No. _____

In the Supreme Court of the United States

STANLEY MARVIN CAMPBELL,
Petitioner,

v.

THE HANOVER INSURANCE COMPANY,
Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Must a party asserting a "new value" defense to a preference claim pursuant to 11 U.S.C. § 547(c)(1) prove the *specific value* "in money or money's worth" of the assets transferred to the debtor, as the Third, Fifth, Ninth, Tenth and Eleventh Circuits have held, or a *mere approximation* of value, as the Fourth Circuit below and the Eighth Circuit, as well as inconsistent Third and Tenth Circuit decisions, have held?

LIST OF PARTIES

Petitioner Stanley Marvin Campbell, in his capacity as Chapter 7 bankruptcy trustee of debtor ESA Environmental Specialists, Inc., was the appellant in the court below. The Hanover Insurance Company was the appellee in the court below.

RULE 29.6 CORPORATE DISCLOSURE STATEMENT

Neither Petitioner Stanley Marvin Campbell (the "Trustee"), the Chapter 7 bankruptcy trustee of ESA Environmental Specialists, Inc. ("ESA" or the "Debtor"), nor ESA, has a parent corporation, and no publicly held company owns 10% or more of either of its stock.

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PETITION FOR A WRIT OF CERTIORARI

The Trustee respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fourth Circuit in this case.

OPINIONS BELOW

The March 1, 2013 opinion of the Court of Appeals for the Fourth Circuit is reported at 709 F.3d 388 and reproduced in the appendix hereto ("App.") at 1-28.

The September 22, 2011 opinion of the United States District Court for the Western District of North Carolina affirming the judgment of the bankruptcy court is unpublished and reproduced at App. at 29-49.

The November 3, 2010 order of the United States Bankruptcy Court for the Western District of North Carolina granting Hanover's motion for summary judgment is unpublished, but available electronically at *Campbell v. Hanover Ins. Co.* (*In re Campbell*), No. 07-31532, 2010 WL 4622513 (Bankr. W.D.N.C. Nov. 3, 2010), and is reproduced at App. at 50-58.

The March 29, 2013 order of the Court of

Appeals for the Fourth Circuit denying the Trustee's petition for rehearing or rehearing *en banc* is reproduced at App. at 59.

JURISDICTION

The judgment of the Court of Appeals for the Fourth Circuit was entered on March 1, 2013. App. at 1-28. On March 29, 2013, the Court of Appeals for the Fourth Circuit denied a timely filed petition for rehearing or rehearing *en banc*. App. at 59. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Section 547(a)(2) of the Bankruptcy Code, 11 U.S.C. § 547(a)(2), provides:

(a)In this section—

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> (2) "new value" means money or money's worth in goods, services, or new credit, or release by a transferee of property previously transferred to such transferee in a transaction that is neither void nor voidable by the debtor or the trustee under any applicable law, including proceeds of such property, but does not include an obligation substituted for an existing obligation[.]

App. at 60.

Section 547(b) of the Bankruptcy Code, 11 U.S.C. § 547(b), provides:

> (b) Except as provided in subsections (c) and (i) of this section, the trustee may avoid any transfer of an interest of the debtor in property—
>
> (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.

App. at 60-61.

Section 547(c)(1) of the Bankruptcy Code, 11 U.S.C. § 547(c)(1), provides:

> (c) The trustee may not avoid under this section a transfer—
>
> (1) to the extent that such transfer was—
>
> (A) intended by the debtor and the creditor to or for whose benefit such transfer was made to be a contemporaneous exchange for new value given to the debtor; and
>
> (B) in fact a substantially contemporaneous exchange[.]

App. at 61.

STATEMENT OF THE CASE

I. INTRODUCTION

This case presents an opportunity for this Court to resolve a conflict among and within the federal circuit and district courts regarding the proper evidentiary standard to apply for the "new value" defense under § 547(c)(1) of the Bankruptcy Code.

"Under the Bankruptcy Code's preference avoidance section, 11 U.S.C. § 547, the trustee is permitted to recover, with certain exceptions, transfers of property made by the debtor within 90 days before the date the bankruptcy petition was filed." *Barnhill v. Johnson*, 503 U.S. 393, 394 (1992). "Section 547(c), in turn, establishes various exceptions to § 547(b)'s general rule permitting recovery of preferential transfers." *Id.* at 402. "Subsection (c)(1) provides an exception for transfers that are part of a contemporaneous exchange of new value between a debtor and creditor". *Id.*[1]

As first delineated by the Supreme Court in

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[1] *See also Union Bank v. Wolas*, 502 U.S. 151, 159 n.13 (1991) ("Thus, for example, § 547(c)(1) exempts a transfer to the extent that it was a 'contemporaneous exchange for new value given to the debtor'....").

Dean v. Davis, 242 U.S. 438 (1917),[2] and subsequently codified in the Bankruptcy Code at 11 U.S.C. § 547(c)(1), to establish the new value defense to a claim of a preferential transfer, a creditor must show that the transfer (i) was intended by the debtor and the creditor to be a contemporaneous exchange for new value given to the debtor; and (ii) was in fact a substantially contemporaneous exchange.[3] The policy rationale for the exception is that "[c]ontemporaneous new value exchanges are not preferential because they encourage creditors to deal with troubled debtors and because other creditors are not adversely affected if the debtor's estate receives new value." *Jones Truck Lines, Inc. v. Cent. States, Se. & Sw. Pension Fund* (*In re Jones Truck Lines, Inc.*), 130 F.3d 323, 326 (8th Cir. 1997).

The application of the "new value" defense is straightforward where the transfers in and out of the debtor's estate have clear "tangible economic value".

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[2] This Court in *Dean v. Davis*, 242 U.S. at 443, held that a mortgage executed and recorded to secure an advance of funds made one week before a bankruptcy filing was not a preference under § 60(b) of the Bankruptcy Act because the mortgage was given for a "substantially contemporary advance" and not for an antecedent debt.

[3] *See Hechinger Inv. Co. of Del., Inc. v. Universal Forest Prods., Inc.* (*In re Hechinger Inv. Co. of Del., Inc.*), 489 F.3d 568, 574 (3d Cir. 2007), *citing Creditors' Comm. v. Spada* (*In re Spada*), 903 F.2d 971, 974-75 (3d Cir. 1990); *Tyler v. Swiss Am. Sec., Inc.* (*In re Lewellyn & Co., Inc.*), 929 F.2d 424, 427 (8th Cir. 1991); *Stevenson v. Leisure Guide of Am., Inc.* (*In re Shelton Harrison*), 202 F.3d 834, 837 (6th Cir. 2000).

Phoenix Rest. Group, Inc. v. Fuller, Fuller & Assocs., P.A. (*In re Phoenix Rest. Group, Inc.*), 316 B.R. 671, 679 (Bankr. M.D. Tenn. 2004). But, as one bankruptcy court observed, "[c]ases are legion concerning the viability of new value defenses," particularly where the value of the alleged exchange is difficult to assess. *Gray v. Chace* (*In re Boston Pub. Co.*), 209 B.R. 157, 174 (Bankr. D. Mass. 1997). For instance, parties facing preference claims routinely assert that something of esoteric or hard-to-quantify value—for example, a guarantee, an insurance policy, a promise of possible or contingent future performance, or a promise to release, waive, or forbear from exercising a right—constitutes alleged "new value", and federal courts apply widely inconsistent standards to reach widely inconsistent conclusions.[4]

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[4] *See* Thomas J. Palazzolo, *New Value and Preference Avoidance in Bankruptcy*, 69 Wash. U. L.Q. 875, 876 (1991) ("Courts have read the Bankruptcy Code's definition of 'new value' expansively. This Note argues that such judicial expansions, unsupported by the statutory definition of 'new value,' tend to undercut the primary bankruptcy objective of facilitating equal distribution of a debtor's assets among creditors."); John F. Wagner Jr., *When is transfer from debtor for "new value" within meaning of §§ 547(a)(2) and 547(c) of Bankruptcy Code of 1978 (11 U.S.C.A. §§ 547(a)(2), 547(c))*, 111 A.L.R. Fed. 409 (1993) (summarizing caselaw in each of these categories and noting inconsistencies across the courts in application); Bruce H. White, *Lessor's Forbearance: Does It Constitute New Value?*, 19-May Am. Bankr. Inst. J. 18, May 2000, at 18-19 (discussing inconsistencies of application); *Miller v. Bodek & Rhodes, Inc.* (*In re Adelphia Automatic Sprinkler Co.*), 184 B.R. 224, 228 (E.D. Pa. 1995) ("New value does not

Most critically—and the central issue raised in this case—courts across the federal system are in clear discord with respect to the proper *evidentiary standard* used to determine new value under § 547(c)(1). Some courts require an exacting standard of "specificity," others require the showing of just "some value," and others evaluate cases without identifying what standard they are employing—in many cases enabling an end run around the ability of the bankruptcy trustees to recall even classic preference payments that Congress targeted in § 547(b), gutting in many cases the effectiveness of § 547(b).[5]

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consist of 'esoteric or intangible benefits' but instead 'must actually and in real terms enhance the worth of the debtor's estate so as to offset the reduction in the estate that the transfer caused.'" (quoting *Aero-Fastener, Inc. v. Sierracin Corp.* (*In re Aero–Fastener, Inc.*), 177 B.R. 120, 138 (Bankr. D. Mass. 1994)).

[5] *See* 8A C.J.S. Bankruptcy § 688 (2013) (Contemporaneous exchanges for new value) ("It has been said that there is no requirement for the valuation of the property given by the creditor to the debtor, and that the substantially contemporaneous exchange exception and the ordinary course of business exception are mutually exclusive. However, it has also been held that a valuation is necessary.") (footnotes omitted); Neil J. Rubenstein, *Preferences in Bankruptcy*, 112 Banking L.J. 422, 440-41 (1995) ("A number of courts have held that a creditor seeking to use the Section 547(c)(1) defense must prove the specific valuation of the money or money's worth in goods, services, or new credit supplied as of the time the transfer occurred and that the defense applies only to the extent of the new value provided. These courts held that the mere fact that the creditor provided some new value, without a

Courts in the Third, Fifth, Ninth, Tenth, and Eleventh Circuits have held that the party asserting the "new value" defense must prove with "specificity" the new value given to the debtor. However, the Fourth Circuit decision below, the Eighth Circuit, and different panels of the Third and Tenth Circuits have held that a mere approximation of "new value" is sufficient. Without a uniform nationwide standard that definitively resolves the deepening circuit split, federal courts will continue to apply a wide variety of inconsistent standards and reach divergent results under similar fact patterns.

The Tenth Circuit first addressed the evidentiary standard for § 547(c)(1) in *Kenan v. Fort Worth Pipe Co. (In re George Rodman, Inc.)*, 792 F.2d 125 (10th Cir. 1986). In *Rodman*, the debtor, within 90 days of filing for bankruptcy, paid a creditor $238,842 to release a lien on an oil and gas well, even though the oil and gas well in question was not producing and was almost worthless. *Id.* at 126. The trustee brought an adversary proceeding against the creditor, claiming the payment was a preference; the creditor responded with a "new value" defense. The bankruptcy court ruled for the trustee, reasoning that "[a] valid but valueless transfer falls outside the definition of 'new value.'" *Id.* at 126. But the Tenth Circuit reversed, reasoning

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determination of what it is worth, is insufficient to insulate the creditor from liability.").

that the release of the lien represented "a contemporaneous exchange for new value". *Id.* at 127. The Tenth Circuit further explained that "[t]he plain language of the definition [§ 547(a)(2)] does not require the valuation of the property transferred [in a § 547(c)(1) transaction]," and added: "We have examined §§ 547(c) and 547(a)(2) in the context of Chapter 5 and the Bankruptcy Code as a whole and cannot conclude that a computation of the value of the exchange is mandated." *Id.* at 128. Thus, the Tenth Circuit ruled that a transferee did not need to prove the specific quantum of "new value" provided to shield itself with the new value defense, thus permitting the transferee to retain all the funds it received from a failing debtor during the preference period while contributing just a fraction of that amount to the debtor's estate—a violation of the letter and spirit of § 547(c)(1).

Two years later, the Eleventh Circuit adopted a contrary approach in *Jet Florida, Inc. v. American Airlines, Inc.* (*In re Jet Fla. Sys., Inc.*), 861 F.2d 1555 (11th Cir. 1988), the leading case requiring a proponent of the new value defense to prove "specificity" of the value of the transferred asset. In *Jet Florida*, the preference defendant argued that § 547(c)(1) requires only proof that the debtor and the creditor intended that the debtor would receive *some unquantified new value* in the exchange but that the actual amount of new value that the debtor received at the time of the exchange was irrelevant. *Jet Florida* at 1558. The Eleventh Circuit rejected this

argument and held that the preference defendant must prove the *specific amount* of the new value that the debtor received, basing its decision on the principle that § 547(c)(1) protects preferential transfers only to the extent of the new value which the debtor received. *Id.* at 1558. The *Jet Florida* court "conclude[d] that Congress was clear in requiring that a party seeking the shelter of section 547(c)(1) must prove *the specific measure of the new value* given to the debtor in the exchange." *Id.* (emphasis added). The court went on to explain the policy rationale:

> American's interpretation of section 547(c)(1) would eviscerate the trustee's power to set aside preferential transfers. A creditor could retain the full value it received in exchange if it could show merely that the debtor and creditor intended for the "new value" to be worth *something*, however hypothetical or ephemeral. Section 547(c)(1) would become nothing more than an anti-fraud provision.

Jet Florida at 1559 (emphasis in the original).[6]

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[6] The Eleventh Circuit in *Jet Florida* distinguished *Rodman* on its facts. 861 F.2d at 1559 n.5. The Eleventh Circuit subsequently reaffirmed its "specificity" standard. *Official Unsecured Creditors' Comm. v. Airport Aviation Servs., Inc.* (*In re Arrow Air, Inc.*), 940 F.2d 1463, 1466 (11th Cir. 1991)

A year later, the Tenth Circuit, in *Lowrey v. U.P.G., Inc.* (*In re Robinson Bros. Drilling, Inc.*), 877 F.2d 32 (10th Cir. 1989), while claiming to interpret rather than overrule *Rodman*, followed the Eleventh Circuit's *Jet Florida* standard, holding that "it is the defendants' burden to prove *with specificity* that Richardson gave new value equivalent to the remainder of the debt not secured by these liens." *Id.* at 34 (emphasis added) (citing *In re Jet Fla. Sys., Inc.*, 861 F.2d at 1559). Subsequent courts then noted the inconsistencies between the *Rodman* and *Robinson Bros.* standards in the Tenth Circuit, with some interpreting *Robinson Bros.* to overrule *Rodman* in this regard,[7] and others observing that there was a need for clarification to resolve the internal circuit split.[8]

("[A] party relying on the protection provided by [§ 547(c)(1)] must prove with *specificity* the measure of new value given the debtor in the exchange transaction he seeks to protect—and the challenged payment is protected *only* to the extent of the specific measure of new value shown.") (emphasis in the original).

[7] *See Creditors' Comm. v. Spada* (*In re Spada*), 903 F.2d 971, 977 (3d Cir. 1990) (opining that the Tenth Circuit reversed *Rodman* with the *Robinson Bros.* decision); *Sulmeyer v. Suzuki* (*In re Grand Chevrolet, Inc.*), 25 F.3d 728, 733 (9th Cir. 1994) (opining that "the holding in *Rodman* has been narrowed by the Tenth Circuit in *In re Robinson Bros. Drilling*…").

