RESPECTING THE PARTIES' INTENT: AN ANALYSIS OF THE EARMARKING DOCTRINE AS A DEFENSE TO A BANKRUPTCY PREFERENCE CLAIM IN LIGHT OF IN RE LEE

*By Kelly A. Myers**

Introduction

The Bankruptcy Code, including the amendments made by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"),[1] includes two fundamental policies: (1) treating creditors within the same class equally, and (2) discouraging creditors from dismembering a financially depressed debtor prior to bankruptcy.[2] To effectuate these policies, the Bankruptcy Code affords the trustee (or Chapter 11 debtor-in-possession) power to avoid transfers made by a debtor within a certain time period before the bankruptcy petition is filed if the transfer gives the recipient an unfair advantage over other similarly-situated creditors.[3]

Section 547(b) of the Bankruptcy Code is known as the preference statute. The preference statute allows a trustee to set aside or "avoid" a "transfer" if such transfer: (1) was to or for the benefit of the creditor;[4] (2) was for or on account of an antecedent debt;[5] (3) was made while the debtor was insolvent;[6] (4) was made within the 90-day period prior to filing the bankruptcy petition or within one year of the filing of a bankruptcy petition if made to an insider;[7] and (5) enabled the creditor to receive a greater percentage of its claim than a creditor would have received had the transfer not occurred and had the debtor's assets been liquidated in a Chapter 7 case.[8] In addition to the specifically enumerated elements of § 547(b), a trustee must also prove that there was a transfer of "an interest of the debtor in property . . . ."[9] Although not specifically identified as an element of a voidable preference, the requirement is set forth in the prefatory language of § 547(b).[10]

In recent years, courts have created and creditors have applied the equitable defense of "earmarking" to a trustee's avoidance claim under § 547(b). The earmarking doctrine provides that a pre-bankruptcy transfer to a creditor will not be avoided as a preference if the transfer was "earmarked" for the creditor by a non-debtor third party. The earmarking doctrine was originally allowed only in cases where the non-debtor party that became the new creditor was obligated to pay the prior debt (i.e., guarantor, surety).[11] Most courts have extended the earmarking doctrine's application to situations where the new creditor is not contractually obligated to pay the debtor's prior debt.

The Earmarking Doctrine

The earmarking doctrine essentially holds that if all that occurs within a "transfer" is the substitution of one creditor for another, then no preference is created because the debtor has not transferred any "property of the estate."[12]

> When a third person makes a loan to a debtor specifically to enable that debtor to satisfy the claim of a designated creditor, the proceeds never become part of the debtor's assets, and therefore, no preference is created. The rule is the same regardless of whether the proceeds of the loan are

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transferred directly by the lender to the creditor or are paid to the debtor with the understanding that they will be paid to the creditor in satisfaction of his claim, so long as such proceeds are clearly "earmarked."

If a creditor asserts the earmarking doctrine as a defense to a preference claim, then the trustee bears the burden of proving that the doctrine does not apply.[14] The earmarking doctrine is widely accepted as a defense to a preference claim, primarily because the assets from the third party were never within the debtor's control. Therefore, payment of these assets to a creditor in no way diminishes the debtor's estate.[15]

Courts use one of three different tests to determine if a transaction qualifies for the earmarking doctrine exception. A number of courts, including those within the Sixth Circuit, apply the "intent test." This test was first espoused in *McCuskey v Nat'l Bank of Waterloo (In re Bohlen Enterprises, Ltd)* and requires:

1. The existence of an agreement between the new lender and the debtor that the new funds will be used to pay a specified antecedent debt;
2. Performance of that agreement according to its terms; and
3. That the transaction viewed as a whole (including the transfer in of the new funds and the transfer out to the old creditor) does not result in any diminution of the estate.[16]

Other courts examine the earmarking defense under the "control test," where courts typically consider "whether the new creditor restricted the use of the funds, whether the debtor had physical control over the funds, and whether the debtor had the authority to direct to whom the funds should be paid."[17] The third test involves the court assessing whether the transfer diminished the debtor's estate.[18]

