

Timing is Everything

By: Kenneth A. Rosen, Esq.

*"It can happen so fast
Or a little bit late
Timing is everything"*

A song by Garrett Helmund from the movie "Country Strong" released in 2010

Some court decisions are worth re-reading despite their age. *Barnhill v. Johnson* (503 U.S. 393 (1992)) is one of those decisions. It has been cited 807 times!

The task of collecting a past due debt often becomes an exhausting exercise consisting of numerous phone calls, broken promises and never-ending negotiations. Many times, it becomes a situation of "get what you can while you can before it's too late to get anything". It is a shame if, after all your hard work, you end up having to repay to a bankruptcy estate money that you worked so hard to collect.

The *Barnhill v. Johnson* decision, issued by the Supreme Court, is one such case that reminds you that time really matters. If you think that your customer is on the verge of disaster, either go and pick up the check yourself or have someone else in your company pick it up. Then, have the check deposited *immediately*. Saying that someone will be there shortly to pick up the check helps to eliminate the "I'll get to it ASAP" excuse. If that is not possible, have the check sent by overnight courier, demand a bank check, or get a wire transfer of the funds. If someone says that you are overreacting, think about the story of the *Barnhill* decision.

In *Barnhill*, the Supreme Court's task was to determine if a transfer occurred within the 90-day preference period where payment by the debtor was made by an ordinary check. The issue was whether the transfer is deemed to occur on the date the check is *presented* to the recipient or on the date the drawee bank *honors* it. What constitutes a transfer and when it is complete is a matter of federal law.

The debtor's check was in payment of a bona fide debt and was delivered to *Barnhill* on November 18 and honored by the drawee bank *two days later* on November 20, the 90th day before the debtor commenced a bankruptcy case.

Johnson, the trustee of the debtor's estate, commenced an adversary action against *Barnhill*, claiming that the payment was recoverable under 11 U.S.C. § 547(b) as a preference.

Johnson asserted that the transfer occurred on the date that the bank honored the check, but *Barnhill* claimed that it occurred on the date that he received the check.

A person with an account at a bank enjoys a claim against the bank for funds in an amount equal to the account balance. Under the U.C.C., a check is simply an order to the drawee bank to pay the sum stated, signed by the maker and payable on demand.

Barnhill argued that the lower Court of Appeals erred in ignoring the interest that passed from the debtor to *Barnhill* when the check was delivered on a date outside the 90-day preference period. However, the Supreme Court disagreed and noted that there can be no assertion that an unconditional transfer of the debtor's interest in property occurred before November 20 because receipt of a check gives the recipient no right in the funds. The recipient may present the check, but if the drawee bank refuses to honor it, the recipient has no recourse against the bank.

Barnhill's argument that delivery of a check should be viewed as a "conditional" transfer also was rejected. Any claim against the debtor that *Barnhill* gained when he received the check could not be characterized as a conditional right to "property or ... an interest in property," since, until the moment of honor, the debtor remained in full control over the money in the account and the account remained subject to a variety of actions by third

parties, such as a stop payment directive or the bank's ability to refuse to honor the check due to insufficient funds.

Finally, the Court noted in its conclusion that no transfer of property occurs until the time of honor is consistent with **§ 547(e) (2)(A) of the Bankruptcy Code**. That section provides that a transfer occurs at the time the transfer "takes effect between the transferor and the transferee...." Because the debtor retained the ability to stop payment on the check until the very last minute, the Court said that the transfer of funds between the debtor and Barnhill did not take effect until the moment of honor.

As it has been said by the Court of Appeals for the Third Circuit: "Dates matter in bankruptcy." *Timothy Ellis v. Westinghouse Electric Co. LLC*, 11 F.4th 221.

About the Author



Kenneth A. Rosen, Esq - Lowenstein Sandler Chair Emeritus, Bankruptcy & Restructuring Department with more than 35 years of proven experience, Ken is the first call for companies seeking a strategic plan for recovery from financial distress.