[8] *See Rocin Liquidation Estate v. Alta AH & L* (*In re Rocor Int'l, Inc.*), 352 B.R. 319, 332 (Bankr. W.D. Okla. 2006) (noting the "somewhat mixed results" based on the differences in the *Rodman* and *Robinson Bros.* decisions); *Dill v. Brewer Oil Co.* (*In re Indian Capitol Distrib., Inc.*), 484 B.R. 394, 407 n.15 (Bankr. D.N.M. 2012) (noting differences in standards between

In 1990, the Third Circuit addressed the issue twice in quick succession and created yet another internal circuit split on the issue. On May 22, 1990, a Third Circuit panel in *Creditors' Comm. v. Spada* (*In re Spada*), 903 F.2d 971 (3d Cir. 1990) adopted the *Jet Florida* standard that a litigant "must prove the *specific measure* of the new value given to the debtor in the exchange." *In re Spada*, 903 F.2d at 976 (emphasis added). But one month later, on June 26, 1990, a different panel of the Third Circuit in *Reigle v. Mahajan* (*In re Kumar Bavishi & Associates*), 906 F.2d 942 (3d Cir. 1990), with one dissenting judge noting the inconsistency, held that proof of specific value was *not* required to sustain a "new value" defense, rejecting the Trustee's argument "that the value of the guarantee was too indeterminate in relation to the money received to satisfy section 547(c)(1)." *Id.* at 946. Instead, the *Kumar Bavishi* court held that the amount contributed to the debtor's estate "was sufficient" in relation to the amount transferred, without making a

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Rodman and *Robinson Bros.* but concluding that it need not resolve the matter because "because there is no dispute about the value of the fuel compared with what Indian Capitol was paying"); *see also* Law of Fraudulent Transactions, *Exceptions—Contemporaneous exchange exception—"New value"*, § 6:43 (2013) ("In *In re Robinson Brothers Drilling, Inc.*, the Tenth Circuit limited the broad language of *George Rodman* to the particular facts in issue (lien released equal to full amount of debtor's transfer), and adopted instead the *Jet Florida Systems* analysis. It may be, however, that the Tenth Circuit has yet to come down dispositively on the new value issue.").

specific determination of the actual new value provided.

That same year, the Ninth Circuit, in *Milchem, Inc. v. Fredman* (*In re Nucorp Energy*), 902 F.2d 729 (9th Cir. 1990), stated generally that "a court must measure the value given to the creditor and the new value given to the debtor in determining the extent to which the trustee may void a contemporaneous exchange," *id.* at 733 (quoting *In re Jet Fla. Sys., Inc.*, 861 F.2d at 1558-59), but failed to articulate any more precisely the standards courts should apply to measure the value. In 1994, in *Sulmeyer v. Suzuki* (*In re Grand Chevrolet, Inc.*), 25 F.3d 728 (9th Cir. 1994), the Ninth Circuit cited *Spada* with approval and held that a party seeking shelter of § 547(c)(1) must "prove the *specific measure* of the new value given to the debtor in the exchange". *Id.* at 733 (emphasis added).

But in 1997, the Eighth Circuit in *Jones Truck Lines, Inc. v. Central States, Southeast and Southwest Areas Pension Fund (In re Jones Truck Lines, Inc.)*, 130 F.3d 323 (8th Cir. 1997), reversed the trend again, following the *Rodman* and *Kumar Bavishi* line of reasoning (although not citing those cases or any sister court decisions). In *Jones Truck Lines*, the debtor transferred $6 million in employee benefit payments to the debtor's pension fund during the 90 day preference period. *See Jones Truck Lines*, 130 F.3d at 325. The trustee argued, in part, that the debtor did not receive back from the pension fund

the same $6 million in value, and that the pension fund "failed to quantify the 'new value' that [the debtor] received." *Id.* at 328 n.4. The Eighth Circuit, however, rejected the argument that the creditor was required to quantify with precision the new value, reasoning that the value of employee services is "*presumed* to equal the wages and benefits the employer contracted to pay." *Id.* (emphasis added).[9] Thus, the Eighth Circuit permitted a creditor to extract $6 million from the debtor during the preference period, without any evidentiary determination that the creditor provided that same value "in money or money's worth" to the debtor's estate.

Finally, in 2005, the Fifth Circuit joined the majority view and held that "it is the *precise benefit* received from the creditor, and not the secondary or tertiary effects thereof, that must fit within one of the five categories of 'new value'—i.e., money, goods, services, new credit, or the release of property—enumerated in § 547(a)(2)." *Baker Hughes Oilfield Operations, Inc. v. Cage* (*In re Ramba, Inc.*), 416 F.3d 394, 399-400 (5th Cir. 2005) (emphasis added). The Fifth Circuit reasoned: "To hold otherwise would render the enumerated categories of 'new value' in § 547(a)(2) essentially superfluous, since virtually any transaction between a creditor and debtor—including

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[9] In 1996, the Eighth Circuit decided another "new value" case, but did not articulate a standard for evidentiary review. *S. Technical Coll., Inc. v. Hood*, 89 F.3d 1381, 1385 (8th Cir. 1996).

the act of paying an antecedent debt—can ultimately be traced to some subsequent financial benefit to the debtor." *Ramba* at 400 n.3.[10]

In light of the majority and minority views summarized above, many courts and observers have noted that the bankruptcy and district courts apply wildly inconsistent evidentiary standards in analyzing the new value defense under § 547(c)(1), leading to inconsistent results under similar fact patterns.[11]

The instant case is just the latest example of the negative consequences flowing from the inconsistency of standards across the federal courts,

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[10] The Fifth Circuit's 2005 decision was consistent with its 2000 unpublished decision in *Southmark Corp. v. Schulte Roth & Zabel* (*In re Southmark Corp.*), No. 99-11401, 239 F.3d 365 (5th Cir. Nov. 7, 2000), which cited *Spada* and *Jet Florida* with approval and held that a creditor asserting the new value defense "is required to demonstrate the 'specific measure' of the new value received by the debtor." 2000 WL 1741550, at *3.

[11] *See* John F. Wagner Jr., *When is transfer from debtor for "new value" within meaning of §§ 547(a)(2) and 547(c) of Bankruptcy Code of 1978 (11 U.S.C.A. §§ 547(a)(2), 547(c))*, 111 A.L.R. Fed. 409 (1993); *see also, e.g., Manchester v. First Bank & Trust Co.* (*In re Moses*), 256 B.R. 641, 652 (B.A.P. 10th Cir. 2000) (requiring a showing that "the estate was replenished by an infusion of assets that are of *roughly equal value* to those that were transferred") (emphasis added); *Riley v. Nat'l Lumber Co.* (*In re Reale*), 393 B.R. 821, 828 (B.A.P. 1st Cir. 2008) ("The value given in a contemporaneous exchange must be the *approximate worth* of the asset transferred.") (emphasis added), *aff'd*, 584 F.3d 27 (1st Cir. 2009).

and provides this Court with an opportunity to clarify those standards. Here, the transferee (Hanover) extracted $1.375 million from the debtor during the preference period, but failed below to quantify with specificity the new value (if any) that it provided to the debtor. While the Fourth Circuit cited the "specificity" evidentiary standard set forth in *Jet Florida* and *Spada*,[12] the Fourth Circuit in fact adopted and applied the minority view (*i.e.*, the Third Circuit in *Kumar Bavishi*, the Tenth Circuit in *Rodman*, and the Eighth Circuit in *Jones Truck Lines*), and permitted Hanover to retain the full value of the funds it extracted, without identifying the alleged "money or money's worth" Hanover had provided in return. Instead, the panel majority merely compared the *face value* of the bonds it provided—*i.e.,* the revenue ESA expected to receive from the projects secured by those bonds, not the value of the bonds themselves—with the cost to the estate, without making any determination of the New Bonds' actual "money's worth":

> Hanover only needed to prove with specificity that the New Contracts *had a [face or nominal] value at least as great as the amount of the alleged preferential transfer in order to demonstrate that ESA's bankruptcy*

[12] In 2010, the Fourth Circuit in *United Rentals, Inc. v. Angell*, 592 F.3d 525, 533 (4th Cir. 2010), in *dicta*, cited with approval the Fifth Circuit's "precise benefit" standard, but did not squarely address the evidentiary standard.

> *estate had not diminished as a result of the transfer.*

App. at 21 (emphasis added).

The Fourth Circuit's reasoning was faulty, and the evidentiary standard was the critical factor in the case here, as it is in many other cases involving § 547(c)(1). The Fourth Circuit relied solely on the face value of *contracts that were secured by Hanover's bonds*, and failed to consider the *actual value of the bonds themselves*. The bonds themselves do not create revenue; they merely represent a contingent obligation for Hanover to ensure the work on the secured contracts is completed if ESA is unable to complete the work itself. Fourth Circuit Chief Judge William Traxler dissented from the panel majority's ruling, correctly reasoning that Hanover was not entitled to the "new value" defense because it had not demonstrated the value *of Hanover's bonds*. App. at 24-28 (Traxler, J., dissenting). The dissent in the Third Circuit's *Kumar Bavishi* decision also made clear that had the majority applied a different evidentiary standard, it would have reached a different result.[13]

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[13] *Kumar Bavishi & Assocs.*, 906 F.2d at 949 (Cowen, J., dissenting) ("In this case the bankruptcy court made no finding as to the value of the Appellee's alleged guarantor service to the debtor. Consequently, the court made no comparison of the relative values of the service and the preferential transfer. In fact, from the record before us it is clear that the Appellee utterly failed to offer proof as to the value of the alleged

Thus, the decision below turned entirely on what evidentiary standard a court should employ in assessing the "new value" defense—a standard that the federal courts should but currently do not apply consistently. This Court should grant certiorari to resolve the conflict exacerbated by the Fourth Circuit's decision below, and settle the standard of evidentiary review consistent with the statutory language, which requires that a preference defendant prove the actual "money or money's worth" of the alleged new value.

II. FACTUAL BACKGROUND

Prior to its bankruptcy on August 1, 2007, ESA operated an environmental, engineering, and construction firm that specialized in providing services to governmental agencies. App. at 2-3, 30, 51-52.

One of ESA's many regular capital requirements was to have funds to pay for

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guarantor service provided to the debtor. Since I 'conclude that a creditor must, as a part of its section 547(c)(1) affirmative defense, prove the specific valuation of the "money or money's worth in goods, services, or new credit" that the debtor received as "new value" in the contemporaneous exchange,' *Jet Florida*, 861 F.2d at 1559, I find, in keeping with this circuit's precedent, that the Appellee has not proven a section 547(c)(1) defense in this case.").

performance and payment bonds for the government construction contracts it serviced, in accordance with federal law. In 2006, in exchange for a fee, Hanover had provided ESA with the Old Bonds. By May 2007, ESA had not completed the work for those "old" government contracts. App. at 2-4, 30-31, 52-53.

On May 4, 2007, ESA requested that Hanover issue new bonds for four new government contracts, totaling $3.9 million in projected potential revenue (the "New Bonds"). Hanover agreed to issue New Bonds with the condition that ESA not only pay a fee, but also provide to Hanover additional security in the form of a letter of credit, which would act as collateral in case of default on the Old Bonds as well as the yet-to-be-issued New Bonds. App. at 2-4, 30-31, 52-53.

On May 14, 2007, Hanover and ESA entered into a letter of credit collateral agreement pursuant to Hanover's demand for additional security for both the Old Bonds and the New Bonds. On May 17, 2007, ESA transferred $1.375 million to SunTrust Bank ("SunTrust"), the issuer of the letter of credit. On May 18, 2007, SunTrust issued to Hanover the letter of credit which acted as collateral for Old Bonds as well as New Bonds. ESA purchased the New Bonds for a fee of $74,701. Hanover then delivered the New Bonds to ESA the same day. App. at 4-5, 31, 52-53.

On August 1, 2007, ESA filed for bankruptcy. App. at 5, 31-32, 53.

On August 6, 2007, Hanover drew the entire $1.375 million of the funds, now securing itself fully with cash from the ESA estate (because the cash securing the letter of credit belonged to the estate) to the detriment of every other ESA creditor that the Trustee is duty-bound to protect. App. at 5, 31-32, 53.

III. PRIOR COURT PROCEEDINGS

On July 31, 2009, the Trustee, as Chapter 7 trustee for ESA, filed a complaint in the United States Bankruptcy Court for the Western District of North Carolina seeking to avoid the preferential transfer of $1.375 million under § 547(b). Hanover moved for summary judgment, asserting defenses under § 547(c). The Trustee opposed. On November 3, 2010, after a hearing, the Bankruptcy Court granted Hanover's motion. The Bankruptcy Court reasoned that the transfer was not an avoidable transfer under § 547(b) because: (1) Hanover demonstrated that the funds were "earmarked" for a specific debt; (2) Hanover had a complete "new value" defense; and (3) on "equitable" grounds. App. at 50-58.

The Trustee filed a timely notice of appeal to the United States District Court for the Western

District of North Carolina. On September 22, 2011, the District Court affirmed the Bankruptcy's Court's dismissal of the Complaint on all three grounds. App. at 29-49.

On October 19, 2011, the Trustee filed a timely notice of appeal to the Fourth Circuit. On October 25, 2012, a three-judge panel of the Fourth Circuit heard oral argument. App. at 1.

On March 1, 2013, the Fourth Circuit panel unanimously reversed the Bankruptcy and District Courts on the "earmarking" defense, holding that the "bankruptcy court erred in its determination that the earmarking defense applies in this case" because "[t]he transfer from Prospect to ESA to SunTrust and later to Hanover lacks a critical element of an earmarking defense: the funds at issue were not used to pay an antecedent debt." App. at 9-15.

The panel also unanimously noted that the Bankruptcy and District Courts' ruling for Hanover on "equitable" grounds was unfounded, reasoning that "neither this court nor any other has recognized that such an equitable defense to a preference action exists." App. at 23 n.12.

Two of the three judges of the panel, however, ruled in favor of Hanover on the "new value" defense. The panel majority concluded that Hanover had sufficiently established its "new value" defense

based solely on one affidavit, which stated that the "government contracts awarded to ESA had a face amount *in excess of $3.9 million* and the New Bonds provided ESA with the ability to proceed with the new government contracts and *to earn revenues in excess of $1.375 million*—the face amount of the Letter of Credit." App. at 16 (emphasis added). The panel relied solely on the "face value" of the possible revenues that might be earned in the future pursuant to contracts secured by the bonds, and made no effort to assess the fair market value of the bonds themselves. App. at 16-23. In doing so, the panel majority critically missed the point – Hanover did not provide *contract revenues* to ESA (in the face amount of ESA's contracts or otherwise), it provided *bonds securing those contracts*, and any determination of the "new value" provided by Hanover turns on the actual "money or money's worth" of the bonds themselves.

Chief Judge Traxler dissented from the panel majority's holding on the new value defense, finding that "Hanover was not entitled to summary judgment on its new-value defense." App. at 24-28 (dissenting opinion). Chief Judge Traxler reasoned:

> Hanover does not argue, and could not argue, that it presented evidence that the New Contracts were goods or services that could be sold for at least $1.375 million in the marketplace. Rather, Hanover

contends that ESA received "new value" of at least $1.375 million in the form of the New Contracts because ESA expected to make that much profit by eventually completing its work under those contracts. *See* J.A. 584 (Cole affidavit). But regardless of what Hanover hoped to eventually receive, what it actually received was only a *conditional promise* to pay ESA money *at some point in the future*. Section 547, however, requires that the debtor's receipt of money, goods, services, new credit or property release be substantially contemporaneous with the debtor's payment. *See In re Teligent, Inc.*, 315 B.R. 308, 317 (Bankr. S.D.N.Y. 2004) (explaining that "[a] promise of future services . . . does not constitute 'new value.'"); *cf. Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 204 (1988) (discussing "new value" exception to absolute priority rule and stating that "[u]nlike 'money or money's worth,' a promise of future services cannot be exchanged in any market for something of value to the creditors *today*").

