

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

In re

Case No. 99-35026

HFC CONSTRUCTION CO., INC.

Debtor

N. DAVID ROBERTS, JR., TRUSTEE

Plaintiff

v.

Adv. Proc. No. 01-3192

JOHN SCHAAD d/b/a SCHAAD'S  
LUMBER & DO-IT CENTER

Defendant/Third Party Plaintiff

v.

MID-STATE SURETY CO., INC. and  
BENCHMARK CONSTRUCTION, LLC

Third Party Defendants

**MEMORANDUM ON MOTIONS FOR SUMMARY JUDGMENT**

**APPEARANCES:** BAILEY, ROBERTS & BAILEY, P.L.L.C.

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**RICHARD STAIR, JR.**  
**UNITED STATES BANKRUPTCY JUDGE**

The court has before it the Motion for Partial Summary Judgment filed on June 21, 2002, by Plaintiff N. David Roberts, Jr., Trustee (Trustee). The court also has before it the Defendant Schaad's Motion for Partial Summary Judgment filed on July 15, 2002, by Defendant/Third Party Plaintiff John Schaad d/b/a Schaad's Lumber & Do-It Center (Schaad). The parties have filed briefs, affidavits, and various documents in support of their respective motions.

This is a core proceeding. 28 U.S.C.A. § 157(b)(2)(E), (F) (West 1993).

## I

As an initial matter, the court must address the timeliness - or lack thereof - of Schaad's reply to the Trustee's summary judgment motion. As noted, the Trustee filed his motion on June 21, 2002. Pursuant to E.D. Tenn. LBR 7007-1, Schaad had twenty days from that date to file a response.<sup>1</sup> At the scheduling conference held on June 27, 2002, the court twice brought the twenty-day response deadline to the attention of Schaad's counsel.<sup>2</sup> Nonetheless, Schaad's Reply

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<sup>1</sup> Local Rule 7007-1 provides in material part:

A motion filed in a proceeding shall be accompanied by a brief setting forth the facts and the law supporting the motion. Unless the court directs otherwise, the opposing party shall respond within twenty days after the date of filing of the motion. Any opposing response shall be supported by a brief setting forth the facts and the law in opposition to the motion. A failure to respond shall be construed by the court to mean that the respondent does not oppose the relief requested by the motion.

E.D. Tenn. LBR 7007-1.

<sup>2</sup>

THE COURT: . . . . But remember you have under our local rule, you've got a 20 day response time to the summary judgment motion and the summary judgment motion--

MR. LEVITT: I haven't seen the motion, yet.

. . . .

THE COURT: . . . . Now, again, under the local rule with the summary judgment motion pending  
(continued...)

to Plaintiff's Motion for Partial Summary Judgment was not filed until July 15, 2002 (four days late), and was not accompanied by a supporting brief. To date, Schaad's counsel has offered no explanation for his failure to comply with the local rules.

The Trustee urges the court to strike Schaad's response - and thereby grant the original summary judgment motion as unopposed. See E.D. Tenn. LBR 7007-1 ("A failure to respond shall be construed by the court to mean that the respondent does not oppose the relief requested by the motion."). Despite the court's frustration with Schaad's deficient filing, the response will nonetheless be considered in light of the issues raised by Schaad's subsequent summary judgment motion and the Trustee's reply to that motion. See *Rooks v. Am. Brass Co.*, 263 F.2d 166, 169 (6<sup>th</sup> Cir. 1959) ("[T]he interests of justice are best served by a trial on the merits[.]").

## II

The Debtor was a corporation engaged in the construction business. On December 31, 1998, it entered into an agreement (Contract)<sup>3</sup> with the Public Building Authority of the County

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<sup>2</sup>(...continued)

there will be a response. Our local rule provides that failure to respond is deemed to mean there's no opposition to the motion, so just-you need to be aware of that, Mr. Levitt. I'm sure you probably already are.

MR. LEVITT: No, Your Honor.

THE COURT: Well, you are now.

MR. LEVITT: Yes, Your Honor.

<sup>3</sup> The Contract is captioned "Standard Form of Agreement Between Owner and Contractor where the basis of payment is a Stipulated Sum." The Contract is supplemented by "The PBA Modified Version of the General Conditions of the Contract for Construction" (General Conditions).

of Knox and the City of Knoxville, Tennessee (PBA), to construct a new “West Knox Branch Library” for PBA.

