U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS
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IN THE UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS
FORT WORTH DIVISION

In re:	§	
	§	**Case No. 01-43345-BJH-7**
PROMEDCO OF NEW ENGLAND,	§	
	§	**Chapter 11**
Debtor.	§	
	§	
	§	
SHAWN K. BROWN, CHAPTER 7 TRUSTEE FOR PROMEDCO OF NEW ENGLAND, INC., AND PMC MEDICAL MANAGEMENT, INC.,	§	
	§	**Adv. Pro. No. 02-04187**
Plaintiff,	§	
	§	
- against -	§	
	§	
ROBERT M. SONTHEIMER,	§	
	§	
Defendant.	§	

I.

FINDINGS OF FACT

1. Shawn K. Brown (the "**Trustee**" and "**Plaintiff**"), is the duly appointed and authorized Chapter 7 Trustee for the Debtors, PMC Medical Management, Inc. ("**PMC Medical**") and Promedco of New England, Inc. ("**New England**") (hereinafter, PMC Medical and New England are collectively referred to as the "**Debtors**").

2. Robert M. Sontheimer (the "**Defendant**" and "**Sontheimer**") is an individual resident of Boston, Massachusetts, who had various connections over time to ProMedCo Management Company (**"Promedco Management"**) and PMC Medical.

3. The Debtors commenced their respective bankruptcy proceedings on May 4, 2001.

4. Promedco Management was, at all relevant times, the owner and holder of all of the equity interest in the Debtors.

5. Promedco Management filed its own bankruptcy proceeding on May 4, 2001, and that proceeding is also pending in this Court.

DEFENDANT'S CONNECTIONS TO PROMEDCO MANAGEMENT AND THE DEBTORS

6. Sontheimer was and is a leader and innovator in the fields of managed health care contracting and operations, and managed care financial risk management, and has a history of involvement in that industry.

7. Sontheimer was an original founder of Health Plans, Inc. ("**Health Plans**") in late 1992, and for four years served as its President and Chief Executive Officer. He was a 38% equity owner of Health Plans at the time of its acquisition by Promedco Management.

8. Effective December 3, 1997, Promedco Management purchased Health Plans and changed the name of the company to "PMC Medical."

9. Sontheimer was asked to stay on as President and CEO of PMC Medical for 3 years, and he served in that capacity until June of 2000.

10. Sontheimer also held the title of a "Vice President" of Promedco Management until June of 2000.

11. On June 29, 2000, Sontheimer met with Promedco Management President Wayne Posey ("**Posey**") and informed him that he intended to leave the Promedco group of companies.

12. Although Sontheimer was asked if he would remain with the Promedco group of companies as an "employee" until some other form of contractual arrangement could attempt to be negotiated, Sontheimer resigned as an officer of the companies at that time.

13. Sontheimer agreed to remain with the companies as an employee. Thereafter, Sontheimer viewed himself as performing in a role equivalent to that of a project manager.

14. All of Sontheimer's former responsibilities for management of physician practice groups were removed and transferred to Promedco Management's Vice President of Operations, Dale Edwards ("**Edwards**").

15. Sontheimer was never employed by, nor had any office, title, or other control position with, New England.

THE PROMEDCO MANAGEMENT CONSULTING AGREEMENT

16. In September 2000, Sontheimer and two officers of Promedco Management (Robert Smith, CFO of Promedco Management, and Edwards), commenced a period of arms-length negotiations which led to the drafting of a proposed consulting agreement (the "**Consulting Agreement**") between Sontheimer and Promedco Management.

17. Once fully negotiated, the proposed Consulting Agreement was presented by Edwards and/or Smith to Posey who signed it on behalf of Promedco Management on October 5, 2000.

18. The Consulting Agreement was also signed by Sontheimer.

19. As finally executed, the Consulting Agreement represents the results of good faith, arms-length negotiations between Sontheimer and Promedco Management. Sontheimer's "bargaining power" in the negotiation was confined to the fact that he did not have to sign any agreement with Promedco Management and could elect to look elsewhere if no satisfactory agreement was reached.

