroll and operating account balance with a balance of $3711.34.[1] (Pl's. Ex. 3.)

11 U.S.C. § 547--Preferences

Generally

Under § 547 of the bankruptcy code, a trustee, or a debtor in possession in a chapter 11 case,[2] may avoid any transfer of an interest of the debtor in property if five elements are met. According to § 547(b),

> any prepetition transfer is preferential and avoidable if five elements of

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[1] The liens that attached to the funds in the Arvest Bank account and Metropolitan National Bank account were not in issue, presumably because the aggregate value of each transfer was less than the preference amount for a non-consumer debt: $5475. *See* 11 U.S.C. § 547(c)(9). Although the gift card account is the primary account at issue, the "aggregate value" of the transfer relating to the Bank of Fayetteville would include the payroll account, even though the payroll and operating account balance is below the amount not subject to a preference under § 547(c)(9).

[2] Section 547(b) makes certain transactions voidable by the trustee. Section 1107(a) gives the debtor in possession the powers of a trustee.

> proof are present. The transfer must be made (1) to or for the benefit of a creditor; (2) for or on account of antecedent debt; (3) while the debtor was insolvent; (4) to a noninsider on or within ninety days of the filing of the bankruptcy case; and such transfer must (5) result in the creditor receiving more than the creditor would have received in a hypothetical liquidation in a chapter 7 case.

Wade v. Midwest Acceptance Corp. (*In re Wade*), 219 B.R. 815, 818-19 (B.A.P. 8th Cir. 1998). The purpose of § 547 is "to discourage creditors from racing to dismember a debtor sliding into bankruptcy and to promote equality of distribution to creditors in bankruptcy." *Jones Truck Lines, Inc. v. Central States, Southeast and Southwest Areas Pension Fund* (*In re Jones Truck Lines, Inc.* [II]), 130 F.3d 323, 326 (8th Cir. 1997). Aided by a rebuttable presumption of insolvency under § 547(f), the debtor in possession has the burden of proof regarding these elements. 11 U.S.C. § 547(g).

The code also lists nine specific defenses to a preference, the occurrence of any of which would prevent the trustee or debtor in possession from avoiding the transfer. 11 U.S.C. § 547(c). Bath Junkie Branson did not identify clearly any of the specific affirmative defenses with regard to the funds held by the Bank of Fayetteville. It relied, instead, upon the debtor's ability to prove the elements of a preference.

Transfer of an Interest

Before looking at the required elements of a preferential transfer, a threshold determination must be made with regard to a transfer of an interest of the debtor. At an earlier relief from stay hearing, Bath Junkie argued that the funds in the Bank of Fayetteville that relate to the gift cards were held in trust for the benefit of the gift card recipients and, accordingly, the account was not property of the estate. If true, Bath Junkie would not have a beneficial interest in the account and the funds (arguably) would not belong to Bath Junkie. In other words, the transfer would not be "of an interest of the debtor" and would not be a preference.

However, on September 9, 2009, when the lien attached and the transfer was made, the

funds were in a simple checking account belonging to Bath Junkie and were subject to execution liens in favor of Bath Junkie Branson. Bath Junkie filed its bankruptcy petition on October 1, 2009. The Court did not impose an implied trust on the funds held by the Bank of Fayetteville until December 3, 2009, when it found and stated unequivocally on the record that the Bank of Fayetteville gift card account was not a trust account; rather, it was a checking account set up as a "pooling" account for the purpose of tracking the gift card transactions. Because the gift card account was in the name of Bath Junkie at the time the petition was filed, and not held in trust until the Court imposed an implied trust post-petition, the Court finds that the Bank of Fayetteville accounts were interests of the debtor in property as required by § 547.

To a Creditor For an Antecedent Debt

Most of the required elements for a preference are not in dispute. Bath Junkie Branson was a creditor of the debtor and received a judgment against Bath Junkie on August 1, 2007. A debt is antecedent for preference purposes if the debt "was incurred before the allegedly preferential transfer." *Jones Truck Lines, Inc. [II]*, 130 F.3d at 329. In this case, there is no dispute that the debt to which the transfer applied was incurred prior to the transfer.

