

**UNITED STATES BANKRUPTCY COURT  
WESTERN DISTRICT OF NEW YORK**

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**In Re:**

**BK. NO. 93-20144**

**INTERCO SYSTEMS, INC.,**

**Debtor.**

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**C. Bruce Lawrence, Trustee,**

**Plaintiff,**

**A.P. NO. 95-2139**

**vs.**

**DECISION & ORDER**

**C & L Supply Company, Inc.,**

**Defendant.**

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**BACKGROUND**

On January 26, 1993, three "Supplier" creditors of the debtor, Interco Systems, Inc. ("Interco"), filed an involuntary Chapter 7 petition alleging that Interco was not paying its debts as they became due. Interco interposed an answer, claiming that the indebtedness alleged by each of the petitioning creditors was in dispute, and requested that the petition be dismissed. At a pretrial conference on March 16, 1993, Interco indicated that it wished to remain in the Bankruptcy Court and attempt to reorganize under Chapter 11. Because Section 706(a) gives a Chapter 7 debtor acting in good faith the absolute right to convert to Chapter 11 if the case has not previously been converted, counsel for the petitioning creditors and Interco agreed to discuss Interco's desire to proceed in Chapter 11 as an alternative to conducting a trial of the issues under Section 303(h). To afford the parties time for such further discussion, a trial on the involuntary petition was scheduled

for April 2, 1993. On April 1, 1993, a stipulation between Interco and the petitioning creditors was filed with the Court. The stipulation agreed that Interco would go forward with a voluntary Chapter 11 case. After some procedural matters were corrected, the case went forward in Chapter 11 with January 26, 1993 deemed to be the order for relief date.

On June 14, 1993, the Creditors Committee formed in the Chapter 11 case filed a motion pursuant to Section 1112(b) which requested that the Interco case be converted to a Chapter 7 case, or, in the alternative, that a trustee be appointed pursuant to Section 1104(a) (the "Conversion Motion"). Full day evidentiary hearings were held on June 18, 21, 23, 28 and July 9, 1993, and oral argument by counsel was presented on July 14, 1993, at which time the Court reserved on the Conversion Motion.

By a written decision issued on July 19, 1993 the Court determined that the Interco Chapter 11 case should be converted to a Chapter 7 case for cause, and thereafter on July 21, 1993 the designation of the Office of the United States Trustee appointing C. Bruce Lawrence as Trustee (the "Trustee") was filed with the Court.

Interco's business can best be described as a buying group (the "Interco Buying Group"). In the late 1970's and throughout the 1980's, it organized "Subscribers," generally small to medium wholesale or retail distributors of electrical and plumbing supplies located all across the country, and placed orders on their behalf with "Suppliers," manufacturers or national wholesalers of plumbing and electrical supplies. Because Interco made such large purchases with the Suppliers, it was able to negotiate volume sales discounts ("VSD's") with the Suppliers, between 1% and 13% of

purchases, which were then split between the Subscribers and Interco. Interco was also providing Suppliers with greater market penetration, since they might not otherwise obtain orders from many of the Interco Subscribers, which further justified the payment of VSD's. Although during this period, in many if not most cases, orders were actually placed directly by Subscribers with the Suppliers and the goods shipped directly to the Subscribers, nevertheless, Interco was paid for the goods by the Subscribers and it was Interco that was billed by and paid the Suppliers. As a result, during the 1980's when there were very few, if any, defaults in payment by Subscribers, Interco was able to generate substantial profits from its share of VSD's, sign-up fees paid by new Subscribers and the significant "float" on monies received by Interco from the Subscribers before the Suppliers' invoices were due. In its best year, 1989, Interco handled purchases of in excess of \$264,000,000, generating income before taxes of in excess of \$2.9 million. After 1989, the recession hit, building was down nationwide, the volume of purchases decreased, and Subscribers began defaulting on their payments to Interco. However, Interco was still legally obligated to pay the Suppliers for the goods, it was not earning as much on the float, and it failed to react quickly to the change in the business environment and reduce its expenses. As a result, before taxes, Interco lost in excess of \$2,000,000 in 1990 and \$3,000,000 in 1991.

In 1992 Interco began trying to negotiate contracts with Suppliers which would provide that although the Suppliers would now bill and receive payment directly from the Subscribers, they would still pay the VSD's to Interco, which Interco would continue to divide between it and the Subscribers. Under these contracts (the "Direct Payment Contracts") Interco would not have any

credit risk in connection with purchases, but it would also no longer be supplying credit support to the Suppliers, an element of value which at least some of the Suppliers had relied heavily upon. Some of the Suppliers entered into these Direct Payment Contracts. Other Suppliers terminated their relationships with Interco, but in some cases continued to deal directly with former or existing Interco Subscribers.

