UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION

IN RE:	)	
	)	
Oxford Health Investors, LLC,	)	Case No. 00-80676C-7D
Harnett Health Investors, LLC,	)	Case No. 00-80677C-7D
Nash Health Investors, LLC,	)	Case No. 00-80678C-7D
Fuquay Health Investors, LLC,	)	Case No. 00-80679C-7D
Rocky Mount Health Investors, LLC,	)	Case No. 00-80680C-7D
Greenville Health Investors, LLC,	)	Case No. 00-80681C-7D
	)	(Consolidated for Administration)
Debtors.	)	
	)	
John A. Northen, Trustee in Bankruptcy for the above-named Debtors,	)	
	)	
Plaintiff,	)	
	)	
v.	)	Adversary No. 00-9074
	)	
Centennial Healthcare Corporation; Centennial Healthcare Management Corporation; Centennial Professional Therapy Services Corporation; and Centennial Employee Management Corporation,	)	
	)	
Defendants.	)	

MEMORANDUM OPINION

This adversary proceeding came before the court on May 9, 2002, for hearing upon a motion by defendants for summary judgment. Mark M. Maloney appeared on behalf of the defendants and J. William Blue, Jr. appeared on behalf of the plaintiff.

I. Background

The controversy involved in this adversary proceeding arose out of a business relationship between the defendants and the debtors in which six nursing homes were managed on behalf of the debtors by one of the defendants, Centennial Healthcare Management

Corporation ("CHMC"). Effective January 1, 1998, each of the debtors acquired the right to operate a nursing home facility from the Northstar Holdings, LLC ("Northstar"). Under the agreements with Northstar, each debtor assumed responsibility for management of a specified nursing home and, as a part of the agreements, each debtor became entitled to the revenue derived from the operation of the nursing home and assumed liability for all expenses resulting from such operation.

Contemporaneous with acquiring the right to operate the nursing homes, each of the debtors entered into a management contract with CHMC under which, for a management fee, CHMC agreed to manage the nursing homes for the respective debtors. Under the arrangement, CHMC received the proceeds from debtors' line of credit with Heller Financial and was responsible for paying the vendors, suppliers and entities providing goods and services at the nursing homes. The employees at the nursing homes were employed by Centennial Employee Management Corporation and CHMC also supplied to Centennial Employee Management Corporation the funds required to meet the payroll for the employees at the six nursing homes. Another Centennial entity, Centennial Professional Therapy Services Corporation, was among the entities that provided services at the nursing homes and also received payments from CHMC. CHMC utilized a single operating account for the deposit of the receipts from the six nursing homes managed for the debtors and paid the expenses of

the six nursing homes from such account. This operating account also was used for a number of other nursing homes managed by CHMC.

CHMC managed the six nursing homes under the management contracts with the debtors from January 1, 1998 through August 31, 1999. Effective September 1, 1999, the debtors terminated their relationship with the Northstar entities and turned over the nursing homes to Northstar. However, CHMC's involvement with the nursing homes continued notwithstanding the termination of the relationship between the Debtors and Northstar. Effective September 1, 1999, CHMC began to manage the nursing homes on behalf of Northstar under an interim arrangement similar to the one that it formerly had with the debtors. Additionally, CHMC continued to have involvement with the operations that it had conducted on debtors' behalf prior to September 1, 1999. This latter involvement on the part of CHMC included paying various expenses related to the pre-September 1 operations. These payments were made from the same operating account that CHMC had used prior to September 1, 1999. Such payments by CHMC included substantial amounts that were paid by CHMC to its related entities, CEMC and CPTSC, for services provided at the nursing homes prior to September 1, 1999, as well as payments to CHMC itself for pre-September 1 management fees. Subsequent to September 1, 1999, CHMC also paid various expenses that were incurred during the post-September 1 operation of the nursing homes. These expenses

likewise were paid from the same operating account that CHMC had used prior to September 1, 1999.

