

**United States Bankruptcy Court
Northern District of Illinois
Eastern Division**

Transmittal Sheet for Opinions for Posting

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Bankruptcy Caption: In re marchFIRST, INC., et al

Bankruptcy No. 01 B 24742

Adversary Caption: Maxwell v. Begler

Adversary No. 03 A 241

Date of Issuance: July 20, 2007

Judge: Judge John D. Schwartz

Appearance of Counsel:

Attorney for Movant or Plaintiff: Steven S. Potts

Attorney for Respondent or Defendant: Thomas G. Griffin

Trustee or Other Attorneys: Trustee - Andrew J. Maxwell

**UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION**

In re:)	
marchFIRST, INC., et al,)	Case No. 01 B 24742
)	
Debtors.)	
)	Honorable John D. Schwartz
_____)	
)	
Andrew J. Maxwell, Trustee,)	Adv. No. 03 A 241
)	
Plaintiff,)	
)	
v.)	
)	
David Begler,)	
)	
Defendant.)	

MEMORANDUM OPINION

This matter comes before the court on an adversary complaint filed by plaintiff, Andrew J. Maxwell, as Trustee (“Trustee”) against debtor and defendant, David Begler (“Begler”). The complaint states causes of action for a judgment pursuant to §547(b) of Chapter 11 of 11 U.S.C. §§101, et seq. (“Bankruptcy Code”) avoiding certain transfers made to Begler by the debtor.

The complaint alleges that during the 90 days preceding the filing of the bankruptcy petitions on April 12, 2001 (“Petition Date”), marchFIRST, Inc. and its subsidiaries and affiliates (collectively “Debtor”) made transfers to Begler totaling \$36,300 (“Transfers”). Begler alleges in his answer that the Transfers were made in the ordinary course of business and that a later transaction provided subsequent new value to the Debtor which should offset any judgment

against him.¹

A trial was held on March 19, 2007. The parties were given ample opportunity to present their evidence. They also submitted post-trial briefs and responses to those briefs. Following are the court's findings of fact and conclusions of law. Judgment will be entered for the Trustee.

Findings of Fact

marchFIRST, Inc. and its subsidiaries and affiliates commenced their bankruptcy cases in the United States Bankruptcy Court for the District of Delaware by filing voluntary petitions for relief under the Bankruptcy Code on April 12, 2001. The Debtor moved to convert its cases to cases under Chapter 7 and on or about April 26, 2001, the Debtor's cases were converted to Chapter 7 cases pursuant to §1112 of the Bankruptcy Code. By order dated July 10, 2001, the Delaware Court transferred the Debtor's cases to the United States Bankruptcy Court for the Northern District of Illinois. Andrew J. Maxwell was appointed to serve as the Chapter 7 Trustee, qualified and has been acting as such.

The Trustee commenced this adversary proceeding by filing his complaint on February 3, 2003. Begler filed his answer and affirmative defenses to the Trustee's complaint on March 28, 2003.

Begler is an individual residing in California and is engaged in business in the copywriting industry. Prior to the Petition Date, Begler performed concept development and copywriting services for the Debtor. Transcript, pages 49-50.

During the 90 days preceding the Petition Date, the Debtor made three payments to

¹Begler alleges additional defenses which were not pursued at trial.

Begler as follows: (1) by check dated February 2, 2001 (clearing February 8, 2001) in the amount of \$20,300; (2) by check dated February 15, 2001 (clearing February 26, 2001) in the amount of \$8,000; and (3) by check dated March 9, 2001 (clearing March 19, 2001) in the amount of \$8,000. Trustee's Exhibits 4, 5, 6, 11, 12 and 13. The first payment was made in satisfaction of invoices dated November 5, 2000 and December 4, 2000. The second payment was made in satisfaction of an invoice dated January 2, 2001 and the third payment was made in satisfaction of an invoice dated February 1, 2001. Trustee's Exhibits 7, 8 and 9.

Begler received the benefit of the Transfers. The Debtor is presumed to have been insolvent at the time of the Transfers. At the time of the trial, the Trustee testified that pre-petition general unsecured creditors are not likely to receive full payment of their claims in the Debtor's case. Transcript, page 30. Had the Transfers not been made, Begler would have held only a non-priority general unsecured claim against the Debtors for the amount of the Transfers. For about six months prior to the preference period, the Debtor paid invoices issued by Begler between 24 and 51 days after the invoice date and on average 32.14 days after the invoice date. Trustee's Exhibits 16, 17, 18, 19, 20, 21, 22 and 23.