Indeed, the facts of this very case demonstrate why receipt of a conditional promise for payment at

> some indefinite future time does not constitute receipt of "new value" in the amount of the promised payment. In a "new value" transaction, the debtor's payment does not reduce the size of the estate because the money paid by the debtor is replaced by money, goods, services, new credit, or property releases of equivalent value. *See Angell*, 592 F.3d at 529. *Here, in contrast, Hanover successfully obtained $1.375 million from the estate without replacing it with equal value.* In so doing, Hanover jumped ahead of ESA's other unsecured creditors and received far more payment via the letter of credit than it otherwise could have received in bankruptcy. Thus, the bankruptcy court erred, in my view, in concluding that Hanover established the new-value defense.

App. at 26-28 (dissenting opinion) (footnotes omitted; emphasis added).

REASON FOR GRANTING THE PETITION

The petition should be granted because the Fourth Circuit's decision conflicts with decisions of other circuit courts, and deepens a circuit split on a

fundamental and recurring issue arising under the Bankruptcy Code. *See* S. Ct. Rule 10(a). This Court should not allow this inconsistent application of bankruptcy law and the resulting confusion to persist, but should grant certiorari to resolve the circuit split and clarify the evidentiary standard applicable to proof of "new value".

A. The Statutory Definition of "New Value", Legislative History, and Policy Rationales All Demonstrate that Congress Intended Courts to Construe "New Value" Narrowly and with Precision

Congress defined "new value" in Section 547 as follows:

> "new value" *means money or money's worth* in goods, services, or new credit, or release by a transferee of property previously transferred to such transferee in a transaction that is neither void nor voidable by the debtor or the trustee under any applicable law, including proceeds of such property, but does not include an obligation substituted for an existing obligation[.]

11 U.S.C. § 547(a)(2) (emphasis added).

This statutory definition demonstrates that Congress intended courts to apply the defense sparingly, in limited circumstances, and only where a party could identify precisely the "money or money's worth" transferred into the estate. The plain language of the statute, identifying new value as "money or money's worth," plainly calls for a precise analysis of the specific fair market value provided by a transfer to a preference defendant, rather than deference to the face amount of a contingent revenue stream secured by the transfer.

The Seventh Circuit has observed that the plain language of the "new value" statute calls for a precise determination of value:

> § 547(a)(2)'s definition of new value is exclusive. *See In re Fuel Supply and Terminaling, Inc.,* 72 B.R. 752, 757–58 (Bankr. S.D. Tex.1987). 11 U.S.C. § 102(3) states that "'includes' and 'including' are not limiting...." Congress, though, did not state that "new value *includes*"; Congress stated that "new value *means.*" Congress knew how to create an open-ended definition, and specifically stated how it would create an open-ended definition. By using "means" instead of "includes" in § 547(a)(2), Congress created an exclusive, rather than open-ended, definition for new value.

> *See* 1 L. King, *Collier on Bankruptcy* ¶ 101.00[2], at 101–15 (15th ed. 1987). ("Those [definitions] stating a definition in terms of 'means' attempt a precise definition"); *see also In re Olson,* 66 B.R. 687, 694 (Bankr. D. Minn.1986) (Waiver of future child support payments not new value because the waiver was not new value within § 547(a)(2)'s definition).

Energy Coop., Inc. v. SOCAP Int'l, Ltd. (*In re Energy Coop., Inc.*), 832 F.2d 997, 1003 (7th Cir. 1987) (emphasis in the original).

The legislative history, while "sparse," *In re Energy Coop. Inc.*, 832 F.2d at 1003, and "not a paradigm of clarity," *Cimmaron Oil Co. v. Cameron Consultants, Inc.*, 71 B.R. 1005, 1009-10 (N.D. Tex. 1987) (examining the legislative history of § 547(a)(2)), also reflects the intent of Congress that the § 547(c)(1) exception be of limited reach. The Senate and House Reports reflecting the purpose of § 547(c)(1) demonstrate that Congress intended to limit the scope of the new value defense, to ensure that values transferred in and out of the estate were precisely measured. The Reports each state, in pertinent part:

> Subsection (c) contains exceptions to the trustee's avoiding power. If a creditor can qualify under any one of

> the exceptions, then he is protected *to that extent*. If he can qualify under several, he is protected by each *to the extent that he can qualify under each*.

S. REP. NO. 95-989, pt. 1, at 88 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5874; H.R. REP. NO. 95-595, pt. 4, at 373 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6329 (emphasis added).

The policy rationale behind the new value defense also supports a requirement that parties establish that the "money or money's worth" transferred into the estate is equivalent to the money transferred out, to ensure that creditors are all treated fairly. The new value defense of § 547(c)(1) "is grounded in the principle that the transfer of new value to the debtor will offset the [preferential] payments, and the debtor's estate will not be depleted to the detriment of other creditors," *Gulf Oil Corp. v. Fuel Oil Supply & Terminaling, Inc. (In re Fuel Oil Supply & Terminaling, Inc.)*, 837 F.2d 224, 228 (5th Cir. 1988), as undeniably occurred here as a direct consequence of the court's using an incorrect evidentiary standard.

B. Contrary to the Fourth Circuit Decision Here, the Majority of the Circuits Considering the Evidentiary Standards for the "New Value" Defense Require Parties to Prove New Value with "Specificity"

Consistent with the statutory text, legislative history and policy rationales, the majority of the federal circuits require parties asserting the new value defense to prove with "specificity" the amount of new value provided.[14] Until the Fourth Circuit decision below, only the Eighth Circuit, and two outlier decisions in the Third and Tenth Circuits, allowed a relaxed, mere approximation standard of proof. The Fourth Circuit's decision is an authoritative addition to the minority view, deepening the circuit split on this important issue of bankruptcy law. Therefore, the Fourth Circuit's decision will likely cause the federal courts to reach even more inconsistent results when faced with the new value defense.[15]

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[14] *See Jet Fla., Inc. v. Am. Airlines, Inc.* (*In re Jet Fla. Sys., Inc.*), 861 F.2d 1555 (11th Cir. 1988); *Lowrey v. U.P.G., Inc.* (*In re Robinson Bros. Drilling, Inc.*), 877 F.2d 32 (10th Cir.1989); *Creditors' Comm. v. Spada* (*In re Spada*), 903 F.2d 971 (3d Cir. 1990).

[15] *See*, *e.g.*, Thomas J. Palazzolo, *New Value and Preference Avoidance in Bankruptcy*, 69 Wash. U. L.Q. 875, 876 (1991) ("Courts have read the Bankruptcy Code's definition of 'new value' expansively. This Note argues that such judicial expansions, unsupported by the statutory definition of "new value," tend to undercut the primary bankruptcy objective of facilitating equal distribution of a debtor's assets among creditors."); John F. Wagner Jr., *When is transfer from debtor for "new value" within meaning of §§ 547(a)(2) and 547(c) of Bankruptcy Code of 1978 (11 U.S.C.A. §§ 547(a)(2), 547(c))*, 111 A.L.R. Fed. 409 (1993) (summarizing caselaw in each of these categories and noting inconsistencies across the courts in application).

As one commentator observed:

> Courts have expanded the definition of new value to include forbearance of an existing remedy, forbearance in perfecting a statutory lien, a release of a letter of credit, and the making and honoring of a guarantee. Expanding the boundaries of new value provides the protection of the new value exceptions to many creditors. This, in turn, makes fewer transfers voidable. The net result is that creditors keep otherwise voidable transfers. This result undercuts the prime bankruptcy goal of equality of distribution among creditors.

Thomas J. Palazzolo, *New Value and Preference Avoidance in Bankruptcy*, 69 Wash. U. L.Q. 875, 883 (1991).

Adopting the minority view, the Fourth Circuit did not employ a rigorous evidentiary standard, and instead "[e]xpand[ed] the boundaries of new value". The Fourth Circuit ruled that Hanover "*did not need to demonstrate any exact figure*" to support the alleged "new value" it provided, and adopted the nominal face value of the contracts secured by the New Bonds as a sufficient

approximation of their value, despite (i) Hanover's failure to submit any evidence of the actual economic "money's worth" of its bonds to the estate, and (ii) the fact that the letter of credit cross-collateralized Old Bonds that plainly provided no new value to the estate. App. at 16-17 (emphasis added). Not requiring specificity severely undercuts the policy rationale behind the "new value" defense because, without proof of specific value, other creditors are adversely affected whenever the debtor's estate receives some purported indeterminate new value (here, a letter of credit as additional collateral for a series of Old and New Bonds) in exchange for an asset of tangible economic value (here, cash, leaving the estate to secure Old and New Bonds).

C. The "Specificity" Standard Was the Dispositive Issue in the Matter Below

The Fourth Circuit's application of the minority view was dispositive to its ultimate ruling in this case. The central question presented below in connection with the "new value" defense was whether the $1.375 million letter of credit that Hanover required ESA to post as collateral (cross-collateralizing pre-existing Old Bonds) before Hanover issued the New Bonds provided *any* "money's worth" in new value to ESA's estate at the time of the transfer on May 18, 2007, and if so, precisely how much.

At most, as Chief Judge Traxler recognized in dissent, the true "value" ESA received in exchange for posting the $1.375 million letter of credit was the purchase price Hanover charged ESA for the New Bonds.[16] Hanover charged ESA $74,701 for the New Bonds *plus* a condition that ESA post a letter of credit. Whatever the precise amount of new value was—$74,701 or some other amount—Hanover bore the burden to prove this new value "with specificity."[17]

Instead, Hanover contended, and a split panel of the Fourth Circuit agreed, that the new value Hanover provided was in the vicinity of the face amount of the contracts secured by Hanover's New Bonds—*i.e.*, $3.9 million. Chief Judge Traxler correctly identified the flaws in this reasoning. No rational economic actor, and certainly not a conservative insurance company like Hanover, would ever *contemporaneously* exchange $3.9 million in net present value for $1.375 million in net present value—a face loss of more than $2.5 million when

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[16] The Trustee in fact contends here that that Hanover's refusal to issue the New Bonds except with the posting of the letter of credit was an act of "forbearance" which does not constitute "new value". *See*, *e.g.*, *Drabkin v. A.I. Credit Corp.*, 800 F.2d 1153, 1159 n.7 (D.C. Cir. 1986) (forbearance from canceling insurance coverage did not constitute new value).

[17] *See* 11 U.S.C. § 547(g) ("[T]he creditor or party in interest against whom recovery or avoidance is sought has the burden of proving the nonavoidability of a transfer under subsection (c) of this section.").

examined at the time of the transaction. Hanover would not stay in business for long entering into transactions of such economically unsound proportions. Yet this is precisely what Hanover and the Fourth Circuit majority claimed Hanover did. The obvious truth is that the bonds issued by Hanover had a "money's worth" of far less than the contract revenues in the vicinity of their actual cost – *i.e.*, $74,701 – for purposes of § 547(c)(1), and Hanover presented no evidence to quantify their true "money's worth".

Chief Judge Traxler's dissent below identifies the fundamental flaw in the panel majority's reasoning. Contingent obligations like insurance or bonding contracts simply do not have a fair market value in "money or money's worth" equivalent—or usually even close—to their "face value". If they did, then a $10 million dollar life insurance policy would cost $10 million, paid up front. And a $3.9 million performance bond would cost exactly $3.9 million, no more and no less. That is not how the value of a contingent obligation is calculated, as Judge Traxler correctly noted. To prove the actual value of its bonds, Hanover would have had to show the contemporaneous "money's worth" as required by § 547(a)(2)—not the mere "face value" accepted without analysis by the panel majority—of its contingent obligation.

Had the lower courts here required Hanover to prove the alleged new value in "money or money's

worth" with specificity, then they would have identified these flaws. The lower courts' failure to require specific evidence of the "money's worth" of the alleged new value resulted in the incorrect outcome.

D. Because the Federal Courts Employ Inconsistent Evidentiary Standards in Assessing the "New Value" Defense, and Because the Decision Below Falls on the Wrong Side of the Split, this Court Should Grant Certiorari

Taken together, the Fourth Circuit's decision below regarding the "new value" defense, the dissent, the decisions of the sister circuits, and the "legion"[18] of inconsistent federal court decisions on the "new value" defense all demonstrate that the federal courts apply widely inconsistent standards in assessing and applying the "new value" defense under § 547(c)(1). This case presents important questions concerning the correct application of the guiding principles of the "new value" defense under § 547(c)(1). This Court should grant this petition for a writ of certiorari to resolve the circuit split, give effect to the plain language of the statute, and implement a uniform nationwide standard of review for "new value" defenses by preference defendants.

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[18] *In re Boston Pub. Co.*, 209 B.R. at 174.

CONCLUSION

For the foregoing reasons, the Trustee respectfully requests that the Court grant its petition for a writ of certiorari.

Date: June 27, 2013

Respectfully submitted,

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Appendix A

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 11–2150

IN RE: ESA ENVIRONMENTAL SPECIALISTS, INC.
Debtor.

STANLEY MARVIN CAMPBELL,
Plaintiff–Appellant,

v.

THE HANOVER INSURANCE COMPANY,
Defendant–Appellee.

Appeal from the United States District Court for the Western District of North Carolina, at Charlotte.

Argued: Oct. 25, 2012.
Decided: March 1, 2013.

Before TRAXLER, Chief Judge, and WILKINSON and AGEE, Circuit Judges

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Affirmed by published opinion. Judge Agee wrote the majority opinion, in which Judge Wilkinson joined. Chief Judge Traxler wrote a dissenting opinion.

COUNSEL

Allen Burton Shuford, The Bain Group, PLLC, Charlotte, North Carolina, for Appellant.

William L. Esser, Parker, Poe, Adams & Bernstein, LLP, Charlotte, North Carolina, for Appellee.

OPINION

AGEE, Circuit Judge:

The Trustee in bankruptcy of ESA Environmental Specialists, Inc. ("ESA") appeals from the affirmance by the district court of the award of summary judgment by the bankruptcy court to The Hanover Insurance Co. ("Hanover"). The bankruptcy court concluded that ESA's transfer of $1.375 million to Hanover within 90 days of ESA's filing a petition for bankruptcy was not an avoidable preference under 11 U.S.C. § 547(b). For the reasons set forth below, we affirm the award of summary judgment to Hanover.

I
Background and Proceedings Below

ESA was an environmental and industrial engineering firm that sought and performed construction projects under contract with the federal government. Pursuant to the Miller Act, ESA was required to obtain and furnish to the government two

types of surety bonds[1] as a condition precedent "[b]efore any contract of more than $100,000 [could be] awarded for the construction, alteration, or repair of any public building or public work of the Federal Government." 40 U.S.C. § 3131(b). These surety bonds functioned to secure ESA's obligation to complete its contract and pay its vendors and subcontractors. *See id.*

In 2006, Hanover issued surety bonds on behalf of ESA prior to the federal government's award of eight contracts to ESA (the "Existing Projects"). In April 2007, ESA borrowed $12.2 million from Prospect Capital Corp. ("Prospect") to, among other things, meet current working capital needs, repay existing indebtedness, and "fund costs associated with entering into and fulfilling government contracts." (J.A. 655.) In May 2007, ESA asked Hanover to issue additional surety bonds (the "New Bonds") in conjunction with seven additional government contracts that ESA sought to obtain (the "New Contracts" and collectively with the Existing Projects, the "Government Contracts"). ESA could not commence work on the New Contracts until it tendered the New Bonds to the appropriate government agencies, as the New Bonds were a condition precedent to the final contract award to ESA. Hanover, concerned about ESA's financial stability, would not issue the New Bonds without

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[1] The surety bonds included performance bonds to protect the government if the contractor failed to complete a contract, 40 U.S.C. § 3131(b)(1), and payment bonds to protect "all persons supplying labor and material in carrying out the work provided for in the contract," *id.* § 3131(b)(2).

additional security over and above the bond premiums. The parties agreed upon a letter of credit as the additional security by which Hanover would agree to issue the New Bonds. ESA was required to obtain an irrevocable letter of credit from SunTrust Bank ("SunTrust") in the amount of $1.375 million with Hanover as the beneficiary (the "Letter of Credit"). The Letter of Credit would collateralize the New Bonds but also all of Hanover's existing guarantees and surety obligations on behalf of ESA. The bond premiums on the New Bonds totaled $74,624, and the face value of the New Bonds totaled $7.9 million.

