UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF TENNESSEE
WESTERN DIVISION

IN RE:

MARK BENSKIN & CO., INC.,

Debtor.

BK #89-22793-WHB
Chapter 7 (Inv.)

GEORGE W. EMERSON, JR.,
Trustee,

Plaintiff,

v.

JERRY KING,

Defendant/Cross-Defendant.

Adversary Proceeding
No. 89-0272

and

THE ESTATE OF AUSENCIO CAMPOS,
STEVE CAMPOS, Executor,

Defendant/Intervenor/
Cross-Plaintiff,

and

GEORGE METHVIN,

Defendant/Intervenor/
Cross-Plaintiff.

MEMORANDUM OPINION AND PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW ON CROSS MOTIONS FOR SUMMARY JUDGMENT

This cause is before the Court on the Motions for Summary Judgment filed by Mr. Emerson, the case Trustee (Trustee); Mr. King, defendant and cross-defendant; Mr. Methvin, defendant, intervenor and cross-plaintiff; and the estate of Ausencio Campos, Steve Campos, Executor (Mr. Campos), defendant, intervenor and cross-plaintiff. The Trustee seeks summary judgment holding that prepetition transfers of $80,000.00 and $45,629.51, respectively, from the debtor to Mr. King are avoidable as preferential transfers of property of the estate. Mr. Methvin seeks summary judgment holding that $25,000.00 of the $80,000.00 transferred to Mr. King are Mr. Methvin's funds, impressed with a trust in his favor. Similarly, Mr. Campos, on behalf of his father's estate, seeks summary judgment holding that $34,977.47 of the $80,000.00 transferred to Mr. King are the Campos' estate's funds, subject to a trust in its favor. Mr. King seeks summary judgment against Messrs. Methvin and Campos, holding that the transfer for $80,000.00 was made to him as a good faith purchaser for value. Mr. King further objects to the Trustee's motion for summary judgment asserting that genuine issues of material fact exist with respect to the preference allegation. At issue in this proceeding is whether it may be determined, as a matter of law, which of these parties has superior rights to or interests in the funds transferred to Mr. King.

The present motions arise out of a core proceeding under 28 U.S.C. §157(b)(2)(F) and (H). The Trustee's motion for summary judgment on the preference count of his complaint and the responses filed thereto involve issues concerning property of the estate and are therefore core pursuant to 28 U.S.C. §157(b)(2)(A), (B), (F) and (O). Accordingly, resolution of these preference issues constitutes findings of fact and conclusions of law pursuant to F.R.B.P. 7052 and 7056. However, to the extent that resolution of the disputes between Mr. King, Mr. Campos, and Mr. Methvin involves nonestate property, it is noncore. Given that it may nonetheless affect the

adjustment of the debtor-creditor relationship and allowance of claims against the estate, resolution of these disputes is "otherwise related" to the Chapter 7 case of Mark Benskin & Co., Inc. 28 U.S.C. §157(c)(1). If the Court were to make a decision at this time on the portion of this memorandum devoted to that noncore undertaking, it would be required to make proposed findings of fact and conclusions of law to be submitted to the United States District Court for the Western District of Tennessee for de novo review and entry of a final order and judgment. 28 U.S.C. §157(b)(3) and (c)(1).[1]

The record in this adversary proceeding reflects that it was commenced on September 22, 1989, with the filing of the Trustee's complaint against Mr. Jerry King seeking to recover, under 11 U.S.C. §547 and 548,[2] allegedly avoidable transfers of $80,000.00 and $45,629.51 made by the debtor to Mr. King on February 7, 1989[3], and March 10, 1989, respectively. Mr. King subsequently filed his answer wherein he admits receipt of the funds transferred but denies or is without sufficient information to admit or deny that the transfers were preferential or fraudulent. Mr. King affirmatively asserts that the transfers were made in the ordinary course of business and according to

[1] The Court notes that Mr. King has requested a jury trial in this matter and resists the Court's subject matter jurisdiction. See, Answer of Jerry D. King, ¶1; cf., In re Mark Benskin & Co., Inc., 135 B.R. 825 at 832 (Bankr. W.D. Tenn. 1991).

[2] The Trustee seeks summary judgment here on the preference count of his complaint only.

[3] Although dated and issued by the debtor on February 7, 1989, the $80,000.00 check was not honored until February 13, 1989. For preference purposes, the date of "honor" is the date of transfer. Barnhill v. Johnson, _____ U.S. _____, 112 S. Ct. 1386, _____ L. Ed. 2d _____ (1992).

ordinary business terms pursuant to 11 U.S.C. §547(c)(2) and that each payment was a "settlement payment" within the meaning of 11 U.S.C. §546(e).