In January, 1995 the Trustee commenced in excess of 350 separate adversary proceedings to recover alleged avoidable preferences, post-petition transfers and fraudulent conveyances. Among these adversary proceedings was this Adversary Proceeding against C & L Supply Company, Inc. (“C & L”), where the Trustee included in his Complaint:

- (1) A cause of action (the “Preference Cause of Action”) to recover, as an avoidable preferential transfer under Section 547, a payment in the amount of \$874.00 made by Interco to C & L on or about November 15, 1992, a date which was within ninety days of the filing of the involuntary petition against Interco, representing the payment of third quarter 1992 VSD’s allegedly due under the applicable Subscriber Agreement, but which the Trustee asserted had not in fact been earned; and
- (2) A cause of action (the “Post-Petition Transfer Cause of Action”) to recover, as an avoidable post-petition transfer under Section 549, a payment in the amount of \$1,273.00 made by Interco to C & L on or about February 15, 1993, a date after the date of the filing of the involuntary petition and the Order for Relief date, representing fourth quarter 1992 VSD’s allegedly due under the applicable Subscriber Agreement, but which the Trustee asserted had not in fact been earned.

C & L interposed an Answer to the Complaint which included a Motion to Dismiss for

Improper Venue (the “Dismissal Motion”), based upon the provisions of 28 U.S.C. Section 1409<sup>1</sup> (“Section 1409”), as well as a request under 28 U.S.C. Section 1412<sup>2</sup> for venue to be transferred to the United States Bankruptcy Court for the Northern District of Oklahoma, the district in which C & L’s business is located.

In its Dismissal Motion, C & L asserted that:

- (1) Venue in the United States Bankruptcy Court for the Western District of New York was improper in connection with the Preference Cause

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<sup>1</sup> Section 1409(a), (b) & (d) provide:

- (a) Except as otherwise provided in subsections (b) and (d), a proceeding arising under title 11 or arising in or related to a case under title 11 may be commenced in the district court in which such case is pending.
- (b) Except as provided in subsection (d) of this section, a trustee in a case under title 11 may commence a proceeding arising in or related to such case to recover a money judgment of or property worth less than \$1,000 or a consumer debt of less than \$5,000 only in the district court for the district in which the defendant resides.
- (d) A trustee may commence a proceeding arising under title 11 or arising in or related to a case under title 11 based on a claim arising after the commencement of such case from the operation of the business of the debtor only in the district court for the district where a State or Federal court sits in which, under applicable nonbankruptcy venue provisions, an action on such claim may have been brought.

<sup>2</sup> Section 1412 provides:

A district court may transfer a case or proceeding under title 11 to a district court for another district, in the interest of justice or for the convenience of the parties.

of Action because the money judgment which the Trustee was seeking on that Cause of Action was less than \$1,000.00, so that Section 1409(b) required that venue must be in the Northern District of Oklahoma, where C & L's business was located; and

- (2) Venue in the United States Bankruptcy Court for the Western District of New York was improper in connection with the Post-Petition Transfer Cause of Action because the action by the Trustee to recover the payment made by Interco of fourth quarter 1992 VSD's in February, 1993 was based on a claim arising after the commencement of the Chapter 11 case from the operation of the business of Interco, so that under Section 1409(d) the proceeding could only be brought in the district where, under nonbankruptcy law venue provisions the claim could have been brought, which was not in the Western District of New York.

The Trustee's Response to the Dismissal Motion (the "Response") asserted that for purposes of Section 1409(b) the Trustee's Adversary Proceeding as a whole was a "proceeding" within the meaning and intent of that subsection, and, therefore, the money judgment sought in his Preference and Post-Petition Transfer Causes of Action must be aggregated. As a result, the money judgment the Trustee was seeking in the "proceeding" was \$2,147.00, an amount in excess of the stated \$1,000.00 amount, so that the limitation on Section 1409(a) contained in Section 1409(b) was inapplicable.

The Trustee also asserted in his Response that: (1) his Post-Petition Transfer Cause of Action was not a claim which arose by reason of the post-petition operation of Interco's business, within the meaning of Section 1409(d); and (2) under the terms of the Subscriber Agreement presumed to have been entered into between Interco and C & L, the Trustee's claim for an improper payment

made under that Agreement could be brought under nonbankruptcy law in the New York State Supreme Court, Monroe County, which is located in the Western District of New York.