As a condition precedent to issuance of the Letter of Credit, SunTrust required ESA to fund a certificate of deposit at Sun–Trust in the amount of $1.375 million (the "CD") as security for the Letter of Credit. ESA had limited cash reserves, so it turned to Prospect for the additional capital necessary to fund the CD. Prospect and ESA then amended their existing credit agreement to increase the principal amount of Prospect's existing loan to ESA by a total of $1.575 million (the "Prospect Loan").[2] On May 8 and May 17, 2007, in two separate transfers, Prospect tendered the Prospect Loan funds directly to ESA, and ESA deposited those funds into its bank

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[2] Prospect and ESA first amended their existing credit agreement on May 7, 2007, to increase the principal amount of Prospect's loan to ESA by $625,000, from $12.2 million to $12.825 million. On May 17, 2007, Prospect and ESA executed a second amendment to their existing credit agreement, increasing the principal amount of the loan by an additional $950,000, from $12.825 million to $13.775 million.

account. On May 17, 2007, ESA transferred $1.375 million of the Prospect Loan proceeds to SunTrust to fund the CD to secure the Letter of Credit for Hanover.[3] SunTrust then issued the Letter of Credit, and Hanover in turn issued the New Bonds, which ESA delivered to the appropriate federal government agencies for final award of the New Contracts.

Despite being awarded the New Contracts, ESA's financial condition continued to deteriorate and it filed a voluntary Chapter 11 petition in the United States Bankruptcy Court for the Western District of North Carolina on August 1, 2007. Hanover then drew on the Letter of Credit, receiving the $1.375 million face amount from SunTrust, which liquidated the CD.

In the course of ESA's bankruptcy proceeding, the bankruptcy court approved the sale of substantially all of ESA's assets to Prospect. As part of that sale, ESA assigned to Integrated Contract Services ("ICS"), an affiliate of Prospect, (i) its rights under the Government Contracts, (ii) all of its litigation claims or causes of action, including its preference and avoidance claims (the "Litigation Rights"), and (iii) its right to the return of any collateral remaining upon the completion of the Government Contracts. Shortly thereafter, ICS ceased operations and assigned ESA's assets, including the Litigation Rights, back to Prospect. Neither ICS nor Prospect commenced work on the Government Contracts, but Hanover remained bound by the surety bonds to

[3] Apparently, ESA used the remaining $200,000 of the Prospect Loan funds in its operations, and that amount is not at issue in this appeal.

provide for successful completion of those contracts.

In February 2008, the bankruptcy court entered an order allowing Hanover to take responsibility for the completion of the Government Contracts. Hanover represents, without contradiction, that "[s]ince entry of that order, Hanover fulfilled its obligations ..., including ensuring that the [G]overnment [C]ontracts were completed and subcontractors paid." (Appellee's Br. 7.)

Also in February 2008, on Prospect's motion, the bankruptcy court entered an order converting ESA's case from Chapter 11 to a Chapter 7 proceeding and directing the appointment of a Chapter 7 trustee. Stanley Campbell was duly appointed as the Chapter 7 trustee for ESA (the "Trustee") and took control of ESA's bankruptcy estate. In July 2009, the bankruptcy court entered an order approving a stipulation agreement between Prospect and the Trustee, under which Prospect assigned the Litigation Rights to the Trustee, and the Trustee agreed to split the proceeds from any successful actions with Prospect.[4]

Subsequently, the Trustee filed an adversarial proceeding against Hanover, alleging that Hanover was an indirect beneficiary of ESA's transfer of the Prospect Loan proceeds into the CD and that this transfer was an avoidable, preferential transfer under 11 U.S.C. § 547. Hanover asserted two affirmative defenses to the Trustee's claims in the

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[4] Under the stipulation agreement, Prospect would receive 75 percent of the balance of any proceeds after costs and fees. ESA's bankruptcy estate would retain the remaining 25 percent for distribution to ESA's creditors, including Prospect.

bankruptcy court: (1) that the transfer was not a preference because the Prospect Loan proceeds were earmarked specifically for payment to Hanover, and (2) that ESA received new value in exchange for the Prospect Loan proceeds. Hanover contended either of these affirmative defenses barred the Trustee's claims as a matter of law and moved for summary judgment.

The bankruptcy court granted summary judgment in favor of Hanover, holding both the earmarking and new value defenses applied to prevent a determination that ESA's transfer of funds was a preferential transfer and avoidable by the Trustee. Further, the bankruptcy court also opined that "[i]t would be inequitable to require Hanover to return the portion of the Prospect [Loan] used to cover the costs to complete the [Government Contracts] when Hanover did the work, and paid the obligations." (J.A. 924.) The Trustee appealed the bankruptcy court's judgment to the United States District Court for the Western District of North Carolina, which affirmed. From the district court's affirmation of the bankruptcy court's grant of summary judgment, the Trustee now timely appeals. We have jurisdiction under 28 U.S.C. §§ 158, 1291.

II
Standard of Review

When considering an appeal from a district court acting in its capacity as a bankruptcy appellate court, we conduct an independent review of the bankruptcy court's decision, reviewing factual

findings for clear error and legal conclusions de novo. *See Banks v. Sallie Mae Serv. Corp. (In re Banks),* 299 F.3d 296, 300 (4th Cir.2002). A bankruptcy court properly grants summary judgment when no genuine issues of material fact exist and "the movant is entitled to judgment as a matter of law." Fed.R.Civ.P. 56(a).

A trustee in bankruptcy

> may avoid any transfer of an interest of the debtor in property—
> (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 ... on or within 90 days before the date of the filing of the petition; ...
> (5) that enables such creditor to receive more than such creditor would receive if ... the transfer had not been made.

11 U.S.C. § 547(b). The trustee bears the burden of proving the avoidability of a transfer under § 547(b). *Id.* § 547(g).

III
Analysis

Hanover does not contest that the Trustee has

presented a prima facie case under § 547(b) for the avoidance of the transfer to it of the $1.375 million. Instead, Hanover contends that it has established three affirmative defenses to avoidance: earmarking, new value, and equity. First, the Trustee argues that the bankruptcy court improperly applied the earmarking defense because ESA did not use the Prospect Loan proceeds to pay an antecedent debt. Second, the Trustee argues that the bankruptcy court improperly applied the new value defense because Hanover did not prove with specificity the amount of the new value it provided ESA and the bankruptcy court clearly erred in its findings of fact. Third, the Trustee argues that the bankruptcy court improperly held in favor of Hanover on independent equitable grounds, which are not recognized as a defense to an avoidance action in bankruptcy. We address each argument in turn.

A
Earmarking

The earmarking defense in bankruptcy is a judicially created exception to the statutory power of the bankruptcy trustee under § 547 to avoid or set aside an otherwise preferential transfer of assets.[5]

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[5] As a judicially created exception to a statutory rule, the earmarking defense must be narrowly construed. *See Sheppard v. Riverview Nursing Ctr., Inc.,* 88 F.3d 1332, 1344 n. 5 (4th Cir.1996) (noting that the "special circumstances" exception under 42 U.S.C. § 2000e–5(g)(2)(B) "is judicially created and should be narrowly construed" (citing *Hatfield v. Hayes,* 877 F.2d 717, 720 (8th Cir.1989))); *see also Storm v. Storm,* 328 F.3d 941, 944 (7th Cir.2003) ("[T]he probate exception, as a

See McCuskey v. Nat'l Bank of Waterloo (In re Bohlen Enters., Ltd.), 859 F.2d 561, 565 (8th Cir.1988). The earmarking defense applies "[w]hen a third person makes a loan to a debtor specifically to enable that debtor to satisfy the claim of a designated creditor." 5 *Collier on Bankruptcy* ¶ 547.03 [2][a] (16th ed. 2011); *see Va. Nat'l Bank v. Woodson (In re Decker),* 329 F.2d 836, 839 (4th Cir.1964) (holding that a transfer was not an avoidable preference when it "was made for the specific purpose of paying at least a portion of a particular debt"). The proceeds of such an "earmarked" loan "never become part of the debtor's assets and therefore no preference is created" because the transfer does not diminish the value of the debtor's estate.[6] 5 *Collier on Bankruptcy* ¶

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judicially created exception to the statutory grant of diversity jurisdiction, should be construed narrowly."); *Love v. Deal,* 5 F.3d 1406, 1410 (11th Cir.1993) ("Because the special circumstances exception is a judicially created concept, we have held that it should be construed narrowly so as not to interfere with the congressional purposes behind the fee award statutes.").

[6] While § 547(a) clearly establishes that the trustee in bankruptcy bears the ultimate burden of proof of the avoidability of a transfer under § 547(b), the burden as to the earmarking defense is not as clear. A majority of the Circuits hold that, once the trustee meets his burden of proving the avoidability of a transfer under § 547(b), the burden "shifts to the defendant in the preference action to show that the funds were earmarked." *Schubert v. Lucent Tech. Inc. (In re Winstar Commc'ns, Inc.),* 554 F.3d 382, 401 (3d Cir.2009) (quoting *Metcalf v. Golden (In re Adbox, Inc.),* 488 F.3d 836, 842 (9th Cir.2007)) (quotation marks omitted); *see Chase Manhattan Mortg. Corp. v. Shapiro (In re Lee),* 530 F.3d 458, 470 (6th Cir.2008) (placing the burden of proving the earmarking

547.03[2][a]; *see Decker,* 329 F.2d at 839 ("As a general rule, such a payment, in and of itself and without more, will not create a voidable preference since there has been no diminution of the value of the estate.").

This Circuit has previously recognized the earmarking defense in *Decker,* but only in the limited circumstance of a direct payment from one creditor to another. 329 F.2d at 839. In *Decker,* the debtor had overdrawn his bank accounts by about $8,000. *Id.* at 838. Shortly before filing for bankruptcy, the debtor's sister paid the bank the existing $8,000 debt to cover the overdrafts and became a creditor of the debtor in approximately the same amount as he had owed the bank. *Id.* at 839. The debtor's trustee in bankruptcy attempted to avoid the $8,000 transfer from the debtor's sister to the bank as preferential, arguing that the payment was in essence a loan to the debtor and that the debtor's estate diminished when the $8,000 was paid to the bank. *Id.*

In considering this argument, we first noted the basic principle of bankruptcy that, "[i]f an unconditional loan is made to a bankrupt, the loan proceeds become part of the bankrupt's free assets."

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defense on the defendant). The Eighth Circuit holds, however, that "the trustee [has] the burden to prove the earmarking defense does not apply." *Kaler v. Cmty. First Nat'l Bank (In re Heitkamp),* 137 F.3d 1087, 1089 (8th Cir.1998). We need not resolve this conflict in order to answer the earmarking issue in this case because the undisputed facts establish that the earmarking defense does not apply as a matter of law, as we more fully discuss below.

Id. We then concluded that "in the case at bar, it is clear ... that the payment of the $8,000.00 by Miss Decker was not an unconditional loan for the benefit of all creditors but was made for the specific purpose of paying at least a portion of a particular debt owed to the bank." *Id.* at 839. We concluded that "[a]s a general rule, such a payment, in and of itself and without more, will not create a voidable preference since there has been no diminution of the value of the estate." *Id.* We then stated that "[t]he test is not what the creditor receives but what the bankrupt's estate has lost. It is the diminution of the bankrupt's estate, not the unequal payment to creditors, which is the evil sought to be remedied by the avoidance of a preferential transfer."[7] *Id.* at 840.

Since our opinion in *Decker,* courts have uniformly held that the earmarking defense applies "whether the proceeds of the loan are transferred directly by the lender to the creditor or are paid to the debtor with the understanding that they will be

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[7] It may be useful to give a generic example of a transfer that should qualify as an earmark that is not an avoidable preference in bankruptcy. If X chose to pay debtor A's debt to creditor Y, there is a preference received by creditor Y when compared to all debtor A's other creditors: that is, Y got paid before any of A's similarly situated creditors were paid. But, for bankruptcy purposes, the debtor's bankruptcy estate is unchanged: its assets are no greater and no less than before the transfer from X to Y. In liquidation of A's bankruptcy estate, A's creditors would receive no less than they would have received had the X to Y transaction never taken place. In effect, the transfer of assets from X to Y resembles a novation as X simply takes the place of creditor Y with respect to debtor A.

paid to the creditor in satisfaction of his claim, so long as the proceeds are clearly 'earmarked.' " 5 *Collier on Bankruptcy* ¶ 547.03[2][a]. Courts continue to recognize, though, that "[a] payment by a debtor with borrowed money ... may constitute a preference when the loan so used was not made upon the condition that it should be applied to the particular creditor to whom it was paid over." 5 *Collier on Bankruptcy* ¶ 547.03[2][a] (citing *Brown v. First Nat'l Bank of Little Rock,* 748 F.2d 490, 492 n. 6 (8th Cir.1984); *Smyth v. Kaufman (In re J.B. Koplik & Co.),* 114 F.2d 40, 42 (2d Cir.1940)).

The bankruptcy court here correctly recognized that the Fourth Circuit adopted the concept of the earmarking defense as an affirmative defense in bankruptcy in *Decker.* However, the bankruptcy court erred in its determination that the earmarking defense applies in this case. The transfer from Prospect to ESA to SunTrust and later to Hanover lacks a critical element of an earmarking defense: the funds at issue were not used to pay an antecedent debt.

The $1.375 million at issue in this case was not transferred directly from creditor to creditor, i.e., from Prospect to Hanover. Instead, ESA received the funds from Prospect, placed the funds in its own bank account, and only later deposited the funds with SunTrust to secure Hanover. The parties argue at length over whether ESA had control over the Prospect Loan proceeds so that those funds could not be deemed earmarked under our precedent in *Decker.* Resolution of that factual dispute, however, is irrelevant to the determination of whether

Hanover's earmarking defense applies because Hanover failed to prove a fundamental element of earmarking—that the transferred funds paid an antecedent debt of the debtor, ESA.

The earmarking doctrine applies only when the debtor borrows money from one creditor and the terms of that agreement require the debtor to use the loan proceeds to extinguish specific, designated, existing debt. *See* 5 *Collier on Bankruptcy* ¶ 547.03[2][a] (citing *Brown,* 748 F.2d at 492 n. 6; *Smyth,* 114 F.2d at 42). "Accordingly, the proper inquiry is ... whether the debtor had the right to disburse the funds to whomever it wished, or whether [the] disbursement was limited to a particular old creditor or creditors under the agreement with the new creditor." *Adams v. Anderson, (In re Superior Stamp & Coin Co.),* 223 F.3d 1004, 1009 (9th Cir.2000). Without the satisfaction of an antecedent debt of the debtor by the new creditor, the concept of earmarking cannot apply: there is no debt by which one creditor is substituted for another. *See Decker,* 329 F.2d at 838 ("It is clear that it was the intention of Vivian Decker[, as a new creditor,] that the $8,000.00 paid by her to the bank was to be applied toward satisfaction of an antecedent debt of Decker[, the debtor in bankruptcy,] to the bank."). In the case at bar, a new debt was created where none previously existed.