Courts are divided on the applicability of earmarking as a defense to a mortgage avoidance action under § 547(b), where a new creditor refinances existing debt pre-bankruptcy but fails to timely perfect its mortgage interest. In a typical case, a debtor refinances his mortgage pre-petition, and borrows funds from a new creditor. The new creditor pays the prior, "antecedent" secured debt directly to the debtor's original secured creditor. The debtor grants a replacement lien in favor of the new lender in the same real property, which property serves as collateral for the new loan. The problem arises when the new creditor fails to perfect its security interest in the refinanced property within the time parameters set forth in § 547(e)(2), i.e., 30 days (10 days pre-BAPCPA) after the transfer "takes effect."[19] A mortgage transfer "takes effect" when the refinance loan is funded.[20]

Are Two Transfers Better than One?

Courts generally agree that the earmarking doctrine protects a trustee's avoidance claim to recover the original creditor's receipt of funds from the new lender. However, courts are divided as to whether the earmarking defense applies to isolate the new creditor from preference exposure for the untimely perfection of its lien. The disagreement stems from competing views regarding the classification of a mortgage refinance transaction.

The "Two-Transfer" Theory

The "two-transfer" theory of applying the earmarking doctrine bifurcates the refinance transaction into two separate and distinct transfers. The first transfer consists of the initial disbursement of funds to the old creditor from the new creditor, and does not result in a transfer of an interest in the debtor's property. This transfer is protected by the earmarking doctrine. The second transfer occurs when the debtor grants a security interest (mortgage) in the refinanced property to the new creditor. If the security interest is not timely perfected under § 547(e)(2), the transfer results in a preferential transfer avoidable by a trustee.

The seminal case supporting the two-transfer theory is *Vieira v Anna Nat'l Bank (In re Messamore)*.[21] "Although earmarking is appropriate in a refinancing situation as a defense for the old creditor who receives borrowed funds as payment on an antecedent debt, it is illogical to say there was no transfer of the debtor's interest in property to the new creditor when the debtor has granted a security interest to that creditor."[22]

The two-transfer view criticizes the "transaction as a whole" view (discussed *infra*) as failing to distinguish between the transfer of borrowed funds to the original creditor, and the subsequent transfer that occurred when the new creditor perfected its security interest in the debtor's property. The two-transfer camp reasons that it is the second transfer that results in the transfer of an interest of the debtor in property and, ultimately, diminishes the bankruptcy estate. This view holds that, until the refinancing creditor perfects its security interest, it remains an unsecured creditor. Hence, the transfer of the debtor's property does not occur until

the refinancing creditor perfects its security interest. If perfection does not occur within the safe-harbor period prescribed by § 547(e)(2), and if the transfer meets the requirements of § 547(b), then the transfer is deemed preferential and avoided.

The two-transfer view also avers that insulating the second transfer from preference recovery undermines the requirement that a refinancing creditor timely perfect its security interest. The courts employing this view contend that the "transaction as a whole" theory improperly expands the safe-harbor time period provided in § 547(e)(2), effectively allowing a refinancing creditor to untimely perfect its security interest and then rely on the earmarking doctrine as a defense to a preference action. As the court held in *Gold v Interstate Financial Corp (In re Schmiel)*, "the 10-day safe harbor provision simply would have no meaning if a secured creditor could perfect its interest any time after the 10 days [pre-BAPCPA] and then depend upon the earmarking doctrine to somehow avoid the operation of the statute when its [security interest] was later perfected."[23]

The "Transaction as a Whole" Theory

The second view adopted by the courts looks at the mortgage refinancing transaction as a whole, and rejects the "two-transfer" bifurcation argument. Applying the earmarking doctrine, this view concludes that no transfer of an interest of the debtor in property occurs because a secured creditor is merely replaced by another and no diminution to the bankruptcy estate results from the transfer.