The Debtors filed for relief under Chapter 7 on March 17, 2000. This adversary proceeding was commenced on May 19, 2000. The complaint, as amended, alleges claims for turnover of property and accounting, for recovery on an alleged account due, for the avoidance and recovery of alleged preferential transfers and for the avoidance and recovery of alleged fraudulent conveyances. In the motion now before the court, the defendants seek summary judgment as to all of the claims alleged by the plaintiff.

II. Standard under Rule 56

Under Rule 56 of the Federal Rules of Civil Procedure which is incorporated into Rule 7056 of the Federal Rules of Bankruptcy Procedure, summary judgment is proper when there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law. "Where the moving party has carried its burden of showing that the pleadings, depositions, answers to interrogatories, admissions and affidavits in the record construed favorably to the nonmoving party, do not raise a genuine issue of material fact for trial, entry of summary judgment is appropriate." Gutierrez v. Lynch, 826 F.2d 1534, 1536 (6th Cir. 1987)(citing Celotex Corp. v. Catrett, 477 U.S. 317, 106 S. Ct. 2548, 91 L.Ed.2d 265 (1986)); In re Speciality Retail Concepts, Inc., 108 B.R. 104 (Bankr. W.D.N.C. 1989); In re Caucus Distributors, Inc., 83 B.R.

921 (Bankr. E.D. Va. 1988).

A summary judgment movant must make a prima facie case for summary judgment by establishing (1) the apparent absence of any genuine dispute of material fact and (2) movant's entitlement to judgment as a matter of law on the basis of the undisputed facts. See MOORE'S FEDERAL PRACTICE, ¶ 56.13[1](3d Ed. 2002). In determining whether the evidence is sufficient to establish the claim, the evidence must be viewed in the light most favorable to the nonmoving party, and inferences to be drawn from the underlying facts must be viewed in the light most favorable to the party opposing the motion. See In re Trauger, 101 B.R. 378 (Bankr. S.D. Fla. 1989); In re Graham, 94 B.R. 386 (Bankr. E.D. Pa. 1988). However, the existence of a factual dispute is material and precludes summary judgment only if the disputed fact is determinative of the outcome under applicable law. See Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248, 106 S. Ct. 2505, 2510, 91 L.Ed.2d 202 (1986).

The party seeking summary judgment bears the initial responsibility of informing the court of the basis of its motion, and also must identify those portions of the record that it believes demonstrates the absence of a genuine issue of material fact. Only after the movant has sustained the initial burden of production does the burden shift to the nonmovant to show the court that there is a genuine issue for trial. The nonmovant must set

forth the specific facts showing there is a genuine issue for trial. Only when the entire record taken as a whole cannot lead a rational trier of fact to find for the nonmoving party, can the court find there is no genuine issue for trial. See In re Trauger, 101 B.R. at 380, citing Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 587, 106 S. Ct. 1348, 1352, 89 L.Ed.2d 538 (1986).

III. Claims for Turnover and Accounting and Account Due

Count 1 asserts a claim for turnover and accounting. The plaintiff alleges that the defendants came into possession of personal property and accounts receivable of the debtors while CHMC was managing the six nursing homes for the debtors and prays for the recovery of any such property or the proceeds thereof "[t]o the extent that any of the Defendants are in possession, custody or control thereof. . . ." To the extent that any of the defendants are in possession of recorded information, including books, documents, records and papers, relating to the property or financial affairs of the debtors, the plaintiff prays that the defendants be required to turnover or disclose such recorded information to the plaintiff.

Count 2 is a claim for account due and is closely related to Count 1. Plaintiff alleges in Count 2 that a separate accounting is required with respect to each of the debtors and prays for the recovery of "any sums due to each as may be shown to be properly

due and owing after a full accounting. . . ."

Under § 542(a) of the Bankruptcy Code an entity in possession, custody or control of property that the trustee may use, sell or lease is obligated to "deliver to the trustee, and account for, such property or the value of such property, unless such property is of inconsequential value or benefit to the estate." An entity that owes a debt that is property of the estate and that is matured, payable on demand or payable on order, is required by § 542(b) to pay such debt to, or on the order of, the trustee. In order to recover under § 542, the trustee must show that the person from whom turnover is sought had possession, either actual or constructive, of the property or its identifiable proceeds during the bankruptcy case. See In re Shearin, 224 F.3d 353, 356 (4th Cir. 2000); Hager v. Gibson, 109 F.3d 201, 210 (4th Cir. 1997).