## **DISCUSSION**

### **I. 28 U.S.C. Section 1409(d)**

Section 1409(d) mandates that venue for claims arising from the post-petition operation of a debtor's business be brought by a Trustee or a debtor-in-possession only in a court where venue would be proper under applicable nonbankruptcy law. In this case, the Post-Petition Transfer Cause of Action is to recover the payment made post-petition by Interco, while it was still operating in Chapter 11, for VSD's which if properly earned, would have been earned by and payable to C & L for the period ending December 31, 1992, a time prior to the filing of the petition. The only act of Interco which occurred post-petition, and could arguably be considered to be part of the post-petition operation of its business, was the forwarding of a check to C & L. The Trustee in his Complaint maintained that the payment for fourth quarter VSD's was improper and avoidable because it was for VSD's which were not properly earned by C & L for the pre-petition quarter ending December 31, 1992.

I find that the Trustee's Post-Petition Transfer Cause of Action is not a claim arising from the operation of Interco's business within the meaning and intent of Section 1409(d). In fact, the

claim arises from the operations of the businesses of both Interco and C & L for the pre-petition period ending December 31, 1992. Therefore, venue is proper under Section 1409(a) in the United States Bankruptcy Court for the Western District of New York.

Furthermore, although the Court has not been presented with a copy of the actual Subscriber Agreement entered into between Interco and C & L, all of the Subscriber Agreements which the Court has reviewed in connection with the numerous other adversary proceedings brought by the Trustee contain a Jurisdiction Provision which specifically states that the Agreement is deemed to have been made within the State of New York and shall be interpreted according to the laws of the State of New York, and allows for service of process by Interco on the subscriber by certified or registered mail at the subscriber's last known address. Clearly this provision, labeled "Jurisdiction" in the Subscriber Agreements prepared by Interco, was intended by the parties to provide for jurisdiction in the State of New York should Interco have a claim arising under the terms of the Subscriber Agreement. Therefore, absent a bankruptcy proceeding, any such claim by Interco arising under the Subscriber Agreement would be proper in the New York State Supreme Court, Monroe County (located within the Western District of New York), where Interco had its principal place of business. Therefore, venue under nonbankruptcy law for a claim for the return of an improper payment under the Subscriber Agreement is proper in the Western District of New York.

By reason of the foregoing, the limitation of Section 1409(d) does not apply to the Trustee's Post-Petition Transfer Cause of Action, and venue is proper in the United States Bankruptcy Court for the Western District of New York under Section 1409(a).



**II. 28 U.S.C. Section 1409(b)**

Since, as discussed above, venue for the Post-Petition Transfer Cause of Action is proper in the United States Bankruptcy Court for the Western District of New York, and that cause of action was properly joined by the Trustee with his Preference Cause of Action, the money judgment the Trustee is seeking in the Adversary Proceeding is in excess of \$1,000.00. Therefore, the limitation of Section 1409(b) does not apply, and venue for the entire “proceeding” is proper in the United States Bankruptcy Court for the Western District of New York under Section 1409(a).

**III. Motion for Transfer of Venue Under 28 U.S.C. Section 1412**

\_\_\_\_\_A party seeking a discretionary venue change must establish grounds for the change of venue by a preponderance of the evidence, and the district in which the underlying bankruptcy case is pending is presumed to be the appropriate district for a proceeding in bankruptcy. In addition, the inconvenience to parties is to be balanced in determining proper venue. *See In re Manville Forest Products Corp.*, 896 F.2d 1384, 1390-91 (2d Cir. 1990). This Court is in the process of handling in excess of 350 similar adversary proceedings involving avoidable preference and post-petition transfer causes of action by reason of Interco’s payment of third and fourth quarter 1992 VSD’s. All of the Debtor’s records with respect to these payments are located within this District, as is the Trustee and his professionals, and the ongoing Chapter 7 liquidation case is being handled here. Consideration of all of the facts and circumstances presented, including judicial economy, the interests of justice and the convenience of the parties, mandates that venue for this Adversary Proceeding remain in the United States Bankruptcy Court for the Western District of New York.

**CONCLUSION**

C & L's Motion to Dismiss for Improper Venue and its Motion to Transfer Venue to the United States Bankruptcy Court for the Northern District of Oklahoma are each in all respects denied.

**IT IS SO ORDERED.**

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/s/  
**HON. JOHN C. NINFO, II**  
**U.S. BANKRUPTCY JUDGE**

**Dated: April 23, 1996**