Even were we to assume, *arguendo,* that Prospect loaned ESA the funds at issue for the specific purpose of securing Hanover, ESA did not use the loan proceeds to pay an existing debt. Here, ESA

borrowed money from Prospect—incurring new debt—and used those funds to collateralize both existing obligations to Hanover as well as the New Bonds—a new debt not previously owed to any creditor. ESA did not use the Prospect Loan funds to pay antecedent or old debt, nor did ESA merely substitute one creditor for another so that the pot available to pay existing creditors was unaffected by the transfer. To the contrary, ESA now owes a much higher total debt than it did before the Prospect Loan, thereby diminishing the share available from ESA's bankruptcy estate for repayment of ESA's existing creditors.

Hanover does not contest that ESA used the Prospect Loan proceeds to secure its obligations to Hanover rather than to pay an antecedent debt. Nor does Hanover assert that ESA in fact substituted one creditor for another. Consequently, the earmarking defense cannot apply in this case. The bankruptcy court therefore erred in holding that an earmarking defense applied to prevent the Trustee from avoiding the transfer to Hanover under § 547.[8]

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[8] Moreover, the bankruptcy court made a legally inconsistent determination that Hanover established both a complete earmarking defense and a complete new value defense. As an element of the earmarking defense, the defendant in an avoidance action must prove that the alleged preferentially transferred funds were used to pay an antecedent debt. As discussed in more detail below, the new value defense applies in the opposite situation—when the allegedly preferentially transferred funds were used not to pay antecedent debt, but, instead, to support a new transaction. *See United Rentals Inc. v. Angell,* 592 F.3d 525 (4th Cir.2010) ("[The new value defense] was designed to prevent trustees from avoiding payments that

B
New Value

In contrast to the judicially created earmarking defense, the "new value" defense is an explicit statutory defense to a § 547(b) preference action:

> The trustee may not avoid under this section a transfer—
> (1) to the extent that such transfer was—
> (A) intended by the debtor and the creditor to or for whose benefit such transfer was made to be a contemporaneous exchange for new value given to the debtor; and
> (B) in fact a substantially contemporaneous exchange.

11 U.S.C. § 547(c)(1). The statute defines "new value" as

> money or money's worth in goods, services, or new credit, or release by a transferee of property previously transferred to such transferee in a

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were clearly intended to support a new transaction, instead of an antecedent debt." (quoting *Batlan v. TransAmerica Comm. Fin. Corp. (In re Smith's Home Furnishings, Inc.),* 265 F.3d 959, 965 n. 4 (9th Cir.2001)) (internal quotation marks omitted)). Thus, at least in most circumstances, the earmarking and new value defenses are mutually exclusive.

> transaction that is neither void nor voidable by the debtor or the trustee under any applicable law, including proceeds of such property, but does not include an obligation substituted for an existing obligation.

11 U.S.C. § 547(a)(2). Congress intended § 547(c)(1) "to encourage creditors to continue to deal with troubled debtors" by "prevent[ing] trustees from avoiding payments that were clearly intended to support a new transaction, instead of an antecedent debt." *United Rentals,* 592 F.3d at 529 (quoting 5 *Collier on Bankruptcy* ¶ 547.04[1]; *Batlan,* 265 F.3d at 965 n. 4) (internal quotation marks omitted). A payment may support a new value defense even if the debtor receives it "from a party other than the creditor." 5 *Collier on Bankruptcy* ¶ 547.04[1][c]. When evaluating a new value defense, the key question is whether the alleged preferential transfer diminished the debtor's estate, i.e., whether the debtor in fact acquired a new asset that offset the loss in value to the estate when the debtor transferred existing assets to acquire the new asset at issue. *See id.*

The party asserting the new value defense (Hanover, in this case) bears the burden of proof. *See United Rentals,* 592 F.3d at 531. As part of that burden, the party asserting the new value defense must prove that (1) "the parties *intend* [ed] the transaction to be substantially contemporaneous" and (2) "the exchange of new value between the debtor and the defendant [was] *in fact* ...

substantially contemporaneous." 5 *Collier on Bankruptcy* ¶ 547.04[1] [a] & [b]. The party bearing the burden of proof also "must prove with specificity the new value given to the debtor." *Jet Fla., Inc. v. Am. Airlines, Inc. (In re Jet Fla. Sys., Inc.),* 861 F.2d 1555, 1559 (11th Cir.1988); *see Lowrey v. U.P.G., Inc. (In re Robinson Bros. Drilling, Inc.),* 877 F.2d 32, 34 (10th Cir.1989); *see also* 5 *Collier on Bankruptcy* ¶ 547.04 n. 6.

As to the new value defense element of intent to make a contemporaneous exchange, § 547(c)(1)(A), the Trustee does not dispute that ESA and Hanover intended the $1.375 million transfer to be a contemporaneous exchange for new value in the form of the New Contracts.[9][10] The Trustee does argue,

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[9] In representations to this Court at oral argument, Hanover proffered that it would use only part of the $1.375 million it received from drawing on the Letter of Credit in fulfilling the New Contract obligations. Hanover stated that it would be in a position to return the remaining collateral, estimated to be between $500,000 and $600,000, to ESA's bankruptcy estate upon final completion of the remaining New Contracts. We consider Hanover's proffer to the Court to be its affirmative obligation to fulfill by tendering the remaining collateral funds to the Trustee on behalf of the bankruptcy estate.

[10] The Chief Judge, in dissent, argues that Hanover failed to meet its burden of proving that the New Contracts had a commercial value of at least $1.375 million. Yet the Trustee admitted that the New Contracts were, in and of themselves, an asset with an ascertainable value. That is not surprising, as the transfer of contracts—whether as an asset for sale or as secured collateral—is a commonplace factor of commercial life. That the New Contracts were indeed a fungible commercial asset—and clearly "new value" for § 547(c) purposes—is well represented by the facts of this case. Not only were the New Contacts an

however, that the bankruptcy court erred in its new value determination for all other § 547(c)(1) purposes in two ways. First, the Trustee contends that Hanover failed to carry its burden of proof in the bankruptcy court to establish with specificity the exact measure of the new value received by ESA and that the bankruptcy court clearly erred in its finding that the New Contracts had a value in excess of $1.375 million. Second, the Trustee argues that the bankruptcy court clearly erred in its conclusion that ESA in fact received the New Contracts in contemporaneous exchange for its transfer to Hanover, notwithstanding the intent of the parties.

Because these arguments focus on the bankruptcy court's findings of fact regarding the value of the New Contracts, we reiterate that we apply clear error review. *Banks,* 299 F.3d at 300. This means that we will not reverse the trial court's finding of fact that has support in the evidence unless that finding is clearly wrong. *Chesapeake Lighterage & Towing Co. v. Balt. Copper Smelting & Rolling Co.,* 40 F.2d 394, 395 (4th Cir.1930). Applying this standard of review, the Trustee's arguments fail.

The Trustee does not contest that the New Contracts have value—he states in his reply brief that the measure of value of these contracts "is the expectation of the parties at the time of the transfer." (Reply Br. 17 (citing *Creditors' Comm. v. Spada (In re Spada),* 903 F.2d 971, 975 (3d Cir.1990)).) Instead, what the Trustee argues is that Hanover failed to meet its burden of proving the value of the New

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item given as collateral, but were indeed bought and conveyed among ESA, ICS, Prospect and, ultimately, Hanover.

Contracts with the requisite specificity. The thrust of the Trustee's position is that Hanover presented evidence demonstrating only a vague assertion that the New Contracts had value "in excess of $1,375,000" and thus failed to prove with specificity the amount of the new value ESA received. We disagree.

Below, Hanover asserted, and the bankruptcy court agreed, that ESA received new value in the form of the New Contracts as a result of the transfer of funds (from Prospect to ESA to SunTrust to Hanover).[11] In finding that the New Contracts constituted new value in excess of the transferred asset, the $1.375 million cash, the bankruptcy court relied on the affidavit of ESA's former Chief Executive Officer, Charles Jacob Cole, (the "Cole Affidavit") who stated that the "government contracts awarded to ESA had a face amount in excess of $3.9 million and the New Bonds provided ESA with the ability to proceed with the new government contracts and to earn revenues in excess of $1,375,000—the face amount of the Letter of Credit." (J.A. 584.) The Trustee introduced no evidence to contradict the Cole Affidavit or to establish any other measure of value for the New Contracts. Neither before the bankruptcy court, the district court, nor this court has the Trustee

[11] The bankruptcy court also concluded that ESA received new value from Hanover in the form of the New Bonds. Because we conclude that the bankruptcy court did not clearly err in its finding regarding the value of the New Contracts, we do not address the bankruptcy court's determination regarding the New Bonds as new value.

contended that Hanover's evidence, the Cole Affidavit, was inherently incredible or that Mr. Cole was being untruthful. The Trustee simply disagreed with Mr. Cole's conclusion.

Once Hanover offered its uncontradicted evidence that ESA received new value in excess of $1.375 million—the amount of the alleged preferential transfer—Hanover did not need to demonstrate any exact figure beyond that amount. Hanover only needed to prove with specificity that the New Contracts had a value at least as great as the amount of the alleged preferential transfer in order to demonstrate that ESA's bankruptcy estate had not diminished as a result of the transfer. Thus, on the record evidence before the bankruptcy court that the value of the New Contracts met or exceeded the amount of the alleged preferential transfer—the $1.375 million—the court did not err in concluding that Hanover had carried its burden to "prove with specificity the new value given to the debtor." *Jet Fla.,* 861 F.2d at 1559.

Relatedly, the Trustee also argues that the bankruptcy court's finding of fact that the New Contracts constituted new value in excess of $1.375 million was clearly erroneous. Although the Trustee disagreed with Hanover's proposed valuation of the New Contracts, the Trustee wholly failed to present any evidence that contradicts Hanover's valuation evidence or conflicts with the bankruptcy court's finding regarding the value of the New Contracts. Once Hanover presented credible evidence regarding the value of the New Contracts, the burden shifted to the Trustee to present some competent evidence

supporting his position to defeat Hanover's motion for summary judgment. The Trustee did not do so. *See Parrish ex rel. Lee v. Cleveland,* 372 F.3d 294, 308–09 n. 17 (4th Cir.2004) ("If the movant presents credible evidence that, if not controverted at trial, would entitle him to a Rule 50 judgment as a matter of law that evidence must be accepted as true on a summary-judgment motion when the party opposing the motion does not offer ... evidentiary material supporting the opposing contention." (quoting 10A Charles Alan Wright et al., *Federal Practice & Procedure* § 2727 (3d ed.1998))). The Trustee simply failed to carry his burden of persuasion once Hanover met its burden of proof. Thus, the bankruptcy court did not clearly err in its finding that the New Contracts constituted new value in excess of $1.375 million.

As to the Trustee's second argument—that any new value ESA received was not, as a matter of fact, contemporaneously exchanged for the $1.375 million transfer of funds—the Trustee conflates two very different concepts, the value of the New Contracts, which have value in and of themselves, and the eventual revenues ESA would have received upon performance of the New Contracts. While the Trustee correctly points out that ESA did not receive the actual revenues under the New Contracts in contemporaneous exchange for the transfer to Hanover, the Trustee fails to recognize that the New Contracts had a value in and of themselves in excess of $1.375 million based on the record in this case. We find no clear error in the bankruptcy court's finding of fact that the flow of funds from Prospect to ESA to

SunTrust (for Hanover) and the award of the New Contracts was in fact a "substantially contemporaneous exchange" of assets. The bankruptcy court's finding recognized the ordinary flow of a commercial transaction in obtaining a loan and conveying its proceeds to acquire a new asset, which in this case was the New Contracts. The bankruptcy court did not clearly err in concluding that ESA received the New Contracts in a substantially contemporaneous exchange for the transfer to Hanover.

The bankruptcy court therefore properly held that Hanover carried its burden to prove all the elements of the new value defense under § 547(c)(1) so as to bar the Trustee from avoiding the transfer of the $1.375 million to Hanover.[12]

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[12] Hanover asserts that the bankruptcy court also ruled in its favor on separate equitable grounds. Because we affirm the bankruptcy court's application of the new value defense, we address Hanover's equitable defense only to note that neither this court nor any other has recognized that such an equitable defense to a preference action exists. *See Norwest Bank Worthington v. Ahlers,* 485 U.S. 197, 206, 108 S.Ct. 963, 99 L.Ed.2d 169 (1988) ("[W]hatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code.") Even the single case that Hanover cites to support its equitable grounds defense provides it no support. *See Kmart Corp. v. Uniden Am. Corp. (In re Kmart Corp.),* 318 B.R. 409, 415 (Bankr.N.D.Ill.2004) (holding that, apart from threshold defenses such as "lack of in personam jurisdiction, service of process, standing, and the like," "the enumerated 547(c) preference exceptions are the exclusive defenses to liability for an otherwise avoidable preferential transfer").

IV
Conclusion

Although the bankruptcy court erred in finding that the earmarking defense applied in this case, we find no error in its determination that Hanover is entitled to the new value defense under § 547(c) to the Trustee's claim of a preferential transfer. We therefore affirm the judgment of the bankruptcy court awarding summary judgment to Hanover.

AFFIRMED

TRAXLER, Chief Judge, dissenting:

Because I believe Hanover was not entitled to summary judgment on its new-value defense, I respectfully dissent.

The Bankruptcy Code's preference section serves two goals. First, it prevents companies "from racing to the courthouse to dismember the debtor during his slide into bankruptcy." *Harmon v. First Am. Bank of Md. (In re Jeffrey Bigelow Design Group, Inc.),* 956 F.2d 479, 487 (4th Cir.1992) (internal quotation marks omitted). And second, it protects "equality of distribution among creditors." *Id.* (internal quotation marks omitted).

Section 547(c) provides exceptions for certain preferential transfers, the avoidance of which would not further the purposes of § 547(b). *See* 11 U.S.C. § 547(b), (c). Section 547(c)(1) provides that a transfer cannot be avoided "to the extent [it] was ... intended by the debtor and the creditor to or for whose benefit

[it] was made to be a contemporaneous exchange for *new value* given to the debtor; and [it was] in fact a substantially contemporaneous exchange." 11 U.S.C. § 547(c)(1) (emphasis added). The statute defines "new value," as is relevant here, as "money or money's worth in goods, services, or new credit, or release by a transferee of property previously transferred to such transferee." 11 U.S.C. § 547(a)(2).

The purpose of the § 547(c)(1) exception is "to encourage creditors to continue to deal with troubled debtors without fear that they will have to disgorge payments received for value given." *Collier on Bankruptcy* ¶ 547.04 (Alan N. Resnick & Henry J. Sommer eds., 16th ed. 2012). As the legislative history demonstrates, § 547(c)(1) was intended to address the "generic problem that those on the verge of bankruptcy still need to buy things and the fact that checks are used (with a brief gap between purchase and payment) ought not render the payment avoidable as one made for an antecedent debt." *United Rentals, Inc. v. Angell,* 592 F.3d 525, 529 (4th Cir.2010) (alterations and internal quotation marks omitted). "Protecting contemporaneous exchanges for new value from avoidance does not harm the preference section's goal of protecting the equality of distribution among the debtors because such exchanges do not diminish the size of the debtor's estate." *Id.*

The Trustee argues that "Hanover did not sustain its burden of establishing Hanover's contemporaneous exchange defense to the Trustee's $1.375 million preferential transfer claim." Appellant's Brief at 55. The Trustee contends that

even assuming that the New Contracts constituted new value, "Hanover failed to present evidence of the extent of the new value." *Id.* I agree.

As stated above, the statute defines "new value," as is relevant here, as "money or money's worth in goods, services, or new credit, or release by a transferee of property previously transferred to such transferee." 11 U.S.C. § 547(a)(2). Under the New Contracts, ESA did not stand to receive any goods, services, new credit, or any release of property. It stood to receive only money. But as the Trustee points out, ESA never received any money under the New Contracts since ESA did not complete the work.

