

IN THE UNITED STATES BANKRUPTCY COURT FOR THE
SOUTHERN DISTRICT OF MISSISSIPPI
JACKSON DIVISION

U.S. BANKRUPTCY COURT
SOUTHERN DISTRICT OF MISSISSIPPI
FILED

MAR 30 1987

MOLLIE C. JONES, CLERK

DEPUTY

IN RE:

ROBERT O. LENOIR
d/b/a SUNFLOWER FOOD STORE
NO. 39, ROBERT O. LENOIR, INC.

BANKRUPTCY CASE
NO. 8501804JC

FIRST BANK OF SOUTHWEST MISSISSIPPI
vs.
ROBERT O. LENOIR

COMPLAINT TO DETERMINE VALIDITY AND PRIORITY OF LIEN
ADVERSARY PROCEEDING NO. 860023JC

MOBILE CHECK EXCHANGE, INC.
vs.
ROBERT O. LENOIR AND
ROBERT G. NICHOLS, JR., TRUSTEE

COMPLAINT FOR PAYMENT OF FUNDS
ADVERSARY PROCEEDING NO. 860044JC

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Trustee

Edward Ellington, Bankruptcy Judge

O R D E R

THIS MATTER came on for hearing on the Complaint to Determine Validity and Priority of Lien filed by First Bank of Southwest Mississippi; Answer filed by Robert O. Lenoir; Answer filed by Mobile Check Exchange, Inc.; and Answer filed by Robert G. Nichols, Jr., Trustee, all pending in Adversary Proceeding No. 860023JC. Consolidated for the purposes of hearing and this Order was a Complaint for Payment of Funds filed by Mobile Check Exchange, Inc., together with an Answer filed by Robert O. Lenoir, an Answer filed by Robert G. Nichols, Jr., Trustee, and an Answer filed by First Bank of Southwest Mississippi, all pending in Adversary Proceeding No. 860044JC.

After examining the facts and considering the same, the Court finds that First Bank of Southwest Mississippi has a valid lien with first priority, but also finds that said lien is only applicable to a portion of the funds requested by its complaint. Thus, First Bank of Southwest Mississippi has a valid claim for \$8,241.62, plus interest, which is held by the Trustee, Robert G. Nichols, Jr.

The Court further finds that Mobile Check Exchange Inc.'s Complaint for payment of funds is well taken in part and should be granted as to a portion of the funds it requested. Thus, Mobile Check Exchange, Inc. is entitled to \$8,024.90, plus interest, which is also held by the Trustee, Robert G. Nichols, Jr.

STATEMENT OF THE CASE

On November 12, 1985, an involuntary petition was filed under Chapter 7 of the Bankruptcy Code for Robert O. Lenoir d/b/a Sunflower Food Store No. 39, Robert O. Lenoir, Inc. (Debtor). Three creditors, First Bank of Southwest Mississippi (First Bank), Distribuco Foods, Inc., and Mobile Check Exchange, Inc. (Mobile) instituted the filing of the involuntary petition. On December 23, 1985, an Order for Relief was entered against Robert O. Lenoir.

The First Meeting of Creditors was held on January 22, 1986. The Debtor's schedules provided that the Debtor was holding \$16,266.52 which was to be paid to Mobile for money orders that the Debtor had sold while still in business.

It is significant to note that the amount of \$16,266.52 is actually the total of two smaller sums, each of which represents a different set of

transactions and circumstances. The first figure, \$8,241.62, represents the amount of a check that had been returned because of insufficient funds. The check had been issued by the Debtor to Mobile for money orders which had been sold by the Debtor. The second figure, \$8,024.90, represents the total amount of money orders sold by the Debtor after he discontinued the use of his checking account and while operating on a cash basis, just prior to the closing of the business.

Subsequent to the First Meeting of Creditors, the funds were turned over to the Trustee until rightful ownership could be determined. Note that the actual amount the Trustee received was \$16,423.66 because interest had accrued during the time in which the Debtor's attorney had held the funds. However, for the purposes of this Order, the Court will refer only to the original amount of \$16,266.52.

On February 12, 1986, First Bank filed a Complaint to Determine Validity and Priority of Lien and claimed that the funds held by the Trustee were actually cash collateral securing their loan and that First Bank was entitled to the money. Similarly, on March 18, 1986, Mobile filed a Complaint for Payment of Funds and claimed that the funds held by the Trustee were cash proceeds from the sale of money orders, and therefore, Mobile was entitled to the money.

