

**UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF COLORADO
Honorable Howard R. Tallman**

In re:)	
)	
KEITH ALAN JONES,)	Case No. 02-12799 DEC
)	
Debtor.)	Chapter 7
_____)	
)	
JON S. NICHOLLS, as Chapter 7 Trustee)	
for the Estate of Keith Alan Jones,)	
)	
Plaintiff,)	Adversary No. 03-1203 HRT
)	
v.)	
)	
GLADYS L. JONES, a/k/a Pinky Jones)	
)	
Defendant.)	
_____)	

ORDER

This case comes before the Court on Plaintiff's Complaint to Avoid Preferential Transfer and for Judgment. The matter was tried to the Court on January 26, 2004. The Court has reviewed the case file along with the evidence and arguments of the parties and is ready to make its ruling.

Factual Background

In this matter, the Court is presented with a fact situation which is somewhat different than the usual preference case. The Defendant, Gladys (Pinky) Jones, is not a commercial creditor, but is the Debtor's mother. Defendant lives at an assisted living facility. She has been diagnosed with heart disease, Parkinson's, Alzheimer's dementia, and depression. Debtor, Keith Alan Jones, is Defendant's only child and, as such, is the person responsible for her care and handles her financial affairs. Debtor holds a general power of attorney for the Defendant. Trustee seeks to avoid two transfers from Debtor to Defendant which total \$16,000.00 and occurred within a year of Debtor's petition date.

The Debtor filed his bankruptcy petition on March 6, 2002. Mr. Jones revealed on his Statement of Financial Affairs that he had made two transfers to the Defendant. He shows that a payment in the amount of \$6,000.00 was made on September 6, 2001, (181 days pre-petition). Another payment in the amount of \$10,000.00 was made on October 17, 2001, (140 days pre-petition). On Schedule F, Debtor schedules a debt to the Defendant in the amount of \$154,196.00

and identifies that debt as a loan made in 2001. According to Debtor's testimony, this loan consisted of various advances for the purpose of acquiring a business and to cover some of the business' expenses.

In June of 2001, Defendant began living at an assisted living facility. On August 9, 2001, Debtor received notification, in his capacity as "Attorney-in-Fact For Gladys Jones," that the Defendant's claim for Assisted Care Facility Benefits had been approved and that benefits would become payable as of September 19, 2001. On October 9, 2001, Debtor received and deposited into his personal bank account a check made out to "Keith Jones as attorney in fact for Gladys Jones." The check was issued by G.E. Capital Assurance in the amount of \$19,526.00. The check was designated as covering "Home Care" from December 1, 2000, through June 8, 2001, and "Assisted Care Facility" from June 11, 2001, through August 31, 2001.

Motion for Discovery Sanctions

As an initial matter the Court must dispose of Plaintiff's FED. R. CIV. P. 37(b)(1), (2) Motion for Sanctions. Plaintiff filed the motion on September 17, 2003, requesting sanctions against Defendant for failure to make herself available for a deposition by the Plaintiff. By an order dated August 25, 2003, this Court had previously directed Defendant to provide responses to discovery requests and to appear for deposition. Plaintiff requested that a default judgment be entered as a sanction with respect to Defendant's failure to comply with the Court's order directing her to appear for a deposition. On October 10, 2003, Plaintiff filed a motion requesting that the sanctions matter be held in abeyance because the Defendant's counsel had provided Trustee with additional pertinent information. On October 14, 2003, the Court so ordered.

Defendant did not appear at trial and counsel for Defendant offered, without objection, Defendant's Exhibit I, an affidavit and letter from a Dr. Jeff Glaves, Defendant's attending physician, who attested to his review of Defendant's medical file. He reviewed chart records from 1998 forward and described the progress of Defendant's treatment from that time to the present. Dr. Glaves concluded:

Ms. Jones has multiple medical problems: Heart disease, Parkinson's, dementia, and depression. She has been thoroughly evaluated on multiple occasions and found to be in need of assistance for even basic tasks. It is therefore my opinion that she is unable to testify on her own behalf and, further, that any attempt to depose her would result in undue stress for her and, possibly, worsen her condition.

In light of the uncontroverted evidence presented by Defendant's counsel, the Court finds that the potential for harm to the Defendant and aggravation of her medical condition outweighs any potential probative value that her testimony may have had in this proceeding. The Court will, therefore, deny Plaintiff's motion for sanctions.