Kaler v Community First Nat'l Bank (In re Heitkamp)[24] is the seminal case championing this theory. In *Heitkamp*, the trustee brought an adversary proceeding to avoid the debtors' second mortgage in their home. The debtors borrowed funds from a new lender to satisfy subcontractors' liens against the property. The funds were paid directly to the subcontractors by the new lender and, in return, the debtors granted the new lender a second mortgage. Due to an oversight, the second mortgage was not perfected until several months after the loan was disbursed. The court applied the earmarking doctrine to protect the new lender's security interest, despite the considerable delay in perfecting its security interest. "Because the transfer of the mortgage interest to the bank merely replaced the subcontractors' security interest, there was no transfer of the [debtors'] property interest avoidable under § 547(b)."[25]

Heitkamp and its progeny hold that if the new creditor's funds are earmarked to pay off an existing debt, the funds never become part of the debtor's estate. Applying this rationale to a refinance situation, no avoidable preference occurs even with an untimely perfection of the refinancing creditor's mortgage interest, since there was no transfer of an interest of the debtor in property.[26] Further, because the refinancing creditor's lien merely replaced the original creditor's lien, no diminution of the bankruptcy estate occurs. Distinguishable from the two-transfer theory courts, the transaction-as-a-whole courts view § 547(e)(2) as nothing more than a timing statute as to when a transfer "is made," and hold that the statute does not affect the application of the earmarking doctrine.[27]

To Diminish or Not to Diminish: That is the Question

Section 547(b)(5) of the Code places the burden of proving diminution of the debtor's estate on the trustee in order to prevail in a preference claim.[28] Diminution of the estate under § 547(b)(5) is an element necessary to establish a preference, which is *separate* and *distinct* from the diminution requirement under the earmarking doctrine.

> This Court is persuaded that, under § 547, it is the Trustee's burden to establish that there was in fact a diminution of the debtor's estate. In this case, the Trustee has not shown diminution inasmuch the value of the estate did not change, in fact, not even the identity of the mortgage holder changed. The Refinance Loan added value to the estate, and the Refinance Mortgage encumbered the estate by the same amount. When a debtor exchanges one secured debt for another, the estate is not diminished.[29]

In an unpublished decision, a panel of the Sixth Circuit Court of Appeals addressed the distinct statutory requirement of diminution under § 547(b)(5).[30] In *Spradlin v Inez Deposit Bank (In re Lowe)*, proceeds from the refinance loan were used by the debtor to purchase his ex-wife's marital interest in the residence and to repay the balance owed to the prior mortgagee on the property. The trustee brought a § 547(b) claim to avoid the refinance mortgage. The most interesting and telling aspect of the *Lowe* decision is the court's determination that the mortgage in question was perfected seven days after the transfer took effect and thus was well within the safe-harbor provision of § 547(e)(2). The court could have simply concluded its analysis at that point. However, the court specifically recognized the case of *Gregory v Community Credit Co (In re Biggers)*, stating:

Because the 1996 loan was secured by a mortgage on Mr. Lowe's residence, the granting of a replacement mortgage did nothing to improve the bank's position. It did not give the bank any greater security interest than it had before, and thus it did not diminish the bankruptcy estate. Absent such diminution, the transfer had no preferential effect. *The fifth prerequisite of voidability, § 547(b)(5), was not satisfied.*

> [A]s we understand Section 547(b), the timeliness of perfection of a transfer is indeed irrelevant if the transferee's position is not improved. That is, *if § 547(b)(5) is not satisfied it makes no difference whether the transfer was on account of antecedent debt, the transfer is not voidable.*[31]

Other Circuits have echoed the statutory diminution requirement for a preference action, as set forth in § 547(b)(5). The Fifth Circuit found in *Southmark Corp v Grosz (In re Southmark Corp)* that of particular importance in determining if funds are property of the debtor's estate is "whether the payment of those funds diminished the resources from which the debtor's creditors could have sought payment."[32] The Seventh Circuit, in *Warsco v Preferred Technical Group*, established that diminution of the estate is required to avoid a preference under § 547(b)(5): "In keeping with our prior precedent and that of other circuits, we continue to consider whether the transfer in question diminished the debtor's estate."[33] The Eighth Circuit held in *Carlson v Farmer Home Admin (In re Newcomb)*: "To be avoidable a transfer must deprive the debtor's estate of something of value which could otherwise be used to satisfy creditors."[34] The Ninth Circuit addressed this issue in *Adams v Anderson (In re Superior Stamp & Coin Co, Inc)*:

