

IN THE UNITED STATES BANKRUPTCY COURT FOR
THE EASTERN DISTRICT OF TENNESSEE

IN RE)
) NO. 3-83-00372
SOUTHERN INDUSTRIAL BANKING)
CORPORATION)
) Chapter 11
Debtor)

THOMAS E. DuVOISIN, Liquidating)
Trustee)
)
Plaintiff)
)
v.) ADV. NO. 3-85-0524
)
PETER A. NESKAUG)
and MARTHA NESKAUG)
)
Defendants)

M E M O R A N D U M

This adversary proceeding is before the court on the complaint of plaintiff Thomas E. DuVoisin, Liquidating Trustee, which seeks the recovery of an alleged preferential transfer of \$40,764.24 made by the debtor to the defendants, Peter A. Neskaug and wife, Martha Neskaug. Having considered the evidence and arguments of the parties, the court now makes its findings of fact and conclusions of law pursuant to Federal Rule of Bankruptcy Procedure 7052.

I.

On February 4, 1983, Mr. Neskaug opened a VIP account at Southern Industrial Banking Corporation ("SIBC") in the name of Peter A. or Martha Neskaug and deposited \$40,814.24 into that

account. On February 11, 1983, within eight days of the opening of the account and within ninety days of the filing of the debtor's Chapter 11 petition on March 10, 1983, Mr. Neskaug withdrew \$40,764.24 from the VIP account, receiving a check in that sum from SIBC made payable to the order of Peter A. Neskaug. The funds represented by this check were shortly deposited in a bank account over which both Mr. and Mrs. Neskaug had individual signature authority.

The trustee contends the check for \$40,764.24 represents a preferential transfer from the debtor to Mr. Neskaug such as is avoidable under the provisions of 11 U.S.C. § 547(b) and for which the Neskaugs are liable under 11 U.S.C. § 550(a)(1), he as an initial transferee, she as one for whose benefit the transfer was made. The parties agree that all the elements of a preferential transfer under § 547(b) have been established in this case, but the Neskaugs argue the transfer is not avoidable because it falls within the provisions of 11 U.S.C. § 547(c)(2), which create an exception for certain transfers made in the ordinary course of business. Mr. Neskaug does not dispute that he is the initial transferee of the debtor or that he is liable to the trustee if his ordinary-course-of-business defense should fail. Mrs. Neskaug also relies on that general defense, but she defends further by denying that she is an "entity for whose benefit the transfer was made. . . ." under § 550(a)(1). The issues before the court, then, are (1) whether the transfer in question falls within the defense commonly

known as the ordinary-course-of-business defense, and (2) whether the initial transfer was made for Mrs. Neskaug's benefit.

II.

Normally, trustees may avoid a preferential transfer by the debtor if the criteria of 11 U.S.C. § 547(b) are met. In this case, it is agreed by the parties that those criteria are met. The Bankruptcy Code, however, provides several exceptions to this general rule, one of which is the exception for transfers made in the ordinary course of business:

(c) The trustee may not avoid under this section a transfer--

(1) . . .

(2) to the extent that such transfer was--

(A) in payment of a debt incurred by the debtor in the ordinary course of business or financial affairs of the debtor and the transferee;

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

(C) made according to ordinary business terms.

11 U.S.C. § 547(c)(2). Once the trustee has established the elements of a preferential transfer, the burden of proving all the elements of the defense provided by § 547(c)(2) falls on the party seeking to take advantage of it, in this case the defendants. They must prove each element of their defense by a preponderance of the

evidence. *Logan v. Basic Distribution Corp. (In re Fred Hawes Organization, Inc.)*, 957 F.2d 239, 243-44 (6th Cir. 1992).

The defendants sought to carry their burden of proof on this issue by offering the testimony of Mr. Neskaug. On direct examination, he gave detailed testimony about his activities on February 11, 1983, when he went into SIBC at about 10:00 a.m. According to his testimony, he made two transactions that day, the first of which was the withdrawal of \$40,764.24 from his VIP account. According to Mr. Neskaug, he approached a teller, asked to withdraw the money, and received a check within a few minutes. This first transaction, which is the subject of this preference action, was, as portrayed by Mr. Neskaug's trial testimony, entirely ordinary and routine and thus completely within the ordinary course of business of both the debtor and the transferee.

Mr. Neskaug's trial testimony went on to describe a second transaction, not the subject of this action, in which he tried to effect an early withdrawal of three certificates of deposit of a total value of about \$65,000. This transaction took until 5:30 p.m. to complete because, according to Mr. Neskaug, SIBC convinced him it would be better to obtain a loan for \$65,000, leaving the certificates of deposit with SIBC as collateral for the loan. He testified the loan was approved at around 2:00 p.m. after what he described as "a considerable amount of telephone calling back and forth," probably between the branch and the main office, which he thought was highly unusual. Trial Transcript at 33, 64. Mr.