Discussion

The Trustee filed this preference action under 11 U.S.C. § 547 on March 17, 2003, and seeks to avoid the transfers made on September 6, 2001, and October 17, 2001. Under § 547, the Trustee may avoid a transfer of “an interest of the debtor in property” if such transfer is:

- (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; or
 - (B) between ninety days and one year before the date of the filing of the petition, if such creditor at the time of such transfer was an insider; and
- (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.

11 U.S.C. § 547(b). “All elements of Section 547(b) must be proven before a transfer will be avoided. The absence of any one of the elements constituting a voidable preference negates the trustee’s claim.” *Gillman v. Scientific Research Products, Inc. (In re Mama D’Angelo, Inc.)*, 55 F.3d 552, 554 (10th Cir. 1995).

It is clearly established by the record before the Court that the Defendant is a creditor of the Debtor and that § 547(b)(1) is satisfied. Also, § 547(b)(4)(B) is satisfied because Defendant is an insider as that term is defined in § 101(31) and the record shows that the subject transfers took place within one year prior to the filing of Debtor’s bankruptcy petition.

Under § 547(b)(2), the Trustee is required to prove that the payments were made on account of an antecedent debt. The typical preference case involves a commercial debtor/creditor relationship. In that context, the issue of whether a payment is on account of a pre-existing debt is rarely subject to much controversy. This case involves Debtor’s mother who is a creditor on account of loans made to the Debtor to acquire a business and then to support the business as it struggled to remain viable. But, Debtor also holds power of attorney for his mother and he receives funds from the Defendant’s insurance company that are directed to him in his capacity as

the Defendant's attorney in fact.¹ Mr. Jones, therefore, not only owes obligations to Defendant as her debtor, he also owes her obligations as her fiduciary. There is also the filial obligation that sons feel toward their mothers to varying degrees.²

The Trustee testified that he had determined that the payments in question were on account of an antecedent debt based upon the wording of item number 3b in the Debtor's Amended Statement of Financial Affairs. That question and the debtor's response appear on the form substantially as follows:

List all payments made within one year immediately preceding the commencement of this case to or for the benefit of creditors who are or were insiders. (Married debtors filing under chapter 12 or chapter 13 must include payments by either or both spouses whether or not a joint petition is filed, unless the spouses are separated and a joint petition is not filed.)

Name and Address of Creditor and Relationship to Debtor	Date of Payment	Amount Paid	Amount Still Owing
Pinky Jones Debtor's mother	9/6/2001: \$6,000 10/17/2001: \$10,000	16,000.00	154,196.00

Trustee's testimony was to the effect that the entry in "amount still owing" must be the amount owed to the creditor after the payments were made and that those payments must relate to the debt reflected in the "amount still owing" column. Of course, that interpretation assumes precisely what Trustee is trying to prove – that the payment is on account of the antecedent debt. The Court finds nothing in the wording of that question that can justify making that assumption. The Trustee's interpretation of the question and response may well be a natural interpretation in the

¹ Debtor testified that the first such payment, in the amount of \$19,526.00, was deposited into his personal bank account and that subsequent payments were deposited directly into the Defendant's bank account. Those subsequent payments have no role in the current controversy.

² Much of the evidence presented by the Trustee went to the character of the Debtor and called into question the transactions entered into between Mr. Jones and his mother. In particular, the Trustee called into question Mr. Jones' testimony that his mother was lucid as could be when it came to loaning him money for his business ventures and allowing him to cash in one of her IRA accounts so that he could make payroll. Yet her multiple medical problems utterly prevent her from offering useful testimony in this proceeding. There may well be other contexts in which such evidence would be of considerable interest to the Court. It is certainly fair to question the quality of Mr. Jones' services to his mother as her fiduciary. Because this was a trial to the Court and not to a jury, some of that evidence was admitted over the Defendant's objections even though it stretched the bounds of relevance. The Court has taken that evidence into account in assessing the credibility of Mr. Jones as a witness in this proceeding, while in large measure discounting the relevance of that type of evidence as to Trustee's case against the Mrs. Jones, the actual Defendant.

context of the usual, one-dimensional, commercial debtor/creditor relationship, but Defendant's evidence rebuts that interpretation.