Mr. Methvin and Mr. Campos were permitted to intervene by order of this Court entered on May 15, 1990. They then filed answers and cross-claims against Mr. King and the Trustee denying that the Trustee is entitled to the full amount of the recovery he seeks and asserting that of the $80,000.00 transferred to Mr. King on February 7, 1989, $25,000.00 rightfully belongs to Mr. Methvin and $34,977.47 belongs to Mr. Campos. Mr. King denies that these defendants/intervenors are entitled to the relief requested and has filed his present motions for summary judgment against each one.

FACTUAL SUMMARY
DELINEATION OF ISSUES

The debtor's Chapter 7 case was commenced with the filing of an involuntary petition on April 14, 1989. Prior to that time, the debtor was operated as a sole proprietorship by Mr. Mark Benskin who acted as an unlicensed investment advisor. Mr. Benskin is also an involuntary, individual Chapter 7 debtor before this Court in case number 89-23263-B. See, In re Mark Benskin & Co., Inc., 135 B.R. 825, 827 (Bankr. W.D. Tenn. 1991) (Findings of Fact No's. 1 and 2). Investors would open "investment accounts" with Benskin and/or his company. The "investment accounts" were usually opened with checks made payable to Mark Benskin & Co., Inc., and Benskin deposited and commingled those checks in a client "escrow fund" account. From that account, Benskin withdrew or transferred funds for operating expenses and some personal expenses. Id; see also, Benskin deposition, July 26, 1991, pp. 45 and 52-53. Meanwhile, Benskin would issue fictitious investment account statements to these investors falsely reflecting that their funds had been legitimately invested. See, e.g., Benskin deposition, July 26, 1991, Ex.'s 4, 7. According to

Benskin, beginning in January 1989, he transferred newly deposited investment funds from new investors to earlier investors as fictitious earnings on their "investments." Benskin deposition, July 26, 1991, pp. 61-64.

As a result of these Ponzi scheme activities, Benskin "turned himself in" to the Federal Bureau of Investigation on April 16, 1989. Benskin deposition, July 26, 1991, pp. 32, 44, 46. He subsequently entered guilty pleas in response to criminal indictments in the United States District Court for the Western District of Tennessee and the Criminal Court for Tennessee's Thirtieth Judicial District at Memphis. He is presently serving a sentence in a federal correctional facility located at Millington, Tennessee. U.S. v. Benskin, 926 F. 2d 562 (6th Cir. 1991); In re Mark Benskin & Co., Inc., 135 B.R. at 827 (Finding of Fact No. 1); Ex.'s 16 and 17 to The Estate of Ausencio Campos' and George Methvin's Motions for Summary Judgment.

As noted above, following his arrest, involuntary Chapter 7 petitions were filed against Benskin and his company. Orders for relief were entered on June 12, 1989, and Mr. Emerson was appointed Trustee in both cases. Pursuant to his investigation, the Trustee filed this and other avoidance actions seeking to recover funds transferred by the debtor prepetition as property of the estate. The Court subsequently determined, in a bifurcated insolvency trial, that both debtors were insolvent for the year preceding the bankruptcy filings. In re Mark Benskin & Co., Inc., 135 B.R. at 829 (Finding of Fact No. 22). However, that insolvency finding is not binding upon defendants, such as Mr. King, who demanded a jury trial. See Order, October 2, 1990, entered in this proceeding on November 20, 1990.

Mr. King, a Memphis police officer, originally became involved with the debtor on August 8, 1986, when he delivered $4,000.00 to the debtor "to open a cash management account to buy options

on stocks." Deposition of Mr. King, July 17, 1991, p. 14; Ex. 1. On September 3, 1986, Mr. King deposited an additional $2,500.00 with the debtor and on June 1, 1987, an additional $80,000.00. Deposition of Mr. King, July 17, 1991, p. 15; Ex. 1. Mr. King believed that the $80,000.00 deposit was invested in government securities. Id. He received periodic statements from the debtor indicating that his funds were legitimately invested. Id. at p. 16. Prior to attaining the funds at issue here, Mr. King had withdrawn $9,000.00 from his $86,500.00 investment with the debtor. Id. at p. 23; Affidavit of Mr. King, ¶'s 5 and 7.

