IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS
ENTERED
TAWANA C. MARSHALL, CLERK
THE DATE OF ENTRY IS
ON THE COURT'S DOCKET

IN RE:	§	
	§	
ML ASSOCIATES, INC.,	§	CASE NO. 00-37462-SAF-7
DEBTOR(S).	§	
	§	
JAMES W. CUNNINGHAM, TRUSTEE,	§	
PLAINTIFF,	§	
	§	
VS.	§	ADVERSARY NO. 02-3387
	§	
MCCARTY & ASSOCIATES, INC.,	§	
DEFENDANT.	§	

MEMORANDUM OPINION AND ORDER

James W. Cunningham, the Chapter 7 trustee of the bankruptcy estate of ML & Associates, Inc., the debtor, seeks to recover under 11 U.S.C. §§ 549 and 550 an unauthorized post-petition transfer of $14,359.50 to McCarty & Associates, Inc., the defendant. McCarty contends that it provided the debtor reasonably equivalent value in exchange for the transfer, that the debtor tendered payment to McCarty in the ordinary course of its business, and that McCarty acted in good faith.

At the trial docket call on February 10, 2003, the parties submitted a draft pretrial order, but counsel for McCarty moved to withdraw as counsel of record. McCarty, acting through its

president Dennis McCarty, agreed to the withdrawal. The court continued the trial docket call to March 10, 2003, to provide McCarty with an opportunity to retain new counsel. McCarty did not retain new counsel. On March 10, 2003, the trustee and Dennis McCarty agreed to submit the matter on the basis of the draft pretrial order tendered to the court on February 10, 2003. Rather than default the corporate defendant, the court agreed to enter the pretrial order and decide the matter on the merits based on that order.

The avoidance of an unauthorized post-petition transfer by the debtor of property of the bankruptcy estate constitutes a core matter over which this court has jurisdiction to enter a final judgment. 28 U.S.C. §§ 157(b)(2)(A) and (O) and 1334. This memorandum opinion contains the court's findings of fact and conclusions of law. Bankruptcy Rules 7052 and 9014.

McCarty provided pre-petition services to the debtor. On August 20, 2000, McCarty submitted an application for payment of $14,359.50 for work performed. On September 9, 2000, McCarty received a change order increasing the amount of services performed by $7,030.00.

On November 20, 2000, the debtor issued a check payable to McCarty in the amount of $14,359.50. The debtor filed its petition for relief under Chapter 11 of the Bankruptcy Code on November 21, 2000. McCarty had no notice of the bankruptcy

filing. The check cleared the debtor's bank and the funds were paid to McCarty on November 24, 2000. The debtor's bank account on which the check was drawn contained the debtor's gross receipts from its various jobs. With the transfer, McCarty did not pursue or perfect lien rights or claims against the third party owner of the subject improved real property or against the debtor's surety bond. The bankruptcy case was converted to a case under Chapter 7 on March 22, 2001.

Section 549(a) of the Bankruptcy Code provides in relevant part: "Except as provided in subsection (b) or (c) of this section, the trustee may avoid a transfer of property of the estate - (1) that occurs after the commencement of the case: and . . . (2)(B) that is not authorized under this title or by the court." 11 U.S.C. § 549(a).

Although the check was dated pre-petition, the date of the transfer for purposes of determining avoidability is the date the check clears the debtor's bank. Barnhill v. Johnson, 503 U.S. 393, 405 (1992); Mora v. Vasquez (In re Mora), 199 F.3d 1024, 1026-27 (9th Cir. 1999). The debtor therefore transferred the funds to McCarty "after the commencement of the case."

The court did not authorize the transfer.

McCarty contends, nevertheless, that the transfer was authorized under the Bankruptcy Code. The debtor filed its case under Chapter 11, thereby making the debtor a debtor in

possession. As a debtor in possession, unless the court orders otherwise, the debtor may operate its business, 11 U.S.C. § 1108, including using its property in the ordinary course of its business. 11 U.S.C. § 363(c)(1). However, the Code's authorization for the debtor in possession to use property of the estate in the ordinary course of its business does not apply to the post-petition payment of pre-petition debts. Still v. Rossville Bank (In re Chattanooga Wholesale Antiques, Inc.), 930 F.2d 458 (6th Cir. 1991). Therefore, the transfer was "not authorized under [the Bankruptcy Code]."

