SO ORDERED.

SIGNED this 26 day of March, 2007.

A. Thomas Small
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF NORTH CAROLINA
RALEIGH DIVISION

IN RE:	**CASE NO.**
JACOBSEN CONSTRUCTION, INC.	**04-03490-5-ATS**
DEBTOR	
JOSEPH N. CALLAWAY, Trustee	
Plaintiff	**ADVERSARY PROCEEDING NO.**
v.	**S-06-00028-5-AP**
KIDDCO, INC.	
Defendant.	

ORDER ALLOWING PARTIAL SUMMARY JUDGMENT

The matter before the court in this adversary proceeding brought by Joseph N. Callaway, trustee for the chapter 7 debtor, Jacobsen Construction, Inc., to recover pursuant to 11 U.S.C. § 547(b), or alternatively pursuant to 11 U.S.C. § 548(a)(1), payments totaling $111,270.34, made by Jacobsen Construction, Inc. to the defendant, Kiddco, Inc., is the plaintiff's motion for partial summary judgment. The plaintiff is seeking in this motion to recover only one of the payments in the amount of $55,625.27, and is

proceeding only pursuant to § 547(b). A hearing took place in Raleigh, North Carolina on January 30, 2007.

This bankruptcy court has jurisdiction over the parties and the subject matter of this proceeding pursuant to 28 U.S.C. §§ 151, 157, and 1334, and the General Order of Reference entered by the United States District Court for the Eastern District of North Carolina on August 3, 1984. This is a "core proceeding" within the meaning of 28 U.S.C. §§ 157(b)(2)(F) and (H), which this court may hear and determine.

Jacobsen Construction, Inc. was the general contractor pursuant to a construction contract with Wake Technical Community College, dated January 27, 2003, to construct the Wake Tech Automotive and Heavy Equipment Technology Complex. Kiddco, Inc. was a subcontractor pursuant to a subcontract with Jacobsen, dated April 7, 2004, and signed on April 12, 2004, to perform grading and grading-related construction services at the project. Def. Ex. 4. The general contract between Jacobsen and Wake Tech and North Carolina General Statute § 44A-26 required a bond that was provided by the Developers Surety and Indemnity Company to assure performance and the payment of subcontractors.

Kiddco performed grading work under the subcontract and issued its first invoice to Jacobsen in the amount of $90,625.27 on May 7, 2004. Although the subcontract called for payment in 30 days, the invoice erroneously stated that the payment was due in 15 days. Jacobsen made a partial payment of $35,000 on June 8, 2004, leaving an unpaid balance of $55,625.27. Kiddco was concerned that the full amount of the invoice was not paid and threatened to leave the job if it did not receive payment for the full amount of the invoice. Jacobsen delivered a $55,625.27 check to Kiddco on June 29, 2004, and although Kiddco had begun to "demobilize" on June 25, with the payment on June 29, Kiddco stayed on the job and was still on the job when Jacobsen stopped work on August 5, 2004. Kiddco issued 2 more invoices, one on June 2, 2004, in the amount of $102,366.70 and one on July 28, 2004 in the amount of $113,878.76, but Jacobsen made no other payments to Kiddco on the Wake Tech project.[1] The bonding company,

[1]Jacobsen did make payments to Kiddco on two other projects. Those payments are the subject of this adversary proceeding, but are not part of this motion for summary judgment.

Developers Surety and Indemnity Company, completed the construction work for Wake Tech and employed Kiddco to do extra work not contemplated by the original contract. On October 11, 2004, Kiddco and the surety executed a ratification agreement that contained mutual releases, including a release by Kiddco to the surety for liability for the Kiddco invoices paid by Jacobsen. Affidavit of Tom Kidd, Ex. 1. Kiddco received partial payment from the bonding company for the outstanding two invoices. Def. Ex. 3, Defendant's Answer to Interroratory #14.

Jacobsen filed a voluntary petition for relief under chapter 7 of the Bankruptcy Code on September 24, 2004, and Mr. Callaway was appointed trustee. The trustee contends that he is entitled to summary judgment because there is no genuine issue with respect to the requirements of § 547(b) and the defendant has offered no facts supporting its defenses.

"[S]ummary 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 moving party is entitled to a judgment as a matter of law.'" Celotex Corp. v.Catrett, 477 U.S. 317, 322, 106 S. Ct. 2548, 2552 (1986). In making this determination, conflicts are resolved in the light most favorable to the non-moving party. United States v. Diebold, Inc., 369 U.S. 654, 82 S. Ct. 993 (1962). Summary judgment should not be granted unless the moving party establishes his right to judgment "with such clarity as to leave no room for controversy." Portis v. Folk Constr. Co., Inc., 694 F.2d 520, 522 (8th Cir. 1982).