As noted above, the $80,000.00 transfer to Mr. King was made with a check drawn on the Benskin escrow account dated February 7, 1989. Mr. King testified that the withdrawal was pursuant to his request. Deposition of Mr. King, July 17, 1991, p. 20. He made that request anticipating that he might need to "pay off" the mortgage on his house because his wife had been hospitalized and may have been unable to return to work. Id. at p. 21. Such a payoff was apparently unnecessary, however, as Mr. King further testified that he had not spent any part of the $80,000.00 as of the date of his deposition. Id. at pp. 21-22, 25-26. Mr. Benskin testified that Mr. King had stated similar reasons to him for requesting the withdrawal. Benskin deposition, July 26, 1991, pp. 68-70. However, Mr. Benskin added that he did not believe Mr. King because he had been informed that his business was "under investigation" and that a few of his clients were also so informed. Id. at pp. 49-51. According to Mr. Benskin, Mr. King was part of the "clique" that knew or should have known of the investigation. Id. at pp. 68-70. On March 10, 1989, Mr. King obtained payments of $20,443.25 and $25,188.26 from the debtor. According to Mr. King, he believed the former payment represented accumulated earnings on his alleged government securities investment of $80,000.00. He stated that he believed the latter check represented funds in his "option account." Id.

at pp. 29-31. Further, according to Mr. King, he decided "to close" those accounts because Benskin was ostensibly beginning to invest client funds in commodities, an undertaking Mr. King felt was "too risky." Id.

Meanwhile, on February 1, 1989, and January 25, 1989, Mr. Methvin and Mr. Campos delivered $25,000.00 and $50,000.00, respectively, for investment with the debtor. Exhibits . . . [to] Campos and Methvin's Motion For Summary Judgment, Ex's. 3 and 5; Benskin deposition, July 26, 1991, pp. 22-29. Benskin subsequently issued "confirmation statements" to Messrs. Methvin and Campos falsely reflecting that Mr. Methvin's deposit had been invested in 500 shares of Kodak stock and that Mr. Campos' deposit had been invested in American Capital Government Securities. Benskin deposition, July 26, 1991, pp. 24-29, Exs. 4 and 7. Actually, Mr. Benskin did not invest these funds that were acquired under false and fraudulent pretenses. Id. at pp. 25, 28, 32. Rather, these funds were deposited into the debtor's "escrow" account and used to pay operating expenses and the claims of earlier investors for returns of their "investments" and/or fictitious earnings. Id. at pp. 63-66. In fact, according to the affidavit of Mr. Jerry Whitehorn, a certified public accountant, bank auditor and undisputed expert witness in this proceeding, the Methvin and Campos deposits were specifically used for the $80,000.00 check issued to Mr. King on February 7, 1989. Mr. Whitehorn based this opinion on his review of the NBC "statements of financial activity for the Mark Benskin & Co., Inc. escrow account for the months of January and February, 1989, and the checks issued by Mark Benskin & Co. and posted to the escrow account from January 26, 1989 through February 13, 1989." Affidavit of Jerry Whitehorn, December 27, 1991, ¶3; Collective Exhibits 14 and 15. According to Mr. Whitehorn, these records reflect that a $52,500.00 deposit made and posted to the Benskin escrow account on January 25, 1989 included Mr. Campos'

$50,000.00 check. Affidavit of Jerry Whitehorn, ¶'s 4, 5, and 6; Exs. 5 and 11. Mr. Whitehorn further stated that the records show that a $25,000.00 deposit made and posted to the Benskin escrow account on February 1, 1989, was solely comprised of a City of Memphis Credit Union check made payable to Mr. Methvin and the Mark Benskin & Co. Escrow. Affidavit of Mr. Whitehorn, ¶'s 7 and 8; Exs. 2, 3, and 14. Exhibits 14 and 18 to the Campos and Methvin Motions for Summary Judgment demonstrate that at the close of business on January 24, 1989, the Benskin escrow account had credits totalling $143,391.81. Between January 25, 1989, and February 1, 1989, the following credits were added: $52,500.00 on January 25 (including Mr. Campos' $50,000.00 check); $6,500.00 on January 27; $700.00 on January 30; $5,911.66 on January 31; and $25,000.00 on February 1 (comprised of Mr. Methvin's $25,000.00 deposit). These exhibits further demonstrate that between January 26, 1989 and February 10, 1989, debits totalling the following amounts were drawn on the account: $5,442.50 on January 26; $54,040.00 on January 27; $10,795.68 on January 30; $3,566.17 on January 31; $3,000.00 on February 1; $455.74 on February 2; $23,105.16 on February 3; $614.16 on February 6; $15,195.66 on February 7; $16,677.68 on February 8; and $13,371.59 on February 10.

The debit of $10,499.06 of the total $13,371.59 debited on February 10th resulted in total debits of $143,391.81, or the amount on deposit prior to the deposits at issue, for the period of January 26, 1989 through February 10, 1989. Ex. 18, p. 1. This is significant because it is Mr. Whitehorn's unrefuted testimony that to adequately trace and determine the disposition of the Campos and Methvin funds, the account activity should be analyzed using the "first in - first out rule" of tracing methodology. According to Mr. Whitehorn, "[t]he first in -first out rule means that the first credits posted to the account are the first credits paid out." Affidavit of Mr. Whitehorn, ¶11.