The final invoice issued by Begler to the Debtor, dated March 1, 2001 was not paid by the Debtor. Transcript, pages 60-61. The work that Begler had been performing for the Debtor was for Apple Computer, which was the Debtor's client. Some time around the Petition Date, Begler and Apple Computer came to an agreement in which Begler would work for Apple directly. As part of that negotiation, Apple agreed to pay the outstanding invoice, for \$11,700. As a result, Begler did not file a claim for the invoice in the Debtor's bankruptcy case. Transcript, pages 62-63.

Conclusions of Law

The issues in this case are the affirmative defenses of ordinary course of business and subsequent new value. The parties stipulated that the Trustee proved his *prima facie* case, that Begler received preferential transfers from the Debtor as such transfers are defined in § 547(b) of the Bankruptcy Code. Transcript, page 127.

Ordinary Course of Business

Begler raises the ordinary course of business defense. 11 U.S.C. §547(c)(2).² The defendant bears the burden of proving this defense by a preponderance of the evidence. Cassirer v. Herskowitz (In re Schick), 234 B.R. 337 (S.D.N.Y. 1999); see 11 U.S.C. §547(g). “In order for a creditor to prevail using the ordinary course of business exception to 547(b), the creditor must show that the debt had been incurred in the ordinary course of business of both the debtor and the creditor; that the payment too, had been made and received in the ordinary course of their businesses; that the payment was made according to ordinary business terms. Matter of Tolona Pizza Products Corp., 3 F.3d 1029, 1031 (7th Cir.1993).

The Ordinary Course of the Parties’ Business

In order to determine whether the payments were made and received in the ordinary

²The court notes that the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 took effect after this case was filed and is therefore inapplicable.

course of the parties' business, "the court must make a factual inquiry into the prior dealings between the parties." Cassirer, 234 B.R. at 348. See also Lovett v. St. Johnsbury Trucking, 931 F.2d 494, 497 (8th Cir. 1991) and In re Fulghum Construction Corp., 872 F.2d 739, 743 (6th Cir. 1989)("the court must engage in a peculiarly factual analysis"). "[T]he cornerstone of this element of a preference defense is that the creditor need demonstrate some consistency with other business transactions between the debtor and the creditor." Lovett, 931 F.2d at 497, (citing In re Magic Circle Energy Corp., 64 B.R. 269, 273 (Bankr.W.D.Okla.1986)). "The creditor must establish a 'baseline of dealings' to enable the court to compare the payment practices during the preference period with the prior course of dealing." Cassirer, 234 B.R. at 348.

Here, the Trustee presented the following evidence that the Transfers were not made in the parties' ordinary course of business. The transfers in bold type are the transfers made during the preference period and which the Trustee seeks to recover.

Invoice date	Payor	Amount	Due date	Date paid	Days late
4/4/00	USWeb/CKS	\$11,200	5/4/00	5/4/00	0
5/3/00	USWeb/CKS	\$8000	6/2/00	5/30/00	-3
6/2/00	USWeb/CKS	\$12,700	7/2/00	7/4/00	2
7/3/00	USWeb/CKS	\$8000	8/2/00	7/27/00	-6
8/2/00	USWeb/CKS	\$11,000	9/1/00	9/5/00	4
9/5/00	marchFirst	\$8500	10/5/00	10/26/00	21
10/2/00	marchFirst	\$8400	11/1/00	10/26/00	-6
11/6/00	marchFirst	\$12,300	12/6/00	2/1/01	57
12/4/00	marchFirst	\$8000	1/3/01	2/1/01	29
1/2/01	marchFirst	\$8000	2/1/01	2/15/01	14

2/1/01	marchFirst	\$8000	3/3/01	3/9/01	6
3/1/01		\$11,700		3/31/01	

This chart³ was prepared by the defendant's counsel and sent to the Trustee's counsel as an enclosure with a letter. Trustee's Exhibit 16. Nevertheless, it tends to support the Trustee's position. The payments made by the Debtor prior to the preference period were almost all on time or early. The payments made in the preference period were late. During the trial, defendant's counsel argued that the payments were late because invoices had to be routed through Chicago after marchFirst merged with USWeb/CKS. Prior to the merger, Begler submitted his invoices to a San Francisco office and the payments were approved and made from the San Francisco office. There was some evidence presented showing that the invoices were routed through the Chicago office from San Francisco during the preference period consisting of date stamps and other markings on the invoices. Trustee's Exhibits 7, 8 and 9. There was, however, no testimony regarding the process from anyone involved in the process.