Section 549(b) does not apply. McCarty argues that § 549(c) does apply. McCarty contends that he acted in good faith. But the good faith provision of § 549(c) only applies to "a transfer of real property." The transfer in this case is not a transfer of real property. Consequently, § 549(c) does not apply.

The trustee has therefore established that the transfer may be avoided.

McCarty further asserts that it provided the debtor with reasonably equivalent value in exchange for the transfer. McCarty contends that it did not perfect its liens nor preserve its claims against the third party owner of the improved property or the surety company. However, McCarty had no secured claim against the debtor that it released. Further, McCarty has not shown that as a result of its release of any claim against the

third party owner, the owner, in turn, released funds to the debtor.

Finally, McCarty asserts, as a matter of equity, that the trustee cannot return McCarty to the status quo as of the petition date and, therefore, should not be able to recover the transfer. McCarty argues that on November 21, 2000, the petition date, McCarty had an unsecured claim against the debtor, but may also have had a lien it could have perfected against the third party owner of the improved real property and a claim against the debtor's surety bond it could have pursued. Thus, McCarty argues it was positioned to be paid in full. But, with the transfer, McCarty asserts it released its claims against the owner and against the surety. And, now, it may have to repay the trustee, leaving it with only its unsecured claim in the bankruptcy case.

However, from the estate's point of view, the debtor paid McCarty from its general unencumbered funds. The transfer to McCarty deprived the other general unsecured creditors from the opportunity to share in the distribution of those funds. The Bankruptcy Code fosters the concept that pre-petition general unsecured creditors should share pro rata in the debtor's unencumbered funds. The debtor violated that concept by the post-petition transfer of $14,359.50 to pay one pre-petition creditor at the expense of the other creditors. The Bankruptcy Code imposes a snap shot of the debtor and its creditors on the

petition date. Unless the court orders otherwise, that snap shot must be preserved until a Chapter 11 plan of reorganization is approved by the court or a Chapter 7 trustee distributes assets to creditors. The post-petition transfer to McCarty violated that basic tenet of the Bankruptcy Code. Section 549(a) allows the trustee to void the transfer, thereby restoring the basic integrity of the Code's treatment of all general unsecured creditors. The trustee is entitled to a judgment voiding the transfer.

Section 550(a) of the Code provides, in relevant part, that "to the extent a transfer is avoided under section . . .549 . . ., the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from - (1) the initial transferee of such transfer. . . ."

The transfer is avoided under § 549. McCarty is the initial transferee of the transfer. The trustee may therefore recover a money judgment equal to the amount of the transfer, to be used for the benefit of the estate.

Section 549(e) protects a good faith transferee who improves the transferred property. McCarty did not improve the transferred property. The subsection does not apply.

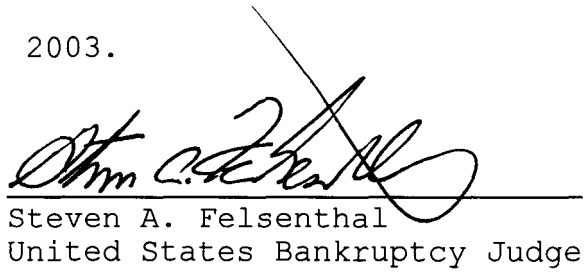
While the trustee is entitled to a money judgment under §§ 549(a) and 550(a), the court is mindful of the impact on

McCarty. After the entry of a judgment, the court is confident that the trustee will engage in settlement discussions with McCarty for the satisfaction of the judgment, if McCarty expresses reasonable, good faith offers.

Based on the foregoing,

IT IS ORDERED that James W. Cunningham, the Chapter 7 trustee, shall recover a judgment under 11 U.S.C. §§ 549(a) and 550(a) against McCarty & Associates, Inc., for $14,359.50, with post-judgment interest at the federal rate. Counsel for the trustee shall prepare a final judgment pursuant to this order.

Dated this 28th day of March, 2003.



Steven A. Felsenthal
United States Bankruptcy Judge