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THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF UTAH

CENTRAL DIVISION

* *

In re:	)	
GRANADA, INC.,	)	87C-00693
Debtor.	)	89PC-401
PETER W. BILLINGS, JR., Trustee for Granada, Inc.,	)	
Plaintiff,	)	Case No. 91-C-0067-S
vs.	)	
RICHARDS WOODBURY MORTGAGE CORPORATION, a Utah corporation, VIRGINIA BEACH FEDERAL SAVINGS BANK, a federally chartered bank, and VIRGINIA BEACH SAVINGS & LOAN ASSOCIATION, a federally chartered association,	)	MEMORANDUM DECISION AND ORDER
Defendants.	)	

* *

This matter is on appeal from an order of the Bankruptcy Court denying Trustee Peter W. Billings, Jr., Esq.'s Motion for Summary Judgment. On June 20, 1989, the Trustee filed a complaint in the Bankruptcy Court instituting the present adversary proceeding against the defendants alleging that certain payments Granada had made to the defendants during the prepetition year are avoidable as

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preferential transfers under 11 U.S.C. § 547(b)[1] and that the value of those transfers is recoverable by him under § 550(a).[2] The defendants deny that the transfers are preferential and that they are parties from whom recovery can be sought under § 550(a). In addition, the defendants have raised defenses under § 547(c)(1), (2) and/or (4). A hearing on the appeal was scheduled for June 24, 1991, at which time Robert P. Rees, Esq. and Bryce Panzer, Esq. agreed to submit supplemental briefings on issues not adequately addressed by the parties' memoranda.[3]

The stipulated facts relevant to the appeal are as follows:

Granada (Debtor) is the general partner of Layton. Together they formed a joint venture for the purpose of developing Layton Industrial Park. Each owned an undivided one-half interest in the project. The joint venture took out a loan from Richards Woodbury Mortgage Corp. (RWM) for $1,035,000.[4] The loan was secured by the

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[1]Unless otherwise stated, all future references to statutory sections are to Title 11 of the United States Bankruptcy Code.

[2]The court is referring to the Trustee's amended complaint.

[3]The questions posed by the court were:

1. If payments by one joint venturer (payor) are made to a creditor whose loan is oversecured by property jointly owned by the payor and another joint venturer, and those payments do not exceed half of the debt owed the creditor, are those payments applied solely to the payors' portion of the debt or to the debt as a whole?

2. Assuming the debt is oversecured and the creditor forecloses, is the equity split 50/50 between the joint venturers or is it divided according to the proportion in which the joint venturers have made payments?

[4]Shortly after originating the loan, RWM sold it to Virginia Beach Federal Savings Bank (Virginia Beach). RWM continued to service the loan as an agent for Virginia Beach. The parties stipulated that RWM be dismissed from this action.

project. Granada made payments to RWM within the year preceding Granada's bankruptcy, which payments totalled over $165,000. The parties stipulated that, during that same year, the value of the project exceeded the amount due on the loan. In other words, the loan was oversecured.

The Trustee is now attempting to bring the payment of approximately $165,000 back into the estate for ultimate distribution to creditors of Granada. The Trustee claims the payments constitute an avoidable preference.

On February 13, 1987, Granada filed a petition for relief under Chapter 11 of the Bankruptcy Code. On June 22, 1987, the court appointed the Trustee, who brought this adversary proceeding seeking the avoidance of prepetition transfers to defendant on June 20, 1989. The Trustee contends that the transfers are avoidable under 11 U.S.C. § 547(b), and recoverable under 11 U.S.C. § 550(a). The defendants assert that the transfers were not preferential and that § 550 does not apply.

On August 19, 1990, the Bankruptcy Court heard the Trustee's motion for summary judgment. The Bankruptcy Court ruled that the stipulated facts did not satisfy § 547(b)(5) and that, accordingly,

no preferential transfers had occurred. On December 12, 1990, the Bankruptcy Court entered judgment in favor of Virginia Beach.

The Trustee appeals, seeking reversal of the Memorandum Opinion and Order, as well as the Judgment, and prays that the matter be remanded for further proceedings in the Bankruptcy Court to address the classification of Virginia Beach as a transferee under § 550(a)(1) or (a)(2) and the § 550(b)(1) defense to liability under § 550(a)(2). The standard of review when, as here, the facts are not in dispute is de novo. In re Golf Course Builders Leasing, Inc., 768 F.2d 1167 (10th Cir. 1985).

The Bankruptcy Court concluded that the transfer at issue was not preferential after analyzing the stipulated facts in light of 11 U.S.C. § 547(b)(5):

> . . . the trustee may avoid any transfer of property of the debtor--
>
> > (5) that enables such creditor to receive more than such creditor would receive if--
> >
> > > (A) the case were a case under chapter y 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.

The parties stipulated that the debt to Appellee was over-secured. Therefore, Virginia Beach did not receive more that it would have received had transfer not been made. However, an exception has evolved from case law that requires the trustee to show that payment to a creditor is not "accompanied by the release of an equivalent value to the estate" in order to establish a preferential transfer when property is oversecured. In re Herman Cantor Corp., 15 B.R. 747, 749 (Bkrtcy. E.D. Va. 1981); In re Zuni, 6 B.R. 449, 452 (Bkrtcy. N.M. 1980).

Accordingly, the relevant question is whether the payments by Granada were accompanied by a release of equivalent value to Granada's estate. The Court posed this question to the parties and sought their input in the form of supplemental memoranda. After reviewing such memoranda, the Court is satisfied that the payments by Granada were not accompanied by a release of equivalent value to Granada's estate.

Appellee admits that any payments made by Granada are applied to the debt as a whole and thus the benefit to Granada is only 50% of the amount of the payment. The Court could evidently recognize a junior lien in Granada's behalf and against Layton for the amount in which Granada's payments have reduced Layton's obligation to

Virginia Beach. However, the Trustee argues that such a lien would be valueless due to the delinquency and ultimate foreclosure of the priority lien.

The evidence available to this Court in the form of stipulated facts indicates that the value of the Layton Industrial Park exceeded the balance of the Virginia Beach loan during the year preceeding bankruptcy. Stipulated Facts, Docket No. 42, ¶ 14. However, in a foreclosure sale, Virginia Beach, as the holder of the priorty mortgage, is not required to bid more than the amount of the remaining debt. Therefore, this Court cannot conclude that because the value of the Layton Industrial Park exceeded the balance of the loan during the prepetition year that Granada's hypothetical junior lien would be secure after foreclosure by Virginia Beach. There is no stipulation of fact which would allow the Court to conclude that, after foreclosure, the excess value of the property would translate to cash which would cover the costs of liquidation in addition to Granada's hypothetical junior lien. Therefore, a junior lien in favor of Granada is potentially valueless.

The Court concludes that the payments in question constitute a preferential transfer because such payments were not accompanied

by a release of equivalent value. The order of the Bankruptcy Court is reversed and the matter is remanded to the Bankruptcy Court for further proceedings consistent with this Memorandum Decision and Order.

It is so ORDERED.

DATED this 17th day of January, 1992.

BY THE COURT:

David Sam

DAVID SAM
U.S. DISTRICT JUDGE