20. PMC Medical was neither a negotiant nor a party to the Consulting Agreement; neither was New England (as it was not yet formed at that point in time).

21. Sontheimer's tenure as an employee of Promedco Management ceased on October 6, 2000. Sontheimer's retention as a consultant to Promedco Management commenced on October 10, 2000. The Consulting Agreement provided for a two-year term, unless earlier terminated, at will, by either party.

22. Sontheimer agreed in the Consulting Agreement that he would devote his time and energies

on a first-priority basis to Promedco Management and its subsidiaries. The effect of the Consulting Agreement's obligation to give "first-priority" to Promedco Management's business needs caused Sontheimer to forego any other professional opportunities while the agreement was in place. In exchange for this exclusivity of services, and to compensate him for lost opportunities elsewhere, Sontheimer negotiated for, and received, a "priority fee" in the amount of $500,000 (paid in three monthly installments) in addition to a monthly consulting fee of $43,500 to be paid over the life of the agreement.

23. The former line responsibilities of Sontheimer at PMC Medical were assigned to Edwards. As a consultant, Sontheimer reported to Edwards. Sontheimer continued to provide services under the Consulting Agreement until shortly after the bankruptcy filings in May 2001.

SPECIFIC PAYMENTS IN QUESTION

24. Sontheimer received the following payments under the Consulting Agreement (collectively referred to hereinafter as the "**Transfers**"):

October 13, 2000	$210,500	(comprising $167,000 priority fee installment and $43,500 monthly fee; check written by PMC Medical)
November 13, 2000	$210,500	(comprising $167,000 priority fee installment and $43,500 monthly fee; check written by PMC Medical)
December 14, 2000	$204,500	(comprising the final priority fee installment of $166,000 and a shorted payment of monthly fee in the amount of $38,500; check written by PMC Medical)
December 21, 2000	$5,000	(to make up the shorted monthly fee payment; check written by PMC Medical)
December 28, 2000		(Sontheimer returned the December 14 payment of $204,500 to PMC Medical, and Trustee does not seek avoidance of the December 14, 2000, payment)
January 2, 2001	$204,500	(a re-issuance of the December 14, 2000 payment to bring Sontheimer's fee current; check written by New England)

25. Sontheimer continued to provide services under the Consulting Agreement after January 2, 2001, but was not paid for those services. The amount of earned but unpaid monies due under the Consulting Agreement for the months of January through May, 2001 was $198,650.

HISTORIC INCOME COMPARISONS

26. Sontheimer's compensation summary over the relevant years is as follows:

COMPENSATION PAYMENTS BY HEALTH PLANS, INC.

(38% Equity Interest)

YEAR	W-2 GROSS WAGES	1099 CONSULTING & MISC.
1993	$256,472.00	$2,200.00
1994	$299,796.59	
1995	$425,766.69	
1996	$574,311.83	
1997	$824,301.36	

COMPENSATION BY DEBTORS AND PROMEDCO MANAGEMENT AFTER PURCHASE BY PROMEDCO MANAGEMENT

(< 1% Equity Interest)

1997 (Dec. only)	$20,000	$560,000 (without 1099) $398,449
1998	$243,593.06	
1999	$313,881.35	
2000	$1,097,278.29	$421,000.00

SOLVENCY OF THE DEBTORS

27. On the dates of the Transfers, the relevant Debtor was insolvent.

PROMEDCO MANAGEMENT'S CASH MANAGEMENT SYSTEM

28. Jeff Kirby ("**Kirby**"), the controller of PMC Medical and/or New England, was the individual at PMC Medical and/or New England who was in charge of handling the Debtors' financial affairs and coordinating such activities with Promedco Management.