The Debtor responded to both complaints and contended that the funds were from the sale of money orders and that Mobile should receive the money. However, the Trustee responded to both complaints by claiming that the funds were property of the estate and that neither First Bank nor Mobile had a valid claim to the money.

DISCUSSION

First Bank, Mobile and the Trustee each contend that they have a valid claim to the funds turned over to the Trustee by the Debtor. However, as noted earlier, the amount of \$16,266.52 is actually the total of two smaller sums representing two different sets of transactions and circumstances. Thus, the Court will address the two figures separately; first, the amount to cover the check returned because of insufficient funds, and second, the amount of the money orders sold just prior to the closing of the business.

I. To Cover The Returned Check - \$8,241.62

The Debtor issued a check to Mobile on August 10, 1985, for money orders which had been sold by the Debtor, but the check was returned because of insufficient funds. Although the check was written from a general fund account of the business, the Debtor testified that the money order sales proceeds were kept in a

cash drawer in his safe separate from other funds of the business until deposited into the checking account. The Debtor stated that special deposit slips were made for the money order amounts in an effort to distinguish those from other type deposits of the business. According to the Debtor, after the check was written, the business was converted to strictly a cash basis operation. He said that in order to cover the returned check, he took \$8,241.62 from the proceeds of the daily business operations. This money was initially turned over to the Debtor's Attorneys in trust and subsequently paid over to the Trustee after the bankruptcy petition was filed.

Mobile contends that this cash money belongs to it because Mobile and the Debtor had a principal/agent relationship and that the funds were being held by the Debtor in trust for Mobile, thus creating a fiduciary relationship. Mobile relies on Sections 75-15-1, 75-15-17 and 75-15-23, Mississippi Code of 1972, to establish that there was a principal/agent relationship between Mobile and the Debtor. Mobile further contends that the commingling of the money order proceeds into the general fund account does not change the relationship from principal and agent to that of creditor and debtor relying on In Re Penn Central Transportation Company, 486 F.2d, 519 (3rd Cir. 1973).

Mobile also argues that since the funds were segregated, identified and created no tracing problems, the money should be turned over to Mobile, citing In Re Martin Fein and Company, 34 B.R. 333 (Bkrctcy. S.D. N.Y. 1983).

After reviewing the state statutes, the Court agrees with Mobile's contention that under state law there existed a principal/agent relationship between Mobile and the Debtor. However, due to the circumstances of this case, this Court finds that once the \$8,241.62 was deposited by the Debtor into his general checking account, commingled and spent, a debtor/creditor relationship also existed. As to this amount, Mobile is relegated to the position of an unsecured general creditor of the estate.

Mobile relies upon Penn Central but the Court finds that the facts of that case are substantially different from the facts of the present case before the Court. Penn Central is a railroad reorganization case pertaining to whether certain interline railroad carriers could take the amounts they owed to the debtor/railroad company and be allowed to set off those amounts against balances that the debtor owed to them. Penn Central involved the system of accounts of interline railroads which is established and governed

by rules promulgated by the Association of American Railroads (AAR). Very simplified,

The AAR interline accounting system is in essence, therefore, a system by which one railroad collects monies owed by shippers to both itself and other railroads. The monies collected belong only in part to the collecting railroad; as to monies owed other railroads, the collecting railroad serves merely as a receiving and transmitting agent.

Penn Central at 523.

In Penn Central, controversy arose when the collecting interline railroads attempted to set off the interline balances they owed Penn Central against amounts owed to them by Penn Central. The question became whether or not the funds which were commingled into general accounts and held by the collecting railroads were held in trust. If the Court determined that a trust was created, the set off would be allowed, but, if no trust existed, there would be no set off.

As an accepted industrial norm, the collecting railroads commingled monies into their general revenues. Penn Central held that while commingling generally indicates a debtor/creditor relationship and not a trust, it is only one characteristic to consider and is not necessarily conclusive. At 524. Thus, the Third Circuit determined that despite commingling, when certain transportation and freight charges were collected, they

were held in trust for the interline carriers, and therefore, could be set off. However, the Court also held that other accounts including car repair accounts, damage accounts, per diem rental accounts and switch accounts were not held in trust and could not be set off.

