IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

IN RE:	)	Chapter 7
AE LIQUIDATION, INC., et al.	)	Case No. 08-13031 (MFW)
Debtors	)	Jointly Administered
JEOFFREY L. BURTCH, CHAPTER 7 TRUSTEE	)	
Plaintiff,	)	
v.	)	Adv. No. 10-55502 (MFW)
TEXSTARS, INC.,	)	
Defendant.	)	

MEMORANDUM OPINION[1]

Before the Court is the Complaint of Jeoffrey L. Burtch, the Debtors'[2] chapter 7 trustee (the "Trustee"), seeking to avoid preferential transfers against Texstars, Inc. ("Texstars"). After a trial on the merits, and for the reasons set forth below, the Court concludes that judgment should be entered for Texstars.

I. FACTUAL BACKGROUND

Eclipse developed and manufactured private jets known as the Eclipse 500. Texstars manufactured composite parts that were

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[1] This Memorandum Opinion constitutes the findings of fact and conclusions of law of the Court pursuant to Federal Rule of Bankruptcy Procedure 7052.

[2] The Debtors are AE Liquidation, Inc. (f/k/a Eclipse Aviation Corporation) and its wholly owned subsidiary EIRB Liquidation, Inc. (f/k/a Eclipse IRB Sunport, LLC) (collectively "Eclipse").

designed specifically for the Eclipse 500. These parts were furnished to Eclipse pursuant to a long-term agreement dated March 9, 2006, which provided for net-30 day payment on all invoices (the "Agreement").

During their business relationship, Eclipse's payment of invoices was inconsistent. Eclipse routinely paid invoices to Texstars outside the net-30 day terms of the Agreement and routinely paid multiple invoices with one check. By November 2007, Eclipse had several invoices with Texstars that were over 120 days. As a result, Texstars sent emails to Eclipse advising that its account was "outside agreed terms and conditions" and needed to "be brought current as soon as possible." (Def. Ex. H.) Texstars also sent a letter warning that "if Eclipse [did] not fully cure this non-payment, Texstars would terminate the Agreement." (Def. Ex. P.) Eclipse ultimately cured this default, and Texstars did not terminate the Agreement.

In June 2008, Eclipse again began having financial difficulties. Despite original manufacturing projections of 83 aircraft a month, in June 2008 Eclipse built only 19 planes. (Pl. Ex. 41.) In August 2008, Eclipse reduced its projections to 4 aircraft per month for the balance of 2008. (Pl. Ex. 41.)

In August 2008, an Eclipse representative notified Texstars by phone that Eclipse would no longer be accepting product and would be stopping production. (Tr. 5/10/2013 at 28.) On August

18, 2008, Eclipse sent a letter to Texstars and its other suppliers notifying them of Eclipse's plan to slow production through the end of 2008 with the intent of revamping production in 2009. Id. This letter also stated that Eclipse intended to pay suppliers upfront for new parts and support and to pay off old accounts within sixty days of receiving new financing. Id. The letter indicated that Eclipse expected this new financing to come through in October 2008. Id.

On August 18, 2008, Texstars sent a letter to Eclipse addressing Elipse's "continuing failure to maintain its accounts receivable current with Texstars" and Eclipse's projected cessation of production. Texstars advised that to restart production would "require the payment by Eclipse of all outstanding invoices and accounts receivable." (Pl. Ex. 30.) After receiving this letter from Texstars, Eclipse made ten payments to Texstars totaling approximately $1.4 million in satisfaction of 241 invoices.

On November 25, 2008, Eclipse filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code (the "Petition Date"). On March 5, 2009, the case was converted to chapter 7 and the Trustee was subsequently appointed.