Further, according to Mr. Whitehorn, from an accounting perspective this tracing methodology is the only one applicable to the factual circumstances here "that produces valid, reliable, and consistent results." Id. This method is the only tracing method on which proof, as opposed to argument, has been offered. Its application demonstrates that the payments described above were made against funds on deposit prior to the January 25th deposit made by Mr. Campos. Ex. 18, p. 1. Additionally, the first in - first out rule, when applied to the facts here, illustrates that the payment to Mr. King was comprised of $34,977.47 of Mr. Campos' deposit made January 25, 1989, and deposits of: $6,600.00 made January 27; $700.00 made January 30; $5,911.66 made January 31; and $25,000.00 made (by Mr. Methvin) February 1, 1989. Id. Consequently, it may be concluded that these intervenors have adequately traced their deposits to Mr. King as a matter of fact. Whether or not this entitles them to recover these funds as a matter of law will be discussed below. Both the Trustee and Mr. King assert that the intervenors are not so entitled. It is the Trustee's position that these funds may be recovered for the estate as they were the subject of a preferential transfer. Mr. King contends that the funds do not qualify as "trust" funds and that even if they do so qualify, he received them as a good faith purchaser for value and therefore holds a claim superior to that of the intervenors. Moreover, according to Mr. King, the Trustee is not entitled to avoid the transfer as a matter of law because the elements necessary to establish a preferential transfer have not been proven with respect to this $80,000.00 transfer and, even if proven, genuine issues of material fact exist with respect to whether the transfer may be excepted from avoidance as a preference pursuant to 11 U.S.C. §547(c).

As noted above, on March 10, 1989, Mr. King was additionally paid $45,629.51 by the debtor pursuant to his request to "close" his accounts with the debtor. This sum was paid by checks

drawn on the debtor's "escrow" account in the amounts of $20,443.25 and $25,188.26 respectively. Complaint of Trustee, Ex. 1. There are no intervening claimants to these funds. The Trustee contends that they are recoverable as property of the estate in that they were the subject of a preferential transfer to Mr. King. Mr. King counters that they are not so recoverable because their transfers were not made on account of an antecedent debt and, thus, do not qualify as preferential transfers. Moreover, according to Mr. King, genuine issues of material fact exist with respect to whether the transfers at issue may be excepted from avoidance as preferential pursuant to 11 U.S.C. §546(e).

SUMMARY JUDGMENT

Summary judgment is available for a moving party only when after consideration of the evidence presented by the pleadings, affidavits, answers to interrogatories, and depositions in a light most favorable to the non-moving party, there remain no genuine issues of material fact. F.R.B.P. 7056(c). Consequently, "[t]he mere existence of some alleged factual dispute between the parties will not defeat an otherwise properly supported motion for summary judgment; the requirement is that there be no genuine issue of material fact." Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 106 S. Ct. 2505, 2511, 91 L. Ed. 2d 202 (1986); Street v. J.C. Bradford & Co., 886 F. 2d 1472 (6th Cir. 1989). Whether a fact is material is to be determined by the substantive law. Street v. J.C. Bradford, 886 F. 2d at 1480.

THE FEBRUARY 13, 1989 $80,000.00 TRANSFER
TRUSTEE V. KING V. METHVIN AND CAMPOS: NONCORE

As discussed above, the debtor's February 13, 1989, transfer of $80,000.00 to Mr. King gives rise to the claims asserted by the intervenors here as well as one of those asserted by the Trustee. Turning first to the dispute between Mr. King and the intervenors, it is the position of Messrs.

Campos and Methvin that they are entitled to $34,977.47 and $25,000.00 respectively, because these amounts are subject to an express or constructive trust in their favor.[4] At the same time, Mr. King asserts that he received the entire $80,000.00 transfer as a good faith purchaser for value.

It is well settled in the bankruptcy context that property of the bankruptcy estate does not include "property of others held by the debtor in trust at the time of the filing of the petition." United States v. Whiting Pools, 462 U.S. 198, 204, 103 S. Ct. 2309, 2313, 76 L. Ed. 2d 515 (1983); 11 U.S.C. §541(d). Moreover, it is equally well settled, in both the bankruptcy and state law contexts, that the claim of a good faith purchaser of trust property for value without notice or knowledge of a breach of the trust is superior to that of any express or constructive trust beneficiaries. See, e.g., Garland v. Higgins, 160 Tenn. 381, 25 S.W. 2d 583 (1930); C. H. Robinson Co. v. Trust Co. Bank, N.A., 952 F. 2d 1311 (11th Cir. 1992); In re Bell & Beckwith, 838 F. 2d 844 (6th Cir. 1988). Consequently, if Mr. King qualifies as such a good faith purchaser for value, his interest will defeat those asserted by Messrs. Methvin and Campos even if they can show that the debtor held their funds in trust. For this reason, the Court shall address this good faith purchaser issue first.