This Court finds that the Third Circuit in Penn Central decided the limited point that under the AAR system of accounts, freight and transportation collections are considered to be held in trust by the collecting railroad. This Court is not convinced that this specific ruling should be applied under the circumstances of the present case. The Court notes significant differences between Penn Central and the case at hand. The debtor in Penn Central was operating under a specific written and regulated accounting system in which the collecting railroads held the monies collected as a receiving and transmitting agent. Although Robert O. Lenoir held the monies he collected as an agent for Mobile, there were no written guidelines or agreements between Lenoir and Mobile which indicated that there was a trust created or that Lenoir was required to keep the money order proceeds separate from his general funds. In fact, testimony was given that Mobile had instructed Lenoir to start making his payments by check, and therefore, knew that

Lenoir was commingling the money order funds into his general account.

Also, in Penn Central there is no indication that the Debtor spent the interline carriers' monies that it had collected in trust. In the present case, Lenoir had deposited the money order funds into his general account and subsequently used the funds for some other purpose of the business, as the check to Mobile was returned because of insufficient funds.

The \$8,241.62 that the Trustee is holding is not the same money that was collected from the sale of money orders. The Debtor testified that the money held by the Trustee came from the proceeds of doing business after the money order funds were deposited and the bad check was written. Thus, the money order funds collected by the Debtor were commingled and spent and the Court cannot conclude that there is a trust created as to the \$8,241.62 held by the Trustee.

Mobile also relies upon In Re Martin Fein and Company, supra, and argues that where a principal/agent relationship exists and funds are segregated, identified and create no tracing problems, the principal is entitled to the funds held by the agent. This Court agrees with the Bankruptcy Court's conclusions in Martin Fein but finds that they do not apply to Mobile and the facts of this case.

Martin Fein pertains to a case in which the debtor is an auctioneer and is placed in an involuntary

Martin Fein pertains to a case in which the debtor is an auctioneer and is placed in an involuntary Chapter 7. The sole stockholder died approximately two months prior to the involuntary petition and, after his death, three envelopes were discovered containing auction sales proceeds with certain parties' names written on them. The debtor did not maintain special accounts and all auction sales proceeds were deposited into the general corporate account, but these particular proceeds were never deposited. The Court found that under state law there existed a principal/agent relationship by concluding that an auctioneer who conducts a sale is, by virtue of such employment, an agent of the seller. Thus, the Court held that since proceeds from auctions conducted by the debtor for the sellers listed on the envelopes were not commingled with the debtor's funds, but, rather were already segregated, identified and created no tracing problems, the Court could not deny the sellers' entitlement to those proceeds.

In the present case before the Court, the Debtor is the agent of Mobile, but the funds that the Debtor received for Mobile were routinely commingled into the Debtor's general account and later spent for some other purpose of the business. The funds were not segregated or identified after they were deposited into

the general account and it would be difficult trying to determine who exactly received the funds. Thus, Mobile became simply a general unsecured creditor as to the \$8,241.62 deposited into the Debtor's general account.

As for the \$8,241.62 currently being held by the Trustee, Martin Fein has absolutely no bearing. These funds came from the sales of inventory after the money order sales were deposited into the general account and spent. No principal/agent relationship exists between Mobile and the Debtor as to these funds, and therefore, there is no connection between Mobile and the \$8,241.62 held by the Trustee.

First Bank claims that it has a valid security agreement upon all fixtures and inventory and proceeds thereof belonging to the Debtor. First Bank contends the \$8,241.62 held by the Trustee came from the sale of its collateral, and therefore, it has a legal right to the money. This Court finds that First Bank's arguments are well taken and concludes that the Trustee should turn the money over to First Bank.

First Bank placed into evidence three (3) promissory notes, a security agreement and two (2) UCC filings, all claiming a security interest in fixtures and inventory. The documents appear to the Court to be in correct order and no party took issue as to their validity. Thus, the Court concludes that First Bank has a good and valid security agreement.

It was the testimony of the Debtor that the \$8,241.62 held by the Trustee came from doing business after the Debtor had converted his business to a cash basis operation. The Debtor further testified that he had no other sources of income at this time and that he withheld the money in order to cover the check to Mobile that had been returned for insufficient funds. Thus, as testimony indicates, the Court finds that the \$8,241.62 came from the sale of First Bank's collateral and First Bank should be entitled to recover the proceeds thereof.