Within the 90 days preceding the Petition Date (the "Preference Period"), Eclipse made nine transfers to Texstars totaling $781,702.61 (the "Transfers"):

Check Number	Check “Cut” Date	Check “Clear” Date	Check Amount
56943	8/28/2008	9/2/2008	$320,087.23
57066	9/3/2008	9/9/2008	$314,167.14
57216	9/10/2008	9/11/2008	$199,346.79
57267	9/17/2008	9/18/2008	$201,309.52
57404	9/24/2008	9/25/2008	$50,481.62
57525	10/1/2008	10/2/2008	$102,326.82
57976	10/15/2008	10/17/2008	$59,288.54
58080	10/22/2008	10/27/2008	$32,475.86
Wire	10/30/2008	10/30/2008	$21,512.20

Also during the Preference Period, Texstars provided $164,654 in new value to Eclipse.[3]

On November 19, 2010, the Trustee commenced the instant adversary proceeding by filing a Complaint against Texstars asserting that the Transfers were avoidable as preferences under section 547(b) of the Bankruptcy Code. On March 14, 2011, Prudential filed an Answer to the Complaint in which it admitted receipt of the Transfers, but denied all other allegations. Texstars also asserted defenses under section 547(c)(2) and (4).

On May 20, 2013, a trial was held, after which the Court took the matter under advisement. Post-trial briefing was completed on August 12, 2013, and the matter is ripe for decision.

[3] Although the parties originally disputed the amount of Texstars’ new value defense, the Trustee has now conceded it to be the amount asserted by Texstars.

II. JURISDICTION

The Court has subject matter jurisdiction over this adversary proceeding pursuant to 28 U.S.C. §§ 1334(b) & 157(b)(1). This proceeding is a core matter pursuant to 28 U.S.C. § 157(b)(2)(A) & (F).

III. DISCUSSION

In the Joint Pretrial Order, Texstars conceded that all the elements of a preferential transfer under section 547(b) of the Bankruptcy Code have been met. At the pretrial conference on May 15, 2013, the Trustee conceded Texstars' new value defense under section 547(c)(4) in the amount of $164,654. Thus, the only issues remaining before the Court are: (1) whether the Transfers fit within the ordinary course of business defense under section 547(c)(2); and (2) if the Transfers were outside the ordinary course of business, whether the Trustee is entitled to prejudgment interest on the avoided Transfers.

A. Ordinary Course of Business Defense

Section 547(c)(2) permits a "safe harbor" for a transferee of a preferential payment if "such transfer was in payment of a debt incurred by the debtor in the ordinary course of business or financial affairs of the debtor and the transferee," and such transfer was (A) "made in the ordinary course of business or financial affairs of the debtor and the transferee," or (B) made according to "ordinary business terms" of the parties or the industry. 11 U.S.C. § 547(c)(2). The burden is on the transferee to prove by a preponderance of the evidence that the transaction between the creditor and debtor meets the ordinary course defense. Miller v. Westfield Steel, Inc. (In re Elrod Holdings Corp.), 426 B.R. 106, 110-11 (Bankr. D. Del. 2010).

The ordinary course of business exception is designed to balance the interests of the debtor and creditors. Fiber Lite Corp. v. Molded Acoustical Prods., Inc. (In re Molded Acoustical Prods., Inc.), 18 F.3d 217, 219 (3d Cir. 1994). In Molded Acoustical, the Third Circuit stated:

> [T]he preference rule aims to ensure that creditors are treated equitably, both by deterring the failing debtor from treating preferentially its most obstreperous or demanding creditors in an effort to stave off a hard ride into bankruptcy, and by discouraging the creditors from racing to dismember the debtor. On the other hand, the ordinary course exception to the preference rule is formulated to induce creditors to continue dealing with a distressed debtor so as to kindle its chances of survival without a costly detour through, or a humbling ending in, the sticky web of bankruptcy.

Id. The Court must be cognizant of a debtor's need to maintain constructive relationships with certain creditors. Thus, when a debtor-creditor relationship "has been cemented long before the onset of insolvency . . . we should pause and consider carefully before further impairing a creditor whose confident, consistent, ordinary extension of trade credit has given the straitened debtor a fighting chance of sidestepping bankruptcy and continuing in business." Id. at 224-225.

The Trustee does not dispute that the Transfers were on account of debt incurred by Eclipse in the ordinary course of business. Texstars is in the business of manufacturing composite aircraft parts, which Eclipse regularly purchased for use on its Eclipse 500 jets. The business relationship between the parties began in March 2006 and continued more than two years. For these reasons, the Court finds that the first prong of section 547(c)(2) is satisfied.

As to the second requirement of section 547(c)(2), Texstars does not contend that the Transfers were made according to "ordinary business terms" of the industry pursuant to section 547(c)(2)(B). Rather, Texstars argues that the Transfers were made in the ordinary course of business between the parties pursuant to section 547(c)(2)(A).