Neskaug further testified that he did not leave the bank until 5:30 p.m., after being continuously present there for at least seven and one-half hours, because his wife, whose signature was required on the note and security agreement, could not be located and brought to the bank until late in the afternoon.

Mr. Neskaug's direct testimony suffered damaging impeachment on cross-examination. Using a deposition given by Mr. Neskaug on February 1, 1994, about three months prior to the trial of this action, the trustee showed that Mr. Neskaug had previously testified under oath that he went to SIBC by himself on the morning of February 11, 1983, and sought to withdraw his money. According to the deposition, Mr. Neskaug did not immediately receive a check for approximately \$40,000, but rather a puzzling "runaround" that lasted all day.

Q. O.K. Who did you talk to when you went in to get your money?

A. I think I talked to everybody.

Q. What was the explanation you were given as to the delay in getting your money?

A. They didn't have one. They just kept giving me the runaround.

Plaintiff's Exhibit 7, Deposition of Peter Neskaug at 35 ("Exhibit 7").

Mr. Neskaug's deposition, which was admitted into evidence without objection, continues in this vein, full of Mr. Neskaug's protestations that he could not possibly understand the cause of

the abnormal delays. He was angry and frustrated at the day-long course of mistreatment dealt him.

Q. All right. So tell me more about this runaround you were getting on February 11, 1983, to try and get your 40 thousand dollars out. What else happened?

A. I just hung in there. I mean, I couldn't understand why it was taking so long.

Q. What did they tell you as to what was the problem?

A. They didn't.

Q. Well, when was it that you finally got your check?

A. Around 5:30 that afternoon.

Q. Did you stay out there continuously from ten o'clock morning until 5:30?

A. I was in their office continuously.

. . . .

Q. Didn't it seem a little unusual for you to be sitting there for six or seven hours?

A. It [sic: I?] got very hot about it.

Q. I would think if it was unusual--you had never had this type of problem with your other banking transactions before, had you?

A. No.

Q. Seems to me that would have been an unusual event that I would remember if I had to sit seven hours at a place trying to get my money out. Do you agree with me on that?

A. It was very unusual. I don't understand it. I still don't understand it.

Q. I think if I was sitting there for seven hours I would be asking people questions as to why I can't get my money.

A. I was. I was threatening them and everything else. I had other things to do.

Q. And nobody gave you any explanation as to why they couldn't write you a check?

A. No.

Exhibit 7 at 39-41.

If the real reason for this delay was the unavailability of his wife for signing the requisite papers, then it seems doubtful that Mr. Neskaug would have been "very hot about it" or that he would threaten SIBC personnel. One does not normally threaten a lender in order to obtain a routine loan, which is how Mr. Neskaug characterized this transaction in his direct testimony at trial. Moreover, if the real reason for the delay had been the unavailability of his wife, it seems likely that he would have remembered that cause and would not have been baffled and amazed by the delays that occurred. Indeed, during his deposition Mr. Neskaug was prompted to bring his wife into the transaction when counsel for the trustee asked him,

Q. Who physically went to SIBC to withdraw the money?

A. I did.

Q. Did your wife go with you?

A. No, she did not.

Exhibit 7 at 34. This unqualified response was not modified at any time during the deposition. Nor did Mrs. Neskaug, either in her deposition or her trial testimony, mention having gone to SIBC on February 11, 1983, for any purpose.

Finally, additional doubt is thrown on Mr. Neskaug's trial testimony that the cause of the delay in question was the unavailability of his wife. In his deposition he testified as follows:

Q. Do you recall going home and having any discussions with your wife about what had transpired during your day sitting around

there for seven hours trying to get your check out?

A. What I said, I don't know. I am sure I did say something.

Exhibit 7 at 43-44.

It is unlikely that Mr. Neskaug would have given that response if his wife's unavailability had caused the delays and if she had actually entered the bank that afternoon. It is also notable that Mrs. Neskaug, who testified as a witness in the trial of this cause, said not a word about visiting SIBC on the day in question.

Finally, an important part of Mr. Neskaug's defense is his trial testimony that he received the check that is the subject of this adversary proceeding in a very ordinary way, upon demand, and within minutes of the time he entered SIBC. Nowhere in his deposition does this version of the event appear. Instead, he testified that he received the very check at issue only after waiting all day.

Q. Let me show you check 044234, dated February 11, 1983, for \$40,764.24. Is that the check that you ultimately got from SIBC after waiting for seven hours?

A. Yes.

Exhibit 7 at 41.

