UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re: CAMBRIDGE INDUSTRIES HOLDINGS, INC., CAMBRIDGE INDUSTRIES, INC. and CE AUTOMOTIVE TRIM SYSTEMS, INC., Debtors.	Chapter 11 Case No. 00-1919 Jointly Administered
JOHN J. CALIOLO, as Liquidating Trustee for the Cambridge Industries, Inc. Liquidating Trust, Plaintiff, v. AZDEL, INC., Defendant.	Adv. Proc No. 02-03293

MEMORANDUM OPINION ON MOTION FOR SUMMARY JUDGMENT
BY DEFENDANT AZDEL, INC.

I. INTRODUCTION

This is an adversary proceeding in bankruptcy (Fed. R. Bankr. P. 7001), seeking to avoid an allegedly preferential transfer. 11 U.S.C. § 547.[1]

Before the Court is the motion of Defendant Azdel, Inc.

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[1] All statutory references herein are to the United States Bankruptcy Code, 11 U.S.C. § 101 et seq., unless otherwise noted.

("Defendant") for summary judgment pursuant to Fed. R. Civ. P. 56 as incorporated by Fed. R. Bankr. P. 7056 [Doc. No. 15].

II. ISSUE

The Defendant presented several issues in its motion for summary judgment. The court denied the Defendant's motion as to all of the issues from the bench after oral argument, except for one issue, which is the subject of this memorandum opinion. That issue is whether § 502(d) of the Code precludes a preference action against a creditor, whose proof of claim in the bankruptcy case has already been allowed by court order.

III. FACTS

The Debtors in these cases filed its voluntary petition for relief under Chapter 11 of the Code on May 10, 2000. The Debtors' Modified Second Amended Joint Consolidated Liquidating Plan of Reorganization was confirmed by Order of August 6, 2001. [Case No. 00-1919 (Doc. No. 15780)] The Liquidating Plan became effective on August 17, 2001.

Two separate administrators are created by the Confirmation Order. The Confirmation Order gives to an entity called the Plan

Administrator the responsibility to resolve disputed claims. [Confirmation Order at 13, ¶ 11] The Order also provides that another entity, called the Liquidating Trustee, shall have the right to bring preference avoidance claims. [Confirmation Order at 15, ¶ 14]

That division of responsibilities appears to be the cause of the present dispute. The disagreement concerning Defendant's proofs of claim was handled, for the bankruptcy estate, by the Plan Administrator. The Plaintiff in this adversary proceeding to avoid preferential transfers in the Liquidating Trustee.

Defendant filed its proof of claim in the amount of $936,700.74 ($303,120.67, secured, and $634,580.07, unsecured). By Order dated August 5, 2002, the Court approved the Stipulated Order Resolving All Claims of Azdel, Inc. [Case No. 00-1919, Doc. No. 2194].

On May 8, 2002, prior to the August 5, 2002, Stipulated Order, the Liquidating Trustee filed the complaint in this action to avoid and recover preferential transfers. The complaint alleges that the Defendant received avoidable preferential transfers in the aggregate amount of $881,777.03. [Complaint ¶ 9, Doc. No. 1]

IV. DISCUSSION

A. Summary Judgment Standard

Fed. R. Civ. P. 56(c) (applicable here by reason of Fed. R. Bankr. P. 7056) provides that summary judgment shall be granted "if the pleadings, depositions, answers to interrogatories, and admission on file, together with the affidavit, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(c); Fed. R. Bankr. P. 7056. The issue before the court involves no disputed facts, so summary adjudication is appropriate.

B. § 502(d)

Section 502(d) states in relevant part:

> Notwithstanding subsections (a) and (b) of this section, the court shall disallow any claim of any entity ... that is a transferee of a transfer avoidable under section . . . 547 . . . of this title, unless such entity or transferee has paid the amount, or turned over any such property, for which such entity or transferee is liable under section ... 550 ... of this title.

Three recent decisions of this court have dealt with the preclusive effect of § 502(d): Cohen v. TIC Financial Systems (In re Ampace), 279 B.R. 145 (Bankr. D. Del. 2002); LaRoche Industries, Inc. v. General American Transportation Corp. (In re

LaRoche), 284 B.R. 406 (Bankr. D. Del. 2002); and, in another adversary proceeding arising from the same bankruptcy case as the matter now before the court, John J. Caliolo, Liquidating Trustee, v. TKA Fabco Corp. (In re Cambridge Industries Holdings, Inc.), 2003 WL 1818177 (Bankr. D. Del. 2003).

The holdings of these three cases are not in conflict. In Ampace, § 502(d) was found to have no preclusive effect upon subsequent preference litigation, because there had been no objection to the defendant's claim.[2] The claim had been deemed allowed, in the absence of objection, pursuant to § 502(a). 279 B.R. at 162-63.