11 U.S.C. § 547(b) states:

> Except as provided in subsection (c) 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 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 yet been made; and

> (C) such creditor received payment of such debt to the extent provided by the provisions of this title.

11 U.S.C. § 547(b).

Kiddco's first defense is that § 547(b) is inapplicable because there was no transfer to Kiddco of "an interest of the debtor in property." Specifically, Kiddco argues that the $55,625.27 payment was not "an interest of the debtor in property" because the funds from which the payment was made were subject to a trust in favor of Kiddco and Jacobsen's other subcontractors. According to Kiddco, the funds paid by the project owner (Wake Tech) to the general contractor (Jacobsen) are subject to a trust in favor of the subcontractors (including Kiddco). Kiddco maintains that Jacobsen was merely a conduit for payments made by Wake Tech. Although in some states, for example the state of Michigan, funds paid to a general contractor are held in trust, see Mich. Comp. Laws § 570.151 (2006), no such trust is created under North Carolina law. North Carolina General Statute § 22C-3 requires a general contractor to pay subcontractors within seven days from the receipt of payment by the general contractor, Statesville Roofing & Heating Co. v. Duncan, 702 F. Supp. 118 (W.D.N.C. 1988), but that statute does not create a trust. Furthermore, no trust is created by the terms of the general contract, which, like the North Carolina statute, requires payment in seven days, or by the terms of the subcontract, which requires payment in 30 days. In the absence of a trust, the funds owed to a general contractor in bankruptcy do not belong to the subcontractors and are part of the general contractor's bankruptcy estate. Grochal v. Ocean Technical Services Corp. (In re Baltimore Marine Industries), 476 F.3d 238 (4th Cir. 2007). There being no trust, the payment made to Kiddco was a "transfer of an interest of the debtor in property" as that term is used in § 547(b).

It is not contested that the trustee has established the elements of a preferential transfer under § 547(b)(1) through (4). There was a transfer (payment of $55,625.27) for or on account of an antecedent debt (invoice for worked performed), owed by the debtor before the transfer was made, while the debtor was insolvent (unrebutted presumption of § 547(f)) within 90 days (on June 29, 2004) before the filing of the petition (on September 24, 2004).

Kiddco, however, does contend that the trustee has not established the requirement under § 547(b)(5) that the payment enabled Kiddco to receive more than it would have received in a chapter 7 case had the payment not been made. Kiddco argues that had the payment not been made by Jacobsen, it would have been paid in full pursuant to the bond. According to Kiddco, its claim would be satisfied whether or not it was paid by Jacobsen and whether or not Jacobsen was a debtor in chapter 7. First of all, it is by no means certain that Kiddco would have been paid in full by the bonding company if it had made good its threat to leave the job. In fact, it received only partial payment from the bond for its two outstanding invoices.

The United States District Court for the Eastern District of North Carolina was confronted with a similar issue under § 547(b)(5) in which a subcontractor, by accepting payment from a contractor, gave up its inchoate right to file a mechanics and materialman's lien. In that case the subcontractor did not prevail. Precision Walls, Inc. v. Crampton, 196 B.R. 299 (E.D.N.C. 1996). Kiddco had no lien rights, inchoate or otherwise, with respect to property of the debtor and gave up no lien rights by accepting payment. The bonding company would have had subrogation rights against Jacobsen if Kiddco had made a claim against the bonding company and if the bonding company had paid Kiddco, but those facts are even further removed from the circumstances that the court found did not support the subcontractor's contention under § 547(b)(5) in Precision Walls.

From the perspective of the debtor's estate, the debtor was insolvent and had insufficient funds to pay all creditors in chapter 7. Kiddco, as already stated, had no specific claim to funds that Jacobsen received from Wake Tech, and, absent the $55,625.27 payment, there were not sufficient assets in the bankruptcy estate to pay that amount to Kiddco. For purposes of applying § 547(b)(5), the court must look to the availability of assets of the estate, not the assets of a bonding company or a third party guarantor. Accordingly, the trustee has meet all of the requirements of § 547(b).

Kiddco also asserts three affirmative defenses under § 547(c)(1), § 547(c)(2) and § 547(c)(4).

Section 547(c)(1) provides that a preferential transfer may not be avoided to the extent 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." 11 U.S.C. § 547(c)(1).

Section 547(a)(2) defines "new value" for purposes of § 547 as being

> 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).

Kiddco contends that it provided contemporaneous new value in two ways. First, it maintains that it provided new value by not leaving the job site, and second, it provided new value by giving up its claim against the bonding company. Neither contention is persuasive.