Hanover does not argue, and could not argue, that it presented evidence that the New Contracts were goods or services that could be sold for at least $1.375 million in the marketplace. Rather, Hanover contends that ESA received "new value" of at least $1.375 million in the form of the New Contracts because ESA expected to make that much profit by eventually completing its work under those contracts. *See* J.A. 584 (Cole affidavit). But regardless of what Hanover hoped to eventually receive, what it actually received was only a *conditional promise* to pay ESA money *at some point in the future.* Section 547, however, requires that the debtor's receipt of money, goods, services, new credit or property release be substantially contemporaneous with the debtor's payment.[1] *See In*

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[1]Hanover also argues that the bonds themselves constituted new value of at least $1.375 million to ESA because the face value of the bonds exceeded that amount. However, the government, not ESA, was the beneficiary on the bonds. If

re Teligent, Inc., 315 B.R. 308, 317 (Bankr.S.D.N.Y.2004) (explaining that "[a] promise of future services ... does not constitute 'new value.' "); *cf. Norwest Bank Worthington v. Ahlers,* 485 U.S. 197, 204, 108 S.Ct. 963, 99 L.Ed.2d 169 (1988) (discussing "new value" exception to absolute priority rule and stating that "[u]nlike 'money or money's worth,' a promise of future services cannot be exchanged in any market for something of value to the creditors *today* ").

Indeed, the facts of this very case demonstrate why receipt of a conditional promise for payment at some indefinite future time does not constitute receipt of "new value" in the amount of the promised payment.[2] In a "new value" transaction, the debtor's payment does not reduce the size of the estate because the money paid by the debtor is replaced by money, goods, services, new credit, or property releases of equivalent value. *See Angell,* 592 F.3d at 529. Here, in contrast, Hanover successfully obtained $1.375 million from the estate without replacing it with equal value.[3] In so doing, Hanover jumped

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Hanover proved any new value to ESA, it was limited to $74,071, the premium ESA paid for the bonds.

[2] Cole's affidavit supports Hanover's factual premise that ESA expected to make a profit of more than $1.375 million by performing the work under the New Contracts, but it does not establish the legal conclusion ESA actually received at least $1.375 million in new value.

[3] ESA's unrealized expectation that it would profit at some point in the future under the New Contracts shows that the contracts may have had "value" in traditional business/commercial parlance. ESA's expectation did not

ahead of ESA's other unsecured creditors and received far more payment via the letter of credit than it otherwise could have received in bankruptcy. Thus, the bankruptcy court erred, in my view, in concluding that Hanover established the new-value defense.[4]

I therefore would reverse the district court order affirming the bankruptcy court.

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replenish the estate, however, and thus the New Contracts did not amount to "new value" within the meaning of § 547(c).

[4] For the reasons stated in the majority opinion, I also believe the bankruptcy court erred in concluding that Hanover established the earmarking defense. *See ante* at 394–97. Additionally, I do not read the bankruptcy court order as ruling for Hanover on equitable grounds independent of the earmarking and new-value defenses.

Appendix B

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF NORTH CAROLINA
CHARLOTTE DIVISION

3:10-CV-578-GCM

IN RE: ESA ENVIRONMENTAL SPECIALISTS, INC.
Debtor.
STANLEY MARVIN CAMPBELL,
Plaintiff–Appellant,
v.

THE HANOVER INSURANCE COMPANY,
Defendant–Appellee.

ORDER

INTRODUCTION

Stanley Marvin Campbell ("Trustee"), Trustee in Bankruptcy for ESA Environmental Specialists, Inc., appeals the Bankruptcy Court's Order granting The Hanover Insurance Company's ("Hanover") Motion for Summary Judgment. Specifically, the Trustee claims that the Bankruptcy Court erred in granting Summary Judgment for Hanover based on the earmarking defense and based on the new value defense. This Court holds that the Bankruptcy Court

was correct to grant Summary Judgment in favor of Hanover. The Bankruptcy Court's order is therefore AFFIRMED.

BACKGROUND

ESA Environmental Specialists, Inc. ("ESA" or the "Debtor") was a full service environmental, construction, architectural, and industrial engineering firm in the business of providing services to third parties, including governmental agencies. Debtor performed federal construction jobs, each of which required Debtor to obtain both a performance and a payment bond under the Miller Act. 40 U.S.C. § 3131.

ESA obtained payment and performance bonds from Hanover in the fall of 2006 in conjunction with eight government contracts (the "Original Bonds"). In the spring of 2007, due to Hanover's concern with ESA's financial ability, Hanover refused to issue new bonds for seven additional government projects (the "New Bonds") unless ESA did all three of the following (the "Requirements"):

(1) paid the bond premiums for the New Bonds;

(2) obtained an irrevocable letter of credit in favor of Hanover in the amount of $1,375,000 (the "Letter of Credit"); and

(3) executed a Letter of Credit Collateral Agreement in the form supplied by Hanover.

ESA could not commence work on the seven government projects until the New Bonds were presented to the requisite government agencies.

To obtain the Letter of Credit, ESA needed to post a certificate of deposit with Sun Trust Bank, which agreed to issue the Letter of Credit. ESA discussed this bonding issued with Prospect Capital ("Prospect") and on May 7, 2007 ESA and Prospect entered into a First Amendment to Credit Agreement. The purpose of the First Amendment was to advance $625,000 to the Debtor. On May 17, 2007, ESA and Prospect entered into a Second Amendment to Credit Agreement. The purpose of the Second Amendment was to advance $950,000 to the Debtor. Prospect then sent two wires to ESA's bank account, the first on May 8, 2007 in the amount of $625,000 and the second on May 17, 2007 in the amount of $925,000 (the "Prospect Funds").

On May 17, 2007, ESA transferred $1,375,000 of the Prospect Funds into a certificate of deposit with SunTrust to collateralize the Letter of Credit. The Prospect Funds were the only funds used by ESA to deposit into the certificate of deposit. Subsequently, on May 18, 2007, SunTrust issued the letter of credit to Hanover. Also on May 18, 2007, ESA delivered the bond premiums and the Letter of Credit Collateral Agreement to Hanover's agent, Knauff Insurance. This satisfied all of the Requirements for issuance of the New Bonds and Knauff delivered the New Bonds to ESA on May 18, 2007. ESA then delivered the New Bonds to the government agencies.

On August 1, 2007, ESA filed a voluntary Chapter 11 petition with the Bankruptcy Court for the Western District of North Carolina. After the filing of the petition, Hanover drew on the Letter of

Credit and received a payment from SunTrust Bank in the amount of $1,375,000.

On September 28, 2007, the Bankruptcy Court entered an order approving the sale of substantially all of the assets of ESA to Prospect Capital (or its designee). (Docket no. 141, 07- 31532). The sale included an assumption and assignment to Prospect Capital's affiliate, ICS, of many of the Hanover bonded contracts and the sale of all avoidance actions under the Bankruptcy Code. ICS failed to complete the Hanover bonded contracts which were assigned and the Court entered an Order on February 15, 2008 permitting Hanover to exercise its rights as surety to complete the jobs.

On July 10, 2009, the Bankruptcy Court entered a "Stipulation between Chapter 7 Trustee and Prospect Capital Corporation and Order Approving Stipulation" (the "Stipulation"), which provided that the Trustee would have standing to pursue avoidance actions (despite the prior sale of such actions) with a split of any proceeds (after payment of the Trustee's fees and costs) in the following percentages: 75% to Prospect and 25% to the Trustee. (Docket No. 256, 07-31532). Additionally, the Stipulation approved an unsecured claim to Prospect in the amount of $11,775,000, which claim was entitled to pro rata distribution along with other unsecured claimants from the 25% recovery of the Trustee. The Bankruptcy Court provided that the Stipulation must be served on all parties in interest, who would thereafter have an opportunity to object and request a hearing. Hanover filed an objection to the Stipulation (Docket No. 266, 07-31532), and the

Bankruptcy Court continued a hearing on the objection until the hearing on Hanover's Motion for Summary Judgment (Docket No. 13, 09-3143).

The Chapter 7 Trustee, subsequent to entry of the Stipulation, filed an adversary proceeding against Hanover of July 31, 2009, claiming that: (1) Hanover was an indirect beneficiary of the transfer of the Prospect Funds into the certificate of deposit and (2) the transfer of the Prospect Funds was avoidable as a preferential transfer under 11 U.S.C. § 547.

On November 3, 2010, the Bankruptcy Court entered an Order granting summary judgment in favor of Hanover in the adversary proceeding. (Docket No. 25, 09-3143). The Bankruptcy Court held that Hanover was entitled to summary judgment as a matter of law because ESA's transfer of the Prospect Funds into the SunTrust certificate of deposit was not an avoidable transfer under § 547(b). First, the Bankruptcy Court found that Hanover demonstrated that it had a complete earmarking defense because the Prospect Funds were not property of ESA or the bankruptcy estate and the Trustee failed to meet his burden of proving under § 547(b) that there was a "transfer of an interest of the debtor in the property." Second, the Bankruptcy Court found that Hanover had a complete new value defense because the transfer of the Prospect Funds was: (1) a contemporaneous exchange for new value given to ESA by Hanover in the form of the New Bonds and the federal government contracts which ESA was able to obtain and (2) a substantially contemporaneous exchange under 11 U.S.C. § 547(c)(1).

The Trustee now appeals the Bankruptcy Court's Order granting Hanover's Motion for Summary Judgment.

ANALYSIS

A. STANDARD OF REVIEW

The Bankruptcy Court's conclusions of law are reviewed *de novo* and its findings of fact are reviewed for clear error. *In re Kielisch*, 258 F.3d 315, 319 (4th Cir. 2001).

B. SUMMARY JUDGMENT

Summary judgment is appropriate when 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 judgment as a matter of law. Fed. R. Civ. P. 56(c); *Celotex Corp. v. Catrett*, 477 U.S. 317, 323-25 (1986). Rule 56 of the Federal Rules of Civil Procedure applies to summary judgment in bankruptcy proceedings. Fed. R. Bankr. P. 7056. When ruling on a motion for summary judgment the court is required to view all inferences drawn from the factual record in a light most favorable to the nonmoving party. *Matsushita Elec. Indus. Co. v. Zenith Radio*, 475 U.S. 574, 587 (1986). Once the moving party has made an initial showing that there is no evidence to support the nonmoving party's case, the party opposing the motion "must do more than simply show that there is some metaphysical doubt as to the material facts." *Id* at 586.

C. THE EARMARKING DEFENSE

The Trustee appeals the Bankruptcy Court's holding that Hanover had a complete earmarking defense. Hanover demonstrated that it had a complete earmarking defense because the Prospect Funds were not property of ESA or the bankruptcy estate and the Trustee failed to meet his burden of proving under § 547(b) that there was a "transfer of an interest of the debtor in property." There was no preferential treatment in fact for the transfer of the Prospect Funds because it did not benefit Hanover out of estate assets to the detriment of other creditors. *Virginia National Bank v. Woodson (In re Decker)*, 329 F.2d 836 (4th Cir. 1964).

The Trustee bears the burden of proving that an alleged avoidable transfer was a "transfer of an interest of the debtor in property." 11 U.S.C. § 547(b). *See also In re Hood*, 118 B.R. 417, 419 (Bankr. D.S.C. 1990). Under the earmarking doctrine, which is a court fashioned doctrine, a third party makes a loan to a debtor so that the debtor is able to satisfy the claim of a designated creditor. *Coral Petroleum, Inc. v. Banque Paribas-London*, 797 F.2d 1351, 1356 (5th Cir. 1986). The loan is not property of the debtor, there is no diminution to the estate, and transfer of the funds to a creditor is not preferential. *In re Hood*, 118 B.R. 417 at 419-420 (citing *Mandross v. Peoples Banking Co. (In re Hartley)*, 825 F.2d 1067 (6th Cir. 1987)). The earmarking doctrine is inapplicable when the trustee can prove, by a fair preponderance of the evidence, that the doctrine does not apply "and that

what was transferred was in fact property in which the debtor had an interest." *In re Safe-T Brake of South Florida*, 162 B.R. 359, 365 (Bankr. S.D. Fla. 1993).

The Fourth Circuit's leading decision on the earmarking doctrine is *Virginia National Bank v. Woodson (In re Decker)*, 329 F.2d 836 (4th Cir. 1964). In *Decker*, the debtor's sister, in exchange for an assignment of the debtor's interest in pool memberships, paid a sum of money to the bank in satisfaction of the debtor's overdraft obligations. Subsequently, the debtor went into involuntary bankruptcy, the trustee sued the bank for recovery of the sum paid by the sister, and the district court ordered turnover of the sum. The Fourth Circuit reversed, noting that the sister's payment "was made for the specific purpose of paying at least a portion of a particular debt owed to the bank..." and that "as a general rule, such a payment... will not create a voidable preference [because] there has been no diminution of the value of the estate." *Id* at 839. The Circuit stated that "[t]he test is not what the creditor receives but what the bankruptcy estate has lost. It is the diminution of the bankrupt's estate, not the unequal payment to creditors, which is the evil sought to be remedied by the avoidance of a preferential transfer." *Id* at 840. The *Decker* Court applied the earmarking doctrine because the debtor's sister insisted that the loan proceeds be used solely to pay the bank that was threatening her brother.

The payment in *Decker*, unlike the payments in this case, were made directly by a third party to the creditor. However, that fact is not determinative

because other courts have held that a transfer of loan funds is not preferential even though the funds were placed into the debtor's account. *See In re Superior Stamp & Coin Co., Inc.,* 223 F.3d 1004, 1009 (9th Cir. 2000) (transfer of loan funds was not preferential despite funds being placed into debtor's bank account; the fact that debtor "may have had the power to divert the loan after it was deposited into [the debtor's] account does not amount to 'control' of the funds by [the debtor]"); *see also Coral Petroleum*, 797 F.2d at 1356 ("If all that occurs in a transfer is the substitution of one creditor for another, no preference is created because the debtor has not transferred property of his estate; he still owes the same sum to a creditor, only the identity of the creditor has changed").

Appellant first argues that the Bankruptcy Court erred in granting summary judgment for Hanover because the antecedent debt requirement is not present in this case. In support of this argument, the Trustee claims that *Decker* did not recognize earmarking in the context present in this case because *Decker* was decided under section 60 of the former Bankruptcy Act and never specifically discussed earmarking as a defense to a preference. The Trustee further argues that there is a dispute as to whether the earmarking defense applies in this case because the source of the funds is not a guarantor. Appellant errantly asserts that the Fourth Circuit's failure to decide any earmarking case means that the elements of the defense have not been established in the Circuit. Therefore, Appellant argues that this Court should adopt tests articulated

by other jurisdictions in either *In re Bohlen Enterprises, Ltd.,* 859 F.2d 561 (8th Cir. 1988) or in *In re Adams*, 240 B.R. 807 (Bkrtcy. D.Me., 1999).

This Court disagrees with Appellant's initial argument because it is clear that the Fourth Circuit did adopt and recognize the earmarking defense in *Decker*. Additionally, the fact that *Decker* was decided under section 60 of the former Bankruptcy Act does not persuade this Court to adopt Appellant's argument because numerous courts recognized the continuing validity of *Decker* under the Bankruptcy Code. *See Hartley*, 825 F.2d at 1071 (following *Decker* and holding that payment of funds to creditor was only voidable to the extent of value of security debtor gave third party in exchange for transfer); *see generally Active Wear, Inc. v. Parkdale Mills, Inc.*, 331 B.R. 669, 671 (W.D. Va. 2005) (citing five circuit courts of appeal which relied upon *Decker* since passage of the Bankruptcy Code). Thus, this Court refuses to follow Appellant's request to disregard Fourth Circuit precedent in favor of relying on tests articulated by Courts outside of this jurisdiction.