Moreover, the Trustee testified that the merger became official on March 1, 2001, well before the preference period so if there were going to be a delay in payments to creditors, one would think the delays would have started shortly thereafter rather than seven months later. Transcript, page 41. Finally, Begler's own chart shows three post-merger payments being made early. Begler's inconclusive evidence that the merger affected the timeliness of the Debtor's payments is insufficient to offset the Trustee's evidence that the payments made during the preference period were paid later than was the ordinary course of business of the parties.

³The court has reproduced the chart without information that the court considers irrelevant to the resolution of this matter, such as invoice and check numbers.

Therefore, Begler failed to prove this prong of the ordinary course of business defense - that the Transfers were made in the ordinary course of business between the parties. Under pre-BAPCPA law this finding is adequate to find for the Trustee on the ordinary course of business defense because the defendant was required to prove both prongs of the test. The parties presented evidence and made arguments on the final prong of the test and the court will address that evidence and those arguments.

Ordinary Business Terms

The final element of ordinary course of business is that the Transfers were made in the ordinary course of business in the industry or “according to ordinary business terms.” Ordinary business terms refers to a range of payment terms encompassing the practices of firms similar to that creditor. Tolona Pizza, 3 F.3d 1029, 1033. It is therefore necessary for a creditor to present some evidence establishing the range of acceptable practices within the industry. In re Midway Airlines, 1995 WL 331053 (N.D.Ill.1995) (unpublished opinion).” Superior Toy & Mfg. Co., Inc., 183 B.R. 826, 836 (N.D. Ill. 1995). “In order to sustain the affirmative defense, the record must establish that the payments made by [the debtor] to [the creditor] were ‘made according to ordinary business terms’ which in turn requires essentially expert testimony as to the manner in which payments are customarily made in the transferee’s industry; [citation omitted].” Globe Building Materials, Inc. v. The RDI Group, 325 B.R. 253, 259 (Bankr. N.D. Ind. 2005), aff’d, 484 F.3d 946 (7th Cir. 2007). The creditor against whom recovery is sought has the burden of proving the nonavoidability of a transfer under §547(c). Id. at 258; 11 U.S.C. §547(g).

In 2003, the Trustee in this case filed hundreds of adversary proceedings to obtain the

return of preferential payments. As he pursued these adversaries, the Trustee filed a motion for summary judgment in May of 2005, in adversary proceeding 03 A 531, Maxwell v. Gaynelle Grover. Ms. Grover's response to the motion included five affidavits of her local competitors, attesting to the fact that invoices in Ms. Grover's industry at the time in question were being paid as late as 120 days from the date of invoice. For that reason, among others, this court found that Ms. Grover had proved that the transfers in question were made in the ordinary course of business and awarded summary judgment to Ms. Grover.

Begler sought to present at trial, as factual evidence, the affidavits submitted by Ms. Grover, the summary judgment papers submitted by the Trustee in the Grover adversary and the court's opinion in the Grover adversary. Transcript, 3-4, Defendant's Exhibits 15-25. The court disallowed the affidavits as hearsay and the court documents because they were not relevant as fact evidence. Begler also made a legal argument that Grover was binding under the doctrine of collateral estoppel.

Collateral estoppel ensures that once an issue is actually and necessarily determined by a court of competent jurisdiction, that determination is conclusive in subsequent suits involving a party to prior litigation. "Prerequisites for application of collateral estoppel are satisfied when issue sought to be precluded is same as that involved in prior action, issue was actually litigated, determination of issue was essential to final judgment, and party against whom estoppel is invoked was fully represented in prior action." Chicago Truck Drivers, Helpers and Warehouse Union (Independent) Pension Fund v. Century Motor Freight, Inc., 125 F.3d 526 (7th Cir. 1997).

Some of the requirements have been met here. The issue of what constituted a late payment in Ms. Grover's industry during a certain period of time was actually litigated, the

ruling was essential to the final judgment and the Trustee was fully represented in the Grover adversary. Begler failed to prove that that issue was the same as in his case.

Begler testified that he saw Ms. Grover's website and read her affidavit and concluded that he is in the same industry as Ms. Grover. Transcript, 56. No foundation was provided for Begler's testimony. The web site was not offered into evidence. Begler's testimony regarding the contents of the web site was found to be hearsay. Transcript, pages 56-57. Begler's self-serving testimony was the only proof offered to show that he is in the same industry as Ms. Grover.

