**The following constitutes the ruling of the court and has the force and effect therein described.**

**Signed July 15, 2021**

**United States Bankruptcy Judge**

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

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| **In re:** | § | **Chapter 7** |
| **ESSENTIAL FINANCIAL EDUCATION, INC.** | § | **Case No. 18-33108** |
| **Debtor.** | § | |
| **DANIEL SHERMAN, CHAPTER 7 TRUSTEE,** | § | |
| **Plaintiff,** | § | |
| **v.** | § | **Adv. Pro. No. 20-3170** |
| **THOMAS J. CAUFIELD, *et al.*,** | § | |
| **Defendants.** | § | |

**ORDER REGARDING MOTION FOR SUMMARY JUDGMENT OF PARAMOUNT STRATEGIES, INC.**

Before this Court is the Motion for Summary Judgment [ECF No. 35] and Brief in Support Thereof [ECF No. 36], as supplemented on May 20, 2021 [ECF No. 59] (together, the "**MSJ**"), filed by Paramount Strategies, Inc. ("**Paramount**"). In the MSJ, Paramount requests summary judgment on all of the claims Daniel J. Sherman, the Chapter 7 Trustee (the "**Trustee**") for Essential Financial Education, Inc. (the "**Debtor**"), has made against Paramount. For the reasons that follow, the Court will grant the MSJ, in part and deny in part.

## I. Jurisdiction

This Court has subject matter jurisdiction over this proceeding pursuant to 28 U.S.C. § 1334. This is a core proceeding under 28 U.S.C. § 157(b). The bankruptcy court has authority to adjudicate this matter pursuant to the United States District Court for the Northern District of Texas Miscellaneous Order No. 33. The following shall constitute this Court's reasoning pursuant to Rule 56 of the Federal Rules of Civil Procedure, as made applicable in adversary proceedings pursuant to Rule 7056 of the Federal Rules of Bankruptcy Procedure.

## II. Factual and Procedural History

The Debtor operated a franchised trading academy in Frisco, Texas under the unregistered, assumed name of Online Trading Academy of Dallas ("**OTA Dallas**"). On April 30, 2018, Paramount and the Debtor entered into an Asset Sale Agreement (the "**ASA**"), whereby Paramount purchased the OTA Dallas franchise and substantially all of the Debtor's other assets. Pl.'s Am. Compl. ¶ 23. The ASA provided, among other things, that $150,000.00 (the "**Withheld Purchase Price**") would be held back for a period of six months following the Closing Date (as defined below) to offset any "**Seller's Liabilities**" which occurred or were incurred prior to the Closing Date. *Id.* ¶ 24. In the ASA, Seller's Liabilities are defined to include, among other things, liabilities or obligations arising out of, or related to, the Debtor's operation of OTA Dallas prior to the

Closing Date, except for those liabilities that Paramount expressly agreed to assume and which are identified in Schedule 3(b) to the ASA. Def.'s Sup. Mot. Summ. J. Ex. 1-A, p. 4. In addition to Seller's Liabilities, the ASA permits Paramount to offset student refunds on services sold prior to the Closing Date up to 90 Days after the Closing Date so long as the services requested were sold before the Closing Date.[1] The sale closed on June 21, 2018 (the "**Closing Date**"). Pl's Resp. to Def.'s Mot. Summ. J. ¶ 9.

On June 20, 2018, the Debtor and Paramount executed an Escrow Holdback Agreement (the "**Escrow Agreement**") with J.P. Barth Law Firm, PLLC (the "**Escrow Agent**") to open an escrow account (the "**Escrow Account**"). Pl.'s Am. Compl. ¶ 26. The Escrow Agreement provided, in relevant part, that:

> The term of this [Escrow] Agreement will be six months from the date hereof. During the term and in accordance with this [Escrow] Agreement, Escrow Agent is authorized and directed to disburse funds from the Escrow Amount to Buyer [(Paramount)] for any liabilities of Depositing Party [(the Debtor)] occurring or which were incurred prior to closing, whether known or unknown as of the Closing Date, but that affect Buyer after closing, including but not limited to reimbursements for refunds for pre-paid education as referenced in the [ASA]. Buyer shall present all requests for draws in writing to Escrow Agent and Depositing Party and include any applicable invoices or evidence of the liabilities incurred by Buyer that are the responsibility of Depositing Party.