The defendants maintain that they are entitled to summary judgment as to the turnover claim because the undisputed facts reflect that no defendant held any property of the debtors as of March 17, 2000, the petition date. The defendants rely upon the affidavit of Andrew Price which states unequivocally that neither CHMC nor any of the other defendants held any property of the debtors as of March 17, 2000. Plaintiff has offered no deposition testimony or affidavits stating that any of the defendants do hold property of the debtors or that dispute the affidavit of Mr. Price. The plaintiff relies upon a February 16, 2000, letter from

Centennial Healthcare Corporation that shows one of the debtors with a substantial positive cash balance as being sufficient to create an issue of fact. However, subsequent correspondence as well as undisputed deposition testimony and the affidavit of Mr. Price, disclose that the letter in question was directed to debtors' parent and was intended to reflect the aggregate balance of all of the facilities referred to in the letter rather than providing the cash positions of the individual facilities. The later correspondence and the affidavit and deposition further reflect that in order to accurately reflect the cash balances of the individual facilities it is necessary to reallocate the cash received from Heller Financial based upon each facility's percentage of the total collections on accounts receivable. Defendants performed such a reallocation and provided the reallocation to the plaintiff. According to the reallocation each of the debtors had a substantial negative cash balance as of September 1, 1999, as well as on December 31, 1999. The deposition testimony of defendants' expert, Alan C. Dahl, and the affidavit of Mr. Price verify the accuracy of the reallocation and the fact that no amount was owed to the debtors when they filed for bankruptcy on March 17, 2000. The plaintiff has brought forward no deposition testimony, affidavits or other evidence that any of the defendants held property of the debtors or were indebted to the debtors when the debtors filed for bankruptcy relief on March 17, 2000. While

the February 16, 2000, letter did reflect a positive balance for one of the debtors, plaintiff has failed to produce evidence that disputes defendants' evidence regarding the need for a reallocation in order to reflect correctly the cash balances of the individual facilities.

In summary, the portions of the record relied upon by the defendants are sufficient to satisfy the initial burden of producing evidence showing that the defendants held no property of the debtors and were not indebted to the debtors on March 17, 2000. The plaintiff has been unable to point to any testimony, exhibit or other evidence that disputes defendants' evidence that no property was held or debts owed by the defendants when the underlying bankruptcy cases were filed. Defendants also have made a showing that they have disclosed and made available to the plaintiff the books and records and available recorded information related to the dealings between the defendants and the debtors. While such documentation and information would have been more readily available and more precise had the defendants utilized separate bank accounts for each of the debtors, the record reflects that defendants have made available the records and recorded information that exists and that such records and recorded information, while not perfect, is sufficient to show that the defendants are not indebted to the plaintiff with respect to any of the six nursing homes. In short, the court is satisfied that from the record,

taken as a whole, a rational trier of fact could not conclude that the defendants are indebted to the plaintiff or that the defendants have failed to provide an accounting to the plaintiff. Summary judgment in favor of the defendants, therefore, is appropriate with respect to the claim for turnover and accounting and with respect to the claim for recovery on an account due.

IV. Preference and Fraudulent Conveyance Claims

The preference and fraudulent conveyance claims involve the payments that were made by CHMC between September 1, 1999, and November 18, 1999. These payments include several large payments that were made to CHMC, Centennial Employee Management Corporation and Centennial Professional Therapy Services Corporation, as well as a number of payments that were made to unrelated vendors who provided goods or services at the six nursing homes. Some of these obligations arose prior to September 1, 1999. The plaintiff contends that the payment of the pre-September 1 obligations constituted preferential transfers that are avoidable pursuant to § 547. The other obligations that were paid by CHMC arose subsequent to September 1, 1999. The plaintiff contends that the payment of these post-September 1 obligations constituted fraudulent transfers that are avoidable pursuant to § 548.