[4] It should perhaps be noted here that the Court has previously found that the funds delivered by Mr. Campos to the debtor were the subject of an express, oral trust. In re Mark Benskin & Co., Inc., 135 B.R. at 834. However, that finding was made with respect to a different defendant following a trial. The evidence presented at that trial is not before the Court and was not considered in this proceeding.

It is undisputed in the instant proceeding that prior to the $80,000.00 payment at issue, Mr. King had deposited a cumulative amount of $86,500.00 with the debtor for investment. It is further undisputed that Mr. King had previously received purported "returns" totalling $9,000.00 from the debtor. Therefore, it is evident that Mr. King had given value for at least $77,500.00[5] of the $80,000.00 transfer at issue. See e.g., C.H. Robinson Co. v. Trust Co. Bank, N.A., 952 F. 2d at 1314 (Trust property is transferred "for value" when the trust property consists of money or negotiable instruments transferred in exchange for extinguishment of an antecedent debt). As such, assuming arguendo, that the funds were subject to a trust, the issue becomes whether Mr. King had knowledge or notice of the debtor's breach of the alleged trust. Not surprisingly, whether Mr. King had "knowledge" of the alleged trust and its breach requires a showing that he actually knew of the intervenor's claim to the funds. In comparison, whether Mr. King had "notice" of the intervenor's asserted claims to the funds requires a demonstration that from the facts and circumstances surrounding the debtor's transfer of the funds, a reasonably prudent person would have inquired as to their source. In re Bell & Beckwith, 838 F. 2d 844, 849 (6th Cir. 1988) (quoting the Restatement of Restitution at §174). From Mr. King's testimony, discussed in the above factual summary, it appears that he requested the $80,000.00 payment at issue because he believed his wife's poor health would necessitate "paying off" their home mortgage. However, Mr. King did not "pay off" the mortgage and Mr. Benskin indicated in his testimony that he believed Mr. King knew or had notice that the debtor's operations were the subject of a police investigation. It is the Court's conclusion that these conflicting testimonies raise a genuine issue of material fact over whether Mr. King may have had

[5] This obviously leaves $2,500.00 for which Mr. King gave no value and which may be subject to a trust in favor of Messrs. Methvin and Campos. However, the facts before the Court do not establish how that $2,500.00 would be divided between the two purported trust beneficiaries.

information that imposed a duty to inquire as to the source of the funds. As such, Mr. King's motions for summary judgments on the crossclaims of Messrs. Methvin and Campos will be denied. The motions of Messrs. Methvin and Campos for summary judgment against Mr. King are likewise denied at least as to the $77,500.00 for which Mr. King gave value to the debtor. It follows that the Trustee's motion for summary judgment as to $59,977.47 of this transfer on his preference complaint must be denied pending a determination of whether this amount is subject to a trust for the benefit of Messrs. Methvin and Campos. Obviously, a finding that the funds are "trust funds" would except them from recovery by the Trustee while the opposite finding would render them potentially subject to avoidance recovery as property of the bankruptcy estate.

The issue next becomes whether the $2,500.00 for which Mr. King gave no value are subject to a trust in favor of these intervenors. The viability of the claims of the Trustee or Mr. King to the funds that Messrs. Methvin and Campos assert are trust funds is initially dependent upon whether these funds amount to "an interest of the debtor in property." 11 U.S.C. §547(b). Thus, essential to resolution of the issues presented here is a determination of whether the $2,500.00 in dispute qualify as property of the bankruptcy estate. Fundamental to this determination is an examination of the nature and extent of the debtor's prepetition interest in the funds. Section 541(a) of the Bankruptcy Code designates any legal or equitable interests of the debtor in property at commencement of the bankruptcy case "property of the estate" and that includes any interests recovered pursuant to applicable avoidance sections of the Code. 11 U.S.C. §541(a)(1) and (3). This is an "admittedly broad definition of includable property;" however, the nature and extent of the debtor's interests referenced by §541(a) are determined by state law applied in a manner consistent with federal bankruptcy law. Patterson v. Shumate, _____ U.S. _____, 112 S. Ct. 2242, 2249, 119 L. Ed. 2d 519