The determination of whether a creditor has met its burden under section 547(c)(2)(A) is a subjective test involving the consistency of transactions between the creditor and the debtor before and during the preference period. SEC v. First Jersey Sec., Inc. (In re First Jersey Sec., Inc.), 180 F.3d 504, 512 (3d Cir. 1999). Courts have considered several factors in determining such consistency: (i) the length of time the parties engaged in the type of dealing at issue; (ii) whether the subject transfers were in an amount more than usually paid; (iii) whether the payments at issue were tendered in a manner different from previous payments; (iv) whether there appears to have been an unusual action by the creditor or debtor to collect on or pay the debt; and (v) whether the creditor did anything to gain an advantage (such as obtain additional security) in light of the debtor's deteriorating financial condition. See Burtch v. Detroit Forming, Inc. (In re Archway Cookies), 435 B.R. 234, 241-42 (Bankr. D. Del. 2010); Hechinger Liquidation Trust v. James Austin Co. (In re Hechinger Inv. Co. of Del., Inc.), 320 B.R. 541, 548-49 (Bankr. D. Del. 2004). No one factor is determinative. Rather, the Court should consider the parties' relationship in its entirety. Burtch v. Revchem Composites, Inc. (In re Sierra Concrete Design, Inc.), 463 B.R. 302, 306 (Bankr. D. Del. 2010).

1. Length of Engagement

In determining whether a creditor can sustain a defense under section 547(c)(2)(A), the Court must first look to the length of the parties' business relationship. Sass v. Vector Consulting, Inc. (In re Am. Home Mortgage Holdings, Inc.), 476 B.R. 124, 136 (Bankr. D. Del. 2012). The Court should determine whether the relationship was "of recent origin," as opposed to being "cemented long before the onset of insolvency." Molded Acoustical, 18 F.3d at 225 ("Bankruptcy policy, as evidenced by the very existence of § 547(c)(2), is to promote such continuing relationships on level terms, relationships which if encouraged will often help a business fend off an unwelcome voyage into the labyrinths of a bankruptcy.”).

In the case at bar, Texstars supplied Eclipse with composite parts for the Eclipse 500 jet for two years. The parties engaged in numerous transactions over this period. The Court finds that this lengthy relationship was sufficient to establish an ordinary course of dealing between the parties. See, e.g., Troisio v. E.B. Eddy Forrest Prods. Ltd., (In re Global Tissue, L.L.C.), 302 B.R. 808, 814 (D. Del. 2003) (holding that the parties’ relationship of 15 months was sufficient); Unsecured Creditors’ Comm. v. CBA Indus., Inc. (In re Color Title, Inc.), 239 B.R. 872, 875 (Bankr. D. Del. 1999) (holding that a relationship that existed for nearly three years was long enough).

2. Similarity of Transfers

Next, the Court must compare transfers made within the preference period to those made in the course of dealing between the parties prior to the preference period. “Courts place particular importance on the timing of payment” in determining the ordinary course of business between parties. Archway Cookies, 435 B.R. at 243 (quoting Radnor Holdings Corp. v. PPT Consulting, LLC (In re Radnor Holdings Corp.), Adv. No. 08-51184(PJW), 2009 WL 2004226, at *5 (Bankr. D. Del. July 9, 2009). Small deviations in timing might not preclude a finding of ordinariness, while greater deviations in timing are more likely to preclude a finding of ordinariness. Archway Cookies, 435 B.R. at 243. Overall, this inquiry is intensely fact specific. Goldstein v. Starnet Capital Grp., LLC (In re Universal Mktg., Inc.), 481 B.R. 318, 327 (Bankr. E.D. Pa. 2012).

The Trustee argues that payments made during the Preference Period were made more quickly and more frequently than those in the pre-Preference Period. Texstars counters that the small deviation in the timing of payments made during the Preference Period is statistically insignificant and thus does not weigh against an ordinary course of business defense.

The Trustee calculated payment timing based on the invoice and check "cut" date, for a Preference Period average of 41.98 days and pre-Preference Period average of 49.68 days from invoice to check cut date. This represents a 15% quicker rate of payment in the Preference Period. The Trustee also notes that, while the range of payment timing spanned from 16 to 456 days prior to the Preference Period, the Preference Period payments fell within the range of 1 to 117 days.