The elements of a preferential transfer under § 547 of the Bankruptcy Code are: (1) a transfer of an interest of the debtor in property; (2) to or for the benefit of a creditor; (3) for or on

account of an antecedent debt owed by the debtor before the transfer was made; (4) made while the debtor was insolvent; (5) made on or within ninety days of the filing of the bankruptcy petition or within one year if at the time of the transfer the creditor was an insider; and (6) the transfer must enable the creditor to receive a greater percentage of its claim than it would under the normal distributive provisions in a chapter 7 liquidation case. See In re Barefoot, 952 F.2d 795, 798 (4th Cir. 1991). Under § 547(g), the plaintiff has the burden of establishing all of the elements of a preferential transfer. See In re Virginia-Carolina Financial Corp., 954 F.2d 193, 196 (4th Cir. 1992).

As pointed out by the defendants, all of the transfers that are included in plaintiff's preference claim occurred between September 1, 1999, and November 18, 1999, which means that the transfers did not occur on or within ninety days of the filing of the bankruptcy petition on March 17, 2000. Although § 547 encompasses transfers to "insiders" that are made within one year of the petition date, the defendants argue that none of the defendants were insiders when the transfers in question were made and that plaintiff's preference claim therefore must fail.

As defined in § 101(31) of the Bankruptcy Code, if the debtor is a corporation, the term "insider" includes (i) director; (ii) officer; (iii) person in control of the debtor; (iv) general partner of the debtor; or (v) relative of a general partner,

director, officer or person in control of the debtor. The term also includes an affiliate of the debtor or an insider of an affiliate as if such affiliate were the debtor, as well as a managing agent of the debtor. See § 101(31)(E) and (F).

Each of the debtors was a special purpose entity which had as its sole purpose the operation of the particular nursing home that was leased from Northstar. It is undisputed that the actual operation of the nursing homes was conducted by CHMC pursuant to the management contracts with CHMC from January 1, 1998, through August 31, 1999. Under these management contracts, CHMC managed every aspect of the operation of the facilities. While conceding that CHMC arguably was in control of the debtors and hence an insider while the debtors were leasing the six facilities and CHMC was managing them, the defendants argue that CHMC ceased to be an insider on August 31, 1999, when the debtors terminated their relationship with Northstar and no longer were leasing the six facilities. Defendants argue that since the debtors no longer had facilities for CHMC to manage after August 31, 1999, they were not controlled by CHMC or any of the other defendants after August 31, 1999. However, there is no evidence in the record that either party took action to terminate the management contracts and, taken in the light most favorable to the plaintiff, the evidence reflects that CHMC continued to perform some of the duties described in the management contracts even after debtors no longer had the right to

continue ongoing operations at the nursing homes. For example, under the management contracts CHMC was obligated to provide for the orderly payment of the accounts payable, employee payroll and other obligations of the facilities to the extent that funds were available. When the operation of the facilities on behalf of the debtors ended on August 31, 1999, the need to provide for the payment of any then-existing obligations of the facilities and the duty of CHMC to do so pursuant to the management agreements did not cease merely because the debtors no longer had any ongoing operational rights. Taken in the light most favorable to the plaintiff, the fact that CHMC continued to make working capital advances to the debtors and to pay obligations that were incurred prior to September 1, 1999, could be construed as CHMC continuing to function under the management contracts. This evidence that CHMC did continue to perform at least some of its duties under the management contracts, together with the absence of any evidence that either party terminated the management contracts, taken in the light most favorable to the plaintiff, point to the management contracts being in effect at the time that the payments in question were made by CHMC. When this circumstance is coupled with the undisputed evidence that the determination of which of debtors' obligations would be paid after August 31, 1999, was completely and totally controlled by CHMC, there is an issue for determination by the trier of fact as to whether the debtors were controlled by CHMC