(1992); In re North American Coin & Currency, Ltd., 767 F. 2d 1573 (9th Cir. 1985), am'd. 774 F. 2d 1390 (9th Cir. 1985); In re Howard's Appliance Corp., 874 F. 2d 88, 93 (2nd Cir. 1989); In re White, 851 F. 2d 170, 173 (6th Cir. 1988). The filing of the bankruptcy petition does not expand the debtor's property interests: the estate succeeds to property only to the extent of the right and title possessed by the prepetition debtor. United States v. Whiting Pools, 462 U.S. 198, 204, n. 8, 103 S. Ct. 2309, 2313 n. 8, 76 L. Ed. 2d 515 (1983). This rule is significant here because, as mentioned above, it is generally held, pursuant to 11 U.S.C. §541(d), where a debtor holds property in trust for another that the debtor's only interest is mere legal title.[6] Id. Moreover, in the bankruptcy context, the claim of the equitable interest holder or beneficiary to trust assets is considered superior to that of the bankruptcy trustee notwithstanding the trustee's judgment lien creditor status or avoidance powers. See, e.g., In re Quality Holstein Leasing, 752 F. 2d 1009, 1012 (5th Cir. 1985); In re Howard's Appliance Co., 874 F. 2d 88 at 93, cf. In re Seaway Express Corp., 912 F. 2d 1125 (9th Cir. 1990). Indeed, the United States Supreme Court has noted that under Bankruptcy Code §541(d), the bankruptcy estate "plainly" does not include "property of others held by the debtor in trust at the time of the filing of the petition." United States v. Whiting Pools, 103 S. Ct. at 2313, n. 10.

Similarly, under both state law and federal bankruptcy law, the equitable interest in property acquired by fraud remains property of its rightful owner to the extent that it is identifiable. See, e.g., Quality Holstein Leasing, 752 F. 2d at 1012; In re Anderson, 30 B.R. 995 (M.D. Tenn. 1983);

[6] Section 541(d) provides in pertinent part: "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."

Covert v. Nashville, C & St. L. Ry., 186 Tenn. 142, 208 S.W. 2d 1008, 1 A.L.R. 2d 154 (1948). Accordingly, the fraudulent acquirer obtains mere title or a possessory interest and is said to hold the property in trust for its beneficiary or rightful owner. Such a trust is "constructed" by a court of equity "to satisfy the demands of justice" and prevent unjust enrichment. In re Anderson, 30 B.R. at 1014. Thus, it is referred to as a "constructive trust." Id. The §541(d) exclusion from property of the estate applies with equal force to constructive and express trusts. See, e.g., In re Howard's Appliance, 874 F. 2d at 93.

In addition to the general trust requirements of a trustee, a beneficiary, and identifiable trust property, a constructive trust requires proof of: "(1) a wrongful act; (2) specific property acquired by the wrongdoer which is traceable to the wrongful behavior; and (3) an equitable reason why the party holding the property should not be allowed to keep it." In re Independent Clearing House Co., 41 B.R. 985, 1000 (Bankr. D. Utah 1984) (citations omitted), on appeal 62 B.R. 118 (D. Utah 1986). See also In re Mark Benskin & Co., 135 B.R. at 833 (citing Kopsombut-Myint Buddhist Center v. State Board of Equalization, 728 S.W. 2d 327, 333 (Tenn. App. 1986)). This latter requirement is ordinarily met when it can be shown that the party holding such property is not a good faith, bona fide purchaser for value. See e.g., CH Robinson Co. v. Trust Co. Bank, N.A., 952 F. 2d 1311 (11th Cir. 1992); Garland v. Higgins, 160 Tenn. 381, 25 S.W. 2d 583 (Tenn. 1930). As discussed above, where such a party qualifies as a good faith purchaser for value, the rights of an express or constructive trust beneficiary are defeated. Garland v. Higgins, 25 S.W. 2d at 585. However, as also discussed above, Mr. King admittedly gave no value for $2,500.00 of the transfer at issue here. Therefore, the issue becomes whether $2,500.00 of the transfer may be subject to an express or constructive trust in favor of Messrs. Methvin and Campos.

Turning first to the question of a constructive trust[7], it is well settled that the burden of proving facts which warrant the imposition of a constructive trust and thus, application of §541(d), is on the claimant. First Federal of Michigan v. Barrow, 878 F. 2d 912, 915 (6th Cir. 1989). If it can be demonstrated that the subject property was acquired by fraud, the claimant must then demonstrate that it can be traced. Id. at 915-916. In the bankruptcy context, sufficient tracing and identification of the trust property is essential to the establishment of a constructive trust when the funds have been commingled with other funds. According to the Sixth Circuit Court of Appeals,

> . . . the predicate for the trust doctrine as applied in bankruptcy is a perpetuated integrity of the trust properties so as to avoid conflict with and between creditor classes; . . . If the trust fund or property cannot be identified in its original or substituted form, the cestui que trust becomes merely a general creditor of the estate.