Having observed the demeanor of Mr. Neskaug during his testimony at trial, and considering the material contradictions between Mr. Neskaug's trial testimony and his discovery deposition, none of which are satisfactorily explained, the court is left with serious

doubts about the reliability of Mr. Neskaug's testimony and which of its versions, if any, to credit. Under these circumstances the court may, and in this case does, reject the witness' testimony entirely. Because his testimony is the only evidence offered to establish the ordinary-course-of-business defense, rejection of Mr. Neskaug's testimony means that the defense fails for lack of proof. It being agreed by the parties that the elements of a preference otherwise exist, judgment for the trustee against Mr. Neskaug is appropriate.

III.

Having found that the ordinary-course-of-business defense is unavailable to the defendants in this cause, the court must now decide whom the preferential transfer can be recovered from. The parties agree that the trustee may recover from Mr. Neskaug because he was the initial transferee within the meaning of 11 U.S.C. § 550 (a)(1).¹ The parties have also agreed that the question of whether Mrs. Neskaug is an immediate or mediate transferee under the provi-

¹ Section 550(a) provides as follows:

(a) Except as otherwise provided in this section, to the extent that a transfer is avoided under section 544, 545, 547, 548, 553(b), or 724(a) of this title, the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from--

(1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or

(2) any immediate or mediate transferee of such initial transferee.

sions of § 550(a)(2) is not before the court.² Because Mrs. Neskaug obviously was not the initial transferee, the only remaining issue is whether she might be an "entity for whose benefit such transfer was made. . ." within the meaning of § 550(a)(1).

The trustee argues that the initial transfer of the check to Mr. Neskaug benefited Mrs. Neskaug because there is evidence that the funds represented by that check were deposited into an account over which both Mr. and Mrs. Neskaug had signature authority. If so, that arguably might make Mrs. Neskaug an immediate or mediate transferee under § 550(a)(2), but it virtually prevents her from being an "entity for whose benefit such transfer was made" because a subsequent transferee cannot be the entity for whose benefit the initial transfer was made. This is because "the phrase 'or the entity for whose benefit such transfer was made' refers to those who receive a benefit as a result of the *initial* transfer from the debtor--not as the result of a *subsequent* transfer." *Merrill v. Dietz (In re Universal Clearing House Co.)*, 62 B.R. 118, 128 n.12 (D. Utah 1986) (emphasis added), *quoted with approval in Danning v. Miller (In re Bullion Reserve of North America)*, 922 F.2d 544, 547 (9th Cir. 1991).

In *Danning v. Miller*, the Ninth Circuit went on to explain the distinction to be drawn between a subsequent transferee, i.e., "im-

² At the close of the trial, the parties refined and limited the issues. The trustee agreed that his complaint did not specifically raise the issue of whether Mrs. Neskaug was an immediate or mediate transferee under § 550(a)(2). Accordingly, he acknowledged that Mrs. Neskaug could be liable only as an "entity for whose benefit [the] transfer was made" under § 550(a)(1).

mediate or mediate" transferee, and one for whose benefit an initial transfer has been made.

A subsequent transferee cannot be an entity for whose benefit the initial transfer was made, even if the subsequent transferee actually receives a benefit from the initial transfer. *Bonded Fin. Servs. v. European Am. Bank*, 838 F.2d 890, 895 (7th Cir. 1988) ("*Bonded*"); see also, *In re Richmond Produce Co.*, 118 B.R. 753, 760 (Bankr. N.D. Cal. 1990) (a subsequent transferee can never be an entity for whose benefit the initial transfer was made). The structure of the statute separates initial transferees and beneficiaries, on the one hand, from immediate or mediate transferees, on the other. The implication is that the entity for whose benefit the transfer was made is different from a transferee, immediate or otherwise. "Someone who receives the money later on is not an 'entity for whose benefit such transfer was made'; only a person who receives a benefit from the initial transfer is within this language." *Bonded*, 838 F.2d at 896.

Danning v. Miller, 922 F.2d at 548.

The trustee in this case offered no evidence of any benefit accruing to Mrs. Neskaug as a direct result of SIBC's transfer of the check to Mr. Neskaug. Instead, the proof was to the effect that Mrs. Neskaug arguably might have been a subsequent transferee to the extent that the moneys in question eventually found their way into an account over which she had signature authority. According to the foregoing authorities, that proof does not make Mrs. Neskaug an entity for whose benefit the initial transfer was made, and, because that is the only legal theory upon which the trustee

has proceeded in this cause, it follows that the trustee cannot recover against Mrs. Neskaug.

The trustee is directed to submit an appropriate order granting judgment for the trustee against Mr. Neskaug and granting judgment for Mrs. Neskaug against the trustee.

JOHN C. COOK
United States Bankruptcy Judge