The Contract provided for progress payments from PBA to the Debtor. See Contract, § 5.1. To receive a progress payment, the Debtor was required to submit an Application for Payment to the project’s architect, documenting the work and materials billed. See *id.*; General Conditions, § 9.3. The architect would then issue to PBA a Certificate for Payment, and PBA would remit the requested funds to the Debtor. See Contract, § 5.1; General Conditions, §§ 9.4, 9.6.1. The Debtor was then required to pay subcontractors and suppliers for the work or materials identified in the Application for Payment. See General Conditions, § 9.6.

The Debtor also executed a Payment Bond with Third-Party Defendant Mid-State Surety Corporation (Mid-State) and Everest Reinsurance Company. The Payment Bond provides in material part:

8 Amounts owed by the Owner [PBA] to the Contractor [the Debtor] under the Construction Contract shall be used for the performance of the Construction Contract and to satisfy claims, if any, under any Construction Performance Bond. By the Contractor furnishing and the Owner accepting this Bond, they agree that all funds earned by the Contractor in the performance of the Construction Contract are dedicated to satisfy obligations of the Contractor and the Surety under this Bond, subject to the Owner’s priority to use the funds for the completion of the work.

Performance Bond, at \*5. Additionally, the Debtor executed a March 12, 1998 General Agreement of Indemnity with Mid-State which in material part provides:

9. If any of the Bonds are executed in connection with a contract which by its terms or by law prohibits the assignment of the contract price, or any part thereof [,] Indemnitor and Indemnitors covenant and agree that all payments received for or on account of said contract shall be held as a trust fund in which the Surety has

an interest [] for the payment of obligations incurred in the performance of the contract and for labor, materials, and services furnished in the prosecution of the work provided in said contract or any authorized extension or modification thereof; and, further, it is expressly understood and declared that all monies due and to become due under any contract or contracts covered by the Bonds are trust funds . . . for the benefit of and for payment of all such obligations in connection with any such contract or contracts . . . .

General Agreement of Indemnity, § 9.

Schaad was a supplier for the West Knox Branch Library project. By his December 7, 2001 Complaint and his February 1, 2002 Amended Complaint, the Trustee seeks to avoid and recover one prepetition payment and one postpetition payment made by the Debtor to Schaad. The prepetition transfer is not at issue in either summary judgment motion now before the court.

The postpetition transfer occurred by the Debtor's check number 12747 dated December 9, 1999, in the amount of \$5,929.69. This payment to Schaad was for materials ordered for the library project between October 12, 1999, and November 29, 1999.<sup>4</sup> It is unclear whether the Debtor's November 11, 1999 progress payment application included a reimbursement request for materials ordered from Schaad between October 12 and November 11, 1999. See July 26, 2002, Affidavit of H. Frank Chambers (the Debtor's President), at ¶ 9. The November 11, 1999 progress payment application did not, however, include reimbursement requests for any materials to be ordered from Schaad after that date. See *id.* at ¶ 8.

The Debtor then filed its Voluntary Chapter 7 Petition on December 10, 1999. Because check number 12747 was not honored by the Debtor's bank until December 14, 1999, a

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<sup>4</sup> The \$5,929.69 included \$2,663.55 for charges accrued prior to November 11, 1999, and \$3,266.14 in charges occurring after November 11, 1999.

postpetition transfer occurred. See *Guinn v. Oakwood Props., Inc. (In re Oakwood Mkts., Inc.)*, 203 F.3d 406, 409 (6<sup>th</sup> Cir. 2000).

### III

Pursuant to Rule 56(c) of the Federal Rules of Civil Procedure, summary judgment is warranted “if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.” FED. R. CIV. P. 56(c); FED. R. BANKR. P. 7056. The court’s function is not to “weigh the evidence and determine the truth of the matter but to determine whether there is a genuine issue for trial.” *Anderson v. Liberty Lobby, Inc.*, 106 S. Ct. 2505, 2511 (1986).