> Under [the diminution of estate doctrine], a transfer of an interest of debtor in property occurs where the transfer "diminish[es] directly or indirectly the fund to which creditors of the same class can legally resort for the payment of their debts, to such an extent that it is impossible for other creditors of the same class to obtain as great a percentage as the favored one."[35]

The Tenth Circuit Bankruptcy Appellate Panel stated in *Manchester v First Bank & Trust Co (In re Moses)* that "the fundamental inquiry under §547(b) will be whether the Debtor had a legal or equitable interest in the property [transferred] such that the transfer at issue diminished or depleted the Debtor's estate."[36]

The Sixth Circuit's Application of Earmarking and Diminution: *In re Lee* and Its Predecessors

Lee's Predecessors

The earmarking doctrine has been recognized by the Sixth Circuit Court of Appeals, as well as various courts within the Sixth Circuit.[37] In *McLemore v Third Nat'l Bank of Nashville (In re Montgomery)*,[38] the debtor paid off unauthorized loans to Third National Bank with commingled funds. The issue was whether the transfer of property to Third National Bank was properly identified, and whether the debtor had an interest in such property. The *Montgomery* court found that the debtor exercised significant control in choosing which creditors to pay off and held in favor of the Trustee. However, the court recognized that "there is an important exception to the general rule that the use of borrowed funds to discharge the debt constitutes a transfer of property of the debtor . . . ."[39]

> [I]f all that occurs in a "transfer" is the substitution of one creditor for another, no preference is created because the debtor has not transferred property of his estate; he still owes the same sum to a creditor, only the identity of the creditor has changed.[40]

In *Peoples Bank & Trust Co v Burns*,[41] the court reviewed the trustee's § 549(a) post-petition avoidance claim in light of the three requirements (intent test) of the earmarking doctrine. The *Burns* court remanded the case for further fact-finding as to whether the *transactions viewed as a whole* resulted in any diminution of the estate.

On June 26, 2008, the Sixth Circuit Court of Appeals adopted the "two-transfer" theory in *Shapiro v Chase Manhattan Mortgage Corp (In re Lee III)*.[42] Judge Cole, delivering the opinion of the court, in which Judge Griffin joined and Judge Merritt dissented, reversed the order of the District Court and reinstated the Bankruptcy Court's judgment in favor of Trustee, rejecting application of the earmarking doctrine as a defense to Trustee's preference claim under § 547(b).

In re Lee I, 326 BR 704 (Bank ED Mich 2003)

On March 23, 2001, David Scott Lee ("Debtor") obtained a $108,000 loan from Flagstar Bank, FSB to purchase real property located at Pontiac, Michigan ("Property"). The Debtor granted Flagstar Bank a mortgage against the Property to secure the loan

evidenced by a promissory note. Flagstar Bank's purchase money mortgage was recorded on April 18, 2001.

Both the promissory note and the purchase money mortgage were assigned to Chase Manhattan Mortgage Corp. ("Chase") on September 1, 2001, by way of an assignment of mortgage, recorded on February 13, 2002.

On October 6, 2003, Chase refinanced the assigned mortgage loan at a substantially-reduced interest rate and a reduced minimum monthly payment. As part of the refinance transaction, Debtor granted Chase a replacement mortgage on the Property to secure the refinance loan. All proceeds from the refinance loan were used to pay off the purchase money loan and discharge the purchase money mortgage. Debtor received no money from the refinance loan.

The refinance mortgage was recorded on December 17, 2003. The purchase money mortgage discharge was executed on October 27, 2003, but was not discharged as of record until January 16, 2004, 30 days after the refinance mortgage was recorded. At all times relevant, there was a recorded mortgage in favor of Chase on Debtor's property.