First Federal of Michigan v. Barrow, 878 F. 2d at 915 (Emphasis added). Whether property has been sufficiently traced is a factual determination. In re General Coffee Corp., 64 B.R. 702, 709, n. 13 (S.D. Fla. 1986), aff'd at 828 F. 2d 699 (11th Cir. 1987). The first in - first out tracing method is apparently accepted in Tennessee, at least outside of the bankruptcy context. In re Mark Benskin & Co., 135 B.R. at 833, citing State ex rel. Robertson v. Bank of Bristol, 165 Tenn. 461, 55 S.W. 2d 771 (1933); State ex rel. Robertson v. Thomas W. Wrenne & Co., 170 Tenn. 131, 92 S.W. 2d 416 (1936); see also, Commerce Union Bank of Nashville v. Alexander, 44 Tenn. App. 104, 312 S.W. 2d

[7] Although the Court has previously found that Mr. Campos' deposit was the subject of an express oral trust, that finding was made with respect to a different defendant following a trial. In re Mark Benskin & Co., Inc., 135 B.R. at 834. The evidence adduced at that trial is not before the Court and was not considered in this adversary proceeding.

611 (1958); Tenn. Code Ann., §47-4-208. Contra, see, R. Banks, A Survey Of The Constructive Trust In Tennessee, 12 Memphis St. L. Rev. 71, 125-26 (1981). Moreover, it is the only tracing method on which uncontradicted proof has been presented in this proceeding.

It is undisputed in this proceeding that the debtor obtained the intervenors' funds by fraud. It is further undisputed that if the "first in - first out" method is used to trace the source of the $80,000.00 payment made to Mr. King, $34,977.47 and $25,000.00 of the payment are derived from the respective deposits of Messrs. Campos and Methvin. Moreover, to the extent Mr. King gave no value for the payment he would be unjustly enriched thereby, and the elements of a constructive trust are clearly present. Thus, the $2,500.00 transfer may be impressed with a constructive trust in favor of the intervenors.

The Court makes this finding notwithstanding the arguments of the Trustee and Mr. King that application of the "first in - first out" tracing method to the facts here is precluded by the "lowest intermediate balance test" discussed by the Court of Appeals for the Sixth Circuit in its Barrow opinion cited above. As this Court discussed in its Emerson v. Hollie (In re Mark Benskin & Co., Inc.), unpub., Bk. No. 89-22793-B, Adv. No. 89-0267 (Bankr. W.D. Tenn. 1992) opinion, the "lowest intermediate balance test" is primarily applicable to situations where tracing or identification of the claimed funds into and beyond the debtor's commingled account to the debtor's payee is absent. Id. at p. 15. Given that identification and tracing of the funds at issue has been factually accomplished here, the Court is satisfied that the requisites for imposition of a constructive trust upon $2,500.00 of the $80,000.00 transfer have been demonstrated. Consequently, in order to avoid a "manifest injustice" to Messrs. Methvin and Campos and prevent the unjust enrichment of Mr. King, this Court, as a court of equity, could recommend the imposition of a constructive trust in

favor of Messrs. Methvin and Campos upon $2,500.00 of the $80,000.00 transfer to Mr. King. In re Anderson, 30 B.R. at 1013. However, as discussed above, the conclusion that these funds are trust funds would exclude them from property of the bankruptcy estate. 11 U.S.C. §541(d). Therefore, such a conclusion is noncore and must be submitted to the United States District Court as a proposed decision. 28 U.S.C. §157(c)(1). Given that the same findings and conclusions could be reached with regard to the remaining claims of Messrs. Campos and Methvin resulting in an additional proposed decision, after trial, the Court shall refrain from issuing a proposed decision on the $2,500.00 until those remaining claims are resolved. This Court wishes to avoid duplication of effort and expense by the parties and the courts. In particular, this Court believes it would not be in the interest of judicial economy to burden the District Court with a noncore, but complex, issue involving only $2,500.00.

In summary, it would appear that Messrs. Campos and Methvin may be entitled to a proposed summary judgment holding that $2,500.00 of the debtor's $80,000.00 transfer to Mr. King is subject to a constructive trust for their joint and individual benefit. However, the Court shall reserve issuing such a proposed decision until a determination regarding the additional alleged trust funds is made. Further, at trial, proof may be offered on how the $2,500.00 should be divided. The motions of Mr. King for summary judgment with respect to the cross-claims of Messrs. Campos and Methvin for $59,977.47, less $2,500.00, of this transfer are denied as are the cross motions of Messrs. Campos and Methvin. Likewise, the Trustee's motion for summary judgment on his preference complaint to the extent he seeks to recover funds claimed by the intervenors is denied.

The Trustee's motion for summary judgment on the preference count of his complaint, to the extent he seeks recovery of the March 10 transfers and the balance of the $80,000.00 transferred to Mr. King, shall be considered in the following core phase of this memorandum.