Def.'s Mot. Summ. J. Ex. 1-C, p. 1. Pursuant to the ASA and the Escrow Agreement, the Withheld Purchase Price was to be held in the Escrow Account. *Id.* ¶ 27. Paramount deposited a total of $2,314,248.09 into the Escrow Account on June 28 and 29, 2018. Def.'s Mot. Summ. J. Ex. 1-E and 1-F. All funds, save and except the Withheld Purchase Price, were transferred to a different escrow maintained by UMB Bank, Inc. (the "**UMB Escrow Account**").

[1] For the sake of simplicity, hereinafter, student refunds will be included in defined term, Seller's Liabilities.

On August 30, 2018, the Escrow Agent released $33,498.00 of the Withheld Purchase Price from the Escrow Account to the Debtor and $116,402.00 to Paramount (the "**Paramount Escrow Transfer**") by agreement of the parties. Pl.'s Am. Compl. ¶¶ 44, 48; Def.'s Mot. Summ. J. Ex. 1-H. Less than a month later, on September 25, 2018, a creditor filed a Chapter 7 Involuntary Petition against the Debtor. Case No. 18-33108, ECF No. 1. The Court entered the Order for Relief on November 15, 2018. Case No. 18-33108, ECF No. 14.

On November 16, 2020, the Trustee initiated this Adversary Proceeding against Paramount and several other defendants when he filed his Original Adversary Complaint to Avoid and Recover Transfers from Insiders and Affiliates [ECF No. 1].[2] The complaint was amended with leave of Court on December 31, 2020 (as amended, the "**Complaint**") [ECF No. 27]. In the Complaint, as it relates to Paramount, the Trustee alleges that the August 30, 2018 Paramount Escrow Transfer was a fraudulent and/or preferential transfer of the Debtor's property. Pl.'s Am. Compl. ¶¶ 48-51; 57-60.

Paramount's primary argument in the MSJ is that there was no transfer of property of the estate for the purposes of Sections 547 and 548 of the Bankruptcy Code. The crux of Paramount's argument is that the Withheld Purchase Price was placed into the Escrow Account for the benefit of Paramount to offset any Seller's Liabilities which occurred or were incurred prior to the Closing Date. Since the funds were held in escrow, Paramount asserts that the Debtor did not have any legal or equitable interest in the property transferred in connection with the Paramount Escrow Transfer.

[2] Transfers made to other defendants in the Adversary Proceeding were made from the UMB Escrow Account and under different circumstances. Thus, these transfers are immaterial to the MSJ.

On June 11, 2021, the Trustee filed his Brief in Support of Response to Paramount's MSJ [ECF No. 63] (the "**Response**"). In his Response, the Trustee contends that the Debtor obtained legal and equitable title to the Withheld Purchase Price on the Closing Date in large part because the Withheld Purchase Price constituted the Debtor's sale proceeds. The Trustee argues that, in the alternative, the Debtor had an equitable interest in at least some of the funds that were transferred in connection with the Paramount Escrow Transfer, because Paramount received funds that were not Seller's Liabilities.

A number of pleadings followed: 1) Paramount's Reply to Trustee's Response to Motion for Summary Judgment [ECF Nos. 67 and 68]; 2) Trustee's Motion to Strike Paramount's Summary Judgment Reply Appendix, or in the Alternative, Motion for Leave to File a Surreply (the "**Motion to Strike**") [ECF Nos. 69, 71, and 74]; 3) Trustee's Motion to File Under Seal his proposed Surreply Appendix (the "**Motion to Seal**") [ECF No. 70]; and 4) Paramount's Response to Trustee's Motion to Strike Paramount's Summary Judgment Reply Appendix, or in the Alternative, Motion for Leave to File a Surreply [ECF No. 73].