On March 4, 2004, Debtor filed a voluntary Chapter 7 bankruptcy petition. The Chapter 7 Trustee filed an adversary complaint against Chase, seeking to avoid Chase's refinance mortgage pursuant to § 547(b).

The parties filed cross-motions for summary judgment. Chase asserted the earmarking doctrine as a defense to Trustee's § 547(b) preference claim. The Bankruptcy Court granted the Trustee's motion for summary judgment and denied Chase's motion for summary judgment.[43] The Bankruptcy Court rejected Chase's argument that it was protected from Trustee's claims under the earmarking doctrine by adopting the "two-transfer" theory. The Bankruptcy Court opined that the first "transfer" (the disbursement of the refinance loan) was protected by the earmarking doctrine, but that the second "transfer" (the debtor's grant of the refinance mortgage) was not. Further, based on this two-transfer theory, the Bankruptcy Court concluded that the second transfer diminished the bankruptcy estate.

In re Lee II, 339 BR 1165 (ED Mich 2006)

Chase appealed to the U.S. District Court for the Eastern District of Michigan, and the District Court issued an order reversing the Bankruptcy Court.[44] Specifically, the District Court found: (1) Trustee failed to prove that the refinance loan and mortgage resulted in any diminution of Debtor's bankruptcy estate under § 547(b)(5), which eliminated Trustee's preference claim; (2) the refinance loan and mortgage was one unitary transaction, *not* two distinct transfers, to which the earmarking doctrine applied; and (3) the refinance mortgage was protected from Trustee's § 547(b) avoidance powers under the earmarking doctrine.

In re Lee III, 530 F3d 458 (CA 6, 2008)

Trustee appealed to the Sixth Circuit Court of Appeals, which adopted the two-transfer theory and concluded that Chase's refinance mortgage was not protected against Trustee's preference claim under the earmarking doctrine. Specifically, the court analyzed the loan transaction and concluded that "the borrower incurs the debt at the time the lender disburses the loan proceeds. Therefore, lenders who advance loan proceeds prior to the recording of the mortgage are undertaking 'a transfer of an interest in the subject property for purposes of § 547.' Such transfers are subject to preferential transfer liability."[45]

Applying this rationale, the court held that Debtor incurred his debt obligation under the refinance loan when Chase disbursed the loan funds on October 6, 2003. Chase did not perfect its refinance mortgage until December 17, 2003, 72 days after the loan proceeds were disbursed and outside the pre-BAPCPA 10-day grace period afforded under § 547(e)(2)(B). Although relying on § 547(e)(1)(A) to determine when the refinance mortgage was perfected, the court rejected Chase's argument that at no time could a bona fide purchaser exist because the purchase money mortgage was not discharged until after the refinance mortgage was recorded. The court opined:

> [T]he fact that third parties may have been on notice of Chase's Original Mortgage [purchase money mortgage] is beside the point. A transfer of an interest in real estate is not necessarily perfected for purposes of § 547(e) when third parties have notice that there *had been* a mortgage on the property. Rather, a transfer of real property "is perfected when a bona fide purchaser of such property from the debtor against whom applicable law permits such transfer to be perfected *cannot acquire* an interest that is superior to the interest of the transferee."[46]

Applying the earmarking doctrine to the Chase refinance transaction, the *Lee III* court rejected what it deemed to be the "minority unitary transaction" view

and adopted the "majority multiple transfers" view. First, the court, in an interesting analysis, determined that the earmarking doctrine did not apply in the subject refinance transaction because Chase was not a "new creditor," as Chase refinanced its own loan.[47] The court went on to further state, however, that even if Chase was deemed to be a new creditor, the earmarking doctrine would not shield it from preference liability as the earmarking doctrine does not protect the "late-perfecting refinancer from preference exposure."[48] The court found that applying a unitary transfer theory, rather than bifurcating the refinance transaction, "would ignore what actually occurred in the transaction and disregard the Bankruptcy Code's plain meaning."[49]