29. Kirby projected the cash needs and direct revenues of the Debtors on a weekly basis through a rolling four week financial forecast. On a weekly basis he would review the applicable Debtors' payables and anticipated direct revenues and submit to Promedco Management his request for the funds necessary to pay amounts owing to creditors of the applicable Debtor. Promedco Management would review Kirby's financial forecast and, to the extent funds were needed, advance those funds to the applicable Debtor within a day or two.

30. The advance of funds to the Debtors was reflected on inter-company accounts between Promedco Management and the Debtors. The Debtors operated as cost centers and thus were net borrowers from Promedco Management and were shown as owing monies to Promedco Management on the inter-company accounts.

31. However, when they were formed, Promedco Management knew that the Debtors would operate as cost centers and never intended that the inter-company accounts would be repaid by either Debtor. The Debtors were operated to provide services largely to the Promedco affiliated group of companies.

32. If Kirby's weekly financial forecast showed excess cash at the subsidiary level, that excess cash was wired to Promedco Management and credited against the outstanding balance on

the inter-company account. In fact, the funds were wired to a Promedco Management account at Bank of America, the lender to Promedco Management, and applied to reduce the outstanding balance on the revolving line of credit provided to Promedco Management by the bank. In this way, interest expense on borrowed funds was minimized at the parent company level.

33. During the October 13, 2000 through January 2, 2001 time period, the Debtors had very little direct revenue. Thus, Promedco Management provided substantially all of the funds needed to pay payables during this time period through borrowings on the bank revolving line of credit.

34. From time to time, Promedco Management would direct Kirby to pay Promedco Management's own obligations through the Debtors' respective accounts. When Kirby was so instructed, Promedco Management would advance the funds needed to make these payments and the applicable Debtor would issue its check to pay Promedco Management's obligation as directed.

THE PAYMENTS TO SONTHEIMER

35. At issue here are the payments made to Sontheimer under the Consulting Agreement.

36. As found previously, Promedco Management had a history of paying some of its own obligations by transferring funds into the account of a designated subsidiary and directing that subsidiary to issue the actual check used to pay Promedco Management's obligation(s).

37. In the case of payments to Sontheimer under the Consulting Agreement, Kirby was instructed by Promedco Management to place any upcoming scheduled payment to Sontheimer on the applicable Debtor's financial forecast which he would send to Promedco Management for review and approval. Promedco Management would then transfer sufficient funds to the applicable Debtor (PMC Medical or New England) to cover the normal payables of the Debtor plus any payments due to Sontheimer.

38. These funds would sit in the applicable Debtor's account for a brief period while administrative processes permitted the printing, signing and transmittal of the checks.

39. When prepared, Kirby would issue the checks to pay Sontheimer as he had been instructed by Promedco Management. The Debtors, through Kirby, handled these funds and performed this duty as directed by Promedco Management.

40. The payments to Sontheimer were, *de facto*, made by Promedco Management, with PMC Medical and/or New England serving as a conduit through which the payments were made.

41. By virtue of the cash management system and the parties' conduct with respect to the payments to Sontheimer, the parties manifested their consent that the Debtors act as Promedco Management's agent with respect to the payments to Sontheimer.

42. While the advance of funds by Promedco Management to PMC Medical and/or New England was reflected on the inter-company account, neither PMC Medical nor New England had any control over the funds used to pay Sontheimer, nor did the officers of either Debtor have any discretion as to how the funds were used. If either Debtor had ultimately refused to pay Sontheimer because it was not obligated to pay him pursuant to the Consulting Agreement, the funds would have been returned to Promedco Management pursuant to the cash management policies in place within the Promedco group of companies.

43. The Debtors' estates were not diminished as a result of the Transfers to Sontheimer because (i) Promedco Management continued to advance all funds needed by the Debtors to pay their direct operating expenses until shortly before these bankruptcy cases were filed; (ii) the inter-company account was never expected to be repaid; and (iii) if the Transfers to Sontheimer had not been made by the Debtors, the funds would have been returned to Promedco Management and would not have been available to pay other creditors of the Debtors (although it appears there were no other creditors who were unpaid at the time of the Transfers).