In LaRoche, The Chapter 11 debtors objected to a creditor's proof of claim. The creditor did not respond to the objection, and an order was entered sustaining the objection and allowing the claim in a reduced amount. Thereafter, pursuant to the debtor's confirmed chapter 11 plan of reorganization, the creditor received a distribution of 162 shares of common stock of the reorganized debtors. Following that distribution to the creditor, the debtors commenced an adversary proceeding against the creditor, to avoid an allegedly preferential transfer in

[2] In Ampace, the Trustee did file a formal objection to the Defendant's claims. But the objection came after time extension orders that were held by the court to have been ineffective. Thus the objection was found to be untimely and, therefore, deemed allowed.

excess of $84,000. LaRoche held that § 502(d) precluded the action and the court granted defendant-creditor's motion for summary judgment. The court observed:

> "Thus § 502(d) stands for the proposition that if a claim is allowed there is no longer a voidable transfer due from that claimant. In essence, a voidable transfer, such as a preference, must be determined, as part of the claims process and not at a later time, especially after distribution under the plan."

284 B.R. at 408-09.

In Cambridge, the facts were similar to LaRoche. The preference avoidance action was commenced after the creditor's claim had been allowed and a cash distribution paid, pursuant to a confirmed chapter 11 plan. Unlike LaRoche, there was no formal objection to the creditor's proof of claim. The parties resolved their differences concerning the allowable amount of the claim without a formal objection. Like LaRoche, an order was entered allowing the claim in the agreed amount. Cambridge also indicates that § 502(d) requires the application of principles of claim preclusion, so that avoidable transfer issues must be raised as part of the claim objection/allowance process.

To review the three holdings:

In Ampace, the creditor's claim was deemed allowed, in the absence of objection. There was no formal objection/allowance procedure and no order of the court resolving a dispute over the

allowable amount of the claim. It was held that § 502(d) was not a bar to a later preference avoidance adversary proceeding against the creditor with the allowed claim.

In LaRoche and Cambridge, there were orders allowing the claims of the creditors in reduced amounts. In LaRoche, a formal objection to the proof of claim was filed; in Cambridge, no objection was filed, as the parties resolved their differences consensually. In both cases, dividends were paid on the creditors' claims, before the filing of the complaints alleging that the creditors had received avoidable transfers. Both LaRoche and Cambridge expressed concerns about the fairness of subjecting a creditor to a claim objection, resolving the objection via a court order, giving the creditor its distribution pursuant to the chapter 11 plan, and then commencing an adversary proceeding against the creditor to recover an allegedly avoidable transfer.

The relevant facts in the matter now before the court differ from the three prior rulings in this district. First, fairness to the creditor/defendant is not an issue. The preference action was commenced before the claim objection was filed. However, the claim dispute was resolved and an order was entered allowing the claim in a reduced amount while this adversary proceeding was

pending.[3]

The distinguishing fact in the three cases discussed above is the presence or absence of an order expressly resolving a dispute over the amount of the creditor's claim. If there is such an order, as opposed to the 'deemed allowance' of a claim, then § 502(d) precludes the commencement or continuance of litigation seeking to recover avoidable transfers from the creditor.

Where, as in the present matter, one entity is responsible for claims objections and another for adversary proceedings to recover avoidable transfers, the preclusive effect of § 502(d) should not cause serious inconvenience. Communication between those entities, especially before the entry of orders concerning disputed claims, will eliminate the possibility of inadvertent preclusion of avoidance actions.

Plaintiff's counsel has correctly noted some surprise in rulings giving preclusive effect to § 502(d), given prior use of independent proceedings for claims objections and preference avoidance, relative to disputes with a single creditor. However,

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[3] Defendant's memorandum in support of this motion for summary judgment [Doc. No. 16 at 12] alleges that Plaintiff was advised, before entry of order on the claim, of Defendant's position that § 502(d) would require dismissal of this adversary proceeding. Since this allegation, which appears only in the text of the memorandum, was unsupported by declaration or otherwise, it is given no weight.

such surprise must be no greater than the surprise of the creditors in cases such as LaRoche and Cambridge, who had a their disputed claims allowed in reduced amounts, received distributions from the bankruptcy estate on account of the claims, and then got sued on the alleged preferences.

In LaRoche, the creditor, GATX, filed a claim for $117,215.84. The claim was allowed in the amount of $103,944.42. The 'dividend' was corporate stock, not cash. The preference avoidance complaint sought to recover $84,271.38 from GATX. In Cambridge, the creditor, TKA Fabco, filed a claim for $173,425.63. The claim was allowed in the amount of $166,672.91. The dividend was a cash distribution of $7,221.46. The subsequent preference avoidance complaint sought to recover $91,227.84 from TKA Fabco.

As noted above, creditor surprise is not an element of the present matter, for the adversary proceeding was filed before the dispute over the allowable amount of the proof of claim was resolved. Nevertheless, the surprises that can be inflicted on creditors, if § 502(d) is ignored, are very real and relevant.