Second, the court established that applying the earmarking doctrine to the transfer of the lien interest, rather than transfer of funds, extends the doctrine beyond its intended use. The challenged refinance mortgage transfer was that of a property interest owned and controlled by Debtor, which met the prefatory element of § 547(b).[50]

Third, the court held that Chase's perfection of the refinanced mortgage diminished the estate because non-exempt equity in the Property that otherwise would have been available to unsecured creditors became encumbered as a result of Chase's refinance mortgage. Hence, Chase could not establish a lack of diminution, the third element necessary for an earmarking defense.[51] Finally, the court found that applying the earmarking doctrine to protect Chase from Trustee's preference claim would "essentially write § 547(e) out of the Bankruptcy Code and, in the process, defeat the sound policy the statute was intended to promote–the discouragement of secret liens."[52]

Turning to the separate and distinct diminution requirement of a preference under § 547(b)(5), the Sixth Circuit relied on its prior analysis of diminution to conclude that Trustee had met this element. The "diminution occurred when *Lee's* [Debtor's] unencumbered, non-exempt equity in the Property once again became subject to perfected lien when the New [refinance] Mortgage was recorded."[53]

In his dissenting opinion, Judge Merritt acknowledged a split in the Circuits on the application of the earmarking doctrine in a loan refinance transaction, and agreed with the rationale espoused in *In re Lee II* and *In re Heitkamp*.

> [W]e should look to the purpose, consequences, details and common sense of the complete refinancing transaction at issue here and not just one little part of the transaction, i.e., the recording of the second mortgage more than 10 days after the execution of the second note and mortgage. We should look to see whether anyone was misled or whether the bankruptcy estate was diminished for reasons prohibited by Congress.[54]

Judge Merritt noted the majority opinion's "mere legalistic manipulation" of §§ 547(b) and (e) to conclude that the earmarking doctrine did not apply to protect Chase's refinance mortgage. From a policy perspective, the court ejected Chase from its security position, despite the fact that Chase had simply agreed to "lighten the load" on Debtor by reducing his interest rate and monthly payments. "Apparently, 'no good deed goes unpunished.'"[55] Especially considering that Chase at all times had a "'perfected' (*i.e.* publicly recorded)" mortgage in place and of public record, Judge Merritt concluded that the court's majority opinion reached an

> unjust and unlawful result by arbitrarily causing the lender [Chase] to lose the entire value of a perfectly valid mortgage for money the lender [Chase] had advanced to the debtor in good faith. No unsecured creditor ever had the slightest basis to believe that he would be entitled to recover his debt from mortgage proceeds. Appellate judges should be aware that subtle incentives exist for trustees to enlarge the bankruptcy estate for a number of reasons–for example, trustees draw additional fees when the estate is enlarged. We must look carefully at interpretations of provisions of the code that enlarge the estate at the expense of secured creditors. In this case, I do not believe it is justified.[56]

The split among the circuits makes this a matured issue for reposit with the U.S. Supreme Court.

Endnotes

1. Title 11 of the United States Code is referred to as the "Bankruptcy Code." Unless otherwise stated, references to the Bankruptcy Code include the amendments made by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"), effective October 17, 2005.
2. *Union Bank v Wolas*, 502 US 151, 161-62; 112 S Ct 527; 116 L Ed 2d 514 (1991).
3. *See* 5 Collier on Bankruptcy, (15th Ed Rev 2005), ¶547.01.

4. 11 USC 547(b)(1).

5. 11 USC 547(b)(2). A transfer is deemed made on account of "antecedent debt" if the debt is incurred prior to the relevant transfer. *See, e.g., Intercontinental Publ'ns, Inc v Perry (In re Intercontinental Publ'ns, Inc)*, 131 BR 544, 549 (Bankr D Conn 1991).

6. 11 USC 547(b)(3). A transfer is made while the debtor was insolvent if, at the time of the transfer, the "fair value" of the debtor's assets is less than the sum of the debtor's debts. *See* 11 USC 101(32).