The Trustee, Mr. Nichols, claims that the \$8,241.62 should be considered property of the Debtor's estate and that Mobile nor First Bank should be allowed to claim the funds. As noted earlier, the Court agrees that Mobile has no valid claim to the funds but finds that First Bank is entitled to recovery. There was no rebuttal testimony or evidence to show that First Bank's security agreement was invalid or that this money was not the result of the Debtor doing daily business by selling inventory in which First Bank had a security interest.

Thus, this Court concludes that First Bank is entitled to recover the \$8,241.62 of the total funds held by the Trustee.

**II. Money Orders Sold Just Prior to Closing
of the Business - \$8,024.90**

After the bad check to Mobile was written, the Debtor converted his business to strictly a cash basis operation. However, the Debtor continued to sell money orders and from August 12, 1985 to August 22, 1985, he sold a total of \$8,024.90.

The Debtor testified that during this time, these money order funds were kept in a cash drawer in a safe; separate from all other business funds. After the business closed, the Debtor took these funds to be held by an attorney, the Honorable Ed Patton, Hazelhurst, Mississippi. Later the funds were transferred to Ms. Chill, the Debtor's bankruptcy attorney, and eventually were received by the Trustee.

Again, Mobile contends that this cash money belongs to it because of the principal/agent relationship existing between Mobile and the Debtor. The Court finds that Mobile's contentions are correct, and thus finds that the \$8,024.90 held by the Trustee should be turned over to Mobile.

The difference between these money order funds and the other funds held by the Trustee for the returned check is the circumstances in which the Debtor handled the money before it was eventually turned over to the Trustee. This \$8,024.90 was directly from the

sale of money orders and was never commingled into the Debtor's general account and remained separate and easily identifiable and traceable at all times. Although there was no written agreement between Mobile and the Debtor, the Court finds that due to their relationship, the funds were held in a trust upon receipt by the Debtor. As noted earlier though, if the funds had been commingled with the other funds of the business, the result would be different. Thus, under these circumstances, the Court follows the decision of Martin Fein and concludes that Mobile is entitled to the funds collected by the Debtor.

First Bank claims that it has a valid security agreement upon all fixtures and inventory and proceeds thereof belonging to the Debtor. First Bank contends the \$8,024.90 held by the Trustee came from the sale of its collateral, and therefore, it has a legal right to the money.

Although the Court finds that First Bank's security agreement is valid, there is no evidence which indicates that this \$8,024.90 is the proceeds of the sale of fixtures or inventory. The money was never commingled with any other business proceeds, thus First Bank's security interest never attached in any way to these funds.

The Trustee claims that the \$8,024.90 should be considered property of the Debtor's estate and that neither Mobile nor First Bank should be allowed to claim the funds. The Court agrees that First Bank has no claim to the funds but finds that Mobile is entitled to recovery. Due to the circumstances in which the money was held by the Debtor and due to the relationship between Mobile and the Debtor, the Court finds that the funds never became part of the Debtor's estate. The funds were merely being held separate and apart and in trust by the Debtor for Mobile.

Thus, this Court concludes that Mobile is entitled to recover the \$8,024.90 of the total funds held by the Trustee.

CONCLUSION

After examining and considering the facts, the Court finds that First Bank of Southwest Mississippi has a valid lien with first priority, but also finds that said lien is only applicable to a portion of the funds requested by its complaint. Thus, First Bank of Southwest Mississippi has a valid claim for \$8,241.62.

The Court further finds that Mobile Check Exchange, Inc.'s Complaint for payment of funds is well taken in part and should be granted only to a portion

of the funds it requested. Thus, Mobile Check Exchange, Inc. is entitled to \$8,024.90.

THEREFORE, IT IS ORDERED that the Trustee, Robert G. Nichols, Jr., shall turn over \$8,241.62, plus any interest that has accrued, to First Bank of Southwest Mississippi.

IT IS FURTHER ORDERED that the Trustee, Robert G. Nichols, Jr., shall turn over \$8,024.90, plus any interest that has accrued, to Mobile Check Exchange, Inc.

SO ORDERED this the 30th day of March, 1987.


U. S. BANKRUPTCY JUDGE