

November 19, 2012

Course of Business Defense Path to Preference Dismissal

Gellert v. Coltec Indus., Inc. (In re Crucible Materials Corp.), 2012 WL 5360945 (Bankr. D. Del. Oct. 31, 2012)

In *Gellert v. Coltec Indus., Inc.*, the Delaware Bankruptcy Court held that the ordinary course of business defense under 11 U.S.C. § 547(c)(2)(A) can be applied on a motion to dismiss, and that a transfer cannot be constructively fraudulent when payment of the transfer resulted in a dollar-for-dollar satisfaction of an antecedent debt.

Crucible Materials Corporation was obligated under a project financing lease to pay periodic interest on bonds and purchase the project for the outstanding full principal amount of the bonds at maturity. Defendant Coltec Industries, Inc.—Crucible’s former parent company—was a guarantor under the bonds. Crucible made payments on the bonds pursuant to its financing agreement for many years prior to its bankruptcy filing. In bankruptcy, the underlying project was sold and Crucible was required to pay off the bonds in full. The liquidating trustee later brought an action against Coltec seeking, among other things, to avoid and recover a periodic interest payment as preferential and to avoid payments made under the financing lease in the two years prior to Crucible’s bankruptcy as constructively fraudulent, under the theory that Coltec was the party for whom the transfers had been made or that the transfers were made for its benefit.

Coltec argued that the court should dismiss the preferential transfer claim pursuant to Federal Rule of Civil Procedure 12(b)(6) on the grounds that the transfer qualified for protection from avoidance as an ordinary course payment under section 547(c)(2)(A). The trustee argued that the ordinary course of business defense is an affirmative defense that cannot be considered on a motion to dismiss and, in any event, the ordinary course of business defense is fact specific and particularly inappropriate for application at the motion to dismiss stage.

Under the facts at issue, the court disagreed with the trustee. As a matter of law, the court held that the ordinary course of business defense can be applied on a motion to dismiss when the “face of the complaint” presents an “insuperable barrier to recovery.” Here, the court noted, the complaint itself alleged that the payment at issue was made in conformity with the schedule for periodic payment under Crucible’s financing and that historically the company made payments pursuant to and consistent with that schedule. Moreover, the court’s opinion does not reflect that the plaintiff—whether under the complaint or in its briefing—made the court aware of any other fact that might counsel against the application of the ordinary course of business defense.

The court also dismissed the trustee’s claim under 11 U.S.C. § 548(a)(1)(B) that the financing lease payments made in the two years prior to Crucible’s bankruptcy filing were constructively

fraudulent. Section 548(a)(1)(B) permits a plaintiff to seek to recover transfers for which the debtor did not receive reasonably equivalent value. Here, the court noted, the payments at issue were made in satisfaction of the debt owed by Crucible under its financing. According to the court, “[w]hen the transfer to a creditor is in dollar-for-dollar satisfaction of an antecedent debt, there can be no claim for constructively fraudulent transfer...This is because the goal of fraudulent transfer law is the preservation of the estate against diminution and a payment which reduces a debt dollar-for-dollar does not diminish the estate.”

Keywords: litigation, bankruptcy, insolvency, Third Circuit, preferential transfer, ordinary course of business defense, constructively fraudulent transfer, reasonably equivalent value, motion to dismiss

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