during the period between September 1, 1999, and November 18, 1999, when the payments in question were made. If this issue were resolved by the trier of fact in favor of the plaintiff, CHMC would be an insider pursuant to § 101(B)(iii). The foregoing evidence also is sufficient to raise a factual issue as to whether CHMC was an "affiliate" of the debtors pursuant to § 101(2)(D), under which an entity which operates a business or substantially all of the property of the debtor under a lease or operating agreement is an affiliate of the debtor. If the issue of whether CHMC was continuing to function under the management contracts were resolved by the trier of fact in favor of the plaintiff, CHMC also would be an insider pursuant to § 101((E) under which an "affiliate" of the debtor is an insider.

If CHMC is an affiliate of the debtors, then each of the other defendants also is an insider. Because it is undisputed that CHMC is a subsidiary of Centennial Healthcare Corporation ("CHC"), CHC is an affiliate of CHMC pursuant to § 101(2)(A) and, hence an insider pursuant to § 101(31)(E). Centennial Professional Therapy Services Corporation would be an insider pursuant to §§ 101(31)(E) and 101(2)(B) because it, too, is a wholly-owned subsidiary of CHC. Centennial Employee Management Corporation likewise would be an insider in that all of its stock is held by an officer of CHC and, as such, is indirectly owned and controlled by an affiliate. It follows that none of the defendants are entitled to summary

judgment based upon the alleged preferential transfers being outside the ninety-day period preceding the bankruptcy filings.

Defendants also argue that summary judgment as to the preference claim is appropriate because the undisputed evidence shows that the alleged preferential payments were not made with funds belonging to the debtors. Rather, defendants argue that the payments were made to serve defendants' business purposes (e.g., preserving business relationships with important vendors) and that defendants used their own money in making the payments. Since the payments were not made with debtor money, defendants conclude that the payments did not diminish the debtors' estates and cannot be the basis for a preference claim under § 547. Additionally, defendants argue that even if the contested payments could be construed to constitute loans to the debtors, the payments nonetheless are not recoverable under § 547 because the earmarking doctrine is applicable with respect to the payments.

Plaintiff argues that CHMC made the payments on behalf of the debtors using checks issued in the names of the debtors and that in order to make such payments, defendants made working capital advances or loans to debtors. Plaintiff contends that upon defendants advancing or loaning funds to the debtors, the loan proceeds became property of the debtors, with the result that debtor money was used to make the payments and preferences thus occurred.

Based upon the source of the funds used to make the contested payments and the manner in which such payments were made as disclosed by the undisputed facts, the court has concluded that such payments, as a matter of law, do not give rise to a valid preference claim under § 547 of the Bankruptcy Code. Although not conceded by plaintiff, the court is satisfied that there is no material factual dispute as to the source of the funds used to pay the pre-September 1 obligations that were paid between September 1 and November 18. It is undisputed that debtors' contracts with Northstar regarding the six facilities were terminated as of August 31, 1999, and that debtors were not generating any income from the six facilities nor receiving any advances from Heller Financial after August 31, 1999. CHMC thus was the source of the funds used to make the contested payments to CHMC and the other Centennial entities who received such payments.[1]

In actuality, the contested payments amounted to CHMC making direct payment of obligations of the debtors without going through the debtors. This occurred by means of CHMC issuing checks on its operating account which were payable to the creditors being paid

---

[1]The only other funds that were available on September 1, 1999, was a $9,845.00 cash balance that CHMC held for Nash Health Investors, LLC. According to the undisputed evidence of the defendants, this entire amount was transferred in the ordinary course of business to Centennial Employee Management Corporation on September 2, 1999, for employee services that had been provided by that entity.

and which were sent directly to such creditors. Such direct payments did not constitute an unconditional loan to the debtors and, in effect, merely substituted a new creditor for the old creditors. Such transactions do not diminish a debtor's estate and therefore do not constitute an avoidable preference within the meaning of § 547. See In re Hartley, 825 F.2d 1067, 1070-71 (6th Cir. 1987); Virginia Nat. Bank v. Woodson, 329 F.2d 836, 839 (4th Cir. 1964).