7. 11 USC 547(b)(4). Section 101(31)(B) and (C) of the Bankruptcy Code defines "insider" to include a "person in control of the debtor." The legislative history reveals that an insider is "one who has a sufficiently close relationship with a debtor that his conduct is made subject to closer scrutiny than those dealing at arms length with the debtor." *In re Schuman*, 81 BR 583, 586 (BAP CA 9, 1987) (citation omitted).

8. 11 USC 547(b)(5).

9. 11 USC 547(b).

10. *See, e.g., Kaler v Community First Nat'l Bank (In re Heitkamp)*, 137 F3d 1087, 1089 (CA 8, 1998); *Krigel v Sterling Nat'l Bank (In re Ward)*, 230 BR 115 (BAP CA 8, 1999); *Int'l Ventures, Inc v Block Properties VII (In re Int'l Ventures, Inc)*, 207 BR 618 (Bankr ED Ark 1997); *Emerson v Federal Sav Bank (In re Brown)*, 209 BR 874 (Bankr WD Tenn 1997); *Tolz v Barnett Bank of S Fla, NA (In re Safe-T-Brake of S Fla, Inc)*, 162 BR 359, 364-65 (Bankr SD Fla 1993). "Property of a debtor's estate includes 'all legal or equitable interests of the debtor in property as of the commencement of the case.'" *Honigman v Comerica Bank (In re Van Dresser Corp)*, 128 F3d 945, 947 (CA 6, 1997) (quoting 11 USC 541(a)(1)).

11. *See, e.g., McCuskey v Nat'l Bank of Waterloo (In re Bohlen Enterprises Ltd)*, 859 F2d 561, 565 (CA 8, 1998); *Manchester v First Bank & Trust Co (In re Moses)*, 256 BR 641, 646 (BAP CA 10, 2000).

12. *See In re Heitkamp*, 137 F3d 1087; *In re Ward*, 230 BR 115; *In re Int'l Ventures, Inc*, 207 BR 618; *In re Brown*, 209 BR 874; *In re Safe-T-Brake of S Fla, Inc*, 162 BR 359.

13. 5 Collier on Bankruptcy, (15th Ed Rev 2005), ¶547.03[2].

14. *See Peoples Bank & Trust Co v Burns*, 95 Fed Appx 801, 2004 WL 834776 (BAP CA 6, 2004). *See also Stingley v AlliedSignal, Inc (In re Libby Int'l, Inc)*, 240 BR 375 (Bankr WD Mo 1999).

15. *See Mandross v Peoples Banking Co (In re Hartley)*, 825 F2d 1067, 1069-70 (CA 6, 1987); *Schilling v Electronic Realty Associates, Inc (In re Hearn)*, 49 BR 143 (Bankr WD Ky 1985); *Hargadon v Cove State Bank (In re Jaggers)*, 48 BR 33, 36-37 (Bankr WD Tex 1985); *see generally Genova v Rivera Funeral Home (In re Castillo)*, 39 BR 45, 46 (Bankr D Colo 1984); *Young v Scandore Paper Box Corp (In re Lucasa Int'l, Ltd)*, 13 BR 596 (Bankr SD NY 1981); *Buckley v Jeld-Wen, Inc (In re Interior Wood Products Co)*, 986 F2d 228 (CA 8, 1993).

16. *See In re Bohlen Enterprises Ltd*, 859 F2d at 566 (cited with approval in *McLemore v Third Nat'l Bank of Nashville (In re Montgomery)*, 983 F2d 1389, 1395 (CA 6, 1993); *Shapiro v Chase Manhattan Mortgage Corp (In re Lee)*, 339 BR 165, 170 (ED Mich 2006) ("*In re Lee II*"), *Gold v Interstate Financial Corp (In re Schmiel)*, 319 BR 520 (Bankr ED Mich 2005)).

17. *See In re Moses*, 256 BR at 650.

18. *Id.*

19. Section 547(e)(2) of the Bankruptcy Code provides:

> (2) For the purposes of this section, except as provided in paragraph (3) of this subsection, a transfer is made–
>
> (A) at the time such transfer takes effect between the transferor and the transferee, if such transfer is perfected at, or within 30 days after, such time, except as provided in subsection (c)(3)(B);
>
> (B) at the time such transfer is perfected, if such transfer is perfected after such 30 days; or
>
> (C) immediately before the date of filing of the petition, if such transfer is not perfected at the later of –
>
> (i) the commencement of the case; or
>
> (ii) 30 days after such transfer takes effect between the transferor and the transferee.