In response, Texstars argues that the "clearing date" of the Transfers is the relevant measure, which results in 45 days between invoice and payment in the Preference Period and 50.2 days between invoice and payment in the pre-Preference Period, or approximately 10% quicker Preference Period payments. Texstars also asserts that all but nine of the hundreds of invoices paid during the Preference Period fall within the eighteen to eighty-two day standard deviation of payment that existed during the pre-Preference Period.

The Court agrees with Texstars that the relevant date for comparison is the clear date rather than cut date, because a creditor is not paid until the check actually clears. If the cut date is used, the calculation could be skewed by the debtor holding the check, by a delay in mail service, and other factors. Regardless of which calculation of payment period is used, however, the Court does not find that a 10 to 15% quicker payment time is significant, given the large deviation in payment timing over the parties' course of dealing (1 to 456 days).

The parties also argue whether the frequency with which Eclipse remitted payment to Texstars is significant. The Trustee argues that, in the Preference period, Eclipse made all but one of its payments (or 89%) to Texstars on a weekly basis. In response, Texstars argues that weekly payments by Eclipse were not unusual in the pre-Preference Period either: thirty-seven of the sixty-one checks (or approximately 61%) during the pre-Preference Period were made within a week of the preceding or following check. Texstars also identifies several extended periods of time in which checks were paid on a weekly basis.

Given the frequency with which Eclipse wrote checks to

Texstars on a weekly basis in the pre-Preference Period, the Court concludes that the weekly payments to Texstars in the Preference Period do not weigh against the ordinariness of the Transfers.

3. Manner of Tender

This factor considers whether any of the Transfers were tendered differently during the Preference Period. See Am. Home Mortg., 476 B.R. at 139. In this case, six of the eight Preference Period checks sent to Texstars cleared one or two days after the check "cut" date, and the final payment was by wire transfer. The Trustee argues that these overnight payments and wire transfer were outside the normal course of business between the parties.

Texstars does not address the overnight checks, but asserts that Eclipse made its last payment by wire at its own discretion, and that a change in the method of payment does not itself take payments out of the ordinary course of business. Logan Square E. v. Peco Energy Co. (In re Logan Square E.), 254 B.R. 850, 856 (Bankr. E.D. Pa. 2000) (holding that while not dispositive, the debtor's payment by cashier's check was a factor the court could consider); Scroggins v. BP Exploration & Oil, Inc. (In re Brown Transp. Truckload, Inc.), 161 B.R. 735, 740 (Bankr. N.D. Ga. 1993) (holding that simple changes in the method of payment by a debtor to a creditor are not enough to make the transaction extraordinary).

The Court concludes that the change in payment method for the sole wire transfer is not significant, where, as here, Texstars did not request payment by wire transfer.[4] See Burtch v. Prudential Real Estate and Relocation Services, Inc. (In re AE Liquidation, Inc.), 08-13031(MFW), 2013 WL 3778141, at * 7 (Bankr. D. Del. July 17, 2013) ("Because Prudential did not insist on the change in payment method, which lasted only three weeks, the last three Transfers will not be considered out of the ordinary course of business for this reason alone.").

As Texstars presented no evidence regarding the existence or frequency of overnight check payment prior to the Preference Period, the Court cannot analyze whether such payments are consistent with the ordinary course of business between the parties.[5] However, because the Court concludes that the timing of payment was not significantly different during the Preference Period, it cannot conclude that the manner of payment (overnight) took the payments outside of the ordinary course of business.

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[4] The Trustee does not argue, or submit any evidence, that Texstars insisted on payment by wire transfer.

[5] The burden is on the Defendant to prove a section 547(c) defense. 11 U.S.C. § 547(g); Elrod Holdings, 426 B.R. at 110-11; Am. Home Mortg., 476 B.R. at 135.