Another critical point is that the debtors at no time had any control over the funds used to make the payments. The funds came from CHMC and went into an account that was maintained and controlled entirely by CHMC. All decisions regarding when and how much to advance, who to pay with the funds, how much to pay and when such payments should be made were entirely controlled and determined by CHMC. Stated differently, CHMC decided upon the payments to be made, then advanced funds solely for purposes of making such payments, and maintained sole control over the "earmarked" funds until the payments were made. Under such circumstances, the payments by CHMC did not result in any diminution of debtors' estates and for that reason, as well, do not constitute preferential transfers under § 547. See In re Superior Stamp & Coin Co., Inc., 223 F.3d 1004, 1008 (9th Cir. 2000); In re Heitkamp, 137 F.3d 1087, 1089 (8th Cir. 1998); Coral Petroleum, Inc. v. Banque Paribas-London, 797 F.2d 1351 (5th Cir. 1986). It

follows that defendants are entitled to summary judgment with respect to the preference claim.

The transfers or payments that are challenged as fraudulent under § 548 involve post-September 1 obligations that were paid by CHMC. Plaintiff's theory regarding these payments apparently is that the post-September obligations could not have been obligations of the debtors and the payment of such obligations with funds belonging to the debtors constituted a fraudulent transfer under § 548. However, as noted previously, the record reflects that all such payments were made with funds supplied by either CHMC or Northstar. Obviously, payments made with funds furnished to CHMC by Northstar could not constitute a fraudulent transfer of property of the debtors. To the extent that payments were made with funds supplied by CHMC, the funds were advanced and paid out by CHMC in the manner previously described. The claim that payments by CHMC were fraudulent transfers therefore fails for the same reasons as the preference claim. Section 548 provides for the avoidance of the transfer of an "interest of the debtor" that is fraudulent within the meaning of § 548. For the reasons already stated, the post-September 1 payments by CHMC did not constitute transfers of property of the debtors and did not diminish the estates of the debtors. Such payments therefore cannot give rise to a valid claim under § 548. See In re Kelton Motors, Inc., 188 B.R. 125, 128 (D. Vt. 1995)(holding that transfers were not avoidable as either

preferential or fraudulent transfers under the earmarking doctrine), aff'd in part, 97 F.3d 22, 25 (2d Cir. 1996). Defendants' motion for summary judgment therefore will be granted as to the fraudulent transfer claim, as well.

CONCLUSION

In accordance with the foregoing, an order will be entered in this adversary proceeding granting the defendants' motion for summary judgment and dismissing this adversary proceeding.

This 3rd day of September, 2002.

William L. Stocks

WILLIAM L. STOCKS
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION

IN RE:	
Oxford Health Investors, LLC,	Case No. 00-80676C-7D
Harnett Health Investors, LLC,	Case No. 00-80677C-7D
Nash Health Investors, LLC,	Case No. 00-80678C-7D
Fuquay Health Investors, LLC,	Case No. 00-80679C-7D
Rocky Mount Health Investors, LLC,	Case No. 00-80680C-7D
Greenville Health Investors, LLC,	Case No. 00-80681C-7D
Debtors.	(Consolidated for Administration)
John A. Northen, Trustee in Bankruptcy for the above-named Debtors,	
Plaintiff,	
v.	Adversary No. 00-9074
Centennial Healthcare Corporation; Centennial Healthcare Management Corporation; Centennial Professional Therapy Services Corporation; and Centennial Employee Management Corporation,	
Defendants.	

ORDER

In accordance with the memorandum opinion filed contemporaneously with this order, it is ORDERED, ADJUDGED AND DECREED as follows:

(1) Defendants' motion for summary judgment is granted;

(2) The plaintiff shall have and recover no relief from the defendants in this adversary proceeding; and

(3) This adversary is hereby dismissed with prejudice.

This 3rd day of September, 2002.

William L. Stocks

WILLIAM L. STOCKS
United States Bankruptcy Judge