20. *See Lim v Chase Home Fin, LLC (In re Comps)*, 334 BR 235 (Bankr ED Mich 2005).
21. 250 BR 913 (Bankr SD Ill 2000).
22. *Id.* at 918-19.
23. *In re Schmiel*, 319 BR at 529.
24. 137 F3d 1087 (CA 8, 1998).
25. *Id.* at 1089.
26. *See, e.g., In re Ward*, 230 BR 115; *Luker v Lewis Auto Glass, Inc (In re Francis)*, 252 BR 143 *(Bankr ED Ark 2000); In re Lee II*, 339 BR 165.
27. See, *e.g., In re Lee II*, 339 BR at 170 ("Chase paid off the existing mortgage and recorded its interest in the Property, albeit outside the ten-day period provided for in § 547(e). The granting of the loan and recording the mortgage are two sides of the same coin, they are one transaction. To view it any other way would be to elevate form over substance."); *Heitkamp*, 137 F3d at 1089 (the court applied the earmarking doctrine to protect the bank's mortgage from trustee's preference claim under 11 USC 547(b), despite the fact that the mortgage was not recorded within the ten-day safe harbor of 547(e)(2)(A)).
28. *See, e.g., Waldschmidt v Mid-State Homes, Inc (In re Pitman)*, 843 F2d 235, 241 (CA 6, 1988); *Nicholson v First Inv Co*, 705 F2d 410, 413 (CA 11, 1983) ("if the transfer did not diminish the bankrupt's estate, then there could be no preference").
29. *In re Lee II*, 339 BR at 169 (citing *Shapiro v Homecomings Financial Network, Inc (In re Davis)*, 319 BR 532, 536 (Bankr ED Mich 2005)); *see also Gregory v Community Credit Co (In re Biggers)*, 249 BR 873, 877-79 (Bankr MD Tenn 2000).
30. *Spradlin v Inez Deposit Bank (In re Lowe)*, 92 Fed Appx 129 (CA 6, 2003).
31. *Id.* at 133 (citations omitted) (emphasis added).
32. 49 F3d 1111, 1117 (CA 5, 1995).
33. 258 F3d 557, 565, n 11 (CA7, 2001).
34. 744 F2d 621, 626 (CA 8, 1984) (citations omitted).
35. 223 F3d 1004, 1007 (CA 9, 2000) (citations omitted).
36. 256 BR at 645 (citations omitted).
37. *See, e.g., In re Schmiel*, 319 BR 520; *Shapiro v Chase Manhattan Mortgage Corp (In re Lee)*, 326 BR 704 (Bankr ED Mich 2005) ("*In re Lee I*"); *Shapiro v Homecomings Financial Network, Inc (In re Davis)*, 319 BR 532 (Bankr ED Mich 2005); *In re Lee II*, 339 BR 165.
38. *In re Montgomery*, 983 F2d 1389.
39. *Id.* at 1395.
40. *Id.* (quoting *Carol Petroleum Inc v Banque Paribas-London*, 797 F2d 1351, 1356 (CA 5, 1986)).
41. *Peoples Bank & Trust Co v Burns*, 95 Fed Appx 801.
42. 530 F3d 458 (CA 6, 2008) ("*In re Lee III*").
43. *See In re Lee I*, 326 BR 704.
44. *See In re Lee II*, 339 BR 165.
45. *In re Lee III*, 530 F3d at 464-65 (citations omitted).
46. *Id* at 466 (emphasis in original).
47. *Id* at 470 (citations omitted).
48. *Id.*
49. *Id.* at 471.
50. *Id.* at 471-72
51. *Id* at 472.
52. *Id.*
53. *Id.*
54. *Id* at 474.
55. *Id* at 475.
56. *Id.*