Debtor's testimony was that the total original debt owed to the Defendant was \$154,196.00 and that he made no deduction from that amount in answering the question as to the "amount still owing" because the payments were unrelated to the antecedent debt. Instead, Debtor claims that the payments relate to insurance benefits, which his mother was approved for and later received, and to the need to pay her expenses. The documentary evidence is consistent with that explanation. Debtor claims that he advanced \$6,000.00 to Defendant after being notified that insurance benefits would be paid so that his mother would have funds in her account to pay current expenses. The evidence shows that the \$6,000.00 payment was made less than a month after he received notice that benefits would be payable and just over a month before the first benefit payment was received. The \$10,000.00 payment was made shortly after the first insurance payment was received by the Debtor and deposited into his personal bank account.

The court finds, by a preponderance of the evidence presented, that the payments made by Debtor to his mother were not payments made on account of the antecedent debt incurred as loans for the Debtor's business, but were related to the anticipated insurance benefit payment and, later, the actual receipt of that payment. Therefore, Trustee has not met his burden as to § 547(b)(2).

The Court also finds that Trustee has not met his burden under § 547(b)(3) to provide proof that Debtor was insolvent at the time of the transfers. The Code provides a rebuttable presumption that a debtor is insolvent during the 90 day period preceding the petition date. 11 U.S.C. § 547(f). However, where a trustee chooses to proceed against an insider for an allegedly preferential transfer which took place outside of that 90 day presumption period, then he must prove, by a preponderance of the evidence, that the debtor was indeed insolvent on the date of the transfer. *Burdick v. Lee*, 256 B.R. 837, 841 (D. Mass. 2001); *Campbell v. Deans (In re J.R. Deans Co., Inc.)*, 249 B.R. 121, 136-37 (Bankr. D. S.C. 2000); *Beckman v. Christerson (In re CSI Enterprises, Inc.)*, 220 B.R. 687, 689 (Bankr. D. Colo. 1998).

In this case, the Trustee has submitted insufficient evidence from which the Court can conclude that Debtor was insolvent on September 6, 2001, and/or on October 17, 2001. The sole evidence relied upon by the Trustee was Debtor's bankruptcy schedules. The Court takes judicial notice of Debtor's schedules as requested by the Trustee. The Debtor's schedules show something in excess of \$2.7 million of unsecured debts; \$264,742.00 of secured debts; and \$498,492.00 of priority debts. Those debts are balanced against \$300,000.00 of real estate assets and \$10,250.00 of personal property assets. The Trustee points out that the Amended Statement of Financial Affairs shows that a vehicle belonging to Debtor's company, WMG, Inc., was repossessed in January of 2002 and that Debtor testified that the repossession followed about 3 months of missed payments. He also points to the fact that nine separate lawsuits are listed on Debtor's Amended Statement of Financial Affairs. Eight of those were pending at the time of Debtor's bankruptcy filing and one had been settled. As of March 6, 2003, Debtor's petition date, the Court has no difficulty finding that the Debtor was insolvent.

The gist of the Trustee's argument is that if Debtor was that insolvent on the petition date, then he must have been insolvent at the time of the transfers, some five to six months earlier. "Courts often utilize the well-established bankruptcy principles of 'retrojection' and 'projection,' which provide for the use of evidence of insolvency on a date before and after the preference date as competent evidence of the debtor's insolvency on the preference date." *In re Mama D'Angelo*, 55 F.3d at 554. But the Trustee has not given the Court any evidence of the Debtor's financial condition at any point in time other than the petition date.

In truth, neither party has presented the Court with substantial evidence with respect to the solvency issue. Defendant called the Debtor to the stand to rebut the Trustee's insolvency evidence and Debtor testified that he was solvent on the dates of the transfers. However, no documents were presented nor did Debtor explain in any detail how his fortunes reversed so rapidly during that six month period.

Nonetheless, because Trustee has not presented the Court with any evidence bearing on Debtor's financial condition at any point in time other than the petition date, the Court finds that the Trustee has failed to carry his burden of proof. The Court may well doubt that a man whose debts exceed his assets by approximately \$2 million on the petition date was financially healthy five or six months earlier. But such doubts cannot form the basis of a factual finding in this proceeding without at least some evidence of the Debtor's financial condition at some point closer in time to the dates of the transfers.