SONTHEIMER'S VALUE GIVEN IN EXCHANGE

44. Promedco Management and/or the Debtors benefitted from Sontheimer's work as a consultant pursuant to the terms of the Consulting Agreement. Sontheimer's principal accomplishments as a consultant (individually and/or by direction of others), insofar as they benefitted the Debtors, include:

    1. Restructured PMC Medical saving approximately $2 million in operating costs while maintaining its core capabilities.
    2. Prevented the loss of key employees at PMC Medical while the restructure was accomplished.
    3. Negotiated the sale of VIPS, a software system owned by PMC Medical that helped manage the risk associated with capitated health care contracts, for approximately $300,000.
    4. Negotiated (i) the elimination of a $300,000 – $500,000 claim flowing from PMC Medical's breach of the Maine HMO contract (which Promedco Management instructed PMC Medical to breach) and (ii) the collection of a $200,000 receivable due for the prior year from Maine HMO.
    5. Continued the operation of the Berkshire Regional Health Initiative which generated substantial fees to PMC Medical (estimated at $300,000 – $400,000 monthly).
    6. Negotiated the sale of certain radiology equipment which resulted in $1,000,000 being received by PMC Medical and $2,000,000 being received by another Promedco Management subsidiary, Berkshire.

45. Edwards, the Promedco Management officer to whom Sontheimer reported as a consultant, testified that these results would not have been realized by the Debtors and/or Promedco Management without Sontheimer's efforts. This testimony was not refuted by the Trustee.

46. Alternatively, and in light of these substantial accomplishments realized through Sontheimer's efforts, if the Transfers to Sontheimer were transfers of an interest of PMC Medical and/or New England in property, the Debtors received reasonably equivalent value in exchange for the Transfers.

47. The Transfers to Sontheimer were not made with any intent to hinder, delay or defraud the Debtors' creditors.

48. In fact, Sontheimer took the Transfers for value and in good faith. He performed in accordance with the terms of the Consulting Agreement until the Promedco companies filed for protection under the Bankruptcy Code. He honored his contractual obligation to serve Promedco Management on a first-priority basis as its consultant, and did not seek or accept positions outside of his work under the Consulting Agreement.

49. To the extent any finding of fact constitutes a conclusion of law, it shall be deemed a conclusion of law.

II.

CONCLUSIONS OF LAW

1. This Court exercises subject matter jurisdiction over this adversary proceeding pursuant to 28 U.S.C. §§ 157 and 1334 and the Standing Order of Reference of Bankruptcy Cases and Proceedings *Nunc Pro Tunc.* This matter is a core proceeding pursuant to 28 U.S.C. §§ 157(b)(2)(A), (F), and (H).

2. Venue is proper pursuant to 28 U.S.C. § 1409.

3. To prevail on a claim under § 548(a)(1)(A), the Trustee must establish (i) that the Debtor has an interest in property; (ii) that the Debtor has transferred this interest; (iii) that the transfer occurred on or within one year prior to the filing of the petition; and (iv) that the transfer was made with the actual intent to hinder, delay, or defraud any entity which was a creditor of the Debtor on or after the date of the transfer. 11 U.S.C. § 548(a)(1)(A); *In re McLaren*, 236 B.R. 882 (Bankr. D.N.D. 1999). The intent to hinder, delay or defraud are three separate elements, and each on its own may make a transfer fraudulent. *In re Brentwood Lexford Partners, L.L.C.*, 292 B.R. 255 (Bankr. N.D. Tx. 2003).

4. The elements of a claim of constructive fraud under § 548(a)(1)(B) are that (i) the Debtor transferred an interest in property; (ii) the transfer of that interest occurred within one year prior to the filing of the petition; (iii) the Debtor was insolvent on the date of the transfer or became insolvent as a result thereof; and (iv) the Debtor received less than reasonably equivalent value in exchange for such transfer. *In re GWI PCS 1 Inc.,* 230 F.3d 788, 805 (5th Cir. 2000).