Second, Appellant argues that the Bankruptcy Court erred in granting summary judgment for Hanover because the earmarking defense does not apply when unsecured debt is replaced by secured debt. In support of this position, the Trustee argues that the secured advance to ESA by Prospect Capital substituted ESA's unsecured obligation to Hanover for ESA's new secured obligation to Prospect Capital. Appellant argues that an unsecured claim was replaced by a secured claim to the detriment of ESA's

unsecured creditors thereby reducing the amount of property available to the unsecured creditors.

Again, Appellant's argument fails because Prospect did not receive any new collateral or security from ESA in exchange for the Prospect Funds. ESA gave no new security or collateral to Prospect and thus no new secured debt was incurred by ESA. It follows that there was no diminution of ESA's estate and no preferential transfer which can be avoided against Hanover. Under the Fourth Circuit's ruling in *Decker*, Hanover, at most, could be held liable only for returning the value of any security given to Prospect in exchange for the Prospect funds. *See In re Decker*, 329 F.2d at 840 (remanding a portion of the case for determination by the District Court of the value of the swimming pool rights transferred from the debtor to the third party in exchange for the third party's payment to the creditor on behalf of the debtor, because the swimming pool rights may actually have been of value to the bankrupt's estate).

Third, Appellant argues that the earmarking defense does not apply because the debtor possessed and controlled the funds. In support of this position the Trustee asserts that: (1) a total of $1,575,000, only $1,375,000 of which was used to acquire the deposit securing the letter of credit, was advanced to ESA; (2) Hanover's submissions show ESA's control over the funds; (3) the funds were in ESA's control and possession for ten days prior to the date ESA collateralized the bonds with the letter of credit; and (4) the Credit Agreement between ESA and Prospect amounted to an unconditional loan.

Appellant's argument again fails. The fact that the funds were in ESA's account is not determinative because other courts have held that a transfer of loan funds is not preferential even when the funds were placed into the debtor's account. *See In re Superior Stamp & Coin Co., Inc.,* 223 F.3d 1004, 1009 (9th Cir. 2000) (transfer of loan funds was not preferential despite funds being placed into debtor's bank account; the fact that debtor "may have had the power to divert the loan after it was deposited into [the debtor's] account does not amount to 'control' of the funds by [the debtor]"); *see also Coral Petroleum*, 797 F.2d at 1356 ("If all that occurs in a transfer is the substitution of one creditor for another, no preference is created because the debtor has not transferred property of his estate; he still owes the same sum to a creditor, only the identity of the creditor has changed"). Furthermore, the factual evidence considered by the Bankruptcy Court in its summary judgment ruling clearly shows that the Prospect Funds were given, not as an unconditional loan, but rather to fund costs associated with entering into and fulfilling government contracts. Under the circumstances facing it, ESA could not enter into and fulfill government contracts without using the Prospect Funds for funding the certificate of deposit to collateralize the letter of credit.

Fourth, Appellant argues that there is a dispute of material fact concerning the earmarking defense. In support of this position, the Trustee claims that the Bankruptcy Court, facing competing affidavits, cannot grant summary judgment on the face of conflicting affidavits because a determination of

credibility is required. *See Davis v. Zahradnick*, 600 F.2d 458, 460 (4th Cir. 1979); *American Metal Forming Corp. v. Pittman*, 52 F.3d 504, 507 (4th Cir. 1995). Appellant claims that the Bankruptcy Court did not hear evidence to determine credibility of various affiants and thus, the Trustee claims that the evidence before the Bankruptcy Court was in conflict.

Again, Appellant's argument fails. The affidavits relied on by the Bankruptcy Court are not in conflict. Rather, both the Declaration of Charles Cole, former CEO of ESA, and the affidavit of John Francis Barry III, CEO of Prospect Capital, show that ESA and Prospect were aware that the Prospect Funds would be used to fund the certificate of deposit to collateralize the letter of credit and that the funds were advanced for this purpose. The fact that the language in the Cole Declaration is not identical to the language in the Barry Affidavit does not create a genuine dispute of material fact when both sworn documents clearly show that ESA would use the Prospect Funds to fund costs associated with entering into and fulfilling government contracts. As stated previously in this Order, ESA could not enter into and fulfill government contracts without using the Prospect Funds for funding the certificate of deposit to collateralize the letter of credit.

Fifth, Appellant argues that the Bankruptcy Court erred in considering matters from the underlying bankruptcy case, including the statement of Prospect's Counsel as evidence of earmarking. This argument is without merit because it was not made before the Bankruptcy Court and Appellant

failed to raise any objection to the Bankruptcy Court's consideration of this matter. A party must timely raise an objection to a court's consideration of the evidence in order to preserve that issue for appeal. "If a party fails to object to the inadmissibility of evidence submitted by its opponent in the summary judgment proceedings, the court may consider the evidence. The failure to raise the issue in the [trial] court constitutes a waiver of objection for purposes of summary judgment." *Moore's Federal Practice* § 56.91[7] (3rd ed. 2011); *see also* Fed. R. Evid. 103. The Fourth Circuit follows this standard. *See Waste Management Holdings, Inc. v. Gilmore*, 252 F.3d 316 (4th Cir. 2001). Also, it worth noting that the Appellant would like this Court to overturn the Bankruptcy Court because of its consideration of the statement of Prospect's Counsel, but at the same time Appellant sees no problem in the Bankruptcy Court considering similar statements cited to and discussed by Appellant in aid of his own position. Appellant cannot raise the issue of the Bankruptcy Court's consideration of matters from the underlying bankruptcy case for the first time on appeal because this argument was not made before the Bankruptcy Court and thus, it has been waived.

Sixth, Appellant argues that the Bankruptcy Court erred by assigning the Trustee with the burden of proof on earmarking. This argument is without merit and is not worth addressing in detail because the Bankruptcy Court concluded that "Hanover has demonstrated that it has a complete earmarking defense." (Docket No. 25, 09-3143).

Although there is a split of authority regarding the formulation of the burden of proof on the earmarking defense that has not been addressed by the Fourth Circuit, the Bankruptcy Court's own language in its order clearly showed that, even if the burden shifted, Hanover met that burden.

Finally, the Appellant argues that the Bankruptcy Court erred in finding that Hanover had a complete earmarking defense because the earmarking defense is not applicable to the facts of this case. The Trustee claims that the Fourth Circuit never sanctioned the use of the earmarking defense outside of the context of a payment directly from a guarantor to a third party creditor because Appellant's characterization of *Decker*, 329 F.2d 836 (4th Cir. 1964), is that the case involved a direct payment from a guarantor to a creditor without passing through the debtor's estate. Thus, Appellant argues that the Bankruptcy Court for the Western District of North Carolina has taken it on its own initiative to grossly expand the law by permitting an earmarking defense outside of the direct payment by a guarantor context.

Appellant's argument that the Bankruptcy Court expanded the law by permitting an earmarking defense outside of the direct payment by a guarantor context is erroneous and deceptive. The words "guarantor" or "guarantee" never appear in the Fourth Circuit's *Decker* opinion. In fact, the payments at issue in *Decker* came from the debtor's sister who had no relationship to the underlying bank overdrafts. The sister never was a guarantor and she never guaranteed her brother's debts with

the bank. It is crystal-clear that the sister was not a guarantor because the Fourth Circuit stated, when then the sister covered the debtor's overdrafts, that "[t]his was the first contact had by any representative of the bank with Vivian Decker concerning this particular transaction and it does not appear that any inquiry was made by the bank employee at that time, or subsequently, as to the nature of the transaction between Decker and his sister." *Decker*, 329 F.2d at 838. The Fourth Circuit applied the earmarking doctrine outside of the guarantor context in *Decker* and thus, the Bankruptcy Court properly applied that precedent to the case at hand.

In sum, this Court finds no clear error in the factual conclusions reached by the Bankruptcy Court underlying its decision that Hanover has a complete earmarking defense. The Prospect Funds were not the property of ESA or of the bankruptcy estate and the Trustee failed to meet his burden of proving under § 547(b) that there was a transfer of an interest of the debtor in property. Furthermore, this Court, reviewing the law *de novo*, finds that *Decker* recognizes the existence of the earmarking defense in the Fourth Circuit and that Hanover has a complete earmarking defense as a matter of law. At the summary judgment stage, the Trustee may not rest on his pleadings, but must demonstrate that specific material facts give rise to a genuine issue. *Celotex Corp. v. Catrett*, 477 U.S. 317, 324 (1986). Once the moving party has made an initial showing that there is no evidence to support the nonmoving party's case, the party opposing the motion "must do

more than simply show that there is some metaphysical doubt as to the material facts. *Matsushita Elec. Indus. Co. v. Zenith Radio*, 475 U.S. at 586. The Appellant failed to demonstrate the existence of specific facts giving rise to any genuine issue regarding the earmarking defense that would preclude the Bankruptcy Court from granting summary judgment in favor of Hanover.

D. THE NEW VALUE DEFENSE

The Trustee appeals the Bankruptcy Court's ruling that Hanover has a complete new value defense. Hanover demonstrated that it had a complete new value defense because the transfer of the Prospect Funds was: (1) a contemporaneous exchange for new value given to ESA by Hanover in the form of the New Bonds and the federal government contracts which ESA was able to obtain and (2) a substantially contemporaneous exchange under 11 U.S.C. § 547(c)(1). The Appellee met its burden of proving new value in excess of the amount of the Prospect Funds by showing that ESA received the New Bonds in the total face amount of $7,889,350.86 and by showing that the New Bonds facilitated ESA's ability to proceed with new government contracts and earn revenue in excess of $1,375,000.

The new value defense is enunciated in the Bankruptcy Code at 11 U.S.C. § 547(c)(1), which states that a bankruptcy trustee cannot recover an alleged preferential transfer if the transfer was "(A) intended by the debtor and the creditor to or for whose benefit such transfer was made to be a

contemporaneous exchange for new value given to the debtor; and (B) in fact a substantially contemporaneous exchange." The purpose of the new value defense is "to encourage creditors to deal with troubled debtors without fear that they will have to disgorge payments received for value given." *United Rentals, Inc. v. Angell*, 592 F.3d 525, 529 (4th Cir. 2010) (citation omitted). § 547 (c)(1) was designed to address the problem that those on the verge of bankruptcy still need to buy things. *Id* (citations omitted). Furthermore, the preference section's goal of protecting the equality of distribution among the debtors is not harmed by protecting contemporaneous exchanges for new value from avoidance because such exchanges do not diminish the size of the debtor's estate. *Id* (citation omitted). "The party against whom recovery or avoidance is sought bears the burden of proving a § 547(c) defense." *Id* at 531.

Appellant's argument, that the Bankruptcy Court erred in finding that Hanover had a complete new value defense, is premised on the position that Hanover failed to meet its burden of proving the amount of the new value. In support of his position, the Trustee claims that neither the face amount of the New Bonds nor the expected revenue from government contracts were new value because Hanover did not provide these items to ESA in exchange for the $1,375,000 Letter of Credit. The Trustee argues that Hanover could not give ESA more than $1,375,000 in value because Hanover charged only $74,071 for premiums on the New Bonds. Further, Appellant claims that the Letter of

Credit was not supplied solely as security for the New Bonds because the Letter of Credit Agreement expressly covers "any other obligations" and therefore, there is no evidence establishing a value for the portion of the Letter of Credit attributable to the New Bonds and the portion attributable to the Old Bonds. In sum, the Trustee argues that the only evidence of value is the $74,071 premium for the New Bonds.

Appellant's argument fails because Hanover did meet its burden of proof as to the new value defense under § 547(c)(1). *United Rentals*, 592 F.3d at 531. Hanover presented significant evidence of new value to the Bankruptcy Court including the total face amount of the New Bonds ($7,889,350.86), the awarding to ESA of seven government jobs (valued at $3,944,675.43) due to ESA's receipt of the New Bonds, and the fact that the New Bonds provided ESA the ability to proceed with new government contracts and to earn revenues in excess of $1,375,000. The fact that the government contracts were not provided to ESA by Hanover does not further Appellant's position because federal courts recognize that new value can be provided by an indirect third party. *See Collier on Bankruptcy* ¶ 547.04[1][c] ("Payment to a creditor may be exempt from avoidance as a preference if the debtor receives contemporaneous new value from a party other than the creditor."); *see also In re Microwave Products of America, Inc.*, 118 B.R. 556 at 572; *In re Kumar Bavishi & Associates*, 906 F.2d 942 (3rd Cir. 1990); *In re Gem Constr. Corp. of Virginia*, 262 B/R/ 638, 646 (Bankr. E.D. Va. 2000). Here, ESA received

contemporaneous new value directly attributable to Hanover's issuance of the New Bonds. Moreover, Appellant's position that the value of the New Bonds was the premiums which ESA paid for them is erroneous because the premiums were charged by Hanover when it received as security a $1,375,000 Letter of Credit. Finally, testimony of Mr. Cole illustrated that the government contracts obtained by ESA would allow ESA to earn at least $1,375,000 in revenue.

This Court finds no clear error in the factual conclusions reached by the Bankruptcy Court underlying its decision that Hanover has a complete new value defense. Hanover did prove that it gave a contemporaneous exchange for new value to ESA in the form of the New Bonds and the federal government contracts which ESA obtained and performed after receipt of the New Bonds. Additionally, Hanover demonstrated that a substantially contemporaneous exchange was made under 11 U.S.C. § 547(c)(1) because the Letter of Credit was provided to Hanover on the same date that Hanover gave ESA the New Bonds. After a *de novo* review of the law regarding the new value defense, this Court is satisfied that the Bankrupcty [sic] Court was correct to hold that Hanover demonstrated a complete new value defense as a matter of law. Moreover, the Bankruptcy Court noted that the Trustee did not present evidence contesting the fact that the exchange was a contemporaneous exchange for new value. At the summary judgment stage, the Trustee may not rest on his pleadings, but must demonstrate that specific

material facts give rise to a genuine issue. *Celotex Corp. v. Catrett*, 477 U.S. 317, 324 (1986). Once the moving party has made an initial showing that there is no evidence to support the nonmoving party's case, the party opposing the motion "must do more than simply show that there is some metaphysical doubt as to the material facts. *Matsushita Elec. Indus. Co. v. Zenith Radio*, 475 U.S. at 586. The Appellant failed to demonstrate the existence of specific facts giving rise to any genuine issue regarding the new value defense that would preclude the Bankruptcy Court from granting summary judgment in favor of Hanover.

CONCLUSION

The Court is satisfied that the Bankruptcy Court made no clear error in any of its factual conclusions. Upon a review of the applicable law, the Court is satisfied that Hanover is entitled to summary judgment and that Hanover demonstrated that it has both a complete earmarking defense and a complete new value defense. Accordingly, the Bankruptcy Court's order granting summary judgment to Appellee is AFFIRMED.

IT IS SO ORDERED

Signed: September 22, 2011
/s/ Graham C. Mullen
United States District Judge

Appendix C

/s/ George R. Hodges
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NORTH CAROLINA
CHARLOTTE DIVISION

Case No. 07-31532
Adversary Proceeding No. 09-3143

STANLEY M. CAMPBELL, *Trustee in Bankruptcy for ESA Environmental Specialists, Inc.*
Debtor

STANLEY M. CAMPBELL, *Trustee in Bankruptcy for ESA Environmental Specialists, Inc.*
Debtor,

v.

THE HANOVER INSURANCE COMPANY,
Defendant.

ORDER GRANTING THE HANOVER INSURANCE COMPANY'S MOTION FOR SUMMARY JUDGMENT

GEORGE R. HODGES, Bankruptcy Judge.