Trustee is also required to satisfy the element under § 547(b)(5) that the transfer allow the Defendant to receive more as a result of the payment than she would have gotten from a chapter 7 case if the transfer had never been made. Without the benefit of testimony or evidence as to this element, Trustee argues, based upon Debtor's schedules, that Defendant would have received nothing in a chapter 7 bankruptcy and that this element is satisfied because she did, in fact, receive \$16,000.00 in transfers.

What is obvious to the Trustee is less clear to the Court. The uncontroverted evidence before the Court is that Debtor received a check from G.E. Capital Assurance in the amount of \$19,526.00 on October 9, 2001. The check was made out to "Keith Jones as attorney in fact for Gladys Jones." It was deposited into Keith Jones' personal bank account. The Court is satisfied, from the evidence before it, that those funds were not the property of the Debtor. The equitable interest in those funds belonged to the Defendant. Had the transfer not been made and had those funds remained intact at the petition date, under § 541(d), only Debtor's legal title and not Defendant's equitable interest would have been part of the estate. Defendant would have been entitled to claim her property. The Court must find from a preponderance of the evidence that the transfers received by Defendant did not allow her to receive more than she would have received from a chapter 7 case if the transfers had never been made.

The Court has deferred to the end its discussion of what is really the first element of Trustee's cause of action. That is whether the transfers involved "an interest of the debtor in

property.” 11 U.S.C. § 547(b). This element brings into focus the policy objectives behind this preference section of the Code. Preferences are not recovered from transferees because the transferee has committed bad acts or was not entitled to the payment or transfer. Most preferences were simply payments of validly owed debts. But the policy behind recovering such transfers focuses on an act by the debtor taken while the debtor was insolvent and in close proximity to a bankruptcy filing. Recipients of such transfers are frequently quite innocent of wrongdoing, nonetheless, such transfers are recoverable because they have the effect of diminishing the debtor’s bankruptcy estate and evading the goal of an equitable distribution to creditors.

Accordingly, the focus of this element in particular and the preference section in general is whether or not the transfer resulted in a diminution of the debtor’s estate and a consequent reduction in property available to be distributed to creditors. *Continental & Commercial Trust & Sav. Bank v. Chicago Title & Trust Co.*, 229 U.S. 435, 443-44, 33 S.Ct. 829, 831 (1913) (“The fact that what was done worked to the benefit of the creditor, and in a sense gave him a preference, is not enough, unless the estate of the bankrupt was thereby diminished.”); *Genova v. Rivera Funeral Home (In re Castillo)*, 39 B.R. 45, 46 (Bankr. D. Colo. 1984) (“Cases subsequent to the Bankruptcy Code’s enactment have also held that for a preference to be voided it is essential that the debtor have an interest in the property transferred so that the estate is thereby diminished.”). If the transaction has not diminished the estate, then no policy is served by recovering the transfer.

The Court finds that when this series of related transactions are viewed as a whole, the bankruptcy estate has not been diminished by the payments made to the Defendant. To the contrary, when viewed as a whole, it is evident that Debtor deposited \$19,256.00 of the Defendant’s funds into his personal bank account and transferred only \$16,000.00 out to the Defendant. At worst, the Debtor broke even and he may have been enriched by \$3,256.00 after the series of transactions. It was Debtor’s testimony that, after his mother was approved for the assisted living benefits but before the arrival of the first benefit check, he transferred \$6,000.00 into her account for the payment of current expenses. After he received the \$19,256.00 benefit payment on her behalf, he transferred \$10,000.00 over to her bank account. Debtor explained that payment by noting that he recouped the earlier \$6,000.00 payment and that he kept the remaining \$3,256.00 as reimbursement for other expenses which he had borne on her behalf. Debtor made no effort to enumerate or document those latter expenses.³

Of course, when the Court views the individual transfers in isolation from one another, it is evident that the \$6,000.00 was property of the debtor at the time it was transferred because he had not received the insurance payment yet, even though it was anticipated. But as to the \$10,000.00 transfer, the evidence clearly establishes that sum was never the Debtor’s property. He held that

³ As the Court discussed in an earlier footnote, this lack of documentation with respect to those funds retained by the Debtor might be quite troubling in another type of case, but in the context of this preference action, that is not a matter that bears upon the issues in the Trustee’s cause of action.

amount for his mother as her “attorney in fact” pursuant to the general power of attorney. Debtor merely transferred to his mother what never belonged to him in the first place. Because the \$6,000.00 was transferred before actual receipt of the insurance benefits, the foregoing analysis of the remaining § 547(b) elements was necessary. That analysis satisfies the Court that these transfers are not of a type that meet the technical elements of the statute nor are they of a type that in any way implicate the policy rationale underpinning the statute.