As noted, the Trustee’s summary judgment motion relates solely to check number 12747, which the Trustee seeks to avoid as an unauthorized transfer of property of the estate. Section 549 of the Bankruptcy Code provides, with exceptions not material to this proceeding, that a trustee may avoid a postpetition transfer of estate property if the transfer was not authorized by the Bankruptcy Code or the court. See 11 U.S.C.A. § 549(a) (West 1993).

In response, Schaad contends that § 549 is inapplicable to the check because no property of the estate was transferred. Instead, Schaad argues, the check merely conveyed progress payment funds held by the Debtor in trust. Schaad cites the above-quoted language from the Performance Bond and General Agreement of Indemnity in support of his trust fund theory. See

*generally Fed. Ins. Co. v. Fifth Third Bank*, 867 F.2d 330, 334 (6<sup>th</sup> Cir. 1989) (Contract provisions can create a construction progress payment trust fund.).

The court need not decide the trust fund issue at this time. Even if a trust was found to exist, Schaad has not submitted evidence tracing the trust funds from PBA through to check number 12747. According to Mr. Chambers' July 26, 2002 Affidavit, the Debtor deposited all PBA funds into an account that was also utilized for \$60,000.00 of Chambers' personal money and funds from all of the Debtor's other contracts. "It is beyond peradventure that, as a general rule, any party seeking to impress a trust upon funds for purposes of exemption from a bankrupt estate must identify the trust fund in its original or substituted form" and, if relevant, trace the fund through a commingled account. *See First Fed. of Mich. v. Barrow*, 878 F.2d 912, 915 (6<sup>th</sup> Cir. 1989). Defendant Schaad's Motion for Partial Summary Judgment must therefore be denied.

The Trustee's Motion for Partial Summary Judgment will be denied as well. In his July 29, 2002 Plaintiff's Brief in Opposition to Defendant's Motion for Partial Summary Judgment, the Trustee concedes that a genuine issue of material fact exists, on the trust fund issue, as to \$2,663.55 of the postpetition transfer.<sup>5</sup>

The Trustee contends, however, that he is entitled to summary judgment as to the remaining \$3,266.14 transferred postpetition. That amount relates to materials not included in the Debtor's (allegedly final) November 11, 1999 progress payment application. The Trustee argues that this portion of the payment could never have held trust fund status because the pertinent materials were

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<sup>5</sup> See *supra* n.4.

never included in an Application for Payment or Certificate for Payment pursuant to the process set forth in the Contract and General Conditions.

The court cannot accept the Trustee's argument. The trust - if a trust ever in fact existed - was created by the language of the Performance Bond and General Agreement of Indemnity. The relevant Performance Bond language states in part that "all funds earned by the Contractor in the performance of the Construction Contract are dedicated to satisfy obligations of the Contractor . . . under this Bond . . . ." The pertinent General Agreement of Indemnity language speaks of "a trust fund . . . for the payment of obligations incurred in the performance of the contract and for . . . materials . . . furnished in the prosecution of the work provided in said contract . . . and, further, it is expressly understood and declared that all monies due and to become due under any contract or contracts covered by the Bonds are trust funds . . . for the benefit of and for payment of all such obligations in connection with such contract or contracts . . . ." These provisions speak generally of obligations of the Debtor, and not of specific, technical compliance with invoicing deadlines. The court is therefore not satisfied, as a matter of law, that the \$3,266.14 - undisputably the payment of an obligation related to the Contract - could not have been paid out of funds held in trust.

In sum, the Plaintiff's Motion for Partial Summary Judgment must be denied. The Defendant Schaad's Motion for Partial Summary Judgment must also be denied. An appropriate Order will be entered.

FILED: August 14, 2002

BY THE COURT

/s/

RICHARD STAIR, JR.  
UNITED STATES BANKRUPTCY JUDGE

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**ORDER**

For the reasons stated in the Memorandum on Motions for Summary Judgment filed this date, the court directs the following:

1. The Plaintiff's Motion for Partial Summary Judgment filed on June 21, 2002, is DENIED.
2. The Defendant Schaad's Motion for Partial Summary Judgment filed by the Defendant/Third Party Plaintiff John Schaad d/b/a Schaad's Lumber & Do-It Center on July 15, 2002, is DENIED.

SO ORDERED.

ENTER: August 14, 2002

BY THE COURT

/s/

RICHARD STAIR, JR.  
UNITED STATES BANKRUPTCY JUDGE