While the Debtor was Insolvent

The transfer must have been made while the debtor was insolvent. Although the debtor in possession has the burden of proof as to the elements of a preference, there is a presumption that the debtor was insolvent "on and during the 90 days immediately preceding the date of the filing of the petition." 11 U.S.C. § 547(f). That presumption shifts the burden of producing at least some evidence that the debtor was solvent to the creditor. *Armstrong v. John Deere Co.*, (*In re Gilbertson*), 90 B.R. 1006, 1009 (Bankr. D.N.D. 1988) ("When the creditor offers no evidence at all as to the debtor's solvency, the trustee may rely on the presumption . . . ."). Because Bath Junkie Branson did not present any evidence that the debtor was solvent, it failed in its burden of production, and the Court finds that the debtor was insolvent at the time of the transfer.

During the Preferential Period

The preference period is "on or within 90 days before the date of the filing of the petition." 11 U.S.C. § 547(b)(4)(A). The alleged preferential transfer occurred on September 9, 2009, the date the writ of garnishment was served on the Bank of Fayetteville. The debtor filed its petition on October 1, 2009, 22 days later, within the 90 day preferential period.

Enabling the Creditor to Receive More Than It Would Receive Under Chapter 7

The remaining issue for the Court is whether Bath Junkie Branson received more as a result of the transfer than it would have received in a hypothetical liquidation in a chapter 7 case. The law is generally well settled that unless creditors would receive a 100% payout, an unsecured creditor who received a payment during the preference period would receive more than it would have received in a chapter 7 liquidation. *Hoffinger Indus., Inc. v. Bunch* (*In re Hoffinger*), 313 B.R. 812, 827 (Bankr. E.D. Ark. 2004) (citing *RDM Holdings, Inc. v. DMAC Invs., Inc.* (*In re RDM Sports Group, Inc.*), 250 B.R. 805, 814 (Bankr. N.D. Ga. 2000); *see also Zachman Homes, Inc. v. Oredson* (*In re Zachman Homes, Inc.*), 40 B.R. 171, 173 (Bankr. D. Minn. 1984) (same).

As with the first four elements, the debtor has the burden of proof with regard to whether Bath Junkie Branson received more than it would have received under a chapter 7 liquidation. Insolvency is a "financial condition such that the sum of such entity's debts is greater than all of such entity's property, at fair valuation." 11 U.S.C. § 101(32). Based on this definition, and recognizing a presumption of insolvency, because an insolvent debtor's debts exceed its assets, it is not possible for all creditors to receive a distribution equaling a 100% payout. As a result, an unsecured creditor that received a transfer during the preferential period, such as Bath Junkie Branson, potentially would have received more than it would have received under a chapter 7 liquidation. In the Fayetteville Division of the Western District of Arkansas, if a debtor is insolvent and the transfer diminishes the debtor's estate, then even in the absence of any evidence to

support the fifth element, as a matter of law, any distribution to an otherwise unsecured creditor would result in the creditor receiving more than it would in a chapter 7 liquidation had the transfer not occurred. *Betty's Homes, Inc. v. Cooper Homes, Inc.*, 411 B.R. 626, 630 (W.D. Ark. 2009).

According to the debtor's amended schedules, which were introduced as Plaintiff's Exhibit 3, the debtor has general unsecured claims in the amount of $486,137.59, assets in the amount of $736,181.72, and secured claims and priority claims in the amount of $568,403.40 (which includes Bath Junkie Branson in the amount of $95,000.00). This results in a payout to unsecured creditors of approximately 35%.[3] According to the debtor's liquidation analysis contained in its disclosure statement, unsecured creditors would receive a payout of approximately 29% under the debtor's plan of reorganization. Because under any scenario creditors would not receive a 100% payout, the Court finds that the transfer did allow Bath Junkie Branson to receive more than it would have received in a chapter 7 liquidation.

Accordingly, the Court finds that Bath Junkie has satisfied its burden of proof and that the attachment of the execution lien as a result of the garnishment action on the Bank of Fayetteville was a preference under the bankruptcy code. Therefore, the Court orders that the transfer be avoided and finds that Bath Junkie Branson is an unsecured creditor in the debtor's case.

IT IS SO ORDERED.

June 10, 2010
DATE

Ben Barry
BEN T. BARRY
UNITED STATES BANKRUPTCY JUDGE

[3] When Bath Junkie Branson is treated as an unsecured creditor, the payout to unsecured creditors increases to approximately 45%.

cc: David G. Nixon, attorney for Bath Junkie, Inc.
Seth M. Haines, attorney for Bath Junkie Branson L.L.C. and Gloria R. Arney