In addition to collateral estoppel not being applicable here, the Grover decision does not bind this court as a matter of precedent for the same reason - Begler failed to show that the facts in his case fell squarely within the facts of the Grover case. With no other evidence to prove that the transfers were made in the ordinary course of business of Begler's industry, Begler failed to meet his burden of proof on this defense.⁴

New Value

Under the new value defense, a preference defendant "has the burden of establishing that new value was extended, which remains unsecured and unpaid after the preferential transfer."

Schwinn Plan Comm. v. AFS Cycle Ltd. (In re Schwinn Bicycle Co.), 205 B.R. 557, 568 (Bankr. N.D. Ill. 1997), citing Matter of Prescott, 805 F.2d 719, 731 (7th Cir. 1986); see Globe Building

⁴Begler filed an objection to the Trustee's Exhibit 14, which is a 2000-2002 Risk Management Assessment Guideline, presented by the Trustee to establish that the Transfers were not in the ordinary course of business in Begler's industry. The court reserved ruling on the objection. This matter is of no concern as Begler failed to meet his burden of proof on this issue.

Materials, Inc. v. The RDI Group, 325 B.R. 253, 259 (Bankr. N.D. Ind. 2005), aff'd, 484 F.3d 946 (7th Cir. 2007). Begler argues that he extended new value to the Debtor in the form of services rendered and reflected in the March 1, 2001 invoice for \$11,700 that was not paid by the Debtor and was paid by Apple Computer. Initially, it should be noted that Begler never established for a certainty that the invoice was unpaid on the Petition Date. Transcript, page 68-71.

The question of whether an invoice remains “unpaid” for the purposes of §547(c)(4) of the Bankruptcy Code when it was paid by a third party has not been addressed by the Seventh Circuit. It has however been addressed by the Eighth Circuit in Kroh Brothers Development Co. v. Continental Construction Engineers, Inc., 930 F.2d 648 (8th Cir. 1991). In Kroh Bros., the debtor real estate developer sought to recover preferential transfers from Continental, a civil engineering firm with which it did a lot of business. The parties agreed that Continental had provided new value to the debtor in the form of services performed, but because Continental had been paid by third parties unrelated to the debtor, the parties could not agree as to whether Continental remained “unpaid.” The Eighth Circuit closely examined the case of In re Formed Tubes, Inc., 46 B.R. 645 (E.D. Mich. 1985), the only bankruptcy court to have considered the question. “In answering the question, the bankruptcy court considered whether the estate had been replenished. ... That is, only the effect on the estate, not the source of payment, is relevant. [Citation omitted]. In the case of payment by a third party with a secured claim against the estate, such payment would preclude a new value defense because the third party’s secured claim would indirectly deplete the estate. That is, the payment would have ‘the same impact upon the estate as a payment made directly by the debtor.’” Kroh Bros. at 653 (citing Formed Tubes, 46

B.R. at 647).

The Eighth Circuit agreed with this analysis, as does this court.

[I]f the creditor receives payment from a third party who has a secured claim against the estate, the relative positions of the creditor and estate change. If allowed to assert the new value defense, the creditor would be entitled to retain the preference to offset against the new value even though the creditor also received a cash payment for the new value from the third party. The position of the creditor would be better than if the preference had not been made. This beneficial effect on the creditor, however, is not decisive. The rationale behind preference avoidance, distributive equality, compels us to consider whether the preference retention is to the detriment of other creditors. In the case of payment by a secured third party, the estate would indeed be diminished. Because the third party who paid the creditor would be able to assert a secured claim against the estate for the amount of the new value, the new value would deplete rather than replenish the estate insofar as unsecured creditors are concerned. See In re Formed Tubes, 46 B.R. at 647 n. 4. *The availability of the defense, then, depends on the ultimate effect on the estate.*

Id. at 654. (Emphasis supplied).

Applying the Eighth Circuit's analysis to this case is simple. Begler, who brought these cases to this court's attention, put in no evidence on the question of how the estate was affected by Apple's payment to Begler. Did Apple file a claim, seeking reimbursement from the estate? If so, what kind of claim and for what level of priority? Begler's counsel had the Trustee on the stand and failed to ask one question eliciting testimony that would support this argument. No documents were submitted to show that Apple did or did not file a claim or adversary proceeding. He argues that "there is nothing in the record to indicate that Apple made any claim for the \$11,700 that it paid to Mr. Begler ..." Begler's Post-Trial Brief, page 15. The burden of

proving this defense is on the party asserting it. See 11 U.S.C. §547(g). It was Begler's burden to prove that there was no effect on the estate and he did not meet it.

Conclusion

For the foregoing reasons, judgment will be granted in the Trustee's favor by separate order.

ENTERED:

Date: July 20, 2007

John D. Schwartz
United States Bankruptcy Judge