Remaining on the job to do work in the future for which it expects to be compensated does not fit within the definition of new value under § 547(a)(2). Furthermore, work to be performed in the future would not be contemporaneous. In this case most, if not all, of Kiddco's work, according to Kiddco's three invoices, was performed before the date of the payment, June 29, 2004. Future work may give rise to a defense under § 547(c)(4), which permits new advances made after the transfer, in some circumstances, to be set off against the preferential transfer, but the future work is not new value under § 547(c)(1).

Kiddco's second argument under § 547(c)(1) is that by accepting the payment it was relinquishing its claim against the bonding company. According to Kiddco, if it had made a claim against the bonding company, the bonding company would have paid Kiddco and the bonding company would have had a claim against Jacobsen's assets, including a claim by subrogation to all sums owing to Jacobsen by Wake Tech arising from the project.

Kiddco cites in support of its position the case of <u>O'Rourke v. Coral Construction, Inc. (In re E.R. Fegert, Inc.)</u>, 887 F.2d 955 (9th Cir. 1989), decided by the United States Court of Appeals for the Ninth Circuit. In <u>Fegert</u>, the court held that two subcontractors gave new value for purposes of § 547(c)(1) by accepting payment from their general contractor and thereby giving up their claims against the bonding

company. That may have constituted new value under the facts of that case, but all of the facts were not recited in the opinion. In the adversary proceeding before this court, Kiddco has not shown that by giving up its claim, it would have been paid in full. In fact, as previously stated, Kiddco was not paid in full by the bonding company for all of the work it performed for Jacobsen. In Fegert, the subcontractors, the contractor and the bonding company were all part of a lawsuit that was pending at the time of the payment. In this case there is no evidence that Kiddco had even contacted the bonding company at the time of the payment.

In Pearlman v. Reliance Insurance Co., 371 U.S. 132, 83 S.Ct. 232 (1962), relied upon by the Ninth Circuit in Fegert, the Supreme Court held that a bonding company that has paid claims of subcontractors is subrogated to funds due to the contractor by the owner of the project. In the adversary proceeding before this court, the funds from which the payments were made to Kiddco came from a payment made by the owner, Wake Tech, to Jacobsen. Kiddco's argument assumes that if it had not been paid by Jacobsen it would have immediately made a claim against the bonding company and that the bonding company would have immediately paid the claim and become subrogated to funds, previously paid and to be paid to Jacobsen by Wake Tech, sufficient to pay the claims of Kiddco and the other project subcontractors. Those assumptions are entirely too speculative. The court will not speculate that Kiddco would have immediately made a claim, that the bonding company would immediately pay the claim, and that the bonding company would have been subrogated to sufficient assets, including past and future payments from Wake Tech, to pay Kiddco and the other subcontractors in full.[2] For these reasons Kiddco has not presented facts that support its defense under § 547(c)(1).

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[2] This court rejected a similar argument under § 547(c)(1) in the previously mentioned adversary proceeding, Precision Walls, Inc v. Crampton (In re The Accord Group, Inc.), Case No. 93-01865-5-ATS (Bankr. E.D.N.C. June 28, 1995), where a subcontractor released inchoate lien rights by accepting payment from the contractor. The court's holding is referred to in the district court's decision in Precision Walls, Inc. v. Crampton, 196 B.R. 299 (E.D.N.C. 1996), but there was no appeal from that part of this court's ruling. In the present adversary proceeding, Kiddco had no lien rights to waive.

Kiddco also has not supported its defense under § 547(c)(2). Section 547(c)(2) provides that the trustee may not avoid a transfer under § 547 to the extent that the transfer was

> (A) in payment of a debt incurred by the debtor in the ordinary course of business or financial affairs of the debtor and the transferee;
> (B) made in the ordinary course of business or financial affairs of the debtor and the transferee; and
> (C) made according to ordinary business terms[.]

11 U.S.C. § 547(c)(2).

Kiddco engaged in extraordinary conduct by threatening to leave the job if it was not paid by Jacobsen. Had the payment been in the ordinary course of business it would not have made that threat. Kiddco may not prevail on its § 547(c)(2) defense, because the payment was not in the ordinary course of its buisness.

Finally, Kiddco's answer to its complaint raises an affirmative defense under § 547(c)(4), which provides that the trustee may not avoid a transfer under § 547 to the extent that the transfer was

> (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[.]

11 U.S.C. § 547(c)(4).

Kiddco has not pursued this defense either in its brief or in its oral presentation. Furthermore, it appears from the record, as previously stated, that most if not all of the work that Kiddco performed for Jacobsen was done prior to the date of payment, June 29, 2004. Accordingly, Kiddco cannot prevail under § 547(c)(4).

To summarize, the trustee has established all of the elements of § 547(b) and Kiddco has not established the elements of its defenses under § 547(c)(1), § 547(c)(2) or § 547(c)(4), and the court concludes that the trustee's motion for partial summary judgment shall be **ALLOWED.**

SO ORDERED.

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