Joinder of all disputes concerning the entitlements of a creditor into a single proceeding should expedite, not delay, the administration of bankruptcy cases. Combining claims objections and transfer avoidance spares all parties the inconvenience of

awaiting the outcome of two proceedings in order to know a creditor's net claim against, or indebtedness to, the bankruptcy estate. If creditors are to be subjected to new or continuing preference litigation after their claims have been allowed, § 502(d) will have no substance.

Consolidation of the claim objection and the adversary proceeding presents no procedural problems. A claim objection is a contested matter, pursuant to Fed. R. Bankr. P. 9014, and preference avoidance is an adversary proceeding, pursuant to Fed. R. Bankr. P. 7001(1). However, consolidation of the two disputes raises no problem, for Rule 9014 automatically applies many of the adversary rules to contested matters and authorizes the court to order application of the other adversary rules. Therefore, contested matters, such as objections to claims, are easily consolidated with adversary proceedings.

As the LaRoche court observed, the legislative history shows that § 502(d) was derived from contemporary law at the time of enactment. H.R.Rep. No. 595, 95th Cong., 1st Sess. 354 (1977), reprinted in App. Pt. 4(d)(i); S.Rep. No. 989, 95th Cong., 2d Sess. 65 (1977), reprinted in App. Pt. 4(e)(i); 1978 U.S.C.C.A.N., pp. 5963, 6310, 5787, 5851. Contemporary law in 1977-78 was § 57(g) of the Bankruptcy Act, which is essentially

the same as the current § 502(d).[4]

In Katchen v. Landy, 382 U.S. 323, 86 S.Ct. 467 (1966), the Court relied upon the integral relationship between claim objections and preference avoidance, as set forth in § 57(g), to uphold the jurisdiction of the bankruptcy court over the preference avoidance part of the dispute with the creditor. 382 U.S. at 330-31. The present matter does not involve a dispute over jurisdiction, but Katchen offers useful insight into the importance of not separating the resolution of a creditor's claim from proceedings to recover avoidable transfers received by the same creditor.

Plaintiff has offered no meaningful reason to excuse the allowance of Defendant's claim, in advance of resolution of the preference issue, as required by § 502(d). Therefore, Defendant's motion for summary judgment should be granted.

V. CONCLUSION

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[4] The Bankruptcy Act § 57(g), 11 U.S.C. § 93(g) provided:

> The claims of creditors who have received or acquired preferences, liens, conveyances, transfers, assignments or encumbrances, void or voidable under this title shall not be allowed unless such creditors shall surrender such preferences, liens, conveyances, transfers, assignments, or encumbrances.

Bankruptcy estates should not be administered as if § 502(d) does not exist. When preference avoidance actions are brought independently of objections to claims of the preference defendant, several problems can arise. If the claim objection is resolved before the preference action is commenced, the creditor who received the allegedly voidable preference may be unfairly surprised by a lawsuit alleging that it still owes money to the bankruptcy estate. If the claim objection and the preference litigation proceed as two pieces of litigation, rather than one, there is danger that the estate is being administered inefficiently. If, as in LaRoche and Cambridge, dividends, in the form of money or stock in the reorganized debtor, are distributed to the creditor before resolution of the preference matter, any judgment against the creditor must then be adjusted to account for the amount of money or the value of the securities previously distributed to the creditor on account of its allowed claim. It may even be necessary for the estate to bring an action against the creditor to recover the distribution to the creditor.

In unusually large bankruptcy cases, there may be efficiencies in having different entities and different law firms responsible for claims objections, on the one hand, and preference avoidance adversary proceedings, on the other.

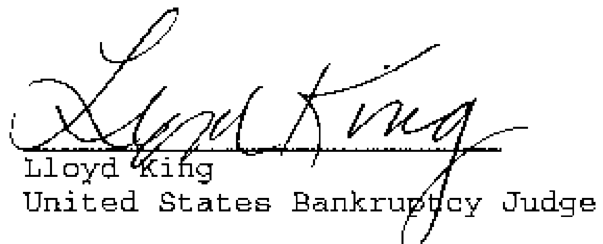
However, as noted above, these efficiencies become illusory when there are creditors who become involved in both claim disputes and preference litigation.

The command of § 502(d) is clear: The preference dispute must be resolved in tandem with the claim objection.

Where there is a court order resolving a dispute over the amount of a creditor's claim, the entry of that order precludes, pursuant to § 502(d), the commencement or continuation of litigation for the recovery from the creditor of allegedly avoidable transfers.

Therefore, since there is such an order concerning Defendant's claim, Defendant's motion for summary judgment in this adversary proceeding will be granted. Summary judgment is appropriate, as there are no factual disputes. The complaint will be dismissed.

July 18, 2003



Lloyd King
United States Bankruptcy Judge