4. Collection Efforts

Unusual collection activity between a debtor and creditor in the preference period can defeat an ordinary course defense. Montgomery Ward, LLC v. OTC Int'l, Ltd. (In re Montgomery Ward, LLC), 348 B.R. 662, 678 (Bankr. D. Del. 2006). Unusual action can include "the potential manipulation of the credit schedules, the threat or initiation of legal action or other unusual behavior designed to improve the lot of one creditor at the expense of the others." Molded Acoustical, 18 F.3d at 225. Telephone calls and other communications may be considered unusual if they represent "a calculated response to a deteriorating creditor-debtor relationship." Am. Home Mortg., 476 B.R. at 139. The Trustee argues that Texstars' August 18, 2008, letter constituted an unusual collection effort sufficient to bring the Preference Period payments outside the ordinary course of business between the parties.

Upon learning that Eclipse would continue to slow down its production through the fall of 2008 and would no longer accept product from Texstars, Texstars sent a letter to Eclipse stating:

> This letter serves as [Texstars'] notice to [Eclipse] of [Eclipse's] continuing failures to maintain its accounts receivable current with Texstars' and of other material breaches of the [Agreement].
>
> Despite repeated assurances by Eclipse that its accounts with suppliers would be maintained as current and that its production schedule would continue to "ramp up" as described in numerous meetings conducted by Eclipse management, it is now clear that neither of those representations is true. Eclipse has failed to

> maintain its account receivables with Texstars as current and, on August 13, 2008, Eclipse advised its suppliers of the complete reversal of its production schedule . . . .
>
> Consequently, in accordance with your request that suppliers respond to Eclipse's radical departure . . . from its previous production schedules, Texstars hereby notifies Eclipse that Texstars will rightsize its business to reflect Eclipse's minimal demand. To restart the cell . . . will require the payment by Eclipse of all outstanding invoices and accounts receivable . . . and a new form of agreement . . . .

(Pl. Ex. 30.)

Texstars denies that this letter was an unusual collection effort. In fact, Texstars' trial witness testified that the letter was not intended as a demand for immediate payment. (Tr. 5/20/2013 at 31.) Rather, Texstars argues that the letter was merely designed to inform Eclipse of the costs that would be incurred as a result of a shut down and subsequent restart of production. As evidence, Texstars points to the November 5, 2007, collection letter, which, in contrast, threatened termination of the Agreement unless receivables were made current. (D. Ex. P.) In the 2007 Letter, Texstars wrote: "This serves as Texstars' notice to [Eclipse] of Eclipse's failure to pay and of pending Material Breach . . . . Further notice is hereby provided that if Eclipse does not fully cure this non-payment . . . Texstars will serve notice of termination of . . . the Agreement." Id.

The Court agrees with Texstars. The August 18 Letter was in response to Eclipse's announced production slow down, in contrast to the 2007 Letter, which was sent solely in response to Eclipse's failure to keep current on its account. While the August 18 Letter complains about Eclipse's "continuing failures to maintain its accounts receivable . . . and of other material breaches," it does not demand immediate payment or threaten to terminate the Agreement. It advises Eclipse that Texstars cannot restart production of the Eclipse 500 parts unless all Eclipse's outstanding accounts receivable are paid in full and a new agreement is reached. However, Texstars does not insist on payment before other creditors nor complain of Eclipse's estimated repayment schedule (October 2008).

In addition, even if the August 18 Letter were unusual collection activity, the Court must still determine whether the Transfers were sent in response to Texstars' collection effort. See In re Craig Oil Co., 785 F.2d at 1566. ("[W]henever the bankruptcy court receives evidence of unusual collection efforts, it must consider whether the debtor's payment was in fact a response to such efforts.").

As discussed above, the payments made by Eclipse after the August 18 Letter (during the Preference Period) did not differ significantly from the payments made during the pre-Preference Period. While Eclipse's accounts receivable balance was reduced during the Preference Period, that was caused in large part by the fact that Eclipse did not buy new product. See, e.g., HLI Creditors Trust v. Metal Techs. Woodstock Corp. (In re Hayes Lemmerz Int'l, Inc.), 339 B.R. 97, 109 (Bankr. D. Del 2006) ("The fact that Defendant significantly reduced its receivables from Debtor during the preference period may be due in part to the fact that Debtor ordered and was shipped substantially less during that period."). Because there is no statistically meaningful difference in the amounts or timing of the payments following Eclipse's receipt of the August 18 Letter from those that preceded the Letter, the Court cannot conclude that the Transfers were paid as a response to the Letter.