In the Defendant’s brief and at trial, Defendant’s counsel made reference to the Debtor as a mere “conduit” of the funds meant for his mother. Trustee’s counsel cited the court to *Kaiser Steel Corp. v. Jacobs (In re Kaiser Steel Corp.)*, 105 B.R. 639, 649 (Bankr. D. Colo. 1989), *rev’d on other grounds*, 110 B.R. 514 (D. Colo. 1990), *aff’d*, *Kaiser Steel Corp. v. Charles Schwab & Co., Inc.*, 913 F.2d 846 (10th Cir. 1990), for the proposition that the “conduit theory” did not provide a defense in the context of this case. The Court quite agrees that the “conduit theory” is inapplicable to the facts of this case. Some courts use the term “conduit” to refer to an innocent third party who may receive funds or property from a debtor, but who merely holds it briefly for another and derives no benefit from the transfer. In those cases, the party who only acts as a “conduit” is not held liable under § 550 as a transferee. The case cited by counsel for the Trustee discusses and dismisses the concept of a “conduit” and prefers instead to analyze the matter under standard agency principles. *Id.*

In this case, the Court need not decide whether the “conduit theory” provides a viable defense. First of all, because it is the Debtor who received the insurance payment on behalf of the Defendant, the “conduit theory,” as typically set out in the cases, does not fit with the fact pattern of this case. But, more importantly, because the Trustee has not met his burden with respect to all of the elements of § 547, the Court does not reach the issue of affirmative defenses.

Because of the timing of the payments, The Court finds that the \$6,000.00 transfer was property of the Debtor at the time it was made. However, the Court cannot find that either of the payments which are the subject of this complaint were made on account of an antecedent debt (§ 547(b)(2)); that they were made while the Debtor was insolvent (§ 547(b)(3)); or that the payments allowed the Defendant to receive more than she would have received as a creditor in a chapter 7 case if the transfers had not been made (§ 547(b)(5)). The Court must, therefore, find in favor of the Defendant in this matter.

The Motion for Directed Verdict

At the end of Plaintiff’s evidence, Defendant made a motion for directed verdict. The Court took that motion under advisement and directed the Defense to proceed with its case in chief. “A trial court should direct a verdict only when the facts and inferences therefrom point so strongly in favor of one party that reasonable men could not come to a different conclusion.” *Wright v. American Home Assur. Co.*, 488 F.2d 361, 364 (10th Cir. 1973); *see, also, Hinds v. General Motors Corp.* 988 F.2d 1039, 1045 (10th Cir. 1993) (“Although a scintilla of evidence is not sufficient to justify submitting a case to the jury, a verdict may not be directed ‘if the evidence is such that a

reasonable jury could return a verdict for the nonmoving party.”) (quoting *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248, 106 S. Ct. 2505, 2510 (1986)).

The Defendant argues that Trustee presented no evidence as to the Debtor’s insolvency and that she is entitled to judgment as a matter of law on that basis. But Plaintiff/Trustee did ask the Court to take judicial notice of Debtor’s schedules during his case in chief. While that evidence is not ultimately strong enough to allow this Court to make a finding that the Debtor was insolvent on the dates of the transfers, the Court cannot say that reasonable men could not come to a different conclusion. Consequently, the Court will deny the motion for directed verdict.

In accord with the foregoing discussion, it is

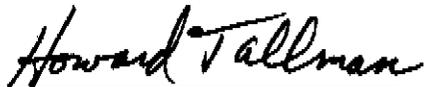
ORDERED that Plaintiff’s FED. R. CIV. P. 37(b)(1), (2) Motion for Sanctions is hereby DENIED; it is further

ORDERED that Defendant’s Motion for Directed Verdict is hereby DENIED; it is further

ORDERED that as to Plaintiff’s Complaint to Avoid Preferential Transfer and for Judgment, the Court finds in favor of the Defendant and against the Plaintiff. The relief requested in Plaintiff’s Complaint is hereby DENIED. The parties shall bear their own costs.

Dated this 5TH day of February, 2004.

BY THE COURT:



Howard R. Tallman, Judge
United States Bankruptcy Court