5. The Trustee bears the burden of proving the elements of a fraudulent transfer under § 548. *In re Maple Mortgage, Inc.*, 81 F.3d 592 (5th Cir. 1996).

6. Plaintiff has failed to show that the Transfers in question meet all of the elements of §548(a)(1)(A) and/or (B). While the Debtors were insolvent when the Transfers were made, the Transfers were not transfers of an interest of either Debtor in property.

7. An agent is a person who consents to act on behalf of and subject to the control of another, the principal, who has consented that the agent shall so act. *Walker Ins. Svcs v. Bottle Rock Power Corp.*, 108 S.W. 3d 538 (Tex. App - Houston, 2003). Under Texas law, agency is a fiduciary relationship and thus an agent who misapplies the funds of his principal is constructively a trustee for the principal. *In re Carolin Paxson Adverstising, Inc.*, 938 F.2d 595 (5th Cir. 1991). The Debtors acted as agents of Promedco Management with respect to the Transfers.

8. Funds passed to a subsidiary corporation by a parent corporation for the sole and express purpose of paying an obligation of the parent corporation creates, in the context of an agency relationship, a trust-like relationship between the parent and the subsidiary until such time as those funds are properly distributed to the intended recipient. Such funds are not properly available for payment of the general creditors of the subsidiary.

9. A mutually agreed arrangement between parent and subsidiary corporations whereby one will receive, hold, and distribute funds belonging to the other establishes an agency with respect to the payment of the funds and creates a trust-like relationship on the part of the entity holding such funds, and places on that entity the fiduciary duty to protect and handle the funds as lawfully directed by their owner.

10. Issuance of a check is not dispositive as to the ownership of the funds represented by such check. *Southmark Corp. v. Grosz (In re Southmark Corp.),* 49 F.3d 1111 (5th Cir. 1995) (fact that subsidiary was identified as payor on a check and on the transferee's W-2 form was not dispositive; funds found to be a transfer of property of the parent).

11. The specifically "earmarked" transfers of funds from Promedco Management to its subsidiary (PMC Medical or New England) for the express purpose of funding subsidiary checks to be issued to discharge the financial obligations of Promedco Management to Sontheimer, did not deprive Promedco Management of ownership of such funds. The checks issued to Sontheimer in accordance with that intended process does not constitute a transfer of an interest of that subsidiary (PMC Medical or New England) in property, when the subsidiary exercised no control over the funds and had no discretion as to their use. *Coral Petroleum, Inc. v. Banque Paribas-London*, 797 F.2d 1351 (5th Cir. 1986).

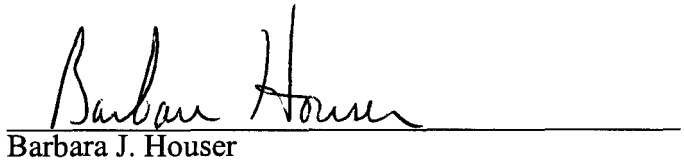
12. The Debtors' estates were not diminished by the Transfers because if the funds were not paid to Sontheimer, they would have been returned to Promedco Management in accordance with the cash management policies in effect within the Promedco group of companies and would not have been available to pay other creditors of the applicable Debtor.

13. Alternatively, if the Transfers were made from an interest of the Debtors in property, the Transfers were not made with any intent to hinder, delay or defraud creditors of the Debtors. Moreover, the Debtors received reasonably equivalent value in exchange for the Transfers.

14. Plaintiff is not entitled to avoid and recover the Transfers from Sontheimer pursuant to §550 of the Bankruptcy Code.

15. To the extent any conclusion of law constitutes a finding of fact, it shall be deemed a finding of fact.

SIGNED: December 18, 2003.



Barbara J. Houser
United States Bankruptcy Judge