This matter came before the Court for hearing on September 15, 2010 on the Motion of The Hanover

Insurance Co. ("Hanover") for Summary Judgment pursuant to Federal Rule of Civil Procedure 56 (made applicable to this adversary proceeding by Federal Rule of Bankruptcy Procedure 7056) (the "Motion") [Docket no. 13]. The Motion was supported by a brief [Docket no. 22], the Affidavit of Tammy M. Laub [Docket no. 14] and the Declaration of Charles Jacob Cole [Docket no. 21]. The Plaintiff–Trustee filed a Response Objecting to Hanover's Motion for Summary Judgment [Docket no. 15] which was supported by a Declaration of Chapter 7 Trustee [Docket no. 17], and an Amended Declaration of Chapter 7 Trustee [Docket no. 18]. The Plaintiff–Trustee also filed a supplemental response in opposition to the Motion [Docket no. 24], to which was attached the Affidavit of John Francis Barry III. Both Plaintiff and Hanover were represented by counsel at the hearing. In addition to the pleadings described above, the Court also considered (without objection) the record, pleadings and transcripts of hearings in the base case, *In re ESA Environmental Specialists, Inc.* (07–31532), including the sworn testimony of witnesses at those hearings and the statements of counsel for Prospect Capital Corporation. Based upon a review of those matters and the arguments of counsel at the hearing, the Court finds that the following are the undisputed facts in this matter.

A. ESA Environmental Specialists, Inc. ("ESA" or the "Debtor") was a full service environmental, construction, architectural, and industrial engineering firm.

B. ESA performed federal construction jobs, each of which required the contractor to provide both a performance bond and a payment bond under the Miller Act. 40 U.S.C. § 3131.

C. ESA obtained payment and performance bonds from Hanover in the fall of 2006 in connection with eight (8) government contracts (the "Original Bonds"). In the spring of 2007, due to Hanover's concern with ESA's financial ability, Hanover refused to issue new bonds for seven (7) additional government projects (the "New Bonds") unless ESA did all three of the following (the "Requirements"): (1) paid the bond premiums for the New Bonds; (2) obtained an irrevocable letter of credit in favor of Hanover in the amount of $1,375,000 (the "Letter of Credit"); and (3) executed a Letter of Credit Collateral Agreement in the form supplied by Hanover. ESA could not commence work on the seven government projects until the New Bonds had been presented to the relevant government agencies.

D. To obtain the Letter of Credit, ESA needed to post a certificate of deposit with SunTrust Bank, which had agreed to issue the Letter of Credit. ESA discussed this bonding issue with Prospect Capital ("Prospect"). On May 7, 2007 ESA and Prospect entered into a First Amendment to Credit Agreement. The purpose of the First Amendment was to advance $625,000 to the Debtor. On May 17, 2007, ESA and Prospect entered into a Second Amendment to Credit Agreement. The purpose of the

Second Amendment was to advance $950,000 to the Debtor. Prospect sent two wires to ESA's bank account, the first on May 8, 2007 in the amount of $625,000 and the second on May 17, 2007 for $950,000 (the "Prospect Funds"). These wire transfers were later described to the Court by Prospect's counsel as follows: "And so Prospect pumps more money into the debtor. In fact, gave the debtor about another million two so that the debtor could post that as cash security so it could keep some bonding going and then Prospect investigated the situation." [Docket no. 90, 07–31532, at 11:2–6].

E. On May 17, 2007, ESA transferred $1,375,00 of the Prospect Funds into a certificate of deposit with SunTrust to collateralize the Letter of Credit. ESA did not use any funds to deposit into the certificate of deposit other than the Prospect Funds. On May 18, 2007, SunTrust issued the letter of credit to Hanover. On May 18, 2007, ESA delivered the bond premiums and the Letter of Credit Collateral Agreement to Hanover's agent, Knauff Insurance. This satisfied all of the Requirements. In exchange, Knauff delivered the New Bonds to ESA on May 18, 2007. ESA then delivered the New Bonds to the governmental agencies.

F. On August 1, 2007, ESA filed a voluntary Chapter 11 petition with this Court. After the filing of the bankruptcy petition, Hanover drew on the Letter of Credit and received a payment from SunTrust Bank in the amount of $1,375,000.

G. On September 28, 2007, the Court entered an order approving the sale of substantially all of the assets of ESA to Prospect Capital (or its designee). [Docket no. 141, 07–31532]. The sale included an assumption and assignment to Prospect Capital's affiliate, ICS, of many of the Hanover bonded contracts, as well as the sale of all avoidance actions under the Bankruptcy Code. ICS failed to complete the Hanover bonded contracts which it had been assigned, and the Court entered an order on February 15, 2008 permitting Hanover to exercise its rights as surety to complete the jobs.

H. On July 10, 2009, the Court entered a "Stipulation between Chapter 7 Trustee and Prospect Capital Corporation and Order Approving Stipulation" (the "Stipulation"). [Docket no. 256, 07–31532]. The Stipulation provided, among other things, that the Trustee would have standing to pursue avoidance actions (despite the prior sale of such actions) with a split of any proceeds (after payment of the Trustee's fees and costs) in the following percentages: 75% to Prospect and 25% to the Trustee. In addition, the Stipulation approved an unsecured claim to Prospect in the amount of $11,775,000, which claim was entitled to pro rata distribution along with other unsecured claimants from the 25% recovery of the Trustee. Because the Stipulation was entered without notice to any parties, the Court provided that it must be served on all parties in interest, who would thereafter have an opportunity to object and request a hearing on the Stipulation. Hanover filed an objection to the

Stipulation [Docket no. 266, 07–31532], and a hearing on that objection was continued until the hearing on the Motion.

I. After entry of the Stipulation, the Chapter 7 Trustee filed this adversary proceeding against Hanover on July 31, 2009 claiming that Hanover was an indirect beneficiary of the transfer of the Prospect Funds into the certificate of deposit and the transfer of the Prospect Funds was avoidable as a preferential transfer under 11 U.S.C. § 547.

J. The Trustee also alleged in the complaint that Hanover was the recipient of a check in the amount of $21,319.42, which was also avoidable as a preference. However, in its pleadings and at the hearing, the Trustee admitted that this check was paid to a party other than Hanover, and consented to the entry of summary judgment with regard to that particular claim.

Based upon the pleadings and record in this case and the base case, and the arguments of counsel at the hearing, the Court concludes that summary judgment in favor of Hanover is appropriate on all of the Trustee's claims because:

1. There are no genuine issues of material fact which would preclude summary judgment under Rule 56 of the Federal Rules of Civil Procedure and Rule 7056 of the Federal Rules of Bankruptcy Procedure.

2 Hanover is entitled to summary judgment as a matter of law because ESA's transfer of the Prospect Funds into the SunTrust certificate of deposit was not an avoidable transfer under § 547(b).

3. First, the Prospect Funds were not really property of ESA or the bankruptcy estate as a practical matter, and the Trustee failed to meet his burden of proving under § 547(b) that there was a "transfer of an interest of the debtor in property." The Prospect Funds which were placed into the SunTrust certificate of deposit were specifically provided by Prospect Capital for ESA to collateralize the Letter of Credit in order to obtain the New Bonds, as specifically stated by counsel for Prospect at the August 8, 2007 first hearing before this Court. There was no diminution to ESA's estate because the Prospect Funds came solely from a third party. The funds placed into the SunTrust certificate of deposit were Prospect's funds that were simply a pass-through in ESA's bank account. Even if the funds could have been characterized as ESA's, they were ESA's only for the specific purpose of putting them into the SunTrust certificate of deposit. Under the Fourth Circuit's opinion *In re Decker,* there was no preferential treatment in fact for this transfer because it did not benefit Hanover out of estate assets to the detriment of other creditors. *Virginia National Bank v. Woodson* (*In re Decker*), 329 F.2d 836 (4th Cir. 1964). Hanover has demonstrated that it has a complete earmarking defense.

4. Second, Hanover has a complete new value

defense. The transfer of the Prospect Funds was: (1) a contemporaneous exchange for new value given to ESA by Hanover in the form of the New Bonds and the federal government contracts which ESA was able to obtain and perform after receipt of the New Bonds and (2) a substantially contemporaneous exchange under 11 U.S.C. § 547(c)(1). The Letter of Credit was provided to Hanover (and the Requirements satisfied) on May 18, 2007, the same date that Hanover (through its agent Knauff) gave ESA the New Bonds.

5. There was no evidence contesting the fact that the exchange was intended to be (and was in fact) a contemporaneous exchange for new value. Rather, the Trustee claimed that Hanover had failed to meet its burden of specifically proving the amount of new value that was given by Hanover. Hanover provided evidence that in exchange for the Prospect Funds, ESA received the New Bonds in the total face amount of $7,889,350.86. Moreover, the New Bonds also provided ESA with the ability to proceed with the new government contracts and to earn revenue in excess of $1,375,000. There being no evidence to the contrary, Hanover met its burden of proving new value in excess of the amount of the Prospect Funds.

6. Third, the Court finds that requiring Hanover to return the funds drawn on the Letter of Credit (the vast majority of which would end up being returned to Prospect) would be a complete travesty in the circumstances as they played out. As a surety, Hanover has been required to expend funds in

connection with the effort to complete ESA's obligations for performance and payment on the bonded contracts and discharge of the bonded obligations secured by the Letter of Credit. This was the very purpose and risk which ESA and Prospect knowingly took when they placed the Prospect Funds in the certificate of deposit to secure the Letter of Credit for Hanover. It would be inequitable to require Hanover to return the portion of the Prospect Funds used to cover the costs to complete the Hanover bonded jobs and pay the associated obligations when Hanover did the work, and paid the obligations, which jobs were supposed to have been completed first by ESA and then by Prospect's affiliate, ICS, when it assumed certain of the jobs.

WHEREFORE, the Motion is GRANTED and SUMMARY JUDGMENT is hereby ENTERED in favor of Hanover.

United States Bankruptcy Court

This Order has been signed electronically.
The judge's signature and court's seal appear at the top of the Order.

Appendix D

Filed: March 29, 2013

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 11–2150

IN RE: ESA ENVIRONMENTAL SPECIALISTS, INC.
Debtor.

STANLEY MARVIN CAMPBELL,
Plaintiff–Appellant,

v.

THE HANOVER INSURANCE COMPANY,
Defendant–Appellee.

ORDER

The court denies the petition for rehearing en banc. No judge requested a poll under Fed. R. App. P. 35 on the petition for rehearing en banc.

Entered at the direction of the panel: Chief Judge Traxler, Judge Wilkinson and Judge Agee.

For the Court

/s/ Patricia S. Connor, Clerk

Appendix E

11 U.S.C. § 547 - Preferences

(a) In this section—

(1) "inventory" means personal property leased or furnished, held for sale or lease, or to be furnished under a contract for service, raw materials, work in process, or materials used or consumed in a business, including farm products such as crops or livestock, held for sale or lease;

(2) "new value" means money or money's worth in goods, services, or new credit, or release by a transferee of property previously transferred to such transferee in a transaction that is neither void nor voidable by the debtor or the trustee under any applicable law, including proceeds of such property, but does not include an obligation substituted for an existing obligation;

(3) "receivable" means right to payment, whether or not such right has been earned by performance; and

(4) a debt for a tax is incurred on the day when such tax is last payable without penalty, including any extension.

(b) Except as provided in subsections (c) and (i) of this section, the trustee may avoid any transfer of an interest of the debtor in property—

(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.

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

(1) to the extent that such transfer was—

(A) intended by the debtor and the creditor to or for whose benefit such transfer was made to be a contemporaneous exchange for new value given to the debtor; and

(B) in fact a substantially contemporaneous exchange;

(2) to the extent that such transfer was in payment of a debt incurred by the debtor in the ordinary course of business or financial affairs of the debtor and the transferee, and such transfer was—

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

(B) made according to ordinary business terms;

(3) that creates a security interest in property acquired by the debtor—

(A) to the extent such security interest secures new value that was—

(i) given at or after the signing of a security agreement that contains a description of such property as collateral;

(ii) given by or on behalf of the secured party under such agreement;

(iii) given to enable the debtor to acquire such property; and

(iv) in fact used by the debtor to acquire such property; and

(B) that is perfected on or before 30 days after the debtor receives possession of such property;

(4) to or for the benefit of a creditor, to the extent that, after such transfer, such creditor gave new value to or for the benefit of the debtor—

(A) not secured by an otherwise unavoidable security interest; and

(B) on account of which new value the debtor did not make an otherwise unavoidable transfer to or for the benefit of such creditor;

(5) that creates a perfected security interest in inventory or a receivable or the proceeds of either, except to the extent that the aggregate of all such transfers to the transferee caused a reduction, as of the date of the filing of the petition and to the prejudice of other creditors holding unsecured claims, of any amount by which the debt secured by such security interest exceeded the value of all security interests for such debt on the later of—

(A)

(i) with respect to a transfer to which subsection (b)(4)(A) of this section applies, 90

days before the date of the filing of the petition; or

(ii) with respect to a transfer to which subsection (b)(4)(B) of this section applies, one year before the date of the filing of the petition; or

(B) the date on which new value was first given under the security agreement creating such security interest;

(6) that is the fixing of a statutory lien that is not avoidable under section 545 of this title;

(7) to the extent such transfer was a bona fide payment of a debt for a domestic support obligation;

(8) if, in a case filed by an individual debtor whose debts are primarily consumer debts, the aggregate value of all property that constitutes or is affected by such transfer is less than $600; or

(9) if, in a case filed by a debtor whose debts are not primarily consumer debts, the aggregate value of all property that constitutes or is affected by such transfer is less than $5,000.

(d) The trustee may avoid a transfer of an interest in property of the debtor transferred to or for the benefit of a surety to secure reimbursement of such a surety that furnished a bond or other obligation to dissolve a judicial lien that would have been avoidable by the trustee under subsection (b) of this section. The liability of such surety under such bond or obligation shall be discharged to the extent of the value of such property recovered by the trustee or the amount paid to the trustee.

(e)

(1) For the purposes of this section—

(A) a transfer of real property other than fixtures, but including the interest of a seller or purchaser under a contract for the sale of real property, is perfected when a bona fide purchaser of such property from the debtor against whom applicable law permits such transfer to be perfected cannot acquire an interest that is superior to the interest of the transferee; and

(B) a transfer of a fixture or property other than real property is perfected when a creditor on a simple contract cannot acquire a judicial lien that is superior to the interest of the transferee.

(2) For the purposes of this section, except as provided in paragraph (3) of this subsection, a transfer is made—

(A) at the time such transfer takes effect between the transferor and the transferee, if such transfer is perfected at, or within 30 days after, such time, except as provided in subsection (c)(3)(B);

(B) at the time such transfer is perfected, if such transfer is perfected after such 30 days; or

(C) immediately before the date of the filing of the petition, if such transfer is not perfected at the later of—

(i) the commencement of the case; or

(ii) 30 days after such transfer takes effect between the transferor and the transferee.

(3) For the purposes of this section, a transfer is not made until the debtor has acquired rights in the property transferred.

(f) For the purposes of this section, the debtor is presumed to have been insolvent on and during the 90 days immediately preceding the date of the filing of the petition.

(g) For the purposes of this section, the trustee has the burden of proving the avoidability of a transfer under subsection (b) of this section, and the creditor or party in interest against whom recovery or avoidance is sought has the burden of proving the nonavoidability of a transfer under subsection (c) of this section.

(h) The trustee may not avoid a transfer if such transfer was made as a part of an alternative repayment schedule between the debtor and any creditor of the debtor created by an approved nonprofit budget and credit counseling agency.

(i) If the trustee avoids under subsection (b) a transfer made between 90 days and 1 year before the date of the filing of the petition, by the debtor to an entity that is not an insider for the benefit of a creditor that is an insider, such transfer shall be considered to be avoided under this section only with respect to the creditor that is an insider.