On June 30, 2021, the Court held a hearing on the MSJ, the Motion to Strike, and the Motion to Seal. The Court granted the Motion to Seal. It denied the Motion to Strike as it related to the Trustee's request to strike Paramount's Summary Judgment Reply Appendix but granted his request for leave to file a surreply. The Court then took up the MSJ, wherein the parties presented argument as to why the MSJ should be granted or denied. After due consideration of those arguments, the parties' pleadings, and the evidence presented in support of their respective arguments, the Court believes that the MSJ should be granted, in part, and otherwise denied.

## III. Summary Judgment Standard

Summary judgment is proper if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the movant is entitled to judgment as a matter of law. See Fed. R. Civ. P. 56, as made applicable by Fed. R. Bankr. P. 7056; *Celotex Corp. v. Catrett*, 477 U.S. 317, 322 (1986). A court's role at the summary judgment stage is not to weigh the evidence or determine the truth of the matter, but rather to determine whether a factual dispute exists for trial. *Peel & Co., Inc. v. The Rug Market*, 238 F.3d 391, 394 (5th Cir. 2001). To support or refute an assertion that a genuine factual dispute exists, the parties must cite to particular parts of the record, show that the materials cited do not establish the absence or presence of a general dispute, or show that an adverse party cannot produce, rather than simply has not produced, admissible evidence to support the fact. Fed. R. Civ. P. 56(c)(1). A factual dispute is genuine, and therefore precludes summary judgment, if the evidence supporting it would allow a reasonable factfinder to return a verdict for the non-movant. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986). Finally, to prevail at summary judgment on a claim on which a party has the burden of proof at trial, the party must establish "beyond peradventure all of the essential elements of the claim or defense." *Bank One, N.A. v. Prudential Ins. Co. of America*, 878 F. Supp. 943, 962 (N.D. Tex. 1995) (quoting *Fontenot v. Upjohn Co.*, 780 F.2d 1190, 1194 (5th Cir. 1986)).

## IV. Analysis

### A. Interest of the Debtor in Property Transferred

The primary question for this Court to decide is whether the Debtor had an interest in the funds transferred to Paramount via the Paramount Escrow Transfer. For purposes of determining whether a debtor has an interest in property in the context of an avoidable transfer, that property

must constitute property of the debtor's bankruptcy estate *but for* the debtor's transfer of such interest. *Cage v. Wyo-Ben, Inc. (In re Ramba, Inc.)*, 437 F.3d 457, 459 (5th Cir. 2006) (citing *In re Criswell*, 102 F.3d 1411, 1416 (5th Cir. 1997)).

"Interest of the debtor in property" is not defined in the Bankruptcy Code. *In re Jenkins*, 617 B.R. 91, 104 (Bankr. N.D. Tex. 2020) (Morris, J.). The Bankruptcy Code does, however, describe property of a debtor's estate, which includes all legal and equitable interests in property as of the commencement of the bankruptcy case. 11 U.S.C. § 541(a)(1). This seemingly broad interpretation of what constitutes property of the estate is tempered by Section 541(d) of the Bankruptcy Code, which provides that: "Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest . . . becomes property of the estate . . . only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold." *Id.* at § 541(d). The Fifth Circuit, in analyzing these provisions, has determined that bare legal title is insufficient for a debtor to have an interest in property. Rather, the debtor must have an equitable interest in the property transferred. *Ramba*, 437 F.3d at 460-61.

"The nature and extent of the debtor's interest in property is analyzed by reference to the applicable state law." *In re Missionary Baptist Foundation of America, Inc.*, 792 F.2d 502, 504 (5th Cir. 1986); *see also Butner v. United States*, 440 U.S. 48, 54 (1979) (Congress, in drafting the Bankruptcy Code, "left the determination of property rights in the assets of a bankrupt's estate to state law."). In Texas, where a grantor executes an escrow agreement and deposits funds into an escrow, the grantor retains legal title of the subject matter, with equitable title passing to the ultimate grantee. *Id.* (citing *Cowden v. Broderick & Calvert,* 131 Tex. 434, 440-41, 114 S.W.2d 1166, 1169 (1938); *Hudgins v. Krawetz,* 558 S.W.2d 131, 134 (Tex.Civ.App.—San Antonio 1977,

no writ)). "The ultimate disposition of the subject matter to the grantor or grantee is determined by the terms of the agreement, upon fulfillment of the necessary conditions." *Id.*