5. Advantage in Light of Eclipse's Condition

A creditor may attempt to take advantage of a debtor's financial condition by requesting additional collateral or security, imposing late fees, or pressuring the debtor for payment. Am. Home Mortg., 476 B.R. at 140. Additionally, a creditor's awareness of the debtor's financial condition can indicate that the creditor is attempting to collect a debt ahead of other creditors. Id. However, if the parties had the same relationship for a substantial time frame prior to the debtor's insolvency, actions that appear to take advantage of the debtor may still be in the ordinary course of business. Color Tile, Inc. v. CBA Industries, Inc. (In re Color Tile), 239 B.R. 872, 875 (Bankr. D. Del. 1999).

The Trustee argues that Texstars sent the August 18 Letter in response to Eclipse's declining financial situation and production slow-down to ensure that Texstars' outstanding accounts receivable would be paid. The Trustee asserts that Texstars was aware of Eclipse's declining financial position. To support this assertion, the Trustee points to several news articles reporting the resignation of Vern Raburn as Eclipse's CEO, cancellations of Eclipse 500 orders, delays in delivery of Eclipse jets, the "release" of approximately 190 temporary Eclipse employees, and an announcement of "cashflow problems." (Pl. Ex. 38.) The Trustee also notes Eclipse's extreme slow down in production, of which Texstars was plainly aware, as evidence of Eclipse's deteriorating condition.

Texstars, on the other hand, argues that the August 18 Letter was merely designed to express displeasure at Eclipse's slow down in production. Texstars asserts that it was led to believe by Eclipse that Eclipse would be receiving new financing and revamping production in the future. Such a revamp would have been the only way for

Texstars to recoup costs it had incurred as an Eclipse supplier. (Tr. 5/20/2013 at 60 ("[T]he only way Texstars was going to recover is for Eclipse to be successful.").) Texstars notes that the August 18 Letter did not demand a change in payment practices or condition the continuing supply of goods and services on accelerated payment of outstanding accounts.

The Court concludes that, while Texstars was aware of Eclipse's financial problems, it did not seek to take advantage of Eclipse's position to the detriment of other creditors. It did not seek immediate payment and instead simply accepted Eclipse's promise to repay it when it obtained refinancing.

Texstars' demand for payment of all of Eclipse's accounts before Texstars would restart its production cell is not relevant. Eclipse was never able to revamp its production and thus did not require Texstars to manufacture any further component parts.

For the foregoing reasons, the Court concludes that Texstars has established that the Transfers were within the ordinary course of business of the parties and not subject to avoidance by the Trustee.

V. CONCLUSION

For the reasons stated above, the Court will enter judgment in favor of Texstars.

Dated: October 2, 2013

BY THE COURT:

Mary F. Walrath
United States Bankruptcy Judge

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FOR THE DISTRICT OF DELAWARE

IN RE:	)	Chapter 7
AE LIQUIDATION, INC., et al.	)	Case No. 08-13031 (MFW)
Debtors	)	Jointly Administered
JEOFFREY L. BURTCH, CHAPTER 7 TRUSTEE	)	
Plaintiff,	)	
v.	)	Adv. No. 10-55502 (MFW)
TEXSTARS, INC.,	)	
Defendant.	)	

O R D E R

AND NOW, this **2nd** day of **October, 2013**, after trial of this proceeding on and upon consideration of the parties' respective post-trial submissions, it is hereby

ORDERED that Judgment is entered in favor of Texstars, Inc.

BY THE COURT:

Mary F. Walrath
United States Bankruptcy Judge

cc: Rebecca L. Butcher, Esquire[1]

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[1] Counsel is to serve a copy of this Order and the accompanying Memorandum Opinion on all interested parties and file a Certificate of Service with the Court.

SERVICE LIST

John D. Mattey, Esquire
Robert W. Pedigo, Esquire
Cooch and Taylor
The Brandywine Building
1000 West St., 10th Floor
Wilmington, DE 19801
Counsel for the Trustee

Rebbeca L. Butcher, Esquire
Landis Rath & Cobb LLP
919 Market St., Suite 1800
Wilmington, DE 19801
Counsel for Texstars, Inc.