THE BALANCE OF THE FEBRUARY 13, 1989 TRANSFER AND THE MARCH 10, 1989 TRANSFERS TRUSTEE V. KING: CORE

The above discussion leaves remaining for resolution the dispute between the Trustee and Mr. King concerning the Trustee's complaint to avoid and recover the transfers to Mr. King as preferential. There are no known intervening claims asserted against the remaining funds at issue. Neither is there a dispute between the Trustee and Mr. King over whether the debtor had an interest in these funds. Thus, under applicable case law, the funds are not excluded from inclusion in the bankruptcy estate. In re Quality Holstein Leasing, Inc., 752 F. 2d at 1012; 11 U.S.C. §541(a). However, in order to be recovered for the benefit of the estate, pursuant to the summary judgment motion at bar, it must be proven that the funds were the subject of avoidable preferential transfers.[8] In order to avoid the transfers as preferential the Trustee must demonstrate that the transfers were:

> . . . of an interest of the debtor in property -
>
> (1) to or for the benefit of a creditor;
>
> (2) for or on account of 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 date of the filing of the petition; . . .

[8] It must be noted that the Trustee has not moved for summary judgment on the fraudulent conveyance count of his complaint.

> (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 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) and (g) (The latter section places the burden of proof of these elements on a trustee).

In light of the absence of any specific trust fund claims against the remaining funds transferred to Mr. King by the debtor it may be concluded that they constitute "an interest of the debtor in property" as required by 11 U.S.C. §547(b). See In re Tinnell Traffic Services, 41 B.R. 1018 (Bankr. M.D. Tenn. 1984). Moreover, it is beyond dispute that the transfers were made within ninety days of the filing of the petition. Thus, the Court must determine whether the additional requisites for a preference have been demonstrated here.

Mr. King is arguably a "creditor" of the debtor within the meaning of the Bankruptcy Code, inasmuch as he claims he had a right to payment of the sums at issue as earnings on his investments. See 11 U.S.C. §101(10) and (5) ("Claim" may arise out of the debtor's breach of an obligation). However, there is inadequate evidence, for summary judgment purposes, regarding whether these transfers were made on account of an antecedent debt. There has been no showing that Mr. King was entitled to "profits" just as there has been no showing that any investments actually transpired. Thus, it may be concluded that §547(b)(2)'s required "antecedent debt" has not been sufficiently established for summary judgment.

Similarly, the Court can make no finding that the debtor's insolvency has been established with respect to this defendant as required by §547(b)(3). See Order, October 2, 1990 entered in this proceeding on November 20, 1990.

Finally, although the Trustee presents a commendable legal argument in support of his assertion that Mr. King received more from the debtor as a result of the transfers than he would have received in Chapter 7 if the transfers had not been made, the Trustee has presented no factual evidence such as that presented by the Trustee in Peterson v. Mr. T's Apparel (In re Washington Mfg., Inc.), unpub., Bankr. No. 388-01467, Adv. Pro. No. 380-0109A (Bankr. M.D. Tenn. 1992), that would support this assertion. Without such facts the Court can reach no dispositive factual finding or legal conclusion regarding whether §547(b)(5) has been satisfied.

The Trustee's motion for summary judgment on his preference claim must be denied. Any other conclusion would perpetuate the myth that the payment of these funds to Mr. King arose out of a transaction with "economic substance" in which his earlier deposits actually had earnings and that he was actually owed the money he received from the payment at issue. Matter of Cohen, 875 F. 2d at 510-511. This result does not, of course, preclude the Trustee from pursuing the preference avoidance at trial or from pursuing his §548 fraudulent conveyance action against Mr. King. "Indeed, courts have ruled for trustees asserting such [fraudulent conveyance] claims against investors in other Ponzi schemes." Id. However, given that the Trustee's motion is not founded on §548, that question is not ripe for resolution.

CONCLUSION

From these findings and conclusions, it is HEREBY ORDERED that:

1. The Trustee's motion for summary judgment against Mr. King on his preference complaint is DENIED;

2. The Trustee's motions for summary judgment against Messrs. Methvin and Campos are DENIED;

3. Mr. King's motion for summary judgment against Messrs. Methvin and Campos are DENIED;

4. Messrs. Methvin and Campos' motions for summary judgment against Mr. King and the Trustee are DENIED in part; and

5. The Court shall not make a proposed decision but shall RESERVE issuance of a proposed decision that $2,500.00 of the $80,000.00 transfer to Mr. King are subject to the imposition of a constructive trust in favor of Messrs. Methvin and Campos pending a trial of the dispute between the parties concerning the $57,477.47 balance.

A status conference on this adversary proceeding, at which the Court will recommend a settlement conference, will be held on Thursday, September 3, 1992, at 9:30 a.m., in Courtroom 680, 200 Jefferson Avenue, Memphis, Tennessee, when a related adversary proceeding is set for motions.

SO ORDERED this 28th day of August, 1992.

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WILLIAM HOUSTON BROWN
UNITED STATES BANKRUPTCY JUDGE

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