*i. Was there a true escrow?*

As a threshold matter, the Court must analyze whether Paramount and the Debtor created a true escrow account arrangement. *Quinlan v. AFI Servs., LLC (In re AFI Servs., LLC)*, 486 B.R. 827, 835 (Bankr. S.D. Tex. 2013). "Under Texas law, an escrow is created only when the parties come to a clear and definite agreement directing that the funds be deposited with a third party and specifying the terms and conditions on which the third party is required to deliver the funds." *Affiliated Computer Sys., Inc. v. Sherman (In re Kemp),* 52 F.3d 546, 551 (5th Cir.1995). Although the parties do not dispute whether an escrow was created by virtue of the Escrow Agreement, the Court will nevertheless briefly address the issue.

Per the Escrow Agreement, dated June 20, 2018, the Debtor, as the Depositing Party, deposited $150,000.00 out of the proceeds of the sale of its business with the Escrow Agent to be held in escrow. Def.'s Mot. Summ. J. Ex. 1-C, p. 1; *see also, Id.* Ex. 1-B, p. 4-5. The Escrow Agreement was signed by all parties. *Id.* Ex. 1-C, p. 4. Under the heading "Terms and Conditions," the terms and conditions upon which the Escrow Agent was required to deliver the Withheld Purchase Price to either Paramount or the Debtor were specified. *See Id.* Ex. 1-C. Thus, under Texas law, as of June 20, 2018 (or, in any event, no later than June 21, 2018, which was the date specified in the Bill of Sale (Pl.'s Resp. to Def.'s Mot. Summ. J. Ex. 2)), the grantor Debtor obtained legal title to the escrowed funds, with equitable title passing to the ultimate grantee.[3]

[3] This conclusion is consistent with the Settlement Statement, also dated June 20, 2018, which provides that the gross amount due to the Debtor was $2.3 million, less a $150,000.00 reduction in the amount "due to Seller" for Escrow Holdback for Chargebacks. Pl.'s Mot. Summ. J. Ex. 1-B, p. 1. Paramount argued that the Escrow Account was actually funded on June 28 or 29, 2018; however, such date is immaterial as the Escrow Account was created by agreement on June 20, 2018 pursuant to the terms of the Escrow Agreement, and the transfer that is being challenged is *not* that of the creation of the Escrow Account.

*ii. Did placing funds into the Escrow Account materially alter the parties' rights?*

Paramount asserts that the Debtor had no interest in the Withheld Purchase Price before the funds were placed into the Escrow Account. As discussed above, Paramount's argument is belied by the terms of the Escrow Agreement (which recites that the Debtor deposited the funds), the Settlement Statement, and by the nature of the transaction, pursuant to which a portion of the sale proceeds were held back to determine *whether* Seller's Liabilities would be incurred. Def.'s Sup. Mot. Summ. J. Ex. 1-A, p. 5. Simply placing the sale proceeds into the Escrow Account did not materially alter the parties' rights. Rather, it extended the status quo under the ASA—the parties' rights would be determined based upon the terms and conditions contained in the Escrow Agreement. *See In re Price*, 589 B.R. 690, 702 (D. Haw. 2018) ("[T]o show that the escrow deposit sufficiently changed Debtor's interest in the funds so that it was without value and did not become part of the bankruptcy estate, it is at least necessary that the escrow deposit altered the status quo").

*iii. Who had an equitable interest in the funds in the Escrow Account?*

The question that remains is whether the terms and conditions of the Escrow Agreement completely divested the Debtor of an interest in the escrowed funds. Stated simply, they did not. In the instance where a contingency occurs pre-petition that would *completely* wipe out a debtor's interest in an escrow fund, the debtor is deemed to have no interest in the property and the transfer is not avoidable. *Missionary Baptist*, 792 F.2d at 506; *In re Newcomb*, 744 F.2d 621, 626–27 (8th Cir. 1984). This is because "to be avoidable a transfer must deprive the debtor's estate of something of value which could otherwise be used to satisfy creditors." *Newcomb*, 744 F.2d at 626. This conclusion is logical as it relates to the vast majority of simple escrows wherein the entirety of the corpus of the escrow (*e.g.*, the purchase price for real estate) goes to one party or the other if the contingency is/is not satisfied. It is more difficult, however, where the choice is not binary, *i.e.*

where the proceeds of escrow could be split in some manner, like pieces of a pie. In that case, a transfer of a *portion* of the proceeds (or a piece of the pie) *does* deprive the debtor's estate of something of value which could otherwise be used to satisfy creditors. The debtor's estate has been diminished by the "missing piece."

In this instance, the Court must look to the substance of the interests transferred at the time the funds were transferred out of the escrow. *See Newcomb*, 744 F.2d at 626. In doing so, Fifth Circuit precedent dictates that the Court should construe "the parties' rights in accordance with applicable state law *and the terms of their contracts*." *Missionary Baptist*, 792 F.2d at 506 (emphasis added). In reviewing the terms of both the ASA and the Escrow Agreement, as *Missionary Baptist* instructs, Paramount and the Debtor were both grantees. Paramount had equitable rights in the escrowed funds in the Escrow Account only to the extent of Seller's Liabilities. The Debtor, on the other hand, had equitable rights in the escrowed funds after accounting for any Seller's Liabilities. In *Missionary Baptist*, the Fifth Circuit took a similar approach where an escrow was involved, holding that, despite the fact that the contingency in that case was satisfied post-petition (where a stronger case can generally be made that escrowed funds are property of the estate), the Trustee could not recover the entire escrow. Instead, he was able to recover the escrowed funds *subject to* proration of taxes and insurance up to the date that the contingency was satisfied, which funds belonged to the non-debtor party to the escrow. *Id.* **In other words, the Fifth Circuit carved the pie.** *See Countryman v. Eisner (In re Eisner)*, No. 06-4154, 2007 WL 2479654, at *5 (Bankr. E.D. Tex., Aug. 28, 2017) (determining that the debtor was not only a depositor, but a grantee with an equitable interest in 74.72% of proceeds of a sale that were placed in escrow, and that the bankruptcy trustee could avoid transfer out of the escrow to non-debtor third parties).

*iv. How should the pie be carved?*

The fact that the parties appear to have agreed to use the Escrow Account to resolve *all* of their claims against each other in connection with the sale by execution of the Authorization for Release of Escrowed Funds (Def.'s Mot. Summ. J. Ex. 1-H) does not alter the substance of the Escrow Agreement, its purpose, or the rights attendant to it. Instead, for purposes of this MSJ, the Court must determine whether Paramount established as a matter of law that some or all of the funds it received via the Paramount Escrow Transfer were Seller's Liabilities pursuant to the terms of the ASA. If they were, the Debtor had no equitable interest in the funds transferred and, thus, the Trustee may not avoid such transfer.

Here, Paramount established as a matter of law, and the Trustee failed to allege a material fact issue, as to:

1) $54,400.00 in student refunds processed, but not funded prior to the Closing Date (*Id.* Ex. 1-G);
2) $8,470.48 in new refunds post-closing (*Id.* Ex. 1-G; Pl.'s Resp. to Def.'s Mot. Summ. J. Ex. 10); and
3) $1,395.00 in vendor payments (Def.'s Mot. Summ. J. Ex. 1-G).

Therefore, the Court will grant summary judgment to Paramount as to $64,265.48. This means that the total amount that is potentially subject to avoidance is **$85,634.52**, which is the starting amount of the Escrow Account, $150,000.00, less the $100.00 draw fee that was paid to the Escrow Agent, less the $64,265.48 in which the Court determines the Debtor did not have an interest as a matter of law. The Court agrees with the Trustee that the starting point of the analysis is $150,000.00 rather than the $116,402.00 that Paramount actually received in connection with the Paramount Escrow Transfer for two reasons. First, $150,000.00 is the whole "pie." In challenging the transfer

that came out of the escrow, the Court must first put the pie back together by reassembling all of the pieces. Secondly, the evidence suggests that Paramount and the Debtor mutually agreed to the $116,402.00/$33,498.00 split after a few mutual offsets that did not necessarily involve the original purpose of the Escrow Agreement. For the reasons stated above, the Debtor had an interest in the entirety of the funds *before the transfer took place*.

In reaching this conclusion, the Court is not weighing in on the propriety of Paramount's ability to offset/recoup amounts owed to it against amounts it owed to the Debtor as Paramount did not move for summary judgment on that defense. It may very well be the case that setoff/recoupment is proper, especially where the corresponding obligations arose out of the same transaction. However, it is inappropriate to do so at this juncture. The Court is also not ruling that the Debtor had an equitable interest in the remaining $85,634.52. Rather, the Court is holding that Paramount did not establish as a matter of law that the Debtor did not have an interest in such funds.

The Court believes that this decision is consistent with its ruling in *Sherman v. OTA Franchise Corporation (In re Essential Financial Education, Inc.)*, No. 20-3092, 2021 WL 1748202 (Bankr. N.D. Tex. May 3, 2021). In that case, the Court analyzed whether the Debtor had an equitable interest in certain funds transferred via an escrow agent to OTA Franchise Corporation ("**OTA**"). OTA argued that it held a perfected lien encumbering all of the Debtor's assets and/or that it held an equitable lien in the same. The Court rejected OTA's argument that it had an equitable interest in the property transferred at the time of the transfers. The Court held that, as a matter of law, OTA did not have a perfected lien encumbering the Debtor's assets or an equitable lien thereon. Therefore, given the escrowed funds in that case were property of the Debtor's estate in the nature of sale proceeds, but for the transfer to OTA, the Debtor would have had an equitable

interest in *all* of the transferred funds. *Id.* at *12. In this case, but for the Paramount Escrow Transfer, the Debtor only had an interest in the transferred funds *to the extent* that they did not constitute Seller's Liabilities. In both cases, the Court is effectuating the purpose of avoidance actions, which is to preserve the property available for distribution to creditors—no more, no less. *See Begier v. I.R.S.*, 496 U.S. 53, 58-59 (1990).

**B. Intent to Hinder, Delay, or Defraud Creditors/Reasonably Equivalent Value**

Paramount next claims that it is entitled to summary judgment on: 1) the Trustee's First and Second Claims because the Paramount Escrow Transfer was not made with the intent to hinder, delay, or defraud creditors; and 2) the Trustee's Third, Fourth, and Fifth Claims as the Debtor received reasonably equivalent value in exchange for the Paramount Escrow Transfer. In rare cases, summary judgment may be appropriate on the question of fraudulent intent, "such as when the defendant admits the fraud, the conveyance instrument is fraudulent on its face, the defendant retains an interest in the property inconsistent with the conveyance alleged, or the evidence indisputably reveals that the transfer was made [with] the intent to defraud." *Hoffman v. AmericaHomeKey, Inc.*, No. 3:12-CV-3806-B, 2014 WL 7272596, at *11 (N.D. Tex. Dec. 22, 2014) (citing *BMG Music v. Martinez*, 74 F.3d 87, 90 (5th Cir. 1996)).

This is not one of those cases. Instead, Paramount has presented conclusory statements reciting its version of the facts in the MSJ, without supporting briefing. The Trustee raised a factual dispute as to intent in his Response; therefore, this Court concludes that there is a material factual dispute regarding whether the Debtor possessed the requisite intent to hinder, delay, or defraud creditors. As to whether the Debtor received reasonably equivalent value, the Court agrees with the Trustee that Paramount did not even make out a *prima facie* showing that it was entitled to judgment as a matter of law on this issue.

**C. Attorneys' Fees**

Lastly, Paramount seeks summary judgment on the Trustee's request for attorneys' fees under Section 362(k) of the Bankruptcy Code and Tex. Civ. Prac. & Rem. Code § 38.001. In light of the Trustee's withdrawal of his request for attorneys' fees under those provisions, the Court will grant the MSJ. For the avoidance of doubt, the Court is not making any ruling as to the Trustee's request for attorneys' fees pursuant to Tex. Bus. & Comm. Code § 24.013, which request was not withdrawn and was not addressed in the MSJ.

Based upon the foregoing:

**IT IS HEREBY ORDERED** that the MSJ is **GRANTED IN PART** and **DENIED IN PART** as